[JOINT COMMITTEE PRINT]

DESCRIPTION AND ANALYSIS OF PROPOSALS RELATING TO THE RECOMMENDATIONS OF THE NATIONAL COMMISSION ON RESTRUCTURING THE INTERNAL REVENUE SERVICE, S. 1096, AND H.R. 2676 AS PASSED BY THE HOUSE

SCHEDULED FOR PUBLIC HEARINGS

BEFORE THE

SENATE COMMITTEE ON FINANCE

BEGINNING ON JANUARY 28, 1998

PREPARED BY THE STAFF

OF THE

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INTRODUCTION

The National Commission on Restructuring the Internal Revenue Service (the "Commission") was established to review the present practices of the Internal Revenue Service ("IRS") and to make recommendations for modernizing and improving its efficiency and taxpayer services. The Commission's report, issued June 25, 1997,[1] contains recommendations relating to executive branch governance and management of the IRS, Congressional oversight of the IRS, personnel flexibilities, customer service and compliance, technology modernization, electronic filing, tax law simplification, taxpayer rights, and financial accountability. S. 1096, the "Internal Revenue Service Restructuring and Reform Act of 1997," introduced on July 30, 1997, by Senators Kerrey and Grassley, generally mirrors the recommendations of the Commission. H.R. 2676, the "Internal Revenue Service Restructuring and Reform Act of 1997," was passed by the House on November 5, 1997.[2] H.R. 2676 is similar in many respects to S. 1096, but contains certain differences which are described in this pamphlet.

The Senate Committee on Finance ("Finance Committee") has scheduled public hearings on the IRS restructuring proposals beginning on January 28, 1998. Finance Committee investigative hearings on IRS practices and procedures were held on September 23–25, 1997. These hearings followed a six-month long investigation under the direction of Chairman Roth, and examined both the internal and public conduct of the IRS.[3] The Finance Committee's Subcommittee on Taxation and IRS Oversight held a field hearing in Oklahoma City, Oklahoma on December 3, 1997, to hear testimony on improving IRS management and operations and to investigate allegations of taxpayer rights abuses in the Oklahoma-Arkansas District. The Finance Committee hearings addressed issues relating to the environment and culture at the IRS, treatment of taxpayers and IRS employees, effectiveness of the Inspections Division and the Taxpayer Advocate, and the ability of the National Office to ensure that National Office policies are consistently followed in the various districts. Two recent IRS internal audit reports (issued after the 1997 Finance Committee hearings), entitled *Review of the Use of Statistics and the Protection of Taxpayer Rights in the Arkansas-Oklahoma District Collection Field Function* (December 5, 1997), and *Use of Enforcement Statistics in the Collection*

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[1] Report of the National Commission on Restructuring the Internal Revenue Service, *A Vision for a New IRS*, June 25, 1997 (the "Commission Report").

[2] The House Committee on Ways and Means ordered reported H.R. 2676 on October 22, 1997 (H. Rept. 105–364, October 31, 1997). H.R. 2676 was amended by the House to include (as new Title VI) the provisions of H.R. 2645 ("Tax Technical Corrections Act of 1997") as reported by the House Committee on Ways and Means (H. Rept. 105–356, October 29, 1997). Title VI of H.R. 2676 is not described in this pamphlet.

[3] See Senate Committee on Finance, *Practices and Procedures of the Internal Revenue Service*, S. Hrg. 105–190 (Government Printing Office), for a transcript of the hearings and witness testimony.

Field Function (January 12, 1998) addressed similar issues. The December 5, 1997 IRS report concluded that the emphasis on productivity and statistics is an integral part of managing the Arkansas-Oklahoma District, and that formal and informal communication of these goals with employees has resulted in the perception among some revenue officers that they are evaluated, at least in part, on whether the individual meets these targets. The IRS audit report did not find direct reference to enforcement statistics or quotas in the official evaluations of revenue officers, but did find the use of some enforcement statistic in the evaluations of some group managers and some groups had established group goals. Further, in the 67 seizure cases reviewed, the IRS audit report did not find any illegal seizures, but did find that actions taken in 23 cases did not meet the IRS procedural requirements or could be viewed as inappropriate treatment of the taxpayer. The January 13, 1998 IRS report concluded that the IRS has created an environment driven by statistical accomplishments that places taxpayer rights and a fair employee valuation system at risk, and that changes in IRS culture should be made to reduce the risk of future lapses in the critical areas of taxpayer rights and performance measures.

This pamphlet,[4] prepared by the staff of the Joint Committee on Taxation ("Joint Committee staff"), contains a description and analysis of the Commission's recommendations and of S. 1096 and H.R. 2676 relating to executive branch governance and Congressional oversight of the IRS (Part One), and a description of the provisions of S. 1096 and H.R. 2676 relating to electronic filing (Part Two) and taxpayer protections and rights (Part Three).[5] Part Four presents the estimated budget effects of the provisions of H.R. 2676 as passed by the House. Appendix A lists the meetings held by the Joint Committee staff with IRS Restructuring Commissioners and others regarding the Commission's study. Appendix B contains a memorandum from the Congressional Research Service to the Commission (June 4, 1997).

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[4] This pamphlet may be cited as follows: Joint Committee on Taxation, *Description and Analysis of Proposals Relating to the Recommendations of the National Commission on Restructuring the Internal Revenue Service, S. 1096, and H.R. 2676 as Passed by the House* JCS–1–98), January 23, 1998.

[5] The provisions of S. 1096 and H.R. 2676 relating to personal flexibilities and budget law changes are beyond the scope of this pamphlet. The revenue offset provision contained in H.R. 2676 is also beyond the scope of this pamphlet.

PART ONE: EXECUTIVE BRANCH GOVERNANCE AND CONGRESSIONAL OVERSIGHT

I. PRESENT LAW AND PRACTICES

A. Organization of the Internal Revenue Service

History

Before the establishment of the Office of Commissioner of Internal Revenue, taxes were collected by "supervisors" of collection districts who were appointed by the President, subject to Senate confirmation. These supervisors worked under the direct control of the Department of the Treasury. The Office of the Commissioner of Internal Revenue was established by an act of Congress (12 Stat. 432) on July 1, 1862, and the first Commissioner of Internal Revenue (the "Commissioner") took office on July 17, 1862.

In 1953, the Bureau of Internal Revenue was renamed the Internal Revenue Service ("IRS"), following a major 1952 reorganization into a three-tier structure with a multi-functional National Office, nine regional offices headed by Regional Commissioners, and a number of district offices within each region, headed by District Directors who reported to the Regional Commissioner. An independent inspection function was established to report directly to the Commissioner. An appellate program was instituted in the offices of the Regional Commissioners. Regional Counsel were appointed as the chief legal advisors to each of the Regional Commissioners.

In 1955, the first service center was established as a pilot program in Kansas City, Missouri. The service center provides a central location for mass returns processing and mathematical verification of returns. In 1956, the second service center was established in Andover, Massachusetts. From 1953 until 1980, the IRS was reorganized almost every year, but no major changes resulted to the three-tier structure. The names of positions changed, certain positions were abolished and re-established, districts were combined and separated, and functions were combined and separated.[6] In 1980, the IRS agreed to develop a multi-year budget and program plan. In 1982, the appeals function was assigned to the Regional Counsels. In 1995, the appeals function was reassigned to the Regional Commissioners. Currently, as the result of the 1995 reorganization, there is a regional commissioner, a regional counsel and a regional director of Appeals for each of the following four regions: (1) the Northeast Region in New York, New York; (2) the

[6] For example, in 1964, the position of Associate Chief Counsel (Technical) was abolished. In 1965, the position of Associate Chief Counsel (Technical) was re-established, and the Deputy Chief Counsel position was abolished. In 1971, the Deputy Chief Counsel position was re-established. The same type of restructuring occurred within the office of the Commissioner: in 1955, the Assistant Commissioner (Planning) was abolished and became the Assistant to the Commissioner. In 1958, the position of the Assistant Commissioner (Planning and Research) was established, replacing the Assistant to the Commissioner.

Southeast Region in Atlanta, Georgia; (3) the Midstates Region in Dallas, Texas; and (4) the Western Region in San Francisco, California. There are 33 district offices, 10 service centers, and three computing centers.

Functional organization

The IRS is organized by function. The functions of the IRS include customer service, forms processing, examination, collection, and criminal investigation. Operations are conducted on a decentralized basis in each region and each district, that is, each district generally has its own Examination Division, Collection Division, Criminal Investigation Division, and Taxpayer Service Division. The IRS structure also contains offices related to two specific areas of tax law: International and Employee Plans & Exempt Organizations.[7] The National Office integrates the specialized functions carried out by each region to provide consistency. For example, the Assistant Commissioner (Collection) provides and supervises nationwide programs for collection of unpaid accounts. The mission of the National Office is to develop broad nationwide policies and programs for the administration of the internal revenue laws and related statutes, and to direct, guide, coordinate, and control the endeavors of the Internal Revenue Service.[8]

The Commissioner is the head of the National Office. The Office of the Commissioner includes: the Commissioner; the Deputy Commissioner; the Chief Inspector; the Taxpayer Advocate;[9] the Chief of Headquarters Operations; the Chief Information Officer; the Chief of Management & Administration; the Chief Operations Officer; and the Chief Financial Officer. The Chief Operations Officer is the official responsible for administering the most public functions of the IRS including Customer Service, Forms Processing, Examination, Collection, Criminal Investigations, Employee Plans & Exempt Organizations, and International. The Chief, Management & Administration, the Chief Information Officer, and the Chief Financial Officer are responsible for administering the support functions of the IRS including human resources, systems development, and the budget.

The Executive Committee is the principal decision and policy making body of the IRS.[10] It generally meets monthly and focuses on high level policy and operational issues.[11] Other internal governing bodies of the IRS include the IRS Investment view Board and the Senior Council for Management Controls.

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[7] See discussion relating to Employee Plans & Exempt Organizations in Part One. I. C., *infra*.

[8] Internal Revenue Manual ("IRM") 1112.21.

[9] It has long been recognized that taxpayers need assistance in dealing with the IRS. In 1979, the Problem Resolution Officer (later Taxpayer Ombudsman) became as assistant commissioner. The Taxpayer Ombudsman identified areas of the tax law that confuse or create inequity for taxpayers and supervised cases handled under the Problem Resolution Program. In 1996, P.L. 104–168 added section 7802(d) to the Code, establishing the Office of the Taxpayer Advocate, whose function is to assist taxpayers in resolving problems with the IRS and propose legislative and administrative changes as appropriate to mitigate such problems.

[10] IRM 1112.231.

[11] The Executive Committee consists of the Commissioner; the Deputy Commissioner; the Chief of Staff; the Chief of Taxpayer Service; the Chief Compliance Officer; the Chief of Management & Administration; the Chief Financial Officer; the Chief Information Officer; the Taxpayer Advocate; the Chief Inspector; the Chief Counsel; the National Director of Appeals; the Executive Officer for Service Center Operations; the four Regional Counsels; and the National President of the National Treasury Employees Union.

The Commissioner receives private sector advice from the Advisory Group to the Commissioner of the Internal Revenue ("CAG"). This group provides an organized public forum for discussions of tax administration issues between IRS officials and representatives of the public. The group has been comprised of tax professionals, members of academia, heads of state departments of revenue and taxation, and corporate executives. The members serve without compensation, and offer constructive observations about broad tax administration and organizational issues. The CAG holds two public meetings each year.

Treasury Office of Inspector General; IRS Office of the Chief Inspector

The Treasury Office of Inspector General is charged with conducting independent audits, investigations and reviews with the objectives of helping the Department of Treasury accomplish its mission, improve its programs and operations, promote economy, efficiency, and effectiveness, and prevent and detect fraud and abuse. Under the provisions of the Inspector General Act of 1978, as amended, Treasury's OIG reports to the Congress semiannually on its activities. Among other duties, the Treasury Inspector General is responsible for oversight of internal audits and investigations by the IRS Office of the Chief Inspector.

The IRS Office of the Chief Inspector (Inspection Service) generally is responsible for carrying out internal audits and investigations that: (1) promote the economic, efficient, and effective administration of the nation's tax laws; (2) detect and deter fraud and abuse in IRS programs and operations; and (3) protect the IRS against external attempts to corrupt or threaten its employees. Since its establishment in 1952, the IRS Inspection Service has functioned as an independent organization. The Chief Inspector reports directly to the Commissioner and Deputy Commissioner of the IRS. The IRS Inspection Service is divided into two functions: Internal Security and Internal Audit. The Internal Security Division is responsible for investigating, among other things, allegations of criminal and serious administrative misconduct by IRS employees (e.g., bribery, embezzlement, unauthorized use or disclosure of taxpayer information, and conflicts of interest). The Internal Audit Division is responsible for providing IRS management with independent reviews and appraisals of all IRS activities and operations. In addition, Internal Audit makes recommendations to improve the efficiency and effectiveness of programs and to assist IRS officials in carrying out their program and operational responsibilities.

B. Appointment of the Commissioner and Chief Counsel

The Commissioner is appointed by the President, with the advice and consent of the Senate.[12] The Commissioner's duties and powers are prescribed by the Secretary of the Treasury. The Secretary has delegated the responsibility to administer and enforce the Internal

[12] Internal Revenue Code ("Code") section 7802(a).

Revenue laws to the Commissioner.[13] The Commissioner has the final authority of the IRS concerning the substantive interpretation of the tax laws as reflected in legislative and regulatory proposals, revenue rulings, letter rulings and technical advice memoranda.[14]

The President appoints the Chief Counsel for the IRS, who is the chief law officer for the Internal Revenue Service. The Chief Counsel's duties are prescribed by the Secretary of the Treasury.[15] The Secretary of the Treasury has delegated authority over the Chief Counsel to General Counsel of the Treasury.[16] The General Counsel has delegated the authority to serve as the legal adviser to the Commissioner to the Chief Counsel.[17]

The duties of the Chief Counsel include the duty to: furnish legal opinions as necessary; to prepare and review rulings and technical advice memoranda; prepare, review or assist in the preparation of proposed legislation, treaties, regulations, and Executive Orders relating to laws affecting the IRS; handle the legal aspects of all matters pertaining to the assessment and collection of federal taxes; review certain claims for refund; make recommendations concerning offers in compromise and closing agreements; and supervise collection of taxes from taxpayers involved in bankruptcy, insolvency, liquidation, receivership or reorganization proceedings. The Office of Chief Counsel conducts tax litigation in Tax Court, and makes recommendations concerning prosecutions and appeals to the Tax Division of the Department of Justice, which conducts Federal tax litigation in all courts other than the Tax Court.

C. Formation and Structure of the Office of Employee Plans and Exempt Organizations

Establishment of EP/EO

Prior to 1974, no one specific office in the IRS had primary responsibility for employee plans and tax-exempt organizations. As part of the reforms contained in the Employee Retirement Income Security Act of 1974 ("ERISA"), Congress statutorily created the Office of Employee Plans and Exempt Organizations ("EP/EO") under the direction of an Assistant Commissioner.[18] EP/EO was created to oversee deferred compensation plans governed by sections 401–414 of the Code and organizations exempt from tax under Code section 501(a).[19]

In general, EP/EO was established in response to concern about the level of IRS resources devoted to oversight of employee plans and exempt organizations. In creating the office, Congress explicitly acknowledged that the regulatory oversight responsibilities delegated to EP/EO differ from the core revenue collection and enforcement functions of the IRS. Both the House and Senate reports on the legislation conclude that, with respect to administration of

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[13] Treasury Department Order ("T.D.O.") No. 150–10 (April 22, 1982). See also Rev. Proc. 64–22, 1964–1 C.B. 689.

[14] T.D.O. No. 150–02, 1994–1 C.B. 721; General Counsel Order ("G.C.O.") No. 4 (July 1, 1997).

[15] Code section 7801(b)(2).

[16] T.D.O. 107–04 (July 25, 1989).

[17] G.C.O. No. 4.

[18] Code section 7802(b).

[19] For a summary of the circumstances surrounding the creation of EP/EO), see Jim McGovern and Phil Brand, "EP/EO—One of the Most Innovative and Efficient Functions Within the IRS," *Tax Notes*, August 25, 1997, pp. 1099–1104.

laws relating to employee plans and exempt organizations, "the natural tendency is for the Service to emphasize those areas that produce revenue rather than those areas primarily concerned with maintaining the integrity and carrying out the purposes of exemption provisions."[20] The Senate report noted:

> Concern has been expressed in the case of the administration of employee benefit plans (and also tax-exempt organizations) as to whether the Internal Revenue Service with its primary concern with the collection of revenues is giving sufficient consideration to the purposes for which these organizations are exempt. Many believe that the present organization of the Service causes it to subordinate concern for the protection of the interest of plan participants (or the educational, charitable, etc., purposes for which the exemptions are provided).[21]

To provide funding for the new EP/EO office, ERISA authorized the appropriation of an amount equal to the sum of the excise tax on investment income of private foundations (assuming a rate of 2 percent[22]) as would have been collected during the second preceding year plus the greater of the same amount or $30 million.[23] The Senate-passed version of ERISA specified that the funds provided by the taxes "are to be used only for activities delegated to this new office and may not be transferred or used by the Internal Revenue Service in any other manner."[24] Despite this expression of legislative intent, amounts raised by the section 4940 excise tax have never been dedicated to the administration of EP/EO, but are transferred instead to general revenues. Table 1 sets forth revenues raised by the section 4940 excise tax for fiscal years 1971 to 1995. Thus, the level of EP/EO funding, like that of the rest of the IRS, is dependent on the amount requested by and granted to the

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[20] S. Rept. 93–383, 108 (1973). See also H. Rept. 93–807, 104 (1974).

[21] S. Rept. 93–383, 107–108 (1973). See also H. Rept. 93–807, 103 (1974).

[22] The Tax Reform Act of 1969 generally imposed a 4-percent excise tax on the net investment income of private foundations. The stated rationale for imposition of the tax was that foundations should share some of the costs of government, particularly the costs of administering the tax law relating to exempt organizations. As part of the Revenue Act of 1978, Congress reduced the section 4940 tax rate to 2 percent, on the grounds that "the tax has produced more than twice the revenue needed to finance the operation of the Internal Revenue Service with respect to tax-exempt organizations." S. Rept. 95–1263, 6981 (1978). In 1984, Congress found that collections from the section 4940 excise tax continued to exceed the costs of administering the employee plan and exempt organizations programs. Joint Committee on Taxation, *General Explanation of the Revenue Provisions of the Deficit Reduction Act of 1984 (H.R. 4170)*, 98th Cong., P.L. 98–369 (JCS–41–84), 672, December 31, 1984. Consequently, Congress further reduced the section 4940 excise tax from 2 percent to 1 percent in cases where there is an equivalent increase in the foundation's qualifying distributions for charitable purposes. No amendment was made to section 7802(b)(2); accordingly, the authorized funding for EP/EO is calculated on the basis of a 2-percent excise tax rate. Thus, amounts of section 4940 excise tax actually collected since 1984 are somewhat lower than the amounts that would actually be used in calculating EP/EO funding under section 7802(b)(2).

[23] Code section 7802(b)(2). As passed by the Senate, the legislation authorized the appropriation of revenues from a proposed annual $1 audit-fee tax to be imposed on employers for each plan participant under section 4974, as well as one-half of the revenue from the 4-percent excise tax on private foundation investment income under section 4940. At that time, the investment income tax on foundations was yielding $56 million and the audit-fee tax was anticipated to raise approximately $30 million. Thus, total funding for EP/EO would have been approximately $58 million. S. Rept. No. 93–383, 109–110 (1973). The $1-per-participant audit fee tax was dropped in conference, however, and the funding calculation changed to its present formulation. H. Rept. No. 93–1280, 333 (1974).

[24] S. Rept. No. 93–383, 110 (1973).

IRS and the Treasury Department through the annual Congressional appropriations process.[25]

Table 1. Section 4940 Excise Tax Collections, 1971–1995

Fiscal year	Collections ($ millions)
1971	24.6
1972	56.1
1973	76.6
1974	60.9
1975	63.8
1976	59.9
1977	78.6
1978	84.0
1979	63.2
1980	65.3
1981	84.1
1982	93.2
1983	112.4
1984	146.8
1985	136.2
1986	217.2
1987	218.1
1988	229.4
1989	168.8
1990	204.3
1991	173.8
1992	204.7
1993	223.1
1994	235.4
1995	213.7

Source: Internal Revenue Service.

Responsibilities of EP/EO

EP/EO is responsible for overseeing the administration and enforcement of Federal tax laws relating to employee benefit plans and tax-exempt organizations. EP/EO's mandate includes not only enforcing applicable Federal tax laws and collecting the proper amount of tax revenue, but also protecting the rights of benefit plan participants and contributors to and beneficiaries of tax-exempt organizations.

The two primary programs through which EP/EO seeks to ensure compliance with the requirements for tax exemption of nonprofit organizations and plan trusts and qualification of employee benefit plans are the determination letter program and the examination process. The determination letter program is one in which the taxpayer applies for a ruling from the IRS as to its qualification for

[25] Funding for EP/EO is a separate line item in the President's budget for the IRS under the general category of "Tax Law Enforcement." Other line items in this category are criminal investigations, examination, collection, statistics of income, chief counsel, tax fraud and financial investigations, international, SOI/compliance research, document matching, and resources management (compliance). *Budget of the United States Government, Fiscal Year 1998, Appendix,* H. Doc. 105–003, Vol. 1., pp. 874–875.

tax-exempt status. In 1996, the IRS received 80,763 applications for exemption from plan trusts and approximately 70,000 applications for recognition of tax-exempt status from nonprofit organizations. In that same year, EP issued approximately 115,000 determination letters for employee plans and EO issued approximately 70,000 determination letters for tax-exempt organizations. Currently, approximately 200 IRS technical specialists process EO determination letters and approximately 140 technical specialists process EP determination letters. Through its examination process, the IRS seeks to ensure that employee benefit plans and exempt organizations continue to meet Federal tax requirements. In calendar year 1993, there were 561,773 returns filed by tax-exempt organizations[26] and 1,156,901 returns filed by employee benefit plans.

EP has primary responsibility relating to the Federal tax qualification of employee plans and related trusts, the tax treatment of employees participating in such plans and their beneficiaries, and deductions for employer contributions to plans. EP National Office provides policy guidance to the EP/EO Key District Offices ("KDOs") (described further below), including examination and training materials and technical advice. In addition, the actuarial branches of EP process funding waiver requests and perform other actuarial analyses. EP administers a number of programs designed to assist employee plans in complying with Federal tax rules, including the Master and Prototype Program (a compliance program created to allow advance approval of model retirement plans), the Administrative Policy Regarding Self-Correction, the Walk-in Closing Agreement Program, the Voluntary Compliance Resolution Program, and the Tax Sheltered Annuity Voluntary Compliance Program.

EO has primary responsibility relating to tax-exempt organizations, including unrelated business income tax rules. EO also oversees Code section 527, which governs the taxation of political organizations. In 1993, EO assumed responsibility for the administration of IRS activities with respect to tax-exempt bonds. EO National Office provides policy guidance to the KDOs, processes rulings on exemption issues referred by KDOs, issues rulings on prospective transactions, and issues technical advice and assistance. EO is developing the Voluntary Compliance Nonresident Alien Withholding Program, a program similar to those administered by EP, in an effort to promote voluntary compliance and self-correction on the part of exempt organizations.

The Field Systems Branch supports the information and data management needs of EP/EO in the field, as well as at the National Office headquarters.

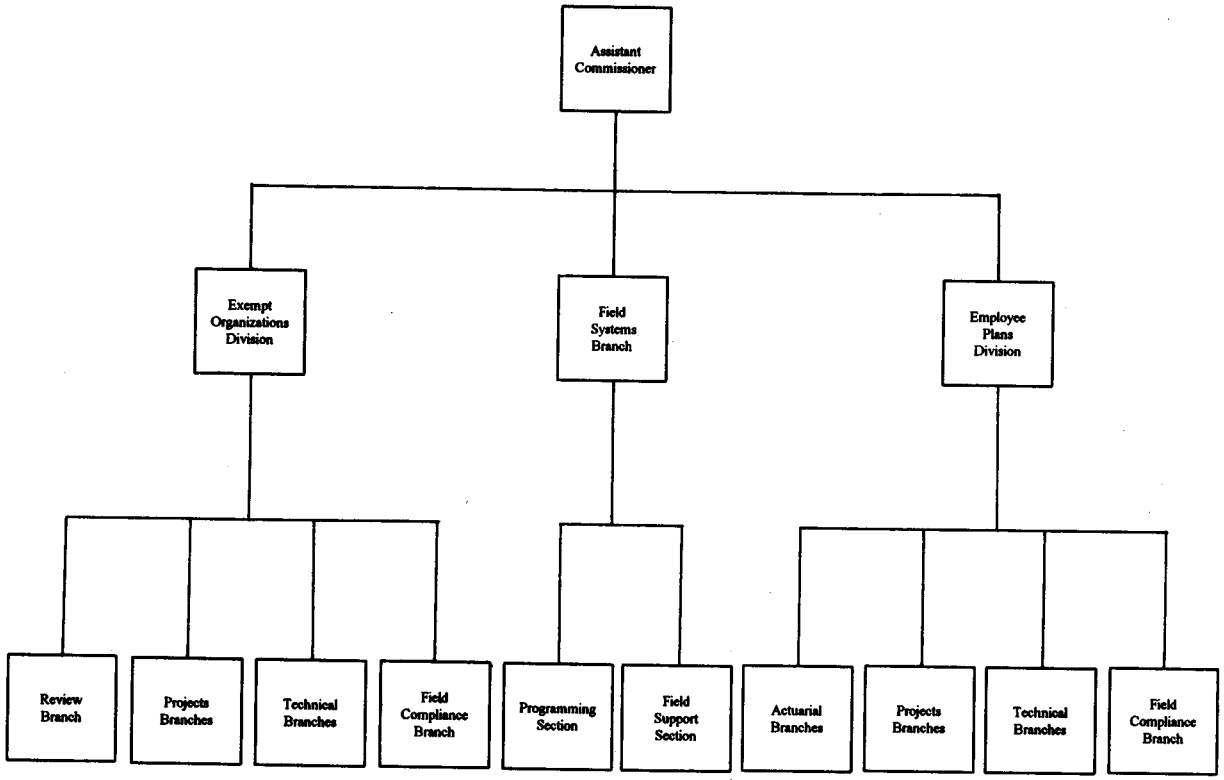
Structure of EP/EO

EP/EO is comprised of National Office headquarters and five key district offices (KDOs). As set forth in the diagram below, the head-

[26] Not all tax-exempt organizations are required to file annual information returns (Form 990). For example, churches and certain small organizations are not required to file Form 990. Thus, as set forth below, the total number of tax-exempt organizations far exceeds the number of returns filed annually.

quarters EP/EO function includes the Employee Plans Division, the Exempt Organizations Division, and the Field Systems Branch.

Office of the Assistant Commissioner, EP/EO



The KDO located in Cincinnati, Ohio, recently has become the centralized determination letter processing site. Examination jurisdiction is vested in four KDOs: Northeast (Brooklyn), Southeast (Baltimore), Midstates (Dallas), and Western (Los Angeles). Although the EP/EO Assistant Commissioner has general programmatic authority over the field offices, there is no direct line authority. Thus, the National Office cannot initiate or oversee the day-to-day conduct of examinations. Rather, such authority is exercised by the District Directors of the respective KDOs.

EP/EO resources

In addition to establishing the Office of Employee Plans and Exempt Organizations, ERISA also statutorily authorized the creation of a number of high-level executive positions for purposes of staffing the new office.[27] Most significantly, the bill authorized an additional 20 so-called "supergrade" positions in EP/EO at the levels of GS–17 and 16.[28] This unprecedented concentration of high level positions attracted a pool of talented people from both within and outside of the IRS to staff the new EP/EO function. Since 1974, as a result of a various internal reorganizations and redefinition of staffing priorities, all but four of these EP/EO "supergrade" positions have been reallocated elsewhere within the IRS and Treasury.

For 1997, EP/EO has 2,117 funded positions. Approximately 250 of these positions are assigned to National Office headquarters and the remainder are assigned to the five KDOs. As set forth on Table 2, the aggregate staffing level remains essentially what it was when EP/EO was formed in 1974. In fact, the 1997 staffing level is approximately 20 percent below the 1989 peak staffing level.

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[27] Section 1051(a) of the Employee Retirement Security Act of 1974 (amending secs. 5108 and 5109 of Title 5 of the United States Code).

[28] As part of a general reorganization of the Federal government civil service personnel structure that took place in 1979, the "supergrade" system was replaced by the Senior Executive Service system.

Table 2. EP/EO Staffing and Budget Authority, 1975–1997

Fiscal year	Funded positions	President's budget authority [1] ($ millions)
1975	2,075	.....
1976	2,175	.....
1977	2,202	.....
1978	2,292	62.2
1979	1,945	64.1
1980	1,870	66.9
1981	1,738	68.9
1982	1,640	55.0
1983	1,770	80.8
1984	1,906	90.4
1985	1,902	94.3
1986	2,099	99.0
1987	2,311	104.9
1988	2,562	120.9
1989	2,573	125.8
1990	2,423	132.8
1991	2,336	132.3
1992	2,461	140.9
1993	2,331	143.1
1994	2,305	129.8
1995	2,304	132.5
1996	2,197	128.8
1997 (est.)	2,117	129.6

[1] Pre–1995 totals include funding for support positions from other divisions of the IRS.

Source: Internal Revenue Service.

Growth of the EP/EO sector

As of 1990, there were approximately 900,000 private retirement plans with nearly 77 million participants, controlling nearly $3 trillion in assets. This compares with approximately 30 million plan participants in 1974, when EP/EO was created. The Federal income tax expenditure (i.e., foregone tax revenues) associated with the net exclusion from income for pension contributions and earnings is estimated to be $87.3 billion for 1998 and $470.7 billion for the five-year period 1998–2002.[29]

Similarly, the number of tax-exempt organizations has nearly doubled since 1974. At the end of 1996, there were approximately 1,280,000 tax-exempt organizations and an estimated 340,000 churches, controlling assets in excess of $1.1 trillion. In contrast, in 1974, there were 690,000 tax-exempt organizations (excluding churches). The Federal income tax expenditure related solely to the deduction allowed for contributions to charities (a subset of all tax-

[29] Joint Committee on Taxation, *Estimates of Federal Tax Expenditures for Fiscal Years 1998–2002* (JCS–22–97), December 15, 1997.

exempt organizations) is estimated to be $23.3 billion in 1998, and $129.0 billion for 1998–2002.[30]

The total volume of all outstanding tax-exempt bonds in 1996 was approximately $1.3 trillion. The total volume of such bonds issued in 1993 was $336 billion. The Federal income tax expenditure related to the exclusion of interest on tax-exempt bonds is estimated to be $25.3 billion for 1998, and $143.7 billion over the five-year period 1998–2002.[31]

D. Congressional Oversight of the IRS and Duties of the Joint Committee on Taxation

Congressional oversight of the IRS

Under the present Congressional committee structure, a number of committees have jurisdiction with respect to IRS oversight. The committees most responsible for IRS oversight are the House Committees on Ways and Means, Appropriations, Government Reform and Oversight, the corresponding Senate Committees on Finance, Appropriations, and Governmental Affairs, and the Joint Committee on Taxation (the "Joint Committee"). While these Committees have a shared interest in IRS matters, they typically act independently, and have separate hearings and make separate investigations into IRS matters. Each committee also has exclusive jurisdiction over certain issues. For example, the House Ways and Means Committee and the Senate Finance Committee have exclusive jurisdiction over changes to the tax laws. Similarly, the House and Senate Appropriations Committees have exclusive jurisdiction over IRS appropriations. The Joint Committee does not have legislative jurisdiction, but, as discussed more fully below, has significant responsibilities with respect to tax matters and IRS oversight.

Joint Committee on Taxation

Creation and history of the Joint Committee on Taxation

In 1924, Senator James Couzens (Michigan) introduced a resolution in the Senate for the creation of a Select Committee to investigate the Bureau of Internal Revenue. At the time, there were reports of inefficiency and waste in the Bureau and allegations that the method of making refunds created the opportunity for fraud. One of the issues investigated by the Select Committee was the valuation of oil properties. The Committee found that there appeared to be no system, no adherence to principle, and a total absence of competent supervision in the determination of oil property values.

In 1925, after making public charges that millions of tax dollars were being lost through the favorable treatment of large corporations by the Bureau, Senator Couzens was notified by the Bureau that he owed more than $10 million in back taxes.[32] Then Treasury Secretary Andrew Mellon was believed to be personally responsible for the retaliation against Senator Couzens. At the time, Treasury

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[30] *Ibid.*

[31] *Ibid.*

[32] According to *Esquire* magazine, the Internal Revenue Commissioner personally handed to Senator Couzens a bill for $10 million. Berendt, John, "The Tax Audit," *Esquire,* February 1994, p. 18.

Secretary Mellon was the principal owner of Gulf Oil, which had benefited from rulings specifically criticized by Senator Couzens.

The investigations by the Senate Select Committee led, in the Revenue Act of 1926, to the creation of the Joint Committee on Internal Revenue Taxation.[33] The first Chief of Staff of the Joint Committee on Internal Revenue Taxation was L.H. Parker, who had been the chief investigator on Senator Couzens' Select Senate Committee. The Revenue Act of 1926 empowered the Joint Committee on Internal Revenue Taxation to investigate the administration of the Federal tax laws and directed the Committee to publish from time to time for public examination and analysis proposed measures and methods for the simplification of internal revenue taxes and required the Joint Committee to provide a written report to the House and Senate by December 31, 1927, with such recommendations as it deemed advisable. The Joint Committee published its initial report on November 15, 1927, and made various recommendations to simplify the Federal tax system, including a recommendation for the restructuring of the Federal income tax title.

In the Revenue Act of 1928, the Joint Committee's authority was extended to the review of all refunds or credits of any income, war-profits, excess-profits, or estate or gift tax in excess of $75,000. In addition, the Act required the Joint Committee to make an annual report to the Congress with respect to such refunds and credits, including the names of all persons and corporations to whom amounts are credited or payments are made, together with the amounts credited or paid to each.

Since 1928, the threshold for review of large tax refunds has been increased from $75,000 to $1 million in various steps and the taxes to which such review applies has been expanded. Other than that, the Joint Committee's responsibilities under the Internal Revenue Code have remained essentially unchanged since 1928.

The Joint Committee is composed of 10 Members, 5 from the Senate Finance Committee (3 majority and 2 minority Members) and 5 from the House Committee on Ways and Means (3 majority and 2 minority).

General duties and powers of the Joint Committee on Taxation

The statutory duties of the Joint Committee include the duty (under sec. 8022 of the Code):

- to investigate the operation and effects of the Federal tax system;
- to investigate the administration of Federal taxes by the IRS or any executive agency charged with their collection;
- to make such other investigations in respect to such system as the Joint Committee deems necessary;
- to investigate measures and methods for the simplification of such taxes, particularly the income tax;
- to publish for public examination and analysis proposed methods and measures for such simplification; and

[33] The name of the Joint Committee on Internal Revenue Taxation was changed to the Joint Committee on Taxation in the Tax Reform Act of 1976.

- to report to the Committee on Finance and the Committee on Ways and Means and, in its discretion, the Senate or the House or both, the results of its investigations and any recommendations.

In order to fulfill its statutory obligations, the Joint Committee is authorized to hold hearings, require the attendance of witnesses and the production of documents, procure printing and binding, and make necessary expenditures. The Joint Committee (or the Chief of Staff) is authorized to secure tax returns, tax return information or data directly from the IRS or any other executive agency for the purpose of making investigations, reports, and studies relating to internal revenue tax matters, including investigations of the IRS' administration of the tax laws (Code secs. 8021 and 8023). The IRS, Office of the Chief Counsel of the IRS, and other executive bureaus and agencies are authorized and directed under section 8022 of the Code to furnish information, suggestions, rulings, data, estimates, and statistics directly to the Joint Committee (or the Chief of Staff) upon request.

The Joint Committee (or the Chief of Staff of the Joint Committee) is also authorized to receive confidential taxpayer return information pursuant to section 6103 of the Code.[34] The Chief of Staff of the Joint Committee is authorized to appoint agents for the receipt of confidential tax return information.

The Joint Committee is closely involved in every aspect of the tax legislative process. Among other things, the Joint Committee staff does the following: (1) prepares hearing pamphlets, committee reports, and conference reports (statements of managers); (2) assists the Offices of Legislative Counsel in the drafting of statutory language; (3) assists Members of Congress with the development and analysis of legislative proposals; (4) prepares revenue estimates of all revenue legislation and estimates requested by Members; and (5) initiates investigations of, and publishes studies on, various aspects of the Federal tax system.

Review of requests for GAO studies

There is presently no specific statutory requirement that requests for investigations by the General Accounting Office ("GAO") relating to the IRS be reviewed by the Joint Committee. However, many (but not all) of the studies that GAO conducts relating to taxation and oversight of the IRS require access under section 6103 of the Code to confidential tax returns and return information. There are two general reasons that they may need section 6103 access. One is that they are gathering information directly from a statistical sample of returns to determine the extent of a particular problem. The second general reason they need section 6103 access is for purposes incidental to the issue they are studying. For example, they are required by statute to perform an annual audit of IRS financial statements. In examining IRS internal financial reporting and management processes, they may incidentally encounter confidential tax returns or return information. They must have section 6103 access to conduct this type of study even though the direct ex-

[34] Section 6103 provides that tax returns and return information are confidential and cannot be disclosed unless one of several exceptions permitting disclosure applies.

amination of returns or return information is not a central part of their study. GAO cannot disclose confidential returns or return information in its published reports or in testimony.

There are three types of GAO studies for which GAO seeks access to tax returns under section 6103 of the Code. One type is studies GAO initiates on its own. Their annual audit of IRS's financial statements is an example of a self-initiated study. The second type is studies that GAO is requested to do by a Member. The third type is studies that the Joint Committee asks the GAO to undertake on its behalf. For example, the Joint Committee has in the past asked the GAO to tabulate information from TCMP audit workpapers that was useful in performing compliance revenue estimates.

Under section 6103, the GAO may inform the Joint Committee of its initiation of an audit of the IRS or other Federal agencies and obtain access to confidential taxpayer information unless, within 30 days, ⅗ths of the Members of the Joint Committee disapprove of the audit. This provision has not been utilized; the GAO generally seeks advance access to confidential taxpayer information from the Joint Committee.

II. DESCRIPTION OF S. 1096 AND COMMISSION REPORT

A. IRS Oversight Board and Appointment of Commissioner and Chief Counsel

IRS Oversight Board

S. 1096 provides for the establishment within the Treasury Department of an Internal Revenue Service Oversight Board (referred to as the "Board"). S. 1096 provides that the Board would "oversee the Internal Revenue Service in the administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws" but would have no responsibilities or authority with respect to "the development and formulation of Federal tax policy relating to existing or proposed internal revenue laws" or "specific law enforcement activities of the Internal Revenue Service, including compliance activities such as criminal investigations, examinations, and collection activities."[35] Similarly, the Report of the National Commission on Restructuring the IRS ("Commission Report") proposed that a Board of Directors be responsible for overall governance of the IRS—in order to guide the direction of long-term strategy at the IRS, appoint and remove its senior leadership, and hold IRS management accountable—but the Board would have "no involvement in specific matters in the areas of interpretation or enforcement of the tax laws."

Under S. 1096, the Board would be composed of 9 members, 7 of whom would be so-called "private-life" members who are not full-time Federal officers or employees. These 7 private-life members would be appointed by the President, with the advice and consent of the Senate (and would be considered "special governmental employees" under Title 18 U.S. Code sec. 202). The remaining 2 members of the Board would be (1) a representative from an organization representing a substantial number of IRS employees, who would be appointed by the President with the advice and consent of the Senate, and (2) the Secretary of the Treasury (or the Secretary could designate the Deputy Secretary of the Treasury). Board members generally would be appointed for 5-year terms; and the 7 private-life members could serve no more than two 5-year terms. Board member terms would be staggered, as a result of a special rule providing that some members first appointed to the Board would serve terms of less than 5 years. The members of the Board would elect a chairperson for a 2-year term. S. 1096 provides that the members of the Board could be removed at the will of the President. S. 1096 further provides that the Secretary of the Treas-

[35] S. 1096 also provides that the Board shall have no responsibilities or authority with respect to "specific activities of the Internal Revenue Service delegated to employees of the Internal Revenue Service pursuant to delegation orders in effect as of the date of the enactment of this subsection, including delegation order 106 relating to procurement authority, except to the extent that such delegation orders are modified subsequently by the Secretary."

ury (or, if so delegated, the Deputy Secretary) would be removed from the Board upon termination of employment, and the representative of IRS employees would be removed from the Board upon termination of employment, membership, or other affiliation with the organization representing IRS employees.[36] S. 1096 provides that the 7 private-life members of the Board would receive $30,000 compensation per year ($50,000 per year for a private-life member who is elected chairperson of the Board). The remaining 2 members of the Board would not be compensated for their services as Board members.

The Commission Report proposes a Board with a similar structure, but the Board would be composed of 7 members appointed by the President, with the advice and consent of the Senate. Five members of the Board would be from private life, and the remaining 2 members would be the Secretary or Deputy Secretary of the Treasury and a representative from the National Treasury Employees Union. Members of the Board would be removable at will by the President. As under S. 1096, the members of the Board of Directors generally would be appointed for 5-year terms and would elect a chairperson for a 2-year term. The Commission Report further states that the Board should hire a small, permanent staff and have a budget to contract with outside experts and consultants to review matters under its jurisdiction.[37]

Appointment of IRS Commissioner

S. 1096 provides that, among the Board's oversight responsibilities, the Board would have the specific responsibility "[t]o provide for . . . the selection and appointment, evaluation, and removal of the Commissioner of Internal Revenue, [and] the review of the Commissioner's selection, evaluation, and compensation of senior managers." The IRS Commissioner would be appointed by the Board—presumably by majority vote—to a 5-year term, and could be reappointed by the Board to subsequent terms. S. 1096 further provides that the IRS Commissioner, in turn, would be "authorized to employ such number of persons as the Commissioner deems proper for the administration and enforcement of the internal revenue laws, and the Commissioner shall issue all necessary directions, instructions, orders, and rules applicable to such persons." In contrast, present-law Code section 7803(a) grants such hiring authority to the Secretary of the Treasury.

The Commission Report proposes, as does S. 1096, that the Board should be vested with the authority to appoint the IRS Commissioner to a 5-year term. Specifically, the Commission Report states that the Board would "[appoint and compensate the Commissioner and review and approve the Commissioner's recommendations regarding the appointment, evaluation, and compensation of

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[36] Under S. 1096, it appears that all members of the Board could be removed at the will of the President, and that the termination of employment of the Secretary or Deputy Secretary of the Treasury, or termination of employment, membership, or affiliation of the IRS employee union representative with the union, would constitute an *additional* basis for removal of such members from the Board.

[37] In contrast, S. 1096 does not specifically provide that the Board shall hire a permanent staff. Instead, on request of the chairperson of the Board, the IRS Commissioner shall detail to the Board such personnel as may be necessary to enable the Board to perform its duties, and the Board may procure temporary and intermittent services under Title 5 U.S.C., section 3109(b).

senior IRS executives." Although S. 1096 is somewhat vague when it provides that the Board will have the responsibility to "review" the Commissioner's "selection, evaluation, and compensation" of senior IRS managers, the Commission Report proposes that the Board "review and approve" the Commissioner's recommendations regarding the appointment, evaluation, and compensation of senior IRS managers. The Commission Report states that, with respect to the hiring of senior IRS officials and other management decisions made by the IRS Commissioner, the Board should "retain final authority regarding all such matters."

Under S. 1096, the IRS Commissioner would be granted specific statutory authority to "administer, manage, conduct, direct, and supervise the execution and application of the internal revenue laws or related statutes and tax conventions to which the United States is a party.

Appointment of IRS Chief Counsel

Under S. 1096, the IRS Chief Counsel would continue to be appointed as under present law—that is, the appointment would be made by the President, with the advice and consent of the Senate. The bill provides, however, that when a vacancy occurs, the IRS Commissioner shall recommend a candidate for appointment as IRS Chief Counsel to the President, and the Commissioner may recommend the removal of the Chief Counsel to the President. The IRS Chief Counsel would be described as the chief law officer for the IRS and would perform such duties as may be prescribed by the Secretary of the Treasury. S. 1096 provides that, to the extent that the IRS Chief Counsel performs duties relating to the development of rules and regulations promulgated under the Internal Revenue Code, final decision making authority shall remain with the Secretary of the Treasury.

In contrast to the mode of appointment of the IRS Chief Counsel provided for by S. 1096, the Commission Report proposed that the IRS Commissioner should recommend the nomination of a Chief Counsel to the Board, but the Board would make the final appointment of the IRS Chief Counsel. This recommendation contained in the Commission Report was designed to "maintain the current parity in which the Commissioner and Chief Counsel are appointed independently." In this regard, the Commission Report states that if, during the course of IRS business, the Commissioner and Chief Counsel cannot reach agreement on an issue, the Commissioner would have decision-making authority.

B. Employee Plans and Exempt Organizations

In general, the Commission recommends that Congress simplify tax administration by limiting the assignment of non-core functions to the IRS. However, the Commission Report acknowledges that, in certain circumstances, the IRS may be uniquely qualified to administer a non tax-collection function, citing the regulation of employee plans and exempt organizations as an example of such a function. The Commission Report indicates that if Congress delegates such a responsibility to the IRS, it should also provide sufficient autonomy and resources to ensure that the non-core function can be ade-

quately carried out without detracting from traditional tax enforcement.

For example, the Commission Report provides that "[t]he EP/EO operation is recognized as one of the most innovative and efficient functions within the IRS" and cites with approval EP/EO voluntary compliance efforts.[38] The Commission Report also notes that, in 1974, Congress elevated supervision of EP/EO to an Assistant Commission and authorized an annual appropriation for EP/EO in recognition of the unique function and responsibilities of EP/EO within the IRS. However, because the designated funding mechanism has never been used, the Commission Report states that "EP/EO constantly struggles with the IRS core tax collection functions for resources to regulate more than $1.2 trillion in tax-exempt assets and $1.7 trillion in retirement plan assets."[39]

S. 1096 would retain the Office of Employee Plans and Exempt Organizations under the supervision and direction of an Assistant Commissioner of the Internal Revenue. As under present law, EP/EO would be responsible for carrying out functions and duties associated with organizations designed to be exempt from tax under section 501(a) of the Code and with respect to plans designed to be qualified under section 401(a). In addition, however, EP/EO's responsibilities would be expanded to include nonqualified deferred compensation arrangements. The bill also would provide that the Assistant Commissioner shall report annually to the Commissioner on EP/EO operations.

As under present law, S. 1096 would provide for an authorization of appropriations equal to the section 4940 excise tax on investment income (assuming a 2-percent excise tax rate) plus the greater of the same amount or $30 million. However, the bill specifies that this authorized appropriation would be used solely to carry out the functions of EP/EO. The bill also would provide that all user fees collected by EP/EO would be dedicated to carry out EP/EO functions.

C. Taxpayer Advocate

S. 1096 would require the Commissioner to obtain the approval of the IRS Oversight Board on the selection of the Taxpayer Advocate. A candidate for the Taxpayer Advocate must have either substantial experience representing taxpayers before the IRS or have substantial experience within the IRS. If the prospective Taxpayer Advocate was an officer or an employee of the IRS before being appointed as the Taxpayer Advocate, the individual would be required to agree not to accept any employment with the IRS for at least 5 years after ceasing to be the Taxpayer Advocate.

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[38] Commission Report, p. 38.

[39] *Ibid.* The Commission heard testimony focusing on the EP/EO function within the IRS from James J. McGovern, former Assistant Commissioner for EP/EO, and from the Exempt Organizations Committee of the D.C. Bar Section of Taxation. See "Regulation of EP/EO in the Twenty-First Century," testimony of James J. McGovern before the National Commission on Restructuring the IRS, *The Exempt Organization Tax Review*, February 1997, p. 209; and "Comments Concerning the Future Regulations of Employee Plans and Exempt Organizations Matter," submission of the Exempt Organizations Committee, Section of Taxation, District of Columbia Bar, to the National Commission on Restructuring the IRS, *The Exempt Organization Tax Review*, June 1997, p. 1075.

The bill would modify the information to be included in the December 31 report to the tax-writing committees. The report identifies areas of the tax law that impose significant compliance burdens on taxpayers or the IRS, including specific recommendations for solving these problems. The Taxpayer Advocate also would be required to work in conjunction with the National Director of Appeals to identify the 10 most litigated issues for each category of taxpayers, and include the list of issues and recommendations for mitigating such disputes in the report. Categories of taxpayers include, for example, individuals, self-employed individuals, small businesses, etc.

Under present law, the Taxpayer Advocate reports are submitted directly to the tax-writing committees, without review by the Commissioner, the Secretary of the Treasury, or any other officer or employee of the Department of the Treasury or the Office of Management and Budget. Under the bill, the Taxpayer Advocate reports would still be submitted directly to the tax-writing committees, without review by the Oversight Board or any of the other persons mentioned above.

In addition, the bill would impose new responsibilities on the Taxpayer Advocate. The Taxpayer Advocate would be required to monitor the coverage and geographical allocation of problem resolution officers and develop guidance that outlines criteria to be used by IRS employees in referring taxpayer inquiries to problem resolution officers. In connection with these responsibilities, the Taxpayer Advocate would be required to work with the IRS District Offices to ensure convenient taxpayer access to the local problem resolution officer. The Taxpayer Advocate would be required to ensure that the local telephone number for the problem resolution officer in each district is published and available to taxpayers.

The Taxpayer Advocate would be required to work with the Commissioner in developing career paths for local problem resolution officers, so that individuals can progress through the General Schedule in the same manner as examination employees, without having to leave the problem resolution system. In that regard, it is contemplated that the compensation levels of local and regional problem resolution officers should be the same as those of IRS personnel operating in other functional units. Under the current system, local problem resolution officers generally must return to an audit or collection function to achieve promotion. This lack of a career path within the problem resolution system reduces the independence of the system.

Effective date.—The provision would be effective on the date of enactment, except that the post-employment restrictions on the Taxpayer Advocate do not apply to an individual holding that position on the date of enactment.

D. Congressional Accountability for the IRS

Congressional oversight

S. 1096 would provide that the Joint Committee on Taxation ("Joint Committee") is to review all requests (other than requests by a Committee or Subcommittee of the Congress) for investigations of the IRS by the General Accounting Office ("GAO") and ap-

prove such requests when appropriate. In reviewing such requests, the Joint Committee is to attempt to eliminate overlapping investigations, ensure that the GAO has the capacity to handle the investigation, and ensure that investigations focus on areas of primary importance to tax administration.

The bill would provide that there shall be two annual joint hearings of members of the Senate Committees on Finance, Appropriations, and Governmental Affairs and the House Committees on Ways and Means, Appropriations, and Government Reform and Oversight. The first annual hearing is to take place before April 1 of each calendar year and is to review the strategic plans and budget for the IRS. The second annual hearing is to be held after the conclusion of the annual tax filing season, and is to review the strategic and business plans for the IRS, the progress of the IRS in meeting its objectives, the budget for the IRS and whether it supports its objectives, the progress of the IRS in improving taxpayer service and compliance, progress of the IRS on technology modernization, and the annual filing season.

The bill would provide that the Joint Committee is to make annual reports to the Committee on Finance and the Committee on Ways and Means on the overall state of the Federal tax system, together with recommendations with respect to possible simplification proposals and other matters relating to the administration of the Federal tax system as it may deem advisable. The Joint Committee is also to report annually to the Senate Committees on Finance, Appropriations, and Governmental Affairs and the House Committees on Ways and Means, Appropriations, and Government Reform and Oversight with respect to the matters that are the subject of the second annual joint hearing of members of such committees.

The Commission's recommendations are substantially similar to the provisions of S. 1096. However, the Commission recommended that, rather than simply expanding the role of the Joint Committee, a new entity, consisting of members of each of the 6 committees of jurisdiction and staffed by the staff of such committees and the staff of the Joint Committee, be created to coordinate oversight of the IRS, hold joint hearings, and approve all requests to the GAO for investigations of the IRS. The Commission also recommended that the Joint Committee reassume its statutory role as the focal point for IRS oversight, that the Joint Committee should have authority to contract with the private sector for oversight reports, and that the staff of the Joint Committee be expanded to meet its new responsibilities.

Tax law complexity

S. 1096 provides that it is the sense of the Congress that the IRS should provide the Congress with an independent view of tax administration and that the tax-writing committees should hear from front-line technical experts at the IRS with respect to the administrability of pending amendments to the Internal Revenue Code.

The bill would provide that the Joint Committee is to provide a "Tax Complexity Analysis" with respect to each bill, amendment, joint resolution, or conference agreement amending the tax laws.

Legislation not containing the required Tax Complexity Analysis would be subject to a point of order.

A Tax Complexity Analysis must be prepared for each provision of a tax bill, amendment, joint resolution, or conference agreement and must address:

- whether the provision is new, modifies or replaces existing law, and whether hearings were held to discuss the proposal and whether the IRS provided input as to its administrability;
- when the provision becomes effective and corresponding compliance requirements on taxpayers;
- whether new IRS forms or worksheets are needed, whether existing forms or worksheets must be modified, and whether the effective date allows sufficient time for the IRS to prepare such forms and educate taxpayers;
- necessity of additional interpretive guidance (e.g., regulations, rulings, notices);
- the extent to which the proposal relies on concepts contained in existing law, including definitions;
- effect on existing record keeping requirements and the activities of taxpayers, complexity of calculations and likely behavioral response, and standard business practices and resource requirements;
- number, type, and sophistication of affected taxpayers; and
- whether the proposal requires the IRS to assume responsibilities not directly related to raising revenue which could be handled through another Federal agency.

The bill would require the Commissioner to provide the Joint Committee with such information as is necessary to prepare each required Tax Complexity Analysis.

The requirement for a Tax Complexity Analysis would be effective with respect to legislation considered on or after the earlier of January 1, 1998, or the 90th day after the date of enactment of an additional appropriation to enable the Joint Committee to perform the Tax Complexity Analysis.

The bill directs the Joint Committee to prepare a study of the feasibility of developing a baseline estimate of taxpayer's compliance burdens against which future legislative proposals could be measured.

S. 1096 substantially mirrors the recommendations of the Commission. However, the Commission recommended that the Tax Complexity Analysis, in addition to the 8 factors that must be addressed under S. 1096, should also identify the kinds of complexity, the extent of that complexity, and whether the provisions could be recast to reduce complexity while still achieving its tax policy goals.

III. DESCRIPTION OF H.R. 2676

A. IRS Oversight Board

Duties, responsibilities, and powers of the IRS Oversight Board

The bill would provide for the establishment within the Treasury Department of the Internal Revenue Service Oversight Board (referred to as the "Board"). The general responsibilities of the Board are to oversee the Internal Revenue Service (the "IRS") in its administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws. The Board has no responsibilities or authority with respect to (1) the development and formulation of Federal tax policy relating to existing or proposed internal revenue laws, (2) law enforcement activities of the IRS, including compliance activities such as criminal investigations, examinations, and collection activities,[40] and (3) specific procurement activities of the IRS (e.g., selecting vendors or awarding contracts). As discussed more fully in Part B., below, the Board also has the authority to recommend candidates for IRS Commissioner to the President, and to recommend removal of the Commissioner. The members of the Board do not have authority to receive confidential taxpayer return information.[41]

The Board would have the following specific responsibilities: (1) to review and approve strategic plans of the IRS, including the establishment of mission and objectives (and standards of performance) and annual and long-range strategic plans; (2) to review the operational functions of the IRS, including plans for modernization of the tax system, outsourcing or managed competition, and training and education; (3) to provide for the review of the Commissioner's selection, evaluation and compensation of senior managers; and (4) to review and approve the Commissioner's plans for major reorganization of the IRS. It is intended that major reorganizations subject to the Board's review and approval are limited to major changes in organizational structure, such as the 1995 IRS reorganization that combined 7 regions into 4 and 63 districts into 33. In addition, the Board will review and approve the budget request of the IRS prepared by the Commissioner, submit such budget request to the Secretary, and ensure that the budget request supports the annual and long-range strategic plans of the IRS. The

[40] This provision is not intended to limit the Board's authority with respect to the review and approval of strategic plans and the budget of the Commission or to preclude the Board from review of IRS operations generally.

[41] The bill does not affect the extent to which the Secretary of the Treasury (or the Deputy Secretary) and the IRS Commission have authority to receive confidential taxpayer return information under present law by virtue of such positions. Any request for information that cannot be disclosed to Board members and any contact relating to a specific taxpayer made by a private-life Board member or the union representative to an employee of the IRS must be reported by such employee to the Secretary and the Joint Committee on Taxation.

Secretary is required to submit the budget request approved by the Board to the President, who is required to submit such request, without revision, to the Congress together with the President's annual budget request for the IRS. The bill does not affect the ability of the President to include, in addition, his own budget request relating to the IRS.

It is intended that the Board will reach a formal decision on all matters subject to its review. With respect to those matters over which the Board has approval authority, the Board's decisions are determinative. It is fully expected that, with respect to those matters over which the Board has approval authority (other than as relates to the development of the budget), the Secretary will exert his or her oversight responsibility over the IRS by working through and with the Board.[42]

The Board is required to report each year to the President and the Congress regarding the conduct of its responsibilities.

It is expected that the Treasury Department will no longer utilize the IRS Management Board once the new Board created by the bill is in place, as the functions of the IRS Management Board would be taken over by the new Board.[43]

Composition of the Board

The Board would be composed of 11 members. Eight of the members are so-called "private-life" members who are not Federal officers or employees. These private-life members would be appointed by the President, with the advice and consent of the Senate. The remaining members are (1) the Secretary of the Treasury (or, if the Secretary so designates, the Deputy Secretary of the Treasury), (2) a representative from a union representing a substantial number of IRS employees, who will be appointed by the President with the advice and consent of the Senate, and[44] (3) the Commissioner of the IRS.

The private-life members of the Board are to be appointed based on their expertise in the following areas: management of large service organizations; customer service; the Federal tax laws, including administration and compliance; information technology; organization development; and the needs and concerns of taxpayers. In the aggregate, the members of the Board should collectively bring to bear expertise in all these enumerated areas.

The private-life members are considered special government employees during the entire period of their appointment. That is, they will be considered to be performing services as a special government employee on each day during their appointment, not just on those days on which they actually perform services. Thus, they will be subject to the ethical conduct rules applicable to special government employees who serve more than 60 days during any 365-day period. Thus, for example, private-life Board members would not be

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[42] The budget is excepted from this expectation because the bill provides a separate mechanism through which the Secretary may act. The procedures relating to the Board permit the President to submit his own budget in addition to that approved by the Board.

[43] As noted in Part I.A., *supra*, the Commissioner receives private sector advice from the CAG. It is possible that the functions of the CAG would also be taken over by the new Board.

[44] In appointing the union representative, the President is not constrained to choose an individual recommendation by a union covering IRS employees, but may choose whoever the President determines to be an appropriate representative of the union.

able to represent clients before the IRS on matters during their term as a Board member. Private-life Board members would also be subject to the 1-year post-employment restriction applicable to senior-level employees. Finally, private-life members would be subject to the public financial disclosure rules generally applicable to special government employees above certain pay grades.[45]

Compensation of Board members

The private-life members of the Board are to be compensated at a rate of $30,000 per year, except that the Chair is to be compensated at a rate of $50,000 a year. Other members of the Board would receive no compensation for their services as Board members. The members of the Board would be entitled to travel expenses for purposes of attending meetings of the Board.

Administrative matters

The 8 private-life Board members and the union representative generally will be appointed for 5-year terms. The private-life members may serve no more than two 5-year terms. Each 5-year term begins upon appointment. Board member terms are staggered, as a result of a special rule providing that some private-life members first appointed to the Board will serve initial terms of less than 5 years. The members of the Board are to elect a chairperson from among the private-life Board members for a 2-year term. Any member of the Board can be removed at the will of the President. In addition, the Secretary of the Treasury (or, if so delegated, the Deputy Secretary) and the IRS Commissioner are removed from the Board upon termination of employment in such positions and the representative of IRS employees is removed from the Board upon termination of their employment, membership, or other affiliation with the organization representing IRS employees.

The Board would be required to meet at least once a month, and would meet at such other times as the Board determines appropriate.

A quorum of 6 members is required in order for the Board to conduct business. Actions of the Board are taken by a majority vote of those members present and voting.

The Board would not have its own permanent staff, but would have such staff as detailed by the Commissioner at the request of the Chair of the Board. The Chair could procure temporary and intermittent services under section 3109(b) of title 5 of the U.S. Code.

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[45] The Secretary of the Treasury (or the Deputy Secretary) and the IRS Commissioner are subject to the ethical conduct rules applicable to regular, full-time Federal employees by virtue of their status as such. These rules are generally more stringent than the rules applicable to special government employees. H.R. 2676 does not impose any special ethical conduct or financial disclosure rules on the Board member that is an IRS employee representative. Thus, the rules such individual would be subject to depends on whether such individual was otherwise a Federal employee—either a special government employee by virtue of his or her membership on the Board or a regular Federal employee. If such individual is not a regular Federal employee, then the rules applicable to private-life Board members may not apply to this individual because the bill does not provide an exception for the pay grade and 60-day rules applicable to special government employees for the IRS employee representative.

Claims against Board members

The private-life members of the Board and the union representative have no personal liability under Federal law with respect to any claim arising out of or resulting from an act or omission by such Board member within the scope of service as a Board member. The bill does not limit personal liability for criminal acts or omissions, wilful or malicious conduct, acts or omissions for private gain, or any other act or omission outside the scope of service of the Board member.

The bill does not affect any other immunities and protections that may be available under applicable law or any other right or remedy against the United States under applicable law, or limit or alter the immunities that are available under applicable law for Federal officers and employees.

Effective date.—The provisions of the bill relating to the Board would be effective on the date of enactment. The President is directed to submit nominations for Board members to the Senate within 6 months of the date of enactment.

B. Appointment and Duties of IRS Commissioner

As under present law, under the bill the Commissioner would be appointed by the President, with the advice and consent of the Senate, and can be removed at will by the President. The Commissioner would be appointed to a 5-year term, beginning with the date of appointment. The Board has the power to recommend candidates to the President for Commissioner. The Board has the authority to recommend the removal of the Commissioner. Although the President is not required to nominate for Commissioner a candidate recommended by the Board (or to remove a Commissioner when the Board so recommends), it is expected that the President will generally give deference to the Board's expertise and familiarity with the needs and functions of the IRS and will act in accordance with the Board's recommendations.

The Commissioner has such duties and powers as prescribed by the Secretary. Unless otherwise specified by the Secretary, such duties and powers include the power to administer, manage, conduct, direct, and supervise the execution and application of the internal revenue laws or related statutes and tax conventions to which the United States is a party and to recommend to the President a candidate for Chief Counsel (and recommend the removal of the Chief Counsel). It is intended that the listed duties codify present delegations. However, if the Secretary changes such orders, they may be subject to the notice requirement of the bill, described below.

If the Secretary determines not to delegate the specified duties to the Commissioner, such determination will not take effect until 30 days after the Secretary notifies the House Committees on Ways and Means, Government Reform and Oversight, and Appropriations, the Senate Committees on Finance, Governmental Affairs, and Appropriations, and the Joint Committee on Taxation.

This provision is not intended to alter the Secretary's existing authority to delegate to agencies other than the IRS the authority to administer and enforce certain portions of the internal revenue

laws. For example, the Secretary currently has delegated to the Bureau of Alcohol, Tobacco and Firearms the authority to administer and enforce the taxes under section 4181 and chapters 51, 52, and 53 of the Internal Revenue Code (regarding excise and other taxes on alcohol, tobacco, firearms, and destructive devices).

The Commissioner is to consult with the Board on all matters within the Board's authority (other than the recommendation of candidates for Commissioner and the recommendation to remove the Commissioner). With respect to those matters within the Board's approval authority (other than with respect to the development of the budget), it is fully expected that the Secretary will exert his or her oversight responsibility over the IRS by working through and with the Board.[46]

Unless otherwise specified by the Secretary, the Commissioner is authorized to employ such persons as the Commissioner deems proper for the administration and enforcement of the internal revenue laws and would be required to issue all necessary directions, instructions, orders, and rules applicable to such persons. Unless otherwise provided by the Secretary, the Commissioner will determine and designate the posts of duty.

The Commissioner is to be compensated as under present law.

Effective date.—The provisions of the bill relating to the Commissioner generally would be effective on the date of enactment. The provision relating to the 5-year term of office applies to the Commissioner in office on the date of enactment. This 5-year term runs from the date of appointment.

C. Structure and Funding of the Employee Plans and Exempt Organizations Division

The bill would retain the Office of Employee Plans and Exempt Organizations under the supervision and direction of an Assistant Commissioner of the Internal Revenue. As under present law, EP/EO is responsible for carrying out functions and duties associated with organizations designed to be exempt from tax under section 501(a) of the Code and with respect to plans designed to be qualified under section 401(a). In addition, however, EP/EO's responsibilities are expanded to include nonqualified deferred compensation arrangements. The bill also provides that the Assistant Commissioner shall report annually to the Commissioner on EP/EO operations.

In addition, the bill repeals the funding mechanism for EP/EO set forth in section 7802(b). Thus, the appropriate level of funding for EP/EO is, consistent with current practice, subject to annual Congressional appropriations, as are other functions within the IRS.

Effective date.—The provision would be effective on the date of enactment.

D. Taxpayer Advocate

The bill would require the Commissioner to obtain the approval of the IRS Oversight Board on the selection of the Taxpayer Advo-

[46] The budget is excepted from this expectation because the bill provides a separate mechanism through which the Secretary may act.

cate. A candidate for the Taxpayer Advocate must have either substantial experience representing taxpayers before the IRS or have substantial experience within the IRS. If the prospective Taxpayer Advocate was an officer or an employee of the IRS before being appointed as the Taxpayer Advocate, the individual is required to agree not to accept any employment with the IRS for at least 5 years after ceasing to be the Taxpayer Advocate.

The bill would modify the information to be included in the December 31 report to the tax-writing committees. The report no longer needs to include information about the extent to which regional problem resolution officers participate in the selection and evaluation of local problem resolution officers. The report identifies areas of the tax law that impose significant compliance burdens on taxpayers or the IRS, including specific recommendations for solving these problems. The Taxpayer Advocate also is required to work in conjunction with the National Director of Appeals to identify the 10 most litigated issues for each category of taxpayers, and include the list of issues and recommendations for mitigating such disputes in the report. Categories of taxpayers include, for example, individuals, self-employed individuals, small businesses, etc.

Under present law, the Taxpayer Advocate reports are submitted directly to the tax-writing committees, without review by the Commissioner, the Secretary of the Treasury, or any other officer or employee of the Department of the Treasury or the Office of Management and Budget. Under the bill, the Taxpayer Advocate reports would still be submitted directly to the tax-writing committees, without review by the Oversight Board or any of the other persons mentioned above.

In addition, the bill imposes new responsibilities on the Taxpayer Advocate. The Taxpayer Advocate is required to monitor the coverage and geographical allocation of problem resolution officers and develop guidance that outlines criteria to be used by IRS employees in referring taxpayer inquiries to problem resolution officers. In connection with these responsibilities, it is anticipated that the Taxpayer Advocate will work with the IRS District Offices to ensure convenient taxpayer access to the local problem resolution officer. For example, the local telephone number for the problem resolution officer in each district should be published and available to taxpayers.

It is intended that the Taxpayer Advocate will work with the Commissioner in developing career paths for local problem resolution officers, so that individuals can progress through the General Schedule in the same manner as examination employees, without having to leave the problem resolution system. In that regard, it is contemplated that the compensation levels of local and regional problem resolution officers should be the same as those of IRS personnel operating in other functional units. Under the current system, local problem resolution officers generally must return to an audit or collection function to achieve promotion. This lack of a career path within the problem resolution system reduces the independence of the system. It is contemplated that, to the extent feasible, regional problem resolution officers should be selected from the available pool of local problem resolution officers.

Effective date.—The provision would be effective on the date of enactment, except that the post-employment restrictions on the Taxpayer Advocate do not apply to an individual holding that position on the date of enactment.

E. Prohibition on Executive Branch Influence Over Taxpayer Audits

The bill would make it unlawful for a specified person to request that any officer or employee of the IRS conduct or terminate an audit or otherwise investigate or terminate the investigation of any particular taxpayer with respect to the tax liability of that taxpayer. The prohibition applies to the President, the Vice President, and employees of the executive offices of either the President or Vice President, as well as any individual (except the Attorney General) serving in a position specified in section 5312 of Title 5 of the United States Code (these are generally Cabinet-level positions). The prohibition applies to both direct requests and requests made through an intermediary.

Any request made in violation of this rule must be reported, by the IRS employee to whom the request was made, to the Chief Inspector of the IRS. The Chief Inspector has the authority to investigate such violations and to refer any violations to the Department of Justice for possible prosecution, as appropriate. Anyone convicted of violating this provision will be punished by imprisonment of not more than 5 years or a fine not exceeding $5,000 (or both).

Three exceptions to the general prohibition apply. First, the prohibition does not apply to a request made to a specified person by a taxpayer or a taxpayer's representative that is forwarded by the specified person to the IRS. This exception is intended to cover two types of situations. The first situation is where a taxpayer (or a taxpayer's representative) writes to a specified person seeking assistance in resolving a difficulty with the IRS. This exception permits the specified person who receives such a request to forward it to the IRS for resolution without violating the general prohibition. The second situation that this first exception is intended to cover is an audit or investigation by the IRS of a Presidential nominee. Under present law (sec. 6103(c)), nominees for Presidentially appointed positions consent to disclosure of their tax returns and return information so that background checks may be conducted. Sometimes an audit or other investigation is initiated as part of that background check. The House bill anticipates that any such audit or investigation that is part of such a background check will be encompassed within this first exception.

The second exception to the general prohibition applies to requests for disclosure of returns or return information under section 6103 if the request is made in accordance with the requirements of section 6103.

The third exception to the general prohibition applies to requests made by the Secretary of the Treasury as a consequence of the implementation of a change in tax policy.

Effective date.—The provision would apply to violations occurring after the date of enactment.

F. Congressional Accountability for the IRS

Review of Requests for GAO Investigations of the IRS

Under the bill, the Joint Committee on Taxation would review all requests (other than requests by the chair or ranking member of a Committee or Subcommittee of the Congress) for investigations of the IRS by the GAO and approves such requests when appropriate. In reviewing such requests, the Joint Committee is to eliminate overlapping investigations, ensure that the GAO has the capacity to handle the investigation, and ensure that investigations focus on areas of primary importance to tax administration.

The provision does not change the present-law rules under section 6103.

Effective date.—The provision would be effective with respect to requests for GAO investigations made after the date of enactment.

Joint Congressional hearings and coordinated oversight reports

Under the bill, there are to be two annual joint hearings of two majority and one minority members of each of the Senate Committees on Finance, Appropriations, and Governmental Affairs and the House Committees on Ways and Means, Appropriations, and Government Reform and Oversight. The first annual hearing is to take place before April 1 of each calendar year and is to review the strategic plans and budget for the IRS (including whether the budget supports IRS objectives). The second annual hearing is to be held after the conclusion of the annual tax filing season, and is to review the progress of the IRS in meeting its objectives under the strategic and business plans, the progress of the IRS in improving taxpayer service and compliance, progress of the IRS on technology modernization, and the annual filing season. The bill does not modify the existing jurisdiction of the Committees involved in the joint hearings.

The bill would provide that the Joint Committee is to make annual reports to the Committee on Finance and the Committee on Ways and Means on the overall state of the Federal tax system, together with recommendations with respect to possible simplification proposals and other matters relating to the administration of the Federal tax system as it may deem advisable. The Joint Committee also is to report annually to the Senate Committees on Finance, Appropriations, and Governmental Affairs and the House Committees on Ways and Means, Appropriations, and Government Reform and Oversight with respect to the matters that are the subject of the annual joint hearings of members of such Committees.

Effective date.—The provision would be effective on the date of enactment.

Funding for century date change

The bill would provide that it is the sense of the Congress that the IRS efforts to resolve the century date change computing problems should be fully funded to provide for certain resolution of such problems.

Financial management advisory group

The bill would direct the Commissioner to convene a financial management advisory group consisting of individuals with expertise in governmental accounting and auditing from both the private sector and the Government to advise the Commissioner on financial management issues.

Effective date.—The provision would be effective on the date of enactment.

IRS participation in drafting legislation

The bill would provide that it is the sense of the Congress that the IRS should provide the Congress with an independent view of tax administration and that the tax-writing committees should hear from front-line technical experts at the IRS during the legislative process with respect to the administrability of pending amendments to the Internal Revenue Code.

Tax complexity analysis

The bill would require the staff of the Joint Committee on Taxation to provide a "Tax Complexity Analysis" for legislation reported by the Senate Committee on Finance and the House Committee on Ways and Means and conference reports amending the tax laws. The Tax Complexity Analysis is to identify those provisions in the bill or conference report that, as determined by the staff of the Joint Committee, add significant complexity to the tax laws, or provide significant simplification. The Tax Complexity Analysis is required to include a discussion of the basis for the determination by the staff of the Joint Committee. It is expected that, in general, the Tax Complexity Analysis will be limited to no more than 20 provisions. If the staff of the Joint Committee determines that a bill or conference report does not contain any provisions that add significant complexity or simplification to the tax laws, then the Tax Complexity Analysis is to contain a statement to that effect.

Factors that may be taken into account by the staff of the Joint Committee in preparing the Tax Complexity Analysis include the following: (1) whether the provision is new, modifies or replaces existing law, and whether hearings were held to discuss the proposal and whether the IRS provided input as to its administrability; (2) when the provision becomes effective and corresponding compliance requirements on taxpayers; (3) whether new IRS forms or worksheets are needed, whether existing forms or worksheets must be modified, and whether the effective date allows sufficient time for the IRS to prepare such forms and educate taxpayers; (4) necessity of additional interpretive guidance (e.g., regulations, rulings, notices); (5) the extent to which the proposal relies on concepts contained in existing law, including definitions; (6) effect on existing record keeping requirements and the activities of taxpayers, complexity of calculations and likely behavioral response, and standard business practices and resource requirements; (7) number, type, and sophistication of affected taxpayers; and (8) whether the proposal requires the IRS to assume responsibilities not directly related to raising revenue which could be handled through another Federal agency.

The bill would require the Commissioner to provide the Joint Committee with such information as is necessary to prepare each required Tax Complexity Analysis.

A point of order would arise with respect to the floor consideration of a bill or conference report that does not contain the required Tax Complexity Analysis. The point of order may be waived by a majority vote.

The House bill legislative report states that it is hoped that the Administration will include a similar complexity analysis when submitting proposed legislation.

Effective date.—The requirement for a Tax Complexity Analysis would be effective with respect to legislation considered on or after January 1, 1998.

IV. ISSUES RELATING TO EXECUTIVE BRANCH GOVERNANCE

A. Constitutional Issues

Both S. 1096 and the Commission Report provide that the IRS Commissioner would be appointed by the Board—presumably by a majority vote by the members of the Board—rather than such appointment being made by the President, with the advice and consent of the Senate (as under present-law). As discussed more fully below, this proposal raises a number of constitutional issues.[47]

1. Constitutional framework

The appointment process for all Federal officers is governed by Article II, section 2, clause 2 of the Constitution—the so-called "Appointments Clause"—which provides that:

> "[The President] . . . shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the Supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments."

Numerous Supreme Court decisions interpreting the Appointments Clause demonstrate that so-called "principal" officers must be appointed by the President, with the advice and consent of the Senate.[48] Congress is prohibited from providing for any other method of appointment of "principal" officers. In the case of "inferior" officers, the Appointments Clause allows some flexibility in the appointments process, but there are specific constitutional constraints. Inferior officers must be appointed by one of the following three methods: (1) by the President alone (or by the President with the advice and consent of the Senate); (2) by a court of law; or (3) by a head of a Federal department. See *Buckley* v. *Valeo*, 424 U.S. 1, 109–143 (1976) (holding that the Appointments Clause was violated by statutory scheme providing that two of six Commissioners of the Federal Election Commission would be appointed by the President and the remaining four Commissioners appointed by congressional leaders, with confirmation of all six Commissioners vested in both the House and the Senate); *Morrison* v. *Olson*, 487 U.S. 654 (1988) (upholding independent counsel provisions of the Ethics

[47] H.R. 2676, as passed by the House, does not raise the same constitutional issues, because it provides that the Commissioner is appointed by the President, with the advice and consent of the Senate.

[48] The term "principal officer" is not expressly included in the text of the Constitution, but has been adopted by the Supreme Court in its Appointments Clause jurisprudence.

in Government Act, under which the Attorney General may request that a special panel of Federal judges appoint an independent counsel to investigate and prosecute certain high-ranking officials); *Freytag* v. *Commissioner*, 111 S.Ct. 2631 (1991)(upholding appointment of special trial judges by Chief Judge of the United States Tax Court); *Ryder* v. *United States*, 115 S.Ct. 2031 (1995)(composition of three-judge panel that court-martialed member of the Coast Guard violated Appointments Clause; actions of those judges were not valid under the de facto officer doctrine). Any appointee exercising "significant authority pursuant to the laws of the United States" is an "officer" who must be appointed in the manner prescribed by the Appointments Clause, and no class or type of officer is excluded because of its special functions. See *Edmond* v. *United States*, 117 S.Ct. 1573 (1997); *Weiss* v. *United States*, 114 S.Ct. 752 (1994).[49]

The Appointments Clause reflects the constitutional distinction between the creation of offices and *appointments* to such offices—the former being a function of the legislature and the latter generally being an executive branch function that is part of executing the laws passed by Congress. The appointing power generally resides with the President, as one of the principles of the Constitution's separation of powers, with certain exceptions provided for "inferior" officers. Congress has, incident to the creation of an office, the power to determine qualifications of the officer (and thus, to some extent, may limit the range of choice of the appointing power[50]) and to regulate the conduct in office of officers and employees of the United States. However, the selection of the individual to occupy a Federal office generally is an Executive branch function. In short, Congress may create an office, but it cannot appoint the officer. As stated by Professors Rotunda and Nowak in their *Treatise on Constitutional Law: Substance and Procedure*: "This appointment process is a practical outworking of the doctrine of separation of powers, with Congress establishing the federal offices and the President, subject to Senate confirmation, choosing the officers. The framers believed such a separation necessary because the same persons should not both legislate and administer the laws." See Rotunda and Nowak, supra, vol. 1, at 669 (quoting from *Buckley* v. *Valeo*). Thus, Congress itself may not appoint executive or judicial branch officers, and the manner in which the President (or others in the case of "inferior" officers) may appoint an officer also is specifically prescribed by the Appointments Clause.[51]

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[49] In contrast to the appointment of Federal *officers*—generally meaning all individuals "exercising significant authority pursuant of the laws of the United States"—there are no constitutional limitations on the process for appointing ordinary Federal "employees." See, e.g., *Buckley* v. *Valeo*, 424 U.S. at 126, n. 162 (describing employees as "lesser functionaries subordinate to officers of the United States"); *Freytag* v. *Commissioner*, 111 S.Ct. at 2640092641. See also Rotunda and Nowak, *Treaties on Constitutional Law: Substance and Procedure* vol. 1, at 660 (2nd ed. 1992) (appointment of employees not subject to constitutional constraints as a "pragmatic concession to the needs of the government bureaucracy").

[50] See Fisher, Louis, *Constitutional Conflicts between Congress and the President*, at 27–28, 32 (3rd ed. 1991). Congressionally imposed qualifications must have a reasonable relation to the office; otherwise, Congress could, in effect, be exercising appointment authority, rather than leaving this to the Executive branch. Rotunda and Nowak, *supra*, vol. 1 at 672.

[51] Congress may, however, appoint its own Members or other individuals to serve on advisory commissions—such as the National Commission on Restructuring the IRS—or other organizations that perform functions of an essentially investigative and informative nature, falling into the same category as those powers which Congress might delegate to one of its town committees.

2. Appointment of IRS Commissioner by the Oversight Board

In general

Undoubtedly, the IRS Commissioner is, and will continue to be, a Federal "officer" for purposes of the Appointments Clause, despite the Board having general authority to oversee management decisions made by the IRS Commissioner. Although some decisions made by the IRS Commissioner would be subject to oversight by the Board under S. 1096 and the Commission Report, the IRS Commissioner will continue to exercise "significant authority"—particularly with respect to tax policy and specific law enforcement activities—such that the Commissioner could not be characterized as a mere "employee" or "lesser functionary" of the Federal Government. See *Buckley* v. *Valeo, supra; Edmond* v. *United States, supra.*

Because the IRS Commissioner historically has been appointed by the President, with the advice and consent of the Senate, there has been (to date) no need to determine whether the Commissioner is a "principal" or "inferior" officer. This mode of appointment is constitutionally valid for either type of officer. The proposed appointment of the IRS Commissioner by the Board, however, raises the following questions under the Appointments Clause: (1) would the IRS Commissioner be a "principal" or "inferior" officer, taking into account the other statutory changes proposed for the management of the IRS and enforcement of the tax laws; and (2) if the IRS Commissioner were an "inferior officer," could the Board collectively be characterized as a "Head of a Department" for purposes of Appointments Clause? Because neither the President nor a court of law would be appointing the IRS Commissioner, the appointment method provided for by S. 1096 and the Commission Report would be constitutionally valid only if *both* the Commissioner were an "inferior" officer *and* the Board collectively constituted a "Head of a Department." If either of these conditions were not satisfied, then appointment of the IRS Commissioner by the Board would not be constitutional.

Supreme Court decisions to date do not definitively resolve the questions regarding the status of the IRS Commissioner and the Board for purposes of the Appointments Clause. Moreover, resolution of the constitutional questions presented would depend on the specific statutory rules (and the precise interpretation of such rules) governing the Board's relationship to the IRS and the extent to which the Board were viewed as having not merely "oversight"

See *Buckley* v. *Valeo*, 424 U.S. at 137. But such functions cannot include enforcement powers, because such power cannot be regarded as merely in aid of the legislative function of Congress; it is the Executive branch that is entrusted the power to take care that the laws are executed. *Ibid.* Citing its earlier decision in *Humphrey's Executor* v. *United States*, 295 U.S. 602, 624 (1935), the Supreme Court noted in *Buckley* that it is not disputed that the Appointments Clause controls the appointment of members of a typical administrative agency even though its functions may be predominantly "quasi-judicial" and "quasi-legislative" rather than executive. 424 U.S. at 139 (Congress may appoint members to commissions that "perform duties only in aid of those functions that Congress may carry out by itself, or in an area sufficiently removed from the administration and enforcement of the public law as to permit their being performed by person not 'Officers of the United States') See also *Metropolitan Washington Airports Authority* v. *Citizens for the Abatement of Aircraft Noise, Inc.*, 111 S.Ct. 2298 (1991) (holding that separation-of-powers doctrine of Constitution was violated by appointment of Members of Congress to serve on Congressionally created review board with veto power over local airport authority, even though Members supposedly served in their individual capacities).

responsibilities but final legal authority over actions taken by the Commissioner. In this regard, S. 1096 is somewhat ambiguous. The introduced bill provides that the Board will have the general responsibility to "oversee" the IRS's administration and management of the execution of the internal revenue laws, and the specific responsibilities to "review and approve" strategic plans of the IRS and to "review" operational functions and plans for reorganization of the IRS. However, the conditions under which the Board might have final authority regarding such matters is not clear in view of the fact that, as introduced, the bill would not alter the general power of the Secretary of the Treasury under present-law Code section 7801(a) to administer and enforce the internal revenue laws, except as otherwise expressly provided by law.[52] If the provisions establishing the Board were construed as granting the Board final authority only with respect to the hiring and firing of the Commissioner, but actions taken by the Commissioner could not be reversed or revoked by the Board, then it is questionable whether the Commissioner could be characterized as an "inferior" officer. On the other hand, if the Board were viewed as having final legal authority to direct and supervise the management decisions of the IRS Commissioner, *and* if the Secretary of the Treasury were to retain authority (as under present-law sec. 7802(a)) to prescribe the duties and powers of the Commissioner in all other (non-management) actions taken by the Commissioner, it appears more likely that the Commissioner could be viewed as an "inferior" officer whose "superior" officers (below the President) are the Board *and* the Secretary of the Treasury. See *Edmond* v. *United States*, 117 S.Ct. at 1581 (discussing divided supervision of officer at issue).

However, S. 1096 provides that the IRS Commissioner, for the first time, would have specific *statutory* authority to "administer, manage, conduct, direct, and supervise the execution and application of the internal revenue laws" (proposed new sec. 7803(a)(2)). In the case of specific law enforcement actions taken by the IRS Commissioner, this new statutory authority granted to the IRS Commissioner could be interpreted to trump the general authority of the Secretary of Treasury under section 7801(a) with respect to the internal revenue laws.[53] If S. 1096 is so construed, the IRS Commissioner would *by statute* be authorized to take final actions on behalf of the United States that could not be reversed by other executive branch officers, which would support the argument that

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[52] The Commission's Report suggested that the Board would have "final authority" regarding any management matter where the Board reviews the decisions of the Commissioner and cannot reach a compromise agreement (Commission Report at 6).

[53] Under present law, the IRS Commissioner is not *statutorily* granted authority to enforce the tax laws. Rather, the Commissioner's authority is derived from delegation orders issued by the Secretary of the Treasury under present-law section 7802(a), which provides that "[t]he Commissioner of Internal Revenue shall have such duties and powers as may be prescribed by the Secretary of the Treasury." The Secretary has delegated to the Commissioner responsibility for the enforcement of the internal revenue laws and the collection of most Federal taxes, but has expressly withheld from the Commissioner authority to issue regulations. See Treasury Department Order 150–10 (April 22, 1982) (superseding Treasury Department Order 150–36 (March 17, 1955)). Therefore, because the IRS Commissioner currently is not vested *by statute* with authority to take actions to enforce the tax laws, but such authority is derived from delegation orders that presumably may be revoked at any time by the Secretary of the Treasury, one could argue that the IRS Commissioner is an "inferior" officer under present law but would more likely become a "principal" officer under S. 1096, which would repeal the Secretary's delegation authority under present-law section 7802(a) *and* would grant specific statutory authority to the Commissioner to administer the execution of the tax laws (proposed new sec. 7803(a)(2)).

the IRS Commissioner was a "principal," rather than an "inferior," officer. See *Edmond* v. *United States*, 117 S.Ct. at 1582.

If the IRS Commissioner were found to be an "inferior" officer under a statutory regime restructuring the IRS, then the second question arises whether the Board (which includes the Secretary of the Treasury) *collectively* could be viewed as a "Head of a Department." In this regard, it is relevant that the Board itself would have no authority with respect to tax policy matters and specific law enforcement activities of the IRS, and only the Secretary of the Treasury apparently would have final authority with respect to tax policy matters (and, perhaps, the IRS Commissioner would have final authority with respect to law enforcement matters under the proposed grant of specific statutory power to the IRS Commissioner). As with the first question above, resolution of this Appointments Clause issue construing "Head of a Department" would depend on the location of ultimate control over a "distinct province" or "separate organization" of the government. See *Freytag* v. *Commissioner*, 111 S.Ct. at 2660 (Scalia, J., concurring) (concluding that "Head of a Department" is not limited to Cabinet-level officials). Thus, even if a reviewing court were to take a flexible view of the modes of appointment allowed for "inferior" officers under the Appointments Clause, the determination whether an appointment at issue had been made by a "Head of a Department" ultimately would turn on the court's view of which person (or possible group of persons) holds the "reins of power" for the department. See *Silver* v. *United States Postal Service*, 951 F.2d 1033 (9th Cir. 1991).[54]

Characterization of IRS Commissioner as "principal" or "inferior" officer

The question whether the IRS Commissioner would be a "principal" or "inferior" officer for purposes of the Appointments Clause is addressed in a memorandum from the Congressional Research Service (CRS), which was prepared upon request by the National Commission on Restructuring the Internal Revenue Service. [55] This CRS memorandum ("CRS Memo") is included in Appendix B. Reviewing Supreme Court decisions (and other case law), the CRS

[54] In *Silver*, the two-judge majority on the Ninth Circuit panel rejected the argument that the Postmaster General's appointment by the nine "Governors" of the Postal Service violated the Appointments Clause. These two judges held that the nine Governors constituted the "Head of a Department" on grounds that "the reins of power reside exclusively with the Governors" who hold the statutory "trump cards" of the power to appoint and remove the Postmaster General, the unilateral power to revoke any authority delegated by the "Board" (which includes all nine Governors, plus the Postmaster General and Deputy Postmaster General), and the authority to designate mail classifications and to set postal rates. 951 F.2d at 1038. In dissent, however, the remaining judge on the Ninth Circuit panel concluded that the full 11-member Board was the "Head of a Department" for purposes of the Appointments Clause, on grounds that all functions and power of the Postal Service, other than votes on rate increases and new classes of mail, are exercised by the Board. 951 F.2d at 1044. Therefore, the dissent argued that the nine Governors acting collectively violated the Appointments Clause when they appointed the Postmaster General to this office. In sum, the different conclusions reached by the majority and dissenting judge on the Appointments Clause question resulted from the judges' different views on which body statutorily was granted authority for most of the functions and powers of the Postal Service.

[55] Congressional Research Service, Memorandum to the National Commission on Restructuring the Internal Revenue Service, "Constitutionality of Vesting the Appointment of a Commissioner of the Internal Revenue Service in an Independent Board of Directors Located in the Treasury Department," June 4, 1997. This memorandum was prepared prior to the publication of the Commission Report and the introduction of S. 1096. (See Appendix B.)

Memo concludes that, although "it is not yet clearly a settled matter" whether the Board could be vested with the authority to appoint the IRS Commissioner, it is "likely" that a reviewing court would conclude that the Commissioner was an "inferior" officer (CRS Memo at 2). In particular, the CRS Memo cites the recent Supreme Court decision in *Edmond* v. *United States, supra,* where the Court held that civilian members of the Coast Guard Court of Criminal Appeals were "inferior" officers who could properly be appointed by the Secretary of Transportation. Justice Scalia, writing for the Court in *Edmond*, stated:

> Generally speaking, the term "inferior officer" connotes a relationship with some higher ranking officer or officers below the President: whether one is an "inferior" officer depends on whether one has a superior. It is not enough that other officers may be identified who formally maintain a higher rank, or possess responsibilities of greater magnitude. If that were the intention, the Constitution might have used the phrase "lesser officer." Rather, in the context of a clause designed to preserve political accountability relative to important government assignments, we think it evident that "inferior officers" are officers whose work is directed and supervised at some level by others who were appointed by presidential nomination with the advice and consent of the Senate. 117 S.Ct. at 1580–81.[56]

Citing this language from *Edmond*, the CRS Memo concludes that, under the restructuring proposals, the IRS Commissioner would likely be viewed to be an "inferior" officer because "[t]he new scheme would relegate the Commissioner to inferior officer status since he would be appointed and overseen by the Oversight Board, the members of which are presidentially appointed with Senate advice and consent, and is removable by that body at its pleasure." (CRS Memo at 8). The precise nature of the proposed "oversight" of the Board, however, could be critical. It is doubtful that the mere fact that an officer is appointed by another officer below the level of the President is sufficient to establish that the appointed officer is an "inferior" officer for purposes of the Constitution.[57] Otherwise, there would never be a violation of the Appointments Clause when an officer was appointed by a "Head of a Department," because the mode of such appointment (and the power to remove, which generally is incident to the power to appoint[58]) could be re-

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[56] Historically, the Supreme Court took the approach that there was no exclusive criterion for distinguishing "inferior" from "principal" officers and that a weighing of all factors was required. *Morrison* v. *Olson,* 487 U.S. at 671–72; *Weiss* v. *United States,* 114 S. Ct. at 768–69 (Souter, J. concurring).

[57] See *Morrison* v. *Olson,* 487 U.S. at 722 (Scalia, J., dissenting) ("Even an officer who is subordinate to a department head can be principal officer").

[58] See *Myers* v. *United States,* 272 U.S. 52, at 161 ("The power to remove . . . is an incident of the power to appoint"). Some statutory restrictions may be placed on the Executive's general power to remove officers. See, e.g., *United States* v. *Perkins,* 116 U.S. 483 (1886) (Congress may place restrictions on the power of head of departments to remove inferior officers appointed by such head); *Humphrey's Executor* v. *United States,* 295 U.S. 602, 624 (1935) (upholding provisions under which President could remove commissioners of Federal Trade Commission only for "inefficiency, neglect of duty, or malfeasance in office," on grounds that the Commission's "duties are neither political nor executive, but predominantly quasi-judicial and quasi-legislative"); *Morrison* v. *Olson,* 487 U.S. at 690–94 (upholding removal provisions with respect to independent counsel, and finding that removal power—which is part of the President's general power to ensure a faithful executive of the laws—had not been "completely stripped" from the President). See, generally, Rotunda and Nowak, *supra,* vol. 1, at 691–702.

lied upon in a form of circular reasoning to prove the "inferior" status of the appointed officer.

Vesting the power to remove one official in another official below the President, by itself, is probably not enough to establish that the official subject to removal is "inferior." Justice Scalia concluded in *Edmond* that judges on the Coast Guard Court of Criminal Appeals were not subject to the "complete" control of the Judge Advocate General, even though the Judge Advocate General both exercised administrative oversight over the Court of Criminal Appeals and had the "powerful tool for control" of being able to remove Court of Criminal Appeals judges from their judicial assignments without cause. Even so, Justice Scalia noted that the Judge Advocate General had no power to reverse decisions of the judges on the Court of Criminal Appeals, but this power did reside in another executive branch entity, the Court of Appeals for the Armed Forces. Therefore, Justice Scalia wrote with respect to this divided supervision: "What is significant is that the judges of the Court of Criminal Appeals [who were held to be "inferior" officers] have no power to render a final decision on behalf of the United States unless permitted to do so by other executive officers." 117 S.C. at 1582. In a similar fashion, the proposed split supervision of the IRS between the Board and (presumably) the Secretary of the Treasury may establish significant control over the totality of activities carried out at the IRS, but a critical factor in determining whether the IRS Commissioner is an "inferior" officer under the restructuring proposals would be whether, and to what extent, the Commissioner would have authority to render decisions on behalf of the United States without being subject to reversal by other executive branch officers. As previously noted, the proposed repeal of the delegation power of the Secretary of the Treasury under present-law section 7802(a), coupled with the proposed grant of specific *statutory* authority to the IRS Commissioner to enforce the internal revenue laws, could be construed so that the Commissioner would have significant authority to enforce the internal revenue laws without being "permitted to do so" by other executive branch officers. Under such an interpretation, the IRS Commissioner could be characterized as a "principal" officer.

Characterization of Board for purposes of the Appointments Clause

The CRS Memo also addresses the issue whether the proposed Board could be characterized for purposes of the Appointments Clause as a "Head of a Department" capable of appointing an "inferior officer." With respect to this issue, the CRS Memo concludes that it is likely that a reviewing court would find that the Board is a "Head of a Department." The author of the CRS Memo reaches this conclusion by reading the recent Supreme Court decision in *Edmond* as reflecting an abandonment of the so-called "diffusion rationale." The concern that a broad construction of the term "Department" would lead to a "diffusion" of the appointment power generally vested in the Executive was one of the arguments relied upon by five Justices in *Freytag* to conclude that the appointment of special trial judges by the Chief Judge of the Tax Court did not constitute appointment by a "Head of a Department." Nonetheless,

such appointment of special trial judges was upheld by the Supreme Court in *Freytag*, with Justice Blackmun, delivering the opinion of the Court, concluding that the special trial judges were "inferior" officers who were appointed by a "Court of Law." In contrast, four Justices reached the same result in *Freytag*, but took a different approach (in a separate concurring opinion written by Justice Scalia), concluding that the appointment of special trial judges by the Chief Judge of the Tax Court did not constitute appointment by a "Court of Law" (which, according to Justice Scalia, should be limited to Article III courts) but was constitutional as appointment by a "Head of a Department."

The prediction of the CRS Memo that, in the future, reviewing courts are likely to place less emphasis on the "diffusion rationale" and, thus, broadly construe the term "Head of a Department" under the Appointments Clause may prove to be accurate. It is possible to read some of the language in *Edmond* in this manner, but the issue of construing the term "Head of a Department" was not presented in *Edmond*, because the appointments at issue had been made by the Secretary of Transportation. At most, the reduced emphasis on the "diffusion" rationale in *Edmond* is implicit in the Court's limiting the *Freytag* holding to its facts and questioning whether all Tax Court judges are "principal" officers.[59] But even if the Supreme Court in the future is inclined to allow a greater number of potential executive branch officials beyond those who sit in the President's Cabinet to have the constitutional ability to appoint "inferior officers," it is an open question whether the Court also will expand the definition of "Head of a Department" to include collective bodies, such as the proposed Board to oversee the IRS. The Ninth Circuit decision in *Silver* (discussed above) apparently is the only reported decision by a court where a collective group was held to be a "Head of a Department" for purposes of the Appointments Clause. The *Silver* court did not cite any case law in support of this particular conclusion, but merely stated that "[w]ithin the corporate framework explicitly established by Congress, the [nine] Governors are the head of the [Postal Service] department." 951 F.2d at 1038. It may be, however, that even if the Supreme Court will be less concerned about the "diffusion" of the appointment power among numerous so-called "department heads" below the constitutional level of the President, a slightly different concern may arise in a case where appointments are made on a group basis, without any one individual officer being accountable. Supreme Court Justices have repeatedly noted that multiple concerns underlie the Appointments Clause, particularly the objective that the public be able to identify the individual who made a particular appointment. See, e.g., *Weiss* v. *United States*, 114 S.Ct. at 766 (Souter, J., concurring)(noting that the "Appointments Clause forbids both aggrandizement and abdication"). As recently as *Ryder* v. *United States*, 115 S.Ct. 2031 (1995), Chief Justice Rehnquist wrote for a unanimous Supreme Court: "The Clause is a bulwark against one branch aggrandizing its power at the expense of another branch, but it is more: it preserves another aspect of the Constitu-

[59] The CRS Memo also notes that the composition of the Supreme Court has changed since Justice Blackmun wrote his opinion for the Court in *Freytag* (CRS Memo at 15).

tion's structural integrity by preventing the diffusion of the appointment power." 115 S.Ct. at 2035. The possibility of diffusion of the appointment power among a collective body (i.e., appointments being made by committee) may be viewed differently from allowing numerous individual agency heads to make appointments of their "inferior" officers. With respect to the Constitution's assignment of appointment responsibility to the Executive branch, Justice Scalia himself in *Edmond* referred to the underlying purpose of the appointments clause to assure a higher quality of appointments: "[T]he Framers anticipated that the President would be less vulnerable to interest-group pressure and personal favoritism than would a collective body. The sole and undivided responsibility of one man will naturally beget a livelier sense of duty, and a more exact regard to reputation." 117 S.Ct. at 1579 (citing A. Hamilton, The Federalist No. 76, at 387). See also *Pennsylvania* v. *United States*, 80 F.3d 796 (1996)("Accountability is ensured and governmental power checked by Congress's assignment of appointing power to the highly accountable head of a federal department like the HHS.")

In any event, even if a separate governmental organization with a corporate framework, as in *Silver*, has a collective body that potentially *may* qualify as a "Head of a Department" (such that appointments of officers formally may be made "by committee"), the question of whether a particular group with oversight responsibilities, in fact, is such a "Head" for Appointments Clause purposes could depend on whether sufficient "reins of power" over a separate governmental organization reside in the group. Thus, the specific statutory powers of the IRS Commissioner, the Board, and the Secretary of the Treasury, relative to each other's actions, could be critical to the determination whether the Board collectively should be viewed as the "Head" of the IRS. A court may well conclude that, despite the proposed Board's power to hire and fire the IRS Commissioner and its oversight responsibilities with respect to IRS management decisions, the Board cannot be the "Head" of the department that is the IRS in view of the Board's lack of *any* authority with respect to the development of tax policy, specific law enforcement activities, and certain procurement matters. See *Buckley* v. *Valeo*, 424 U.S. at 120 ("The Appointments Clause prevents Congress from dispensing power to freely"); *Burnap* v. *United States*, 252 U.S. 512, 515(1920)(the term "Head of a Department" means person "in charge of a great division of the executive branch").[60]

[60] It seems doubtful that a reviewing court would accept a tautological argument that the proposed Board is not the "Head" of the IRS in its entirety but is "Head" of a "Department" which oversees the IRS (i.e., the Board is the "Head" of itself). Under such an argument, the constitutional limitations on the appointment process for "inferior" officers could effectively be nullified, as various "appointment officers" could be created, each of whom would be the "Head" of their own appointment department, and they could then attempt to appoint "inferior" officers to serve in one or more other departments. Such a scheme clearly would undermine the Appointments Clause. See *Freytag* v. *Commissioner*, 111 S. Ct. at 2642 (the Constitution limits "possible repositories" of appointment power). But see *ibid*, 111 S. Ct. at 2660 (Scalia, J., concurring) (briefly discussing, but not resolving, whether cross-department appointments are permitted). Thus, it would seem that the "independent establishments" and "separate organizations" referred to by Justice Scalia that may constitute a "Department" within the meaning of the Appointments Clause should carry out executive branch activities largely independent of other departments. See *ibid*, 111 S. Ct at 2657–2660 (Scalia, J., concurring) (noting that if the Tax Court were a subdivision of the Treasury Department—as the Board of Tax Appeals used to be—it would *not* qualify as a "Department" within the meaning of the Appointments Clause, but, for example,

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3. Additional Constitutional issues

In addition to the above issues raised under the Appointments Clause with respect to the proposed appointment of the IRS Commissioner by the Board, S. 1096 and the Commission Report raise several other questions of constitutional dimension. The answers to these additional questions will depend (at least in part) on the analysis ultimately adopted by a reviewing court in addressing whether the IRS Commissioner is an "inferior" officer and whether the Board is a "Head of a Department." Additional constitutional questions raised by the proposals include the following.

(a) Would the Board alone have the power to remove the IRS Commissioner, or would the Board's removal power supplement the President's power to remove the IRS Commissioner, which arguably can be derived under the President's authority granted in Article II, section 3 of the Constitution to "take care" that the laws are faithfully executed? See *Myers* v. *United States*, 272 U.S. 52, 164 (1926). If the IRS Commissioner is viewed as conducting "pure" or "core" executive functions (as opposed to "quasi-judicial" or "quasi-legislative" functions), then restrictions on the President's removal power would be suspect. See *Morrison* v. *Olson*, 487 U.S. at 691–92 ("the real question is whether the removal restrictions are of such a nature that they impede the President's ability to perform his constitutional duty, and the functions of the officials in question must be analyzed in that light"). See, generally, Rotunda and Nowak, *supra*, vol. 1, at 691–92, 702.[61]

(b) The Commission Report proposes that the IRS Chief Counsel be appointed, and subject to removal, by the Board. This proposal raises the same constitutional issues as would the proposed appointment, and removal, by the Board of the IRS Commissioner. In contrast, S. 1096 would not alter the present-law rules under which the IRS Chief Counsel is appointed by the President, with the advice and consent of the Senate, thus, obviating the need to determine whether the Chief Counsel is an "inferior" officer.

(c) S. 1096 provides for appointment of senior IRS officials by the IRS Commissioner. If, however, the Board could not formally adopt (or overrule) the IRS Commissioner in this regard, then the Commissioner would himself be appointing "inferior" officers (in contrast to present law, where the Secretary has final authority to appoint all IRS officials). If the Board were found to be the "Head of a Department" and, thus, had the constitutional power to appoint the Commissioner, then could one argue at the same time that the IRS Commissioner also is the "Head of a Department" for appointment purposes? In this regard, Justice Scalia's opinions in *Freytag* and *Edmond* can be read to imply that all "Heads of Departments" are "principal" officers who are required to be appointed by the

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the Central Intelligence Agency should qualify as a "Department"). See also *Weiss* v. *United States*, 114 S. Ct at 770 (Scalia, J., concurring) (the Judge Advocate General for each military branch is *not* one of the "few potential recipients of the appointment power").

[61] Although S. 1096 and the Commission Report provide that the President would have authority to remove Board members at will, the President's ability to exercise such authority with respect to Board members may not ensure that the IRS Commissioner also is effectively subject to removal by the President. Even if the President were to remove all Board members, the IRS Commissioner presumably could continue to serve until the earlier of (1) such time that as new Board members are appointed *and* confirmed by the Senate, and the new Board then exercises its authority to remove the Commissioner, or (2) the expiration of the Commissioner's five-year term.

President, with the advice and consent of the Senate. If so, then either the proposed Board's appointment of the IRS Commissioner would be improper (because the Commissioner is a "principal" officer), or, if the Commissioner is an "inferior" officer subject to appointment by the Board, then the Commissioner him- or herself cannot be a "Head of a Department" under the Appointments Clause. The Commission Report proposals would avoid the issue of the constitutionality of the Commissioner's appointment power by vesting final authority with the Board with respect to the hiring of all IRS officials.

(d) The proposed set-aside of one seat on the Board for a representative of an organization representing a substantial number of IRS employees raises the question whether the office has been defined with too much specificity—i.e., has Congress so narrowed the President's field of choice that, in effect, Congress is attempting to appoint the officer? See, generally, Rotunda and Nowak, *supra,* vol. 1, at 672; Fisher, *supra,* at 28. In the past, Congress has provided that certain commission or board positions must be filled by a representative of a particular industry, or even a political party. It could be argued, however, that specifying that a particular position be filled by representative of one particular organization constitutes an undue constraint upon the President's constitutional appointment authority.[62] Moreover, if the term "representative" is construed to mean someone who is designated by the union itself (and not any union member who the President determines to be representative of the union membership as a whole), then a more significant constraint on the President's authority would be involved. See *Weiss* v. *United States,* 114 S.Ct. at 770 (Scalia, J. concurring) (violation of the Appointments Clause occurs not only when Congress may be aggrandizing itself but also when Congress effectively lodges appointment power in any person other than those whom the Constitution specifies).

(e) If a person involved in a court proceeding were to raise a timely objection to the constitutionality of the appointment of the IRS Commissioner, then that person would be able to challenge the validity of the Commissioner's actions to enforce the internal revenue laws. See *Ryder* v. *United States,* 115 S.Ct. at 2034–35) (holding that so-called de facto officer doctrine confers validity upon acts performed by a person acting under the color of official title even though it is later discovered that the legality of that person's appointment is deficient, but that doctrine is no defense to the Government in a case where a timely Appointments Clause objection was made during the proceedings). In *Freytag,* the Supreme Court went so far as to exercise its discretion to hear the petitioners' Appointments Clause challenge, even though the petitioners had specifically consented to assignment of their case to a special trial judge. The majority of Justices in *Freytag* were willing to consider the petitioners' Appointments Clause challenge in view of the "strong interest of the federal judiciary in maintaining the constitutional plan of separation of powers." 111 S.Ct. at 2639. The four remaining Justices in *Freytag* concluded that the petitioners had

[62] Apparently there is currently only one union that represents a substantial number of IRS employees.

waived their Appointments Clause challenge by not making a timely objection. But the ease with which Appointments Clause challenges could be raised—and the potential proliferation of such challenges among taxpayers involved in disputes with the IRS—is shown by Justice Scalia's remark in *Freytag* that "[a]ny party who objects to such assignment [to the special trial judge whose appointment was at issue], if so inclined, can easily raise the constitutional issue." 111 S.Ct. at 2650.

B. Issues Relating to the Ability of Changes in Management Structure to Improve Performance of the IRS

The recommendations of the National Commission on Restructuring the Internal Revenue Service ("the Commission"), S. 1096 and H.R. 2676 are designed to increase the performance and public perception of the IRS through various modifications in the management structure of the IRS. The extent to which these proposals are likely to transform the IRS depends on a variety of factors. The following discussion addresses issues that arise in determining whether any of the proposed changes, particularly the creation of the Oversight Board, are likely to have the desired effect.

1. Problems associated with present IRS governance and management

The Commission identified a lack of sufficient continuity and accountability as the primary problems associated with the present system of IRS governance and management. The proposals for an Oversight Board contained in the Commission's Report, S. 1096, and H.R. 2676 are intended to address these problems, as well as to facilitate the accomplishment of the restructuring goals discussed below.

Perceived lack of continuity and accountability in IRS governance and management

A lack of sufficient continuity in IRS governance and management is perceived by many to limit the ability of the IRS to succeed in a number of essential areas. In particular, the ability of the IRS to create and execute effective long-term strategies for the administration of the tax system, to design and implement necessary technological modernization, to properly train its workforce, and to accomplish needed reforms of its culture may be impaired by this lack of continuity.

The most frequent reason suggested for the lack of continuity in IRS governance and management is the relatively high turn-over rate of senior executive officials, including the Commissioner, who are charged with supervision of the IRS. While the position of Deputy Secretary of the Treasury, to whom the Commissioner reports, would not necessarily turn over at the same time as the Commissioner, the breadth of the Deputy Secretary's other, nontax responsibilities is such that he may not be able to provide sufficient continuity from one Commissioner to another. Frequently, a change in the identity of the Commissioner is accompanied by new programs and initiatives, which are themselves superseded by later programs and initiatives with the appointment of the next Commissioner.

A lack of sufficient accountability was identified by the Commission Report as the other primary problem with IRS governance and management. If senior management is not held accountable for the design and successful implementation of the policies and programs necessary to achieve an organization's goals, the chances those goals will be achieved are substantially reduced. Implementation of sufficient accountability includes not only the establishment of proper lines of authority and review, but also making sure that appropriate officers of the organization are held accountable for each of the organization's goals.

Many of the factors identified as contributing to a lack of continuity, as well as the lack of continuity itself, contribute to the perceived lack of accountability. While the Commissioner reports and is accountable to the Deputy Secretary of the Treasury, ten other senior government officials are as well. Some have questioned whether the Deputy Secretary has the necessary time and resources to devote to the review of the Commissioner and the IRS.

Need for greater continuity

The turnover in officials, programs and initiatives is an impediment to the creation and implementation of effective long-term strategies. Given the lack of continuity, an IRS Commissioner will likely focus on those short- and mid-term strategies that are more likely to be implemented successfully during his or her tenure, rather than longer term initiatives that would necessarily rely on the active participation of one or more successor Commissioners for successful implementation. Even if the successor Commissioners accept their predecessor's strategy, progress may be disrupted during the transition or newer initiatives given precedence, making successful implementation of the original long-term strategy less likely.

The lack of continuity is also perceived as an impediment to the ability of the IRS to design and implement necessary technological modernization. Continuity must be present during the period of time needed to design and implement new information technology systems. Where such continuity is lacking, frequent changes in focus and direction may prevent a project from ever reaching a successful conclusion. Further, a lack of continuity can allow failures of essential elements of the modernization project to remain undetected for significant periods of time, wasting resources and preventing the successful completion of other elements of the project which may be dependent on the failed element. Some have suggested that such a lack of continuity in the management and governance of the IRS was a contributing factor in the failure of the Tax System Modernization project.

It is also suggested that the lack of sufficient continuity in IRS governance and management may lead to inadequate training of IRS personnel and to the establishment and continuation of a culture that prevents the IRS from accomplishing its strategic objectives. The Commission Report describes the IRS as a "stovepipe operation," one in which each functional unit is allowed to set and implement its own priorities and objectives, with minimal regard for how they fit with the priorities and objectives of the organization as a whole. Although the Commission recognized that the IRS

had made progress in breaking down barriers between the stovepipe functions, it did not feel that the IRS had eliminated them to the degree necessary. The inability of the IRS to fully eliminate its stovepipe barriers may in large part be a reflection of the lack of continuity that exists at the highest supervisory level, the only level able to see over the individual stovepipes.

The establishment of an independent Oversight Board is proposed as a part of the solution to the perceived problem of insufficient continuity and accountability in IRS governance and management.

Under the proposals, the private sector members of the Oversight Board would serve staggered 5–year terms, so that a majority of the Board would not be expected to turn over in any year. Each private sector member of the Oversight Board would be eligible to serve two 5–year terms. This suggests the likelihood that there would be significant continuity in the membership of the Oversight Board, providing a continuity of governance and management that does not exist under present law. Whether such continuity in fact would result from would depend in part on whether qualified individuals are willing to serve on the Board for a full 5-year term.

Accountability and problems of conflicting authority

Many commentators believe that the present system of IRS governance and management results in the IRS being pulled in too many different directions, answerable to too many different authorities with contradictory agendas. In this view, because the IRS is accountable to and tries to satisfy all of these different authorities, it ends up satisfying and being accountable to none of them. As discussed above, the lack of a single direction from the Congress is a factor contributing to this problem. The IRS is subject to the jurisdiction of 6 Congressional committees, each of which has different objectives and concerns that change from year to year. This structure has been cited as impeding the formation of long-term objectives because it pulls the IRS in several different directions at once and requires the IRS to prepare for a number of possible outcomes. It also may impede progress toward fulfilling goals, because those goals may be changed in the near future.

Some commentators believe that an Oversight Board will ameliorate the IRS's problem of needing to answer to different authorities with contradictory agendas. These commentators see an Oversight Board as providing a single authority to which the IRS would be accountable, as well as creating a buffer between the IRS and the Congressional and Administration authorities to which it is otherwise answerable. In this view, actions taken by the IRS under the supervision of the Oversight Board, in conformity with Oversight Board reviewed plans and programs, would not be subject to challenge and influence by other authorities.

Supporters of this view point to the expertise the private sector members of the Oversight Board will bring to their positions. They suggest that Congress and the Administration ultimately will be more willing to defer to the judgment of a board composed of experts on such issues as information technology and service organization management.

Other commentators believe that an Oversight Board will only add one voice (or potentially more voices, one for each member of the Board) to the cacophony of authority to which the IRS is presently answerable. They doubt that Congressional and Administration authorities will willingly cede any of their influence over the IRS, regardless of the perceived or actual expertise of the Oversight Board. Even if the authority of the Oversight Board is respected by Congressional and Administration authorities, the Commissioner will be directly responsible to many individuals with potentially differing objectives.

Whether an Oversight Board will ameliorate or worsen the perceived problem of too many sources of conflicting authority may depend on the strength of the Oversight Board and its members, as well as the credibility of the Oversight Board with Congress and the Administration. If Congress and the Administration are unwilling to accept the role of the Oversight Board and insist on continuing their current level of the involvement with the IRS, it may be difficult for the Oversight Board to contribute effectively to the resolution of this problem.

2. Functions of the IRS and measures of performance

A primary function of the IRS is to collect the proper amount of taxes.[63] In order to successfully accomplish this purpose it must be able to accurately determine the amount of taxes owed and insure that collection takes place. As most taxes are paid voluntarily, it must also be able to assist taxpayers in accurately determining the amount of taxes they owe, understand where and how those taxes are to be paid, and encourage them to make the necessary payments. In cases where taxpayers fail to make the payments required by the tax laws, the IRS must identify the failure and require its correction.

As noted above, the Commission Report found that the organization of the IRS along functional lines has led to the creation of a "stovepipe operation". Under this view, the degree of independence granted the various functions of the IRS may also be seen as a problem. It is not sufficient that a function be held accountable for the successful completion of its activities if it is not also held accountable for its contribution to the overall goals of the organization.

Some commentators believe that the Oversight Board proposed in the Commission Report, S. 1096, and H.R. 2696 will improve the IRS ability to fulfill its functions. They view the Oversight Board as uniquely qualified to judge the contributions each separate function makes to the primary goal of the collection of the proper amount of tax. These judgments can then be used to develop, implement and adjust as needed the integrated long-term strategies that are necessary to achieve the IRS' goals. These commentators see the Oversight Board as providing the continuity needed to carry out this function. The Board members' experience in the

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[63] The mission statement of the IRS provides that:

> The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost; serve the public by continually improving the quality of our products and services; and perform in a manner warranting the highest degree of public confidence in our integrity, and fairness.

management of large service organizations, information technology, organization development, and other areas is seen as providing the expertise needed to design and implement necessary measures of performance.

Other commentators have expressed concerns with the ability of the Oversight Board to provide integrated governance and management of the IRS, as well as the level of expertise of its potential members. The authority of the Oversight Board is limited to issues of tax administration; issues of tax policy and specific law enforcement (under H.R. 2676, law enforcement) are not within its sphere of responsibility. Although a degree of separation between these functions exists today, the formalization of that separation through the creation of the Oversight Board is seen by these commentators as more likely to reinforce the negative aspects of the functional division of responsibility in the tax area rather than integrating them.

These commentators have also expressed concern with the stated qualifications required to be the sole basis for the appointment of Oversight Board members from the private sector.[64] In particular, they have expressed their concern that knowledge of the Federal income tax law and its rules of accounting are excluded from the list of qualifications under S. 1096 and the Commission Report. While recognizing the desirability of providing private sector input on disciplines such as service organization management, information technology, and organization development; these commentators believe that such skills cannot effectively be brought to bear in the absence of a knowledge of the rules of the Federal income tax. In their view, an Oversight Board whose private sector members will not be expert in the rules of the Federal income tax will either be dominated by the public sector member of the Board with the greatest tax expertise (probably the designate of the Secretary of the Treasury) or, if they resist the input of the public sector members, susceptible of pursuing programs that may be naive or ineffective. These concerns may be ameliorated somewhat under H.R. 2676, which clarifies that knowledge of the Federal tax laws is also a qualification. Of greater concern may be the view that the Oversight Board could focus exclusively or primarily on a bottom line view that measures taxes collected against the costs incurred to collect them, leading to tax administrative initiatives that do not respect the rights and needs of the taxpaying public.

3. Duties of the Oversight Board

In general

Under S. 1096, the Board would oversee the IRS in the administration, management, conduct, direction and supervision of the execution and application of the internal revenue laws or related stat-

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[64] Proposed section 7802(b)(2) would require that private members of the Oversight Board be appointed solely on the basis of their professional experience and expertise in the areas of:

(i) management of large service organizations;
(ii) customer service;
(iii) compliance (under H.R. 2676, Federal tax laws, including tax administration and compliance);
(iv) information technology;
(v) organization development; and
(vi) the needs and concerns of taxpayers.

utes and tax conventions to which the United States is a party. In addition, the Board would have specific responsibilities for approving strategic and operational plans, selecting the Commissioner, reviewing the appointment of senior managers and approving the appointment of the taxpayer advocate, reviewing IRS reorganization plans,[65] and reviewing and approving the budget request prepared by the IRS Commissioner.

However, the Board would be specifically denied any responsibility or authority with respect to (1) the development and formulation of Federal tax policy; (2) specific law enforcement activities of the Internal Revenue Service;[66] or (3) specific activities delegated to employees of the IRS pursuant to delegation orders in effect as of the date of enactment. The Board also would not have access to confidential taxpayer return information under section 6103 of the Code.

A principal issue that has been raised is the extent to which a Board should have appointment and budget authority, as opposed to functioning as a source of oversight and advisory input. Some contend that the Board should not have appointment and budget authority, particularly in a situation where many of the actual functions of the IRS—including the development and formulation of Federal tax policy through directions for its implementation—are not within the scope of the Board's authority. Others contend that absent direct line authority, the Board's potential impact would be too limited.

Appointment of the IRS Commissioner[67]

Some contend that the Board's authority to appoint and remove the IRS Commissioner under S. 1096 would be inappropriate, and that this authority should remain with the President. First, it is argued that the IRS Commissioner will have responsibility for all aspects of IRS activity, while the Board is specifically not authorized to affect either tax policy or various aspects of particularized tax administration. Making the Commissioner accountable to a Board that has no authority over major aspects of IRS activity arguably may create less rather than greater accountability, by diffusing lines of authority and providing no mechanism to resolve differences of opinion. A related concern is that there may be areas where it is difficult to distinguish clearly between "tax policy" and other aspects of tax administration.

It is also argued that the IRS Commissioner heads one of the most pervasive functions of government, and should not be removed from the accountability of and to the President. Some view the removal of the Commissioner from the President's appointment authority as a down-grading of the importance of the Commissioner's position, and are concerned that so doing could make it more difficult for the Commissioner to perform the functions of the

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[65] H.R. 2676, as passed by the House, provides that the Board has the authority to approve major reorganization plans.

[66] H.R. 2676, as passed by the House, clarifies that the Board does not have authority over law enforcement activities of the IRS.

[67] These issues do not arise under H.R. 2676, as passed by the House, because it provides that the Commissioner is appointed by the President, with the advice and consent of the Senate. Under H.R. 2676, the Board recommends candidates to the President, but the President is not required to choose as Commissioner a candidate recommended by the Board.

office. In addition, the appointment of the IRS Commissioner by one authority and the IRS Chief Counsel by a separate authority might affect the interaction of those officers, whose agreement may be desirable for effective IRS administration.

Others argue that the power of the President to appoint and remove Board members should satisfy any concerns about lack of accountability. Without direct accountability to the Board, it is argued that recommendations of the Board would less likely be implemented. Further, it is argued that accomplished persons might be less likely to serve on a Board that did not have authority other than a power of oversight and recommendation.

Some contend that the additional structures under this proposal would add little and might be cumbersome or perceived as downgrading the position of the IRS Commissioner even if the Commissioner is appointed by the President. Others contend that the proposal could contribute to continuity and to additional input useful to IRS.

Budget authority

Under S. 1096 and H.R. 2676, the Board is expected to review and approve the budget request of the IRS prepared by the Commissioner, submit such budget request to the Secretary of the Treasury, ensure that the budget request supports the IRS annual and long range strategic plans (which the Board must also review and approve), and ensure appropriate financial audits of the IRS. The Secretary of the Treasury shall submit the Board-approved IRS budget to the President, who shall submit such request, without revision, to Congress together with the President's annual budget request for the IRS.

Some have expressed concern that the power to "approve" the IRS Commissioner's budget is in effect the power to direct tax policy, notwithstanding the apparent denial of authority to the Board in that area. It is argued that the Board, by setting overall budget levels, as well as through particular budget directions, may effectively prevent the IRS from directing resources to enforce tax policy in one or more areas, or may require application of resources to another area, thus effectively determining the actual implementation of any tax policy. There is concern that the Board should not be involved in tax policy in this way, because the Board is not expected to be composed principally of individuals with tax expertise, and because the private sector members of the Board may have real or perceived conflicts of interest. Also, some have expressed concern that the Board-approved budget might conflict with the tax policy goals of the Treasury Department and the President.

Others contend that the budget procedure envisioned in the proposals merely requires the direct submission of a Board-approved IRS budget to the President and Congress, leaving the Secretary of the Treasury arguably free to submit a different request. The Board-approved budget could thus be viewed as an avenue for IRS views to be presented more directly to those making the budget decisions. However, some argue that the Board's power to approve a budget does not assure that the independent recommendations of the IRS Commissioner would become available to the Congress for use in its budgetary decision making. Further, it is argued that it

is unclear to what extent the IRS Commissioner would as a practical matter be considered able to work with the Secretary of the Treasury to advocate or develop a budget requesting different resources in a particular area if the Board had not approved an IRS budget including that particular allocation of resources.

Some contend that the Board's role in the budget process could add insight and continuity. Others have expressed concern that any potential for separate Treasury and Board-approved budget requests would make the budget process more difficult.

Interpretation of "tax policy"

Under S. 1096 and H.R. 2676, the Board does not have authority with respect to tax policy. Some are concerned that the practicable impossibility of distinguishing what is tax policy and what is tax administration may further diffuse IRS management and lines of decision making—since the Commissioner may be responsible to the Board with respect to some issues and to the Secretary of the Treasury for others.

For example, as discussed above, it is arguable that budgetary decisions, including overall budget levels as well as any budget decisions directing resources to particular areas or methods of enforcement or compliance, in effect direct the development and implementation of tax policy. Similarly, the Board's authority to review and approve strategic plans of the IRS, including the establishment of mission and objectives, and standards of performance relative to either, arguably may overlap with the power to develop tax policy.

The IRS traditionally devotes resources to issuing guidance to its field personnel regarding the types of issues to be examined, as well as procedures regarding the nature and scope of information that will be required from taxpayers. Some examples of these types of guidance are Revenue Procedures, industry specialization papers, or audit manual instructions. The proposal does not make clear to what extent any of these types of activities might fall under the realm of administration and management over which the Board may exercise authority, or alternatively under the realm of tax policy, over which the Board has no authority. Also, the IRS traditionally develops regulations interpreting or implementing tax laws, issues Revenue Rulings stating the litigating position of the IRS, and makes decisions regarding the types of cases that should be litigated. IRS also makes decisions regarding the extent and application of audit resources and other enforcement and compliance activities. IRS attempts to answer certain taxpayer inquiries by telephone. IRS also issues to taxpayers private letter rulings in numerous areas. In the context of mission and objectives of the IRS, issues could arguably arise that could affect some or all of these areas and activities.

S. 1096 and H.R. 2676 also reflect an intention that the IRS be more involved in the drafting of legislation; and in particular that the IRS be available to comment on administrative issues raised by proposed legislation. Some have argued that the proposed Board structure makes it less likely that the IRS will be involved in this way, because commenting on legislation—even with respect to ad-

ministrative issues—likely would involve and affect issues of tax policy.

In the event that disagreements arise regarding the scope of the Board's authority, or the accountability of the IRS Commissioner to the Board on the one hand or to Treasury on the other, the proposal does not contain an explicit mechanism for resolution of any such disputes. The President would retain the power to remove and replace any or all members of the Board at will. However, removal of one or more Board members (or of an IRS Commissioner by the Board under S. 1096, or the President under H.R. 2696), with replacements subject to the advice and consent of the Senate, is a relatively extreme step. Thus, it is arguably an unlikely method to resolve most ordinary disagreements that may arise over IRS management or direction. Some argue, however, that in practice most such issues would reach a resolution without such extreme measures, just as under the present system a balance between the tax policy and tax administration functions of Treasury and the IRS has developed.

4. Qualifications of Board members and composition of the Board

Treasury Secretary (or Deputy Secretary)

Some have questioned the inclusion of the Treasury Secretary (or Deputy) on the Board under S. 1096 and H.R. 2696, which gives the Board certain separate decision-making authority. It has been suggested that the Treasury Secretary (or Deputy) might exercise undue influence upon the other members by virtue of his or her position. Others, however, contend that the presence of this position is important to assure adequate presentation of any Treasury Department view or input to assist the Board in its decision making. Furthermore, the Treasury representative is only a single member, who cannot control the decisions of the other eight members. Further, it is contended that the presence of the Treasury position can effectively act as a check to defuse possible concerns about potential conflicts of interest (or the appearance of such conflict) with respect to the private sector board members.

IRS employee representative

Some contend that it is inappropriate for an IRS employee representative to be on the Board. Some who share this view argue that it is inappropriate to have any one specific individual or position designated for the Board that represents particular interests, and that such a designation may lead to appointment of Board members who represent special interests, rather than members who have appropriate expertise. Others argue that it is inappropriate to have an employee representative oversee management.

On the other hand, some argue that having an employee representative on the Board may make more palatable and effective any change to the IRS personnel and compensation structure. Some argue that while many corporate boards do not have employee representatives, it is not unusual.

Some also suggest that if an employee representative is on the Board, a management representative also should be—although it

may not be clear who the management representative would be (e.g., whether the IRS Commissioner would be viewed as being a management representative).

Under S. 1096, it is also argued that it is inappropriate for the IRS Commissioner to be appointed by a Board that includes a representative of IRS employees. Others, contend, however, that the employee representative is but one of many Board members, and thus cannot control decisions of the Board.

Other members of the Board

Some contend that the particular enumerated areas of expertise under S. 1096 and H.R. 2676, and the intent that the private life members collectively bring to bear expertise in the enumerated areas, may limit the number of points of view from persons with similar expertise, thus potentially granting too much influence to each Board member in the area of his or her expertise. Some are further concerned that knowledge of Federal income tax law is not required under S. 1096. Also, some contend that the Board has the potential to become a vehicle for appointment of representatives of different interest groups or types of industries, rather than of persons with significant hands-on expertise in management review. An additional view is that requiring expertise in particular areas affecting IRS operations could increase the potential for perceived or actual conflicts of interest.

Others argue that each of the areas of expertise enumerated is important to IRS administration. Furthermore, it is contended that the Board selection process can function to provide actual management expertise and input that would contribute to IRS operations. Thus, it is argued that a Board providing expertise in each of the enumerated areas can best contribute to the improvement of IRS management.

Some view the part-time nature of the private sector Board members as a potential detriment to their involvement and commitment to their Board responsibilities. On the other hand, others contend that the demands on the Secretary and Deputy Secretary of the Treasury, who have direct authority over the IRS, make full-time attention to the IRS impossible. In addition, it is argued that the part-time nature of the activity would encourage participation of experienced private sector members who can provide desirable input with respect to IRS management.

5. Conflicts of interest of Board members [68]

Under S. 1096, the Board would consist of 9 members, 7 serving on a part-time basis from the private sector (H.R. 2676 would have a Board of 11 members, 8 of which would serve on a part-time basis from the private sector). Some view this structure as raising difficult issues of actual or perceived conflicts of interest, which could undermine the goal of improving public perceptions and interactions with the IRS. It is argued that the very factors contributing to an individuals' required expertise may also contribute to an actual or perceived conflict. For example, a person with exper-

[68] See also Part One. III.C., *infra,* for additional discussion of certain issues regarding conflicts of interest.

tise in information technology may be or have been an officer or employee of an organization that might potentially contract with the IRS to provide such technology. Similarly, a person familiar with "the needs and concerns of taxpayers" might be or have been a taxpayer advocate, with personal clients (or affiliated with a firm that has clients) that could be affected by IRS actions. A Board member could be a current or former executive of a company that might pay less in taxes if certain generic types of administrative or compliance activities are not undertaken. It is also argued that every private individual or organization is potentially affected by the actions of the IRS; thus, the greater the number of persons on the Board, the greater the numerical chance of a conflict or appearance of a conflict involving a Board member or an organization with which such person is or was affiliated. Some contend these concerns could be reduced by limiting private sector Board membership to persons retired from other employment.

Some argue that the Board has no authority to become involved in specific cases and thus the likelihood of actual conflicts of interest is remote. However, others contend that even if actual conflicts of interest are unlikely or can be dealt with through recusals if necessary, and even if Board members act with perfect propriety, the likelihood of perceived conflicts of interest is inherent in the Board structure and could further erode the confidence of taxpayers in the IRS. For example, if the Board is composed of members (or former members) of business entities, and if the business audit rate were reduced for any reason, the general public may view this as Board members benefitting themselves, even if there were in fact no actual conflict on a particular matter or otherwise. As another example, if any taxpayer with which a Board member is or was directly or indirectly connected experiences a favorable outcome in an IRS matter, or is otherwise arguably favorably affected by any IRS action, there could be a perception of influence even if it had not occurred. Those who hold this view argue that it would be impossible to overcome such perceived conflicts.

Others argue that the appointment and removal process would address conflicts concerns. Also, it is argued that most existing government appointments (including the present structure of the Treasury Department) involve the appointment of persons who come from and may return to private employment, often in the areas directly affected by the department in which they are employed. In addition, traditional ethical practices applicable to boards of directors could be applied to the IRS Board, including practices of recusal and disclosure. H.R. 2676 clarifies that the conflict of interest rules that apply to special government employees generally would apply to the private-life members of the Board. Further, it is argued that the benefits to be derived from the input of the various members would outweigh the potential for additional conflicts or perceptions of conflicts. Thus, it is argued that the Board structure could improve overall performance of the IRS, enhancing public confidence.

6. Ability to affect all levels of IRS activity

Whether or not any proposal to improve the performance and perception of the IRS will be effective depends in part on the abil-

ity to transform all levels of the IRS. For example, hiring new, better trained, and more capable managers will not affect IRS performance if personnel policies prevent the carrying out of management objectives. Some commentators have suggested that the Oversight Board would not be able to affect all levels of IRS activity even if future IRS personnel policies otherwise allow for the effective implementation of management objectives, because the Board does not directly review all personnel.

Other commentators have rejected this concern. They point out that a path of accountability can be traced from every IRS employee to someone whose performance will be reviewed either directly or indirectly by the Oversight Board. Boards of Directors in the private sector do not typically involve themselves in personnel matters below the senior officer level. However, since the performance of those officers depends at least in part on the performance of those who report to them, the Board is able to impact activity at all levels of the organization.

7. Effect of the Board on the public perception of the IRS

The Commission Report found that the public perception of the IRS had been damaged in a number of ways, many of which reflect a view that the IRS is unable to efficiently manage its affairs. The perceived inability of the IRS to consistently provide correct answers to those taxpayers seeking its guidance, to apply the tax laws in a consistent manner, to resolve administrative disputes in a timely manner, to treat taxpayers with courtesy, and to manage its affairs in an efficient manner have all led to an unnecessarily negative public perception of the IRS.

It should be understood that the IRS, as the collector of taxes, may always have a negative perception from a public that desires to limit the amount of taxes that it pays. Some commentators have criticized the Commission Report as unrealistic in suggesting that restructuring IRS management could change that.

On the other hand, the Commission found that management failures had contributed to an unnecessary and excessively negative perception of the IRS. To the extent that the Oversight Board can improve the management of the IRS and help it better focus on the performance of its duties, it may be expected to improve the public perception of the IRS. On the other hand, should decisions of the Oversight Board result in more aggressive collection practices or cost saving steps that reduce taxpayer service, the public perception of the IRS could be further eroded.

The contribution of the Oversight Board to the improvement of the public perception of the IRS may also turn on the public perception of the Oversight Board. If the Oversight Board is perceived as improving the management of the IRS, that positive perception is likely to be transferred to some degree to the IRS. On the other hand if the Oversight Board is perceived negatively, whether because of perceived conflicts of interest or for other reasons, the public perception of the IRS could be further damaged.

8. Resources available to the Board and the IRS

Whether the Oversight Board is ultimately able to improve the performance of the IRS may in part be determined by the Board's

role in insuring adequate access to resources by the IRS. Many contend that the IRS needs to be able to obtain assurances of adequate funding over a period of years. The Commission saw stable funding as necessary in order to undertake the proper planning necessary to rebuild the foundation of the IRS and recommended stable funding of the IRS over the next three years. The Commission Report also noted that a stable budget would allow the IRS to plan and implement operations that will improve taxpayer service and compliance, such as technological modernization and employee training.

The Oversight Board would not control the proposed budget for the IRS that is submitted to Congress by the Administration. However, it would review, approve and separately submit the budget proposal developed by the IRS Commissioner. Some feel that this process will provide additional legitimacy to IRS budget requests and increase the likelihood that adequate resources will be made available to the IRS. Others suggest that the revised process may make it less likely the IRS will obtain adequate resources, since there is less incentive for Treasury to obtain sufficient resources for the IRS in the Administration budget proposal, and Congress may be adverse to increasing the budget of the IRS.

9. Qualifications of IRS Commissioner

Under S. 1096, the Board would appoint an IRS Commissioner for a five-year term. The appointment is to be made on the basis of demonstrated ability in management. Under H.R. 2696, the Board recommends a candidate to the President, who is not required to nominate the candidate selected by the Board.

Some have observed that many of the individuals who have held the post of Commissioner in the past have been tax professionals, often with principal managerial responsibility for a relatively small legal staff. It is argued that a background in the tax law and awareness of its complexities is important to understanding administrative and operational issues the IRS faces—including, for example, the difficulties of training IRS employees to apply the tax law either in the course of audits or in the case of taxpayer inquiries during the filing season, and the difficulties of developing systems that can most efficiently select tax returns for audit or other compliance measures. It is also argued that the absence of a tax background could affect the relationship of the IRS Commissioner and the IRS Chief Counsel with respect to matters that affect tax policy as well as tax administration. However, it is also recognized that selection of a person with demonstrated ability in management would not preclude the selection of a person with a tax background, if considered desirable.

Others observe that the traditional background of many IRS Commissioners may limit the scope of their ability to deal with important operational and technological issues facing the IRS today. It is argued that other areas of expertise may be even more essential to IRS concerns. Also, it is argued that the Chief Counsel of the IRS, appointed by the President and dealing with issues of tax policy, would continue to provide the opportunity for the IRS to obtain the input and direction of experienced tax professionals.

10. Issues relating to the Office of Chief Counsel [68a]

The Chief Counsel is the chief law officer for the Internal Revenue Service. The Office of Chief Counsel plays a tax policy role by providing tax guidance for its client, in the form of private letter rulings, technical advice memoranda, revenue rulings, and regulations. All regulations are signed by the Commissioner, and constitute statements of Federal tax policy. The Office of Chief Counsel plays an enforcement role, as well as a tax policy role, when acting as a litigator. As the client, the Internal Revenue Service has final decision authority on whether to litigate a case or not, and may veto a litigation strategy proposed by the Chief Counsel. However, the delegation order which grants authority to the Chief Counsel provides that "any legal matter involving Treasury policy about which the Commissioner disagrees with the advice given to him/her by the Chief Counsel will be submitted by the Commissioner to the Secretary or the Deputy Secretary for resolution." [69]

S. 1096 would not change the way that the Chief Counsel is appointed. The President would continue to appoint the Chief Counsel, with the advice and consent of the Senate. Under current law, the Chief Counsel is an Assistant General Counsel of the Treasury Department, reporting to the General Counsel of the Treasury Department. Under S. 1096, the Chief Counsel would report directly to the Secretary. The proposal raises issues relating to the relationship between the Chief Counsel and the Commissioner. Under current law, both the Chief Counsel and the Commissioner are appointed by the President and can be removed by the President. Under the Commission's proposal, the Commissioner would be appointed by the Board and may be removed by the Board. This difference in appointment method may cause tensions between the two officials.

As the responsibilities of the Chief Counsel are focused on tax policy and enforcement, which are specifically excluded from the Board's supervisory authority, some argue that it is unlikely that the Commissioner and the Chief Counsel will have disagreements as a result of the Board's oversight. Others contend that tax policy and tax administration may not be readily separable. However, if the Commissioner, under the direction of the Board, did disagree with the Chief Counsel, under the direction of the President, the proposal does not address a means of solving such disagreement. The Commissioner would not have authority to fire the Chief Counsel, and the President would be unlikely to do so if the Chief Counsel is acting consistently with the President's will, albeit in conflict with the will of the Board. Similarly, the President could not fire the Commissioner under the proposal, but could only remove the Board members.

The creation of the Board may serve to increase further the importance of the Chief Counsel with respect to tax policy and procedure. The Commission Report provides that the Board would not address issues of tax policy, and also contemplates that the IRS Commissioner need not be a tax law expert, but should be someone

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[68a] These issues do not arise under H.R. 2676, as passed by the House, because it retains present law with respect to the Office of the Chief Counsel.

[69] G.C.O. No. 4 (July 1, 1997).

with management expertise. This represents a significant departure from past practice, under which IRS Commissioners in recent decades have generally been respected practitioners in the field of tax law and accounting. If the IRS Commissioner's duties are largely executive, the tax policy and tax procedural responsibilities currently carried out by the IRS Commissioner could fall upon the Chief Counsel's office, including the responsibility to grant final approval over the issuance of regulations and other tax guidance publications. Arguably this could increase the workload and the number of decisions that would need to be made by that office. Some argue that this might merely change the locus of the decision-making process, without providing any increase in efficiency or improving the "user-friendliness" of the IRS for taxpayers. In fact, delays could be exacerbated without added staff to absorb any workload increase. On the other hand, some might argue that the Board, together with a more managerial type of IRS Commissioner, could anticipate and address these types of problems, with resulting increases in efficiency of operation.

11. Tax simplification

The Commission Report observed a "clear connection" between the complexity of the Internal Revenue Code and the difficulty of tax law administration and taxpayer frustration. The Commission strongly recommended that the Congress and the President work toward simplifying the tax law wherever possible.

The Commission observed that uncertainty adds to complexity and to the cost of compliance; and that uncertain interpretation of the tax law results in compliance problems. Various steps were recommended to reduce complexity, including increased involvement of IRS personnel in the development and drafting of legislation, and consideration of various other ways to identify complexity in legislation.[70] Others have also commented that tax law complexity makes training extremely difficult for the IRS, potentially increasing the likelihood that taxpayers may experience additional difficulties with both compliance and customer service IRS functions.

The Board would not have any direct authority over tax simplification. The simplification of tax statutes would remain within the domain of the Congress (subject to the veto power of the President). Tax policy issues within the IRS, including tax policy decisions affecting the complexity of tax law interpretation of administration, also would not be within the Board's domain.

C. Issues Relating to the Conduct of Business by the Oversight Board

The Commission's proposal provides only general outlines for the conduct of business by the Board. The Board would elect a chairperson for a two-year term. The Board is to meet at least once each month. The Board is to make a report on the conduct of its responsibilities each year to the President and Congress. The lack of specificity regarding the operations of the Board raises technical issues that should be clarified in any final legislation. Some of these issues are discussed below.

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[70] See discussion in Part One. IV.B., *infra.*

1. Rules for the conduct of business

In general, a board of directors for a corporation will adopt bylaws for such corporation that contain provisions for managing the business and regulating the affairs of the corporation. Bylaws may be general or specific, depending on the needs of the business. However, bylaws for any business generally provide procedures for calling a meeting of the board and quorum requirements for holding such meeting. The bill does not say whether the Board has the ability to address such issues. That authority should be clarified.

The proposal provides that any vacancy on the Board shall not affect the powers of the Board. This provision raises the concern that the Board could take action even if it had only one member (which, for example, could be the employee representative). A quorum requirement would ease this concern. The Model Business Corporation Act provides that a majority of the fixed number of directors constitutes a quorum.[71] In addition, it may be appropriate to provide rules requiring a larger quorum or more than a majority vote for certain actions of the Board, such as the removal of the Commissioner.

Corporate bylaws also generally provide for the qualifications of directors. The proposal describes the qualifications of the Board in terms of their expertise. In light of perceived concerns about potential conflicts of interest,[72] it may be appropriate to further restrict eligibility to serve on the Board. As an example, it may not be appropriate for the chief executive officer of a corporation which has a large procurement contract with the IRS to serve on the Board. Other rules to avoid the appearance of a conflict of interest could also be adopted, such as recusal requirements. The proposal contains safeguards against actual and perceived conflicts of interest by reference to the rules for ethical conduct of government employees. Under the proposal, the Board members would be special government employees. As special government employees within the meaning of 18 U.S.C. sec. 202(a), the Board members are subject to criminal sanctions for acts affecting a personal financial interest.[73] Government employees are prohibited from participating personally and substantially in an official capacity in any particular matter in which, to their knowledge, they or any person whose interests are imputed to them has a financial interest, if the particular matter will have a direct and predictable effect on that interest.[74] Unless the employee receives a waiver, the employee must refrain from participation in the matter.[75] A government employee must also demonstrate impartiality in the performance of official duties, and should not participate in a matter where the circumstances would cause a reasonable person with knowledge of the relevant facts to question his impartiality in the matter, unless the employee has informed the agency of the appearance problem and received authorization to participate.[76] Other than the President, it is unclear who would have the authority to grant a Board member

[71] Section 8.24(a)(1) of the Model Business Corporation Act ("MBCA").
[72] See discussion relating to conflicts of interest in Part One. III.B.5., *supra*.
[73] 18 U.S.C. sec. 208(a).
[74] 5 C.F.R. sec. 2635.402(a).
[75] 5 C.F.R. sec. 2635.402(c).
[76] 5 C.F.R. sec. 2635.502(a).

a waiver for an actual or perceived conflict of interest. Accordingly, a reference to the rules for ethical conduct of government employees may not be sufficient to resolve the perception of conflicts of interest by the private sector members of the Board. On the other hand, the application of the criminal sanctions of the governmental ethics rules could have a chilling effect on the recruitment of Board members with the necessary expertise. Final legislation should clarify the application of governmental ethics rules to the Board members. It should be considered whether special conflict of interest rules applicable to the Board members should be included.

2. Application of Freedom of Information Act, Sunshine Act, and Federal Advisory Committee Act

Freedom of Information Act

The IRS is an administrative agency. The IRS's status as an administrative agency means that administrative law, statutory and decisional, which limits the exercise of power and controls the processes of all administrative agencies, applies to its actions. The Administrative Procedure Act ("APA"),[77] including the provisions of the Freedom of Information Act ("FOIA"),[78] currently apply to the IRS.

FOIA requires most written material produced by agencies to be made public. The purpose of FOIA is to ensure that citizens are informed about actions taken by their government, so that citizens can operate as a check against corruption by holding their government accountable. Unless agency information is exempt from FOIA, it must be made available to the public. The proposal does not address FOIA, so current law would govern the application of FOIA to the Board's written work product. As the Board would be the governing body of the IRS, FOIA would apply to written material produced by the Board. However, much of the material produced by the Board would probably be exempt from FOIA under the exemption for intra-agency memoranda.[79] This exemption protects intra-agency memoranda that are part of an agency's deliberative or policy-making processes, which would generally not be discoverable in a court case on a claim of governmental or deliberative process privilege. The purpose of the exemption is to encourage and protect a free and candid exchange of ideas during the decision-making process. As the proposal does not discuss FOIA, it may be appropriate to clarify whether it is intended that FOIA apply to the Board's work product, either in the statute or the legislative history.

Sunshine Act

Meetings of the heads of agencies with a multimember decision-making body were made public by the Government in the Sunshine Act ("Sunshine Act").[80] The purpose of the Sunshine Act, like FOIA, is to provide citizens an opportunity to witness the decision-making processes of their government. The proposal does not ad-

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[77] 5 U.S.C. secs. 551 et seq.
[78] 5 U.S.C. sec. 552.
[79] 5 U.S.C. sec. 552(b)(5).
[80] 5 U.S.C. secs. 552b.

dress the Sunshine Act, so current law would govern the application of the Sunshine Act to the Board's oral communications. As the Board would be a multi-member decision-making body, its meetings with the Commissioner would be covered by the Sunshine Act.

The concept of meetings covered by the Sunshine Act is extremely broad and may include not only sessions at which formal action is taken but also those at which a quorum of members deliberates regarding the conduct or disposition of agency business. For those meetings covered by the Act, an agency must announce, at least one week prior to a meeting, the meeting's date, location and other information. Although an agency can close a particular meeting to the public, on the grounds that the meeting may have an adverse impact on the rights of individuals or on the ability of the government to function properly, an agency cannot by rule or internal procedure close groups or categories of meetings.[81] Meetings which relate solely to the internal personnel rules and practices of the agency[82] or would be likely to significantly frustrate implementation of a proposed agency action[83] are exempt from the Sunshine Act.

Some have commented that the goals of the Board could not be accomplished if open meetings were required, as open meetings might discourage the Commissioner and the Board from expressing frank views about progress towards goals of tax administration. On the other hand, one purpose of the Board is to foster public confidence in the IRS, and it could be argued that closing meetings to the public would be inconsistent with that purpose. As the proposal does not discuss the Sunshine Act, it may be appropriate to clarify whether it is intended that the Sunshine Act apply to the Board's oral communications, either in the statute or the legislative history.

Federal Advisory Committee Act

The Federal Advisory Committee Act ("FACA")[84] was designed to improve public access to the decision-making processes of advisory committees, which are constituted of private individuals who gather to advise the government. Under the proposal, the FACA probably would not apply to the Board, as it would be a decision-making body rather than an advisory committee.[85]

Under FACA, advisory committees are broken down into two types: groups "established by" the agency and groups that are "utilized by" the agency. An "established" committee must be rechartered every two years, and is subject to Congressional and administrative review. There is no exclusion for frustration of agency action or for "intra-agency" memoranda under FACA. Judicial decisions have concluded that requiring meetings between outside groups and the agency to be public neither inhibits candid exchanges with the agency nor decreases the information available to

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[81] See *Pacific Legal Foundation* v. *CEQ*, 636 F.2d 1259 (D.C. Cir. 1980).
[82] 5 U.S.C. sec. 552b(c)(2).
[83] 5 U.S.C. sec. 552b(c)(9)(B).
[84] 5 U.S.C. App. 1.
[85] An advisory committee is established "in the interest of obtaining advice or recommendations." *Id.* at section 3(a).

the agency.[86] As noted above, some have argued that one of the goals of oversight would be frustrated if meetings and work product of the body providing oversight were required to be public. One way to exempt the activities of an oversight body from FACA is to designate all members as special government employees. In *Association of American Physicians and Surgeons, Inc.* v. *Hillary Clinton*,[87] which involved a challenge to the President's Task Force on National Health Care Reform, the court agreed with Mrs. Clinton that the FACA did not apply because all members of the Task Force were officers or employees of the government (including Mrs. Clinton). Any proposal involving an advisory committee should clarify whether it is intended that FACA apply.

D. Issues Relating to the Structure and Funding of the Employee Plans and Exempt Organizations Division

Nature of EP/EO mandate

As the Commission Report notes, Congress frequently directs the IRS to perform functions not directly related to its core purpose of collecting the proper amount of Federal tax revenues at the least cost. While EP/EO is not the only example of such a non-core function, it is one of the most visible, with responsibility for regulating sectors of the national economy estimated to represent approximately $135.9 billion in annual Federal income tax expenditures in fiscal year 1998—an amount equal to approximately 25 percent of total estimated Federal income tax expenditures for that fiscal year.

EP/EO was formed primarily to exercise regulatory supervision over employee benefit plans and exempt organizations with the goal of protecting the interests of employee benefit plan participants and of contributors to and beneficiaries of tax-exempt organizations. However, the office is also charged with the more traditional IRS function of revenue collection and tax law enforcement. These two functions can lead to conflicting results. For example, in the pension context, a plan sponsor or employer may be responsible for violations that disqualify the plan from Federal tax benefits. However, the plan participants would suffer the primary unfavorable consequences of plan disqualification. Similarly, revocation of exemption of a tax-exempt organization may primarily harm the charitable class that relies on the organization for goods or services (or contributors to the organization) rather than the individuals who may have diverted the organization's funds for private benefit. These potentially conflicting mandates have led EP/EO to develop innovative and effective voluntary compliance programs that seek to encourage retirement plans and tax-exempt organizations to comply with Federal tax obligations and limit the necessity for traditional enforcement actions. The Commission cites the EP/EO operation, and particularly its voluntary enforcement efforts, as "one of the most innovative and efficient functions within the IRS."

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[86] See *Nader* v. *Dunlop*, 370 F. Supp. 177 (D.D.C. 1973).
[87] 997 F.2d 898 (D.D.C. 1993).

Need for additional EP/EO resources

Because the IRS does not have infinite financial resources, it must constantly determine how best to allocate its available resources among its myriad functions. Inevitably, such an allocation process will favor the IRS' core tax collection function at the expense of non-core functions. Congress acknowledged this tension at the time it established EP/EO by elevating supervision of the office to an Assistant Commissioner and by dedicating a source of funding for the office. However, the designated funding mechanism has never been utilized and EP/EO, along with the rest of IRS, is funded out of Treasury Department general appropriations.

As set forth in Table 2 (in Part One.I.C., above), the level of EP/EO staffing in 1997 is essentially the same as it was upon formation of the office in 1974, and is, in fact, approximately 20 percent lower than it was at its peak in 1989. Given the tremendous increase in the number of organizations and plans—and the value of assets—within EP/EO's jurisdiction, as well as an expansion of EP/EO's responsibilities to include tax-exempt bonds, the EP/EO staffing level has been a source of Congressional concern in recent years. Twenty years after creation of EP/EO, the Subcommittee on Oversight of the House Committee on Ways and Means concluded that "the IRS does not have sufficient resources allocated to ensure compliance by public charities with applicable tax rules,"[88] and recommended that "the staffing and funding levels allocated for IRS's exempt organization examination and compliance activities be increased to a level consistent with the number, size, and diverse activities of tax-exempt organizations."[89] Similarly, in its 1994 review of IRS program areas within the jurisdiction of the House Committee on Ways and Means, the General Accounting Office testified that limited resources at the IRS have influenced the level of oversight of ERISA.[90]

EP/EO is not unique within the IRS in its need for additional financial resources. However, the magnitude of the sectors EP/EO is charged with regulating as well as the nature of its mandate support the Commission's conclusion that Congress should provide sufficient resources for EP/EO to carry out its functions.

Source of funding

The Commission recommends the reinstatement of the funding mechanism in Code section 7802(b)(2) (described in Part II.C. above), modified to provide that such funds can only be used to fund EP/EO.[91] In addition, S. 1096 includes an additional funding source, dedicating all user fees collected by EP/EO to carry out the functions of that office.

Although the bill attempts to tighten the connection between the excise taxes collected on investment income of private foundations under Code section 4940 and the funding of EP/EO, the office's funding would, as under present law, be subject to the appropria-

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[88] Subcommittee on Oversight of the Committee on Ways and Means, *Report on Reforms to Improve the Tax Rules Governing Public Charities* (WMCP 103–26), iv (1994).

[89] *Ibid*, pp. 18–19.

[90] *1993 Comprehensive Oversight Initiative of the Committee on Ways and Means*, H.Rept. 103–450, 3 (1994).

[91] H.R. 2676, as passed by the House, eliminates the EP/EO funding mechanism set forth in Code section 7802(b)(2).

tions process and there is no guarantee that the designated amounts actually would be appropriated. Initial legislative intent has been ignored for over 20 years in spite of periodic revisiting of the issue by Congress. Further, the section 4940 excise tax is not without its flaws as a funding source. Because the tax is based on investment income, the amount collected under the tax is very much subject to the vissicitudes of the financial markets. Such uncertainty makes short- and long-range organizational planning difficult. In addition, if the dedication of the section 4940 excise tax to the EP/EO function is deemed appropriate, it may be equally appropriate for other areas of the IRS to retain excise taxes collected from taxpayers under their jurisdiction.

The dedication of user fees collected by EP/EO to carry out its functions raises a number of similar issues. In general, Federal user fees are charges for a specific service, requested by and beneficial to identifiable persons. A user fee must satisfy three characteristics: (1) it must be voluntary; (2) the user must benefit from the fee; and (3) the fee must be based on the actual cost of providing the service (e.g., providing a copy of a tax return). Prior to 1988, the IRS did not charge user fees. However, as part of the Revenue Act of 1987, Congress directed the Secretary of Treasury to establish a program requiring the payment of user fees for requests to the IRS for letter ruling, opinion letter, determination letter, and other similar requests.[92] Absent specific statutory authority, user fees are paid directly into the Treasury general fund as miscellaneous receipts. However, IRS's 1995 appropriation permitted the IRS to retain up to $119 million per fiscal year in fee revenue derived from new fees and increases in existing fees, in addition to its regular appropriation.[93] Table 3 contains total EP/EO user and compliance[94] fees since inception of the IRS user fee program. Table 4 sets forth EP/EO user and compliance fees for fiscal years 1994 through 1996, broken out between EP and EO, and National Office and field offices.

[92] Section 10511 of PL. 100–203, 101 Stat. 1330–382, 1330–446, enacted December 22, 1987. The fees applied to requests made on or after February 1, 1988, and before September 30, 1990. Subsequent legislation extended the fee authority through September 20, 2003. Sec. 2 of P.L. 104–117, 1996–34 I.R.B. 19.

[93] The IRS publishes revised user fee schedules annually. For example, Revenue Procedure 97–8, 1997–1 I.R.B. 187 sets forth current user fees applicable to matters within the jurisdiction of EP/EO.

[94] Compliance fees may be imposed as part of one of the voluntary self-correction programs administered by EP/EO. Such fees do not qualify as "user fees" and, thus, would not be includible for purposes of calculating EP/EO funding under the bill. Compliance fees represented approximately $1.4 million of total fees collected by the National Office in 1994, $1.6 million of 1995 fees, and $2.1 million of 1996 fees.

Table 3.—EP/EO User and Compliance Fees, 1988–1996

Fiscal year	Fees collected ($ millions)
1988	18.2
1989	33.7
1990	29.4
1991	36.9
1992	34.8
1993	36.0
1994	39.7
1995	76.1
1996	40.3

Source: Internal Revenue Service.

Table 4.—EP/EO User and Compliance Fees, 1994–1996

	FY 1994		FY 1995		FY 1996	
	EP	EO	EP	EO	EP	EO
National Office	$3,029,000	$618,000	$2,882,000	$638,000	$3,384,000	$622,000
Field Offices	$20,857,000	$15,173,000	$56,938,000	$15,599,000	$20,885,000	$15,386,000
Total Receipts	$39,677,000		$76,057,000		$40,277,000	

Source: Internal Revenue Service.

As Tables 3 and 4 illustrate, user fees are not necessarily a consistently stable source of revenue. The level of total receipts may be influenced significantly by factors beyond the IRS' control. For example, collections in fiscal year 1995 were almost double those in fiscal years 1994 and 1996; this increase is attributable largely to the effects of reforms in the tax law governing employee benefit plans contained in the Tax Reform Act of 1986 and subsequent legislation that necessitated plan amendments and caused employee benefit plans to seek requalification with the IRS as qualified employee benefit plans. In addition, if the dedication of EP/EO user fees to the EP/EO function is deemed appropriate, it may be equally appropriate for other areas of the IRS to retain user fees collected from taxpayers under their jurisdiction. Because the level of user fees collected does not always correlate to financial resources required, such an approach could result in a misallocation of resources within the IRS.

Finally, it is not clear that the formula set forth in the bill would result in the correct level of funding for EP/EO. There appears to be widespread agreement that the current level is too low. Based on current collections, the formula set forth in the bill would result in a funding level of approximately $465.6 million for EP/EO in 1997.[95] This amount is approximately three and one-half times the level of EP/EO proposed funding ($129.6 million). Such a funding level may be too high, or it may still be inadequate. Dedicating certain revenue sources to the funding of EP/EO would mean that EP/EO does not have to compete for scarce resources within the IRS. However, it does not necessarily result in the correct level of funding. This task requires an ongoing assessment by Congress as to the appropriate funding level, rather than a formula that may or may not approximate current—or future—needs. As the Commission concluded, Congress must provide sufficient resources when asking IRS to assume non-core functions such as those carried out by EP/EO. To preserve the ability of the IRS to carry out its core functions, however, such resources must be in addition to, and not in lieu of, resources appropriated to carry out such core functions.

[95] The funding level would be calculated as follows: $213.7 million (sec. 4940 excise tax collections for second preceding year (1995)) + $213.7 million (greater of $213.7 million or $30 million) + $38.2 million (1996 user fees) = $465.6 million. In fact, the actual amount would be somewhat different because, as discussed above, the section 7802(b) formula assumes a 2-percent excise tax rate; actual collections reflect the fact that certain foundations pay at a 1-percent rate.

V. ISSUES RELATING TO CONGRESSIONAL ACCOUNTABILITY FOR THE IRS

A. Congressional Oversight

Coordinated hearings

As discussed above, there are currently 6 Congressional committees with legislative jurisdiction over the IRS. In addition, part of the statutory duties of the Joint Committee is IRS oversight. The Commission Report points out that one of the factors contributing to lack of a long-term strategic plan for the IRS is that it receives differing views from each of the Congressional committees. Each committee has its own concerns and agenda, and the result may not be a cohesive plan for IRS activities. In addition, the need for the IRS (and the Treasury Department) to respond to each committee may result in duplicative efforts and the wasting of resources that could be put to other uses.

In order to address this issue, S. 1096 provides for at least two coordinated hearings a year with the 6 legislative committees and for reports to such committees on the IRS and the state of the Federal tax system by the Joint Committee. The Commission recommended a similar approach, but would have created a new joint committee to hold the hearings and provide the reports.

The bill may serve to provide some coordinated oversight between the various committees; it will at least ensure that the same information is available to all relevant committees at the same time. In addition, to the extent that issues are addressed by the IRS at the joint hearings, it may reduce the need for duplicative hearings or IRS responses to the various committees. The extent to which the coordinated hearings actually help to streamline and coordinate the oversight process depends in part on whether the coordinated hearings do in fact reduce the number of hearings to which the IRS must respond or simply add additional hearings and the extent to which the coordinated hearings foster discussions that result in a more coordinated oversight effort and a more cohesive direction from the Congress.

The bill's approach may be preferable to that of the Commission Report because it utilizes existing resources. The Commission approach may have added additional complexity by creating a new entity which would largely duplicate the current duties of the Joint Committee.

Some argue that it may be difficult to provide truly coordinated Congressional oversight of the IRS as long as more than one committee has jurisdiction over the IRS. On the other hand, some point out that many Federal agencies are subject to Congressional oversight by multiple committees and that this form of oversight does not necessarily impede the development of appropriate goals and achievement of such goals.

Requests for GAO investigations of the IRS

According to the Commission Report, requiring a single place for coordination of GAO reports relating to the IRS is intended to eliminate overlapping reports, ensure that the GAO has the capacity to handle the report, and ensure that investigations focus on areas of primary importance to tax administration. The Commission Report would require coordination with respect to all GAO reports. S. 1096 is similar, but would not require Joint Committee approval of requests from Congressional Committees or Subcommittees. As discussed above, the Joint Committee already reviews requests for GAO investigations that involve access to confidential taxpayer information. However, the GAO does perform investigations that do not require access to such information, and requests for such investigations are not necessarily reviewed by the Joint Committee.

Requiring Joint Committee approval of GAO investigations relating to the IRS may not necessarily reduce the number of requests. One reason is that the requirement does not apply to requests from House or Senate committees or subcommittees, even if the committee or subcommittee does not have jurisdiction over IRS matters. In addition, it may be difficult for the Joint Committee to deny a request for an investigation from a Member of Congress.

On the other hand, requiring Joint Committee approval may have the desired effect. The Joint Committee may be able to combine several similar requests into a single request (to the extent the GAO does not now do so). In addition, the Joint Committee may be able to address the issue without a study or may be able to direct the inquiry to a source better able to deal with it, thus reducing the number of investigations.

B. Tax Law Complexity

Complexity analysis

The requirement for a Tax Complexity Analysis highlights complexity as an issue in developing tax legislation. Complexity is only one of many factors that are involved in the consideration in tax legislation, and there is disagreement as to whether it is appropriate to elevate complexity over other factors. Even those who agree that complexity is a critical issue do not all agree that the proposed Tax Complexity Analysis is necessary to focus attention on complexity or that the Analysis will be effective. Assuming the proposal for a Tax Complexity Analysis is adopted, there are issues relating to the content of the analysis that should be addressed.

Those who support the proposal for a Tax Complexity Analysis argue that requiring such an analysis appropriately recognizes that complexity is an important factor to consider in developing tax legislation. Many would argue that complexity is the critical issue facing the current tax system and that, despite frequent statements supporting simplification by the Administration and Members of Congress, recent tax bills, including the Tax Relief Act of 1997, have made some areas of the tax law significantly more complex. They argue that complexity of the income tax laws is a key reason for taxpayer dissatisfaction with the tax system in general and

with the IRS and that taxpayer approval of the IRS cannot substantially increase unless the tax laws are simplified.

Certainly, complexity can lead to more involvement of taxpayers with the IRS. Taxpayers desiring clarification from the IRS may attempt to contact the IRS through telephone calls, letters, or more formal means such as requests for private letter rulings. In addition, complexity may result in more mistakes by taxpayers in preparing their tax returns, and may also lead to more disputes with the IRS. Particularly in areas where there is lack of certainty in the law, taxpayers and the IRS may come to different conclusions about tax liability given the same set of facts. The need for such interactions and involvement with the IRS may increase taxpayer dissatisfaction with the IRS and the tax system.

On the other hand, some argue that the Tax Complexity Analysis places undue emphasis on complexity as an issue. They argue that simplicity is only one objective of a tax system, and that other factors are at least as important and, in some cases, more important. Issues in addition to complexity that are generally considered in evaluating tax legislation include the effect of the proposal on the fairness of the tax system, economic efficiency, and the Federal budget. Nontax policy issues also arise, as the tax laws are frequently used to encourage or discourage certain types of behavior. Those who share this view are concerned that identifying a provision as complex would stigmatize the provision, even though the provision may be favorable to taxpayers or otherwise supported by sound policy.

Some complexity may benefit taxpayers. For example, complexity often gives taxpayers greater flexibility in structuring transactions and choosing behavior that results in the desired tax consequences. Some complexity mirrors the complicated economic system and complicated transactions that occur in the market place. Some complexity may lead to a fairer tax system.

Taxpayers are generally willing to accept complexity when it benefits them. For example, the home mortgage interest deduction adds to complexity and additional calculations that would not have to be made if the deduction were not available. However, taxpayers who are eligible for deduction are probably more than willing to deal with the additional complexity and record keeping because it reduces their tax liability.

While recognizing that reducing complexity is a key goal, some argue that the Tax Complexity Analysis merely adds additional procedural requirements without any real benefit. They argue that the fact that a provision adding to complexity is adopted does not mean that the Congress and the President were not aware of the complexity, but an indication that they believed other factors outweighed concerns about complexity.

Some point out that there are many formal and informal means by which the Congress learns of complexity regarding proposed legislation. Hearings are held relating to legislation at which interested groups testify and questions about complexity are generally raised in the hearing process. In addition, Members and their staffs speak frequently with interested groups regarding legislative proposals, including groups representing taxpayers, tax practitioners, and others concerned with complexity. The staffs of the House and

Senate Offices of the Legislative Counsel, the Ways and Means and Senate Finance Committees, the Joint Committee, and the Administration advise Members regarding the complexity of proposed legislation. This input often results in changes to proposals throughout the legislative process.

Some also argue that, even if the Tax Complexity Analysis added new information, it comes too late in the legislative process to provide useful input to Members. Those who do not support the complexity analysis argue that at best it will result in additional boiler plate language in committee and conference reports, and at worst will result in legislative delays due to procedural battles or distract resources from the task of trying to draft legislation in the simplest possible way.

Supporters of the Tax Complexity Analysis argue that the Analysis may provide additional information to Members and that, even if it does not, it will make Congress, the Administration, and taxpayers more aware of complexity and may result in changes in legislation.

Members of Congress and the President generally focus on the major issues and policy objectives of legislation, but often will not be familiar with all the details which may give rise to complexity. This may be especially true with respect to Members who are not on the tax writing committees and who were not or did not have staff who were directly involved in the development of proposals. Supports of the Tax Complexity Analysis argue that it serves to make Members aware of the fact that they are adopting complex provisions. Moreover, the fact that the complexity analysis has to be included may cause Members to focus more on complexity while considering legislation and may cause them to change proposals in the hope that a provision will not be discussed in the complexity analysis. Thus, even if the analysis merely formalizes the advice given to Members during the legislative process, the analysis may in fact change the debate over legislation at all stages of the legislative process.

Assuming that a tax complexity analysis is required to be included in tax legislation, it may be appropriate to consider revising the content of the analysis in order to provide a more meaningful discussion of complexity. Issues that may need to be addressed include the following.

First, the proposed analysis does not actually appear to require a determination that a provision is complex—but merely to address the 8 specified factors. Many of these factors do not have a direct relationship with complexity. For example, whether or not a provision is new or amends existing provision in the tax law is not an indication of complexity. A new provision may reduce complexity, where an amendment to an existing provision could increase it. Similarly, whether or not a provision requires a change to IRS forms does not indicate whether complexity is increased. A provision that greatly increases simplification, such as reducing the number of people who have to file tax returns, may require a change to IRS forms.

Second, the complexity analysis also does not require an identification of provisions that reduce complexity or result in significant simplification. It may be useful for Members to know of such provi-

sions. If proponents of the analysis are correct that members will not want to see a provision on a list of complex items, including a discussion of items that simplify the tax code might spur members to try to develop such provisions.

Third, the requirement that an analysis be made with respect to each provision of a bill may be unduly burdensome and unrealistic given the numerous tax provisions in some bills. The legislative process may not provide the time necessary to provide such an analysis, and waiting for the analysis may unduly interfere with the legislative process.

Feasibility study of compliance burden estimates[96]

S. 1096 requires the Joint Committee to study the feasibility of developing a numerical standard for determining compliance burdens of proposed tax legislation. Some have shown interest in such a proposal because they feel it would provide an easy shorthand method of determining complexity. It would also allow a shorthand way of comparing the complexity of completely unrelated proposals. However, any sort of complexity index is likely to be controversial and subjective. It is likely to be difficult to develop any sort of consensus among interested parties as to what factors should be taken into account, how the factors should be weighed, or how the results of any complexity analysis should be presented. Any simplistic numerical analysis is likely to be more misleading than helpful, and may mask issues.

If there is continuing concern about complexity, it may be more appropriate to provide for a more flexible Tax Complexity Analysis such as that in the bill that allows for a qualitative, as well as quantitative analysis where appropriate (e.g., the estimated number of taxpayers affected). Such an approach is likely to provide the Congress with more insight and useful information. For example, such an approach could include the reasons for the complexity, which would provide an indication of how a proposal could be modified to reduce complexity.

Role of the Internal Revenue Service

In analyzing proposed legislation, it is useful to obtain the views of IRS personnel responsible for administering the provisions affected by the legislation. IRS personnel are in a unique position to evaluate the measures that will be needed to ensure compliance (e.g., information reporting), whether it is reasonable to expect a reasonable level of compliance under the proposal, and what changes in IRS forms or procedures would be necessary. Because IRS personnel deal with enforcement and compliance issues on a day-to-day basis, they can advise Congress with respect to burdens proposed legislation may impose on taxpayers as well as the IRS.

The Commission determined that in some cases the Congress may not have adequate access to IRS personnel. Others also have voiced the concern that, while the Treasury Department may be involved in legislative proposals, IRS representatives often are not.

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[96] These issues do not arise under H.R. 2676, as passed by the House, because it does not contain the proposal relating to compliance burden estimates.

The bill addresses concerns about access to the IRS by providing that it is the sense of the Congress that IRS personnel should be available to the Congress during the consideration of legislative proposals. The bill is an indication that the Congress wants to hear more, and more directly, from the IRS during the consideration of legislation. The extent to which there is more IRS involvement in developing legislation will depend, in part, on the extent to which Congress chooses to involve the IRS. Such involvement could take various forms. For example, IRS representatives could be asked to testify regarding administrative issues involved in particular legislative proposals. In addition, IRS representatives could be involved in the drafting of proposals. In the past, the IRS has often been involved in drafting, but not in all cases.

Some point out that legislation should not be necessary to obtain more input from the IRS regarding legislative proposals, and that lines of communication can and should be reestablished in the absence of legislation.

Whether receiving more input from the IRS will reduce complexity in tax legislation is unclear; it depends in part on the extent to which the Congress and the Administration focus on complexity as an issue, and whether other competing concerns cause additional complexity to be unavoidable.

PART TWO: ELECTRONIC FILING

A. Electronic Filing of Tax and Information Returns

Present Law

Treas. Reg. section 1.6012–5 provides that the Commissioner may authorize, at the option of a person required to make a return, the use of a composite return in lieu of a paper return. An electronically filed return is a composite return consisting of electronically transmitted data and certain paper documents that cannot be electronically transmitted. Form 8453 is a paper form that must be received by the IRS before any electronically filed return is complete. Form 8453 provides signature information to the IRS.

The IRS conducted the first test of electronic filing in 1986, for a limited number of tax year 1985 returns.[97] In 1990, the IRS permitted nationwide electronic filing of returns that had refunds owing.[98] In 1991, the IRS accepted electronically filed returns that had balances due.[99] In 1993, the IRS established an electronic filing goal of 80 million tax returns by 2001. During the 1997 tax filing season, the IRS received approximately 20 million individual tax returns electronically.

S. 1096 (sec. 201 of the bill)

Description of Proposal

S. 1096 states that the policy of Congress is to promote paperless filing, with a long-range goal of limiting paper returns to 20 percent of all tax returns by the year 2007. The bill would require the Secretary of the Treasury to establish a strategic plan to eliminate barriers, provide incentives, and use competitive market forces to increase taxpayer use of electronic filing.

The Secretary would be required to create an electronic commerce advisory group comprised of representatives from the tax practitioner, preparer, and computerized tax processor communities and other representatives from the electronic filing industry. Under the bill, the Chairperson of the IRS Oversight Board, together with the Secretary and the Chairperson of the electronic commerce advisory group, would be required to report annually to the tax-writing committees on the IRS's progress in implementing its plan to meet the goal of 80 percent electronic filing by 2007.

To promote electronic filing, the bill would require the Secretary to implement procedures providing for the payment of incentives to transmitters of qualified electronically filed returns. A qualified electronically filed return excludes those for which the taxpayer is

[97] Rev. Proc. 86–4, 1986–1 C.B. 423.
[98] Rev. Proc. 90–62, 1990–2, C.B. 659.
[99] Rev. Proc. 91–69, 1991–2, C.B. 893.

charged the cost of transmission. The bill also would exclude transmitters that file paper returns after the end of 2004 from the incentive program. This bill would not be intended to override section 1205 of the Taxpayer Relief Act of 1997,[100] which prohibits the IRS from paying fees to credit card companies in connection with receiving tax payments by credit card.

Effective Date

The provision would be effective on the date of enactment.

H.R. 2676 (sec. 201 of the bill)

Description of Proposal

The H.R. 2676 provision is identical to that in S. 1096.

B. Extension of Time to File for Electronic Filers

Present Law

In general, individual federal income tax returns must be filed by April 15 of the year following the close of the calendar year to which the return pertains, regardless of whether the returns are filed on paper or electronically. Corporate income tax returns must be filed by the 15th day of the third month following the close of the taxable year to which the return pertains, regardless of whether the returns are filed on paper or electronically.

Information such as the amount of dividends, partnership distributions, and interest paid during the tax year must be supplied to taxpayers by the payors by January 31 of the year following the calendar year for which the return must be filed. The payors must file an information return with the IRS with the information by February 28 of the year following the calendar year for which the return must be filed. Under present law, the due date for information returns is the same whether such returns are filed on paper, on magnetic media, or electronically. Most information returns are filed on magnetic media (such as computer tapes) which must be physically shipped to the IRS.

Under regulations, a partnership must file its income tax return on or before the 15th day of the fourth month following the end of the partnership's taxable year (on or before April 15th, for calendar year taxpayers). The Taxpayer Relief Act of 1997 adds a requirement that partnerships with more than 100 partners must file partnership income tax returns on magnetic media.[101]

S. 1096 (sec. 202 of the bill)

Description of Proposal

S. 1096 would provide an incentive to electronic filers by extending the due date for filing such returns. In the case of individual income tax returns, the time for filing would be extended to the fifth month of the year following the taxable year to which the re-

[100] Public Law 105–34 (August 5, 1997).
[101] *Ibid* (Act sec. 1224).

turn relates. For most individuals, this would push the filing date back to May 15th. In the case of corporate income tax returns, the time for filing would be extended to the 15th day of the fourth month following the close of the taxable year. With respect to information returns, the time for filing would be extended from February 28 under present law to March 31 of the year following the calendar year to which the return relates. The bill would not change the requirement that payors must supply taxpayers with the applicable information by January 31. The bill generally would require partnership income tax returns to be filed on or before the 15th day of the third month following the close of the taxable year of the partnership, except for electronically filed partnership income tax returns, which would be required to be filed on the 15th day of the fourth month following the close of the taxable year of the partnership. The bill also would permit the return of a partnership consisting entirely of nonresident aliens to be filed on or before the 15th day of the sixth month following the close of the taxable year of the partnership.

Effective Date

The provision would apply to individual, corporate, and information returns required to be filed after December 31, 1999. The provision would apply to partnership returns for taxable years beginning after December 31, 1998.

H.R. 2676 (sec. 202 of the bill)

Description of Proposal

H.R. 2676 would provide an incentive to filers of information returns to use electronic filing by extending the due date for filing such returns from February 28 (under present law) to March 31 of the year following the calendar year to which the return relates. The bill does not change the requirement that payors must supply taxpayers with the applicable information by January 31. The House bill contemplates that the IRS would cooperate with interested private sector filers of information returns in facilitating to the maximum extent feasible the utilization of electronic filing for such forms.

Effective Date

The provision would apply to information returns required to be filed after December 31, 1999.

C. Paperless Electronic Filing

Present Law

Code section 6061 requires that tax forms be signed as required by the Secretary. The IRS will not accept an electronically filed return unless it has received a Form 8453 providing signature information on the filer.

Generally, a return is considered timely filed when it is received by the IRS on or before the due date of the return. If the requirements of Code section 7502 are met, timely mailing is treated as

timely filing. If the return if mailed by registered mail, the dated registration statement is prima facie evidence of delivery. As an electronically filed return is not mailed, section 7502 does not apply.

The IRS periodically publishes a list of the forms and schedules that may be electronically transmitted, as well as a list of forms, schedules, and other information that cannot be electronically filed.

S. 1096 (sec. 203 of the bill)

Description of Proposal

S. 1096 would require the Secretary to develop procedures that would eliminate the need to file a paper form relating to signature information. The Secretary would be required to develop procedures for the acceptance of signatures in digital or other electronic form. Until the procedures are in place, the bill would require the Secretary to accept electronic returns with typewritten signatures, but the filers would be required to retain a signed paper original of all such filings.

The bill would provide authorization for return preparers to communicate with the IRS on matters included on electronically filed returns.

The bill would require that the Secretary establish procedures to receive all forms electronically by December 31, 1998.

Effective Date

The provision would be effective on the date of enactment.

H.R. 2676 (sec. 203 of the bill)

Description of Proposal

H.R. 2676 would require the Secretary to develop procedures that would eliminate the need to file a paper form relating to signature information and to develop procedures for the acceptance of signatures in digital or other electronic form. Until the procedures are in place, the bill authorizes the Secretary to waive the requirement of a signature or to provide for alternative methods of subscribing all returns, declarations, statements, or other documents. The bill treats documents subscribed under such alternative methods as signed for all purposes, both civil and criminal, and provides a rebuttable presumption that any such return, declaration, statement or other document was actually submitted and subscribed by the person on whose behalf it was submitted. The House bill contemplates that the IRS will establish procedures for rebuttal of the presumption.

The bill would provide rules for determining when electronic returns are deemed filed, and for authorization for return preparers to communicate with the IRS on matters included on electronically filed returns.

The bill would require that the Secretary establish procedures, to the extent practicable, to receive all tax forms electronically by December 31, 1998.

Effective Date

The provision would be effective on the date of enactment.

D. Regulation of Preparers

Present Law

Present law does not provide for the regulation of return preparers.

S. 1096 (sec. 204 of the bill)

Description of Proposal

S. 1096 would provide that the Secretary may establish uniform procedures to regulate the practice of return preparers. The bill would provide that the Secretary shall not require persons that are solely engaged in return preparation to demonstrate character, reputation, qualifications, or competency. The bill also would create a "Director of Practice" within the Treasury Department.

Effective Date

The provision would be effective on the date of enactment.

H.R. 2676

Description of Proposal

H.R. 2676 does not contain a proposal relating to return preparers.

E. Paperless Payment

Present Law

Under the Taxpayer Relief Act of 1997,[102] the IRS is authorized to accept payment by any commercially acceptable means that the Secretary deems appropriate, to the extent and under the conditions provided in regulations. This includes, for example, electronic funds transfers, including those arising from credit cards, debit cards, and charge card.

S. 1096 (sec. 205 of the bill)

Description of Proposal

S. 1096 would provide rules that are essentially similar to those enacted in the Taxpayer Relief Act of 1997.

Effective Date

The provision would be effective on the date that is nine months after the date of enactment.

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[102] Section 1205 of Public Law 105–34 (August 5, 1997). This provision is effective nine months after enactment (May 5, 1998).

H.R. 2676

Description of Proposal

H.R. 2676 does not contain a proposal relating to paperless payment.

F. Return-Free Tax System

Present Law

Under present law, taxpayers are required to calculate their own tax liabilities and submit returns showing their calculations.

S. 1096 (sec. 206 of the bill)

Description of Proposal

S. 1096 would require the Secretary or his delegate to study the feasibility of and develop procedures for the implementation of a return-free tax system for taxable years beginning after 2007. The Secretary would be required annually to report to the tax-writing committees on the progress of the development of such system, including what additional resources the IRS needs to implement the system, the changes to the Internal Revenue Code necessary to facilitate the system, the procedures developed to date, and the number and classes of taxpayers who are permitted to use such a system. The Secretary would be required to make the first report on the development of the return-free filing system to the tax-writing committees by June 30, 1999. The Senate bill contemplates that the return-free filing system will be initially targeted at taxpayers who had taxable income from wages, interest, dividends, pensions, and unemployment compensation; did not itemize deductions; and did not take any tax credits other than the earned income tax credit.[103]

Effective Date

The provision would be effective on the date of enactment.

H.R. 2676 (sec. 204 of the bill)

Description of Proposal

The H.R. 2676 provision is identical to that in section 206 of S. 1096.

G. Access to Account Information

Present Law

Taxpayers who file their returns electronically cannot review their accounts electronically.

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[103] See *The President's Tax Proposals to Congress for Fairness, Growth, and Simplicity*, at 115 (May 1985) and U.S. General Accounting Office, *Report on Tax Administration Alternative Filing Systems* (October 1996).

S. 1096 (sec. 207 of the bill)

Description of Proposal

S. 1096 would require the Secretary to develop procedures under which a taxpayer filing returns electronically could review the taxpayer's account electronically not later than December 31, 2006. The bill contemplates that all necessary privacy safeguards are in place by that date.

Effective Date

The provision would be effective on the date of enactment.

H.R. 2676 (sec. 205 of the bill)

Description of Proposal

The H.R. 2676 provision is identical to that in section 207 of S. 1096, except that the provision in H.R. 2676 would be effective only if all necessary privacy safeguards are in effect as of December 31, 2006.

PART THREE: TAXPAYER PROTECTIONS AND RIGHTS

I. PROVISIONS OF S. 1096

A. Expansion of Authority to Issue Taxpayer Assistance Orders (sec. 301 of the bill)

Present Law

Taxpayers can request that the Taxpayer Advocate in the Internal Revenue Service ("IRS") issue a taxpayer assistance order ("TAO") if they are suffering or about to suffer a significant hardship as a result of the manner in which the internal revenue laws are being administered (sec. 7811). A TAO may require the IRS to release property of the taxpayer that has been levied upon, or to cease any action, take any action as permitted by law, or refrain from taking any action with respect to the taxpayer.

Description of Proposal

The bill would provide that in making the hardship determination, the Taxpayer Advocate should consider the following four factors: (1) whether the IRS employee to whom the order would be issued is following applicable published administrative guidance, including the Internal Revenue Manual ("IRM"); (2) whether there is an immediate threat of adverse action; (3) whether there has been a delay of more than 30 days in resolving the taxpayer's account problems; and (4) the prospect that the taxpayer will have to pay significant professional fees for representation.

Effective Date

The provision would be effective on the date of enactment.

B. Expansion of Authority to Award Costs and Certain Fees (sec. 302 of the bill)

Present Law

Any person who substantially prevails in any action by or against the United States in connection with the determination, collection, or refund of any tax, interest, or penalty may be awarded reasonable administrative costs incurred before the IRS and reasonable litigation costs incurred in connection with any court proceeding. In general, only an individual whose net worth does not exceed $2 million is eligible for an award, and only a corporation or partnership whose net worth does not exceed $7 million is eligible for an award.

Reasonable litigation costs include reasonable fees paid or incurred for the services of attorneys, except that the attorney's fees will not be reimbursed at a rate in excess of $110 per hour (indexed for inflation) unless the court determines that a special factor, such as the limited availability of qualified attorneys for the proceeding, justifies a higher rate. Awards of reasonable litigation costs and reasonable administrative costs cannot exceed amounts paid or incurred.

Once a taxpayer has substantially prevailed over the IRS in a tax dispute, the IRS has the burden of proof to establish that it was substantially justified in maintaining its position against the taxpayer. A rebuttable presumption exists that provides that the position of the United States is not considered to be substantially justified if the IRS did not follow in the administrative proceeding (1) its published regulations, revenue rulings, revenue procedures, information releases, notices, or announcements, or (2) a private letter ruling, determination letter, or technical advice memorandum issued to the taxpayer.

Description of Proposal

The bill would: (1) provide that the difficulty of the issues presented or the local availability of tax expertise can be used to justify an award of attorney's fees of more than the statutory limit of $110 per hour; (2) move the point in time at which both the position of the United States is determined and after which reasonable administrative costs can be awarded to also encompass the date on which the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the IRS Office of Appeals is sent; (3) permit the award of attorney's fees (in amounts determined by the court to be appropriate) to specified persons who represent the taxpayer for no more than a nominal fee; (4) raise the net worth limitation above which attorney's fees may not be awarded to $5 million (from $2 million) for individuals and $35 million (from $7 million) for corporations and partnerships; and (5) provide that "the position of the United States was not substantially justified if the United States has not prevailed on the same issue in at least 3 United States Courts of Appeal."

Effective Date

The provision would apply to proceedings beginning after the date of enactment.

C. Civil Damages for Negligence in Collection Actions (sec. 303 of the bill)

Present Law

A taxpayer may sue the United States for up to $1 million of civil damages caused by an officer or employee of the IRS who recklessly or intentionally disregards provisions of the Internal Revenue Code or Treasury regulations in connection with the collection of Federal tax with respect to the taxpayer.

Description of Proposal

The bill would provide for up to $100,000 in civil damages caused by an officer or employee of the IRS who negligently disregards provisions of the Internal Revenue Code or Treasury regulations in connection with the collection of Federal tax with respect to the taxpayer.

Effective Date

The provision would be effective with respect to actions of officers or employees of the IRS occurring after the date of enactment.

D. Disclosure of Criteria for Examination Selection (sec. 304 of the bill)

Present Law

The IRS examines Federal tax returns to determine the correct liability of taxpayers. The IRS selects returns to be audited in a number of ways, such as through a computerized classification system (the discriminant function ("DIF") system).

Description of Proposal

The bill would require that IRS add to Publication 1 ("Your Rights as a Taxpayer") "a statement which sets forth in simple and nontechnical terms the criteria and procedures for selecting taxpayers for examination." The statement must not include any information the disclosure of which is detrimental to law enforcement. The statement must specify the general procedures used by the IRS, including the extent to which taxpayers are selected for examination on the basis of information in the media or from informants. Drafts of the statements are required to be submitted to the House Committee on Ways and Means, the Senate Committee on Finance, and the Joint Committee on Taxation.

Effective Date

The addition to Publication 1 would have to be made not later than 180 days after the date of enactment.

E. Archive of Records of the IRS (sec. 305 of the bill)

Present Law

In general

The IRS is obligated to transfer agency records to the National Archives and Records Administration ("NARA") for retention or disposal. The IRS is also obligated to protect confidential taxpayer records from disclosure. These two obligations have created conflict between NARA and the IRS. Under present law, the IRS is the sole determiner of whether records contain taxpayer information. Once the IRS has made that determination, NARA is not permitted to examine those records. NARA has expressed concern that the IRS may be using the disclosure prohibition to improperly conceal agency records with historical significance.

IRS obligation to archive records

The IRS, like all other Federal agencies, must create, maintain, and preserve agency records in accordance with section 3101 of title 44 of the United States Code. NARA is the Government agency responsible for overseeing the management of the records of the Federal government.[104] Federal agencies are required to deposit significant and historical records with NARA.[105] The head of each Federal agency must also establish safeguards against the removal or loss of records.[106]

Authority of NARA

NARA is authorized, under the Federal Records Act, to establish standards for the selective retention of records of continuing value.[107] NARA has the statutory authority to inspect records management practices of Federal agencies and to make recommendations for improvement.[108] The head of each Federal agency must submit to NARA a list of records to be destroyed and a schedule for such destruction.[109] NARA examines the list to determine if any of the records on the list have sufficient administrative, legal research, or other value to warrant their continued preservation. In many cases, the description of the record on the list is sufficient for NARA to make the determination. For example, NARA does not need to inspect Presidential tax returns to determine that they have historical value and should be retained. In some cases, NARA may find it helpful to examine a particular record. NARA has general authority to inspect records solely for the purpose of making recommendations for the improvement of record management practices.[110] However, tax returns and return information can only be disclosed under the authority provided in section 6103 of the Internal Revenue Code. There is no exception to the disclosure prohibition for records management inspection by NARA.[111]

In connection with its evaluation of the record management system of the IRS, NARA noted several instances where the disclosure prohibitions of Code section 6103 complicated their review of many IRS records.

NARA is also responsible for the custody, use and withdrawal of records transferred to it.[112] Statutory provisions that restrict public access to the records in the hands of the agency from which the records were transferred also apply to NARA. Thus, if a confidential record, such as a Presidential tax return, is transferred to NARA for archival storage, NARA is not permitted to disclose it. In general, the application of such restrictions to records in the hands of NARA expire after the records have been in existence for 30 years.[113] The issue of whether the specific disclosure prohibition of section 6103 takes precedence over the general 30–year expira-

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[104] 44 U.S.C. sec. 2904.
[105] 5 U.S.C. sec. 552a(b)(6).
[106] 44 U.S.C. sec. 3105.
[107] 44 U.S.C. sec. 2905.
[108] 44 U.S.C. sec. 2904(c)(7).
[109] 44 U.S.C. sec. 3303.
[110] 44 U.S.C. sec. 2906.
[111] *American Friends Service Committee* v. *Webster.* 720 F.2d 29 (D.C. Cir. 1983).
[112] 44 U.S.C. sec. 2108.
[113] 44 U.S.C. sec. 2108.

tion of restrictions generally applicable to records in the hands of NARA has not been addressed by a court, but an informal advisory opinion from the Office of Legal Counsel of the Attorney General concluded that the 30–year expiration provision would not reach records subject to section 6103.[114]

Confidentiality requirements

The IRS must preserve the confidentiality of taxpayer information contained in Federal income tax returns. Such information may not be disclosed except as authorized under Code section 6103. Section 6103 was substantially revised in 1976 to address Congress' concern that tax information was being used by Federal agencies in pursuit of objectives unrelated to administration and enforcement of the tax laws. Congress believed that the widespread use of tax information by agencies other than the IRS could adversely affect the willingness of taxpayers to comply voluntarily with the tax laws and could undermine the country's self-assessment tax system.[115] Section 6103 does not authorize the disclosure of confidential return information to NARA. Section 6103(n) does permit disclosure of return information to any person to the extent necessary in connection with the storage or reproduction of such information. The interagency agreement between IRS and NARA contemplates NARA's photocopying of return information pursuant to requests by the IRS.

Section 6103 restricts the disclosure of returns and return information only. Return means any tax or information return, declaration of estimated tax, or claim for refund, including schedules and attachments thereto, filed with the IRS. Return information includes the taxpayer's name; nature and source or amount of income; and whether the taxpayer's return is under investigation. Section 6103(b)(2) provides that "nothing in any other provision of law shall be construed to require the disclosure of standards used or to be used for the selection of returns for examination, or data used or to be used for determining such standards, if the Secretary determines that such disclosure will seriously impair assessment, collection, or enforcement under the internal revenue laws." Section 6103 does not restrict the disclosure of other records required to be maintained by the IRS, such as records documenting agency policy, programs and activities, and agency histories. Such records are required to be made available to the public under the Freedom of Information Act ("FOIA").[116]

The Internal Revenue Code prohibits disclosure of tax returns and return information, except to the extent specifically authorized by the Internal Revenue Code (sec. 6103). Unauthorized disclosure is a felony punishable by a fine not exceeding $5,000 or imprisonment of not more than five years, or both (sec. 7213). An action for civil damages also may be brought for unauthorized disclosure (sec. 7431).

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[114] Department of Justice, Office of Legal Counsel, Memorandum to Richard K. Willard, Assistant Attorney General (Civil Division) (February 27, 1986).

[115] S. Rept. 94–938, p. 317 (1976).

[116] FOIA does not require disclosure of records or information that would frustrate law enforcement efforts. 5 U.S.C. 552(b)(7).

Description of Proposal

The bill would provide an exception to the disclosure rules to require IRS to disclose IRS records to NARA, upon written request from the Archivist,[117] for purposes of scheduling such records for destruction or retention in the National Archives. The present-law prohibitions on and penalties for disclosure of tax information would generally apply to NARA.

Effective Date

The provision would be effective for requests made by the Archivist after the date of enactment.

F. Study of Confidentiality of Tax Return Information

(sec. 306 of the bill)

Present Law

The Internal Revenue Code prohibits disclosure of tax returns and return information, except to the extent specifically authorized by the Internal Revenue Code (sec. 6103). Unauthorized disclosure is a felony punishable by a fine not exceeding $5,000 or imprisonment of not more than five years, or both (sec. 7213). An action for civil damages also may be brought for unauthorized disclosure (sec. 7431). No tax information may be furnished by the IRS to another agency unless the other agency establishes procedures satisfactory to the IRS for safeguarding the tax information it receives (sec. 6103(p)).

Description of Proposal

The bill would require the Joint Committee on Taxation to conduct a study on provisions regarding taxpayer confidentiality. The study would examine present-law protections of taxpayer privacy, the need for third parties to use tax return information, and the ability to achieve greater levels of voluntary compliance by allowing the public to know who is legally required to file tax returns but does not do so.

Effective Date

The findings of the study, along with any recommendations, would be required to be reported to the Congress no later than one year after the date of enactment.

G. Freedom of Information (sec. 307 of the bill)

Present Law

The Freedom of Information Act ("FOIA") requires most written material produced by Federal agencies to be made public.[118] The

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[117] It is not intended that such a request be required to provide a detailed description of the item to be excluded from the disclosure rules. Such a requirement could frustrate the intent of the provision, as NARA would not be able to describe the item in detail if it were protected from disclosure.

[118] 5 U.S.C. sec. 552.

purpose of FOIA is to ensure that citizens are informed about actions taken by their government, so that citizens can operate as a check against corruption by holding their government accountable. Unless agency information is exempt from FOIA, it must be made available to the public. The IRS is required to make records specifically described and requested by any person promptly available, unless the records are published in the Federal Register or are available in one of the IRS public reading rooms for inspection and copying.

The IRS publishes the following types of information: (1) descriptions of its central and field organization; (2) statements of functions; (3) rules of procedure and descriptions of forms and where forms may be obtained; (4) substantive rules of general applicability and statements of general policy; and (5) amendments to the matters described in (1) through (4). The IRS makes available for inspection and copying the following types of information: (1) final opinions, including concurring and dissenting opinions, and orders; (2) statements of policy and interpretations that have not been published in the Federal Register; and (3) administrative staff manuals and instructions to staff that affect a member of the public. The IRS makes available on request all other records that are under the control of the IRS and are not subject to an exception to FOIA.[119]

Requests must be made in writing, signed by the requester, and must reasonably describe the records requested.[120] The reasonable description requirement is generally met if the request gives the name, subject matter, location, and years in issue for the requested records. The initial determination of whether a request for records will be granted is to be made within 10 working days of the date of receipt of the request. The IRS may have a 10-day extension of this time only if the requester agrees. The requester is entitled to file an administrative appeal within 35 days after the denial of the request or the expiration of the 10-day initial determination period (with extensions). The requester is entitled to judicial review of the initial determination if the administrative appeal has not been granted within 20 working days.

In 1996, Congress amended the applicable statute to provide new procedures, applicable to all Federal agencies, for processing FOIA requests.[121] The amendments, known as the Electronic Freedom of Information Act ("EFOIA") became effective 180 days after October 2, 1996. Recognizing that many Federal agencies had a significant backlog of FOIA requests that prevented processing in a timely fashion, EFOIA provides that the initial determination of whether a request will be granted is to be made within 20 working days of the date of receipt of the request. If the agency anticipates that it cannot make the initial determination within the specified time period, it must notify the requester and give the requester an opportunity to limit the scope of the request so that the determination may be made within the time period or to arrange an alternative time frame with the agency.

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[119] 26 C.F.R. sec. 601.702(c).
[120] 26 C.F.R. sec. 601.702(c)(3).
[121] Public Law 104–231; October 2, 1996.

EFOIA requires each agency to promulgate regulations providing for expedited processing of requests for records if the requester demonstrates a compelling need.[122] A "compelling need" includes, with respect to a request made by the media, urgency to inform the public concerning actual or alleged Federal Government activity. The determination of whether expedited processing will be granted shall be made within 10 working days of the request.

EFOIA also requires agencies to make an annual report to the Attorney General about the number of FOIA requests received and processed, the status of pending requests and appeals, and the time and resources used to respond to FOIA requests.

Description of Proposal

The bill would require the Secretary of the Treasury to develop procedures for expedited processing of FOIA requests when (1) there exists widespread and exceptional media interest in the requested information, and (2) expedited processing[123] is warranted because the information sought involves possible questions about the government's integrity which affect public confidence.

Under the bill, the IRS would be required to provide an explanation to the requester if the request is not satisfied within 30 days. If the request for information is not granted within 60 days, the requester would be eligible to seek judicial review.

The Secretary of the Treasury would be required to submit drafts of the procedures for expedited processing to the House Committee on Ways and Means, the Senate Committee on Finance, and the Joint Committee on Taxation.

Effective Date

The procedures required by the bill would be developed not later than 180 days after the date of enactment.

H. Offers-in-Compromise (sec. 308 of the bill)

Present Law

Section 7122 of the Code permits the IRS to compromise a taxpayer's tax liability. In general, this occurs when a taxpayer submits an offer-in-compromise to the IRS. An offer-in-compromise is a bill to settle unpaid tax accounts for less than the full amount of the assessed balance due. An offer-in-compromise may be submitted for all types of taxes, as well as interest and penalties, arising under the Internal Revenue Code.

Taxpayers submit an offer-in-compromise on Form 656. There are two bases on which an offer can be made. The first is doubt as to the liability for the amount owed. The second is doubt as to the taxpayer's ability fully to pay the amount owed. An application can be made on either or both of these grounds. Taxpayers are required to submit background information to the IRS substantiating their application. If they are applying on the basis of doubt as to the taxpayer's ability fully to pay the amount owed, the taxpayer

[122] 5 U.S.C. 552(a)(6)(E).

[123] The bill does not appear to provide any coordination with the provisions of EFOIA, which, as described above, also provide for expedited processing of FOIA requests.

must complete a financial disclosure form enumerating assets and liabilities.

As part of an offer-in-compromise made on the basis of doubt as to ability fully to pay, taxpayers must agree to comply with all provisions of the Internal Revenue Code relating to filing returns and paying taxes for five years from the date the IRS accepts the offer. Failure to observe this requirement permits the IRS to begin immediate collection actions for the original amount of the liability.

Description of Proposal

The bill would require the IRS to develop and publish schedules of national and local allowances to ensure that taxpayers entering into an offer-in-compromise have an adequate means to provide for basic living expenses. The bill would also require the IRS to prepare a statement on the rights of taxpayers and the obligations of the IRS relating to offers in compromise.

Effective Date

The provision would be effective on the date of enactment.

I. Elimination of Interest Differential on Overlapping Periods of Interest on Income Tax Overpayments and Underpayments (sec. 309 of the bill)

Present Law

A taxpayer that underpays its taxes is required to pay interest on the underpayment at a rate equal to the Federal short term interest rate plus three percentage points. A special "hot interest" rate equal to the Federal short term interest rate plus five percentage points applies in the case of certain large corporate underpayments.

A taxpayer that overpays its taxes receives interest on the overpayment at a rate equal to the Federal short term interest rate plus two percentage points. In the case of corporate overpayments in excess of $10,000, this is reduced to the Federal short term interest rate plus one-half of a percentage point.

If a taxpayer has an underpayment of tax from one year and an overpayment of tax from a different year that are outstanding at the same time, the IRS will typically offset the overpayment against the underpayment and apply the appropriate interest to the resulting net underpayment or overpayment. However, if either the underpayment or overpayment has been satisfied, the IRS will not typically offset the two amounts, but rather will assess or credit interest on the full underpayment or overpayment at the underpayment or overpayment rate. This has the effect of assessing the underpayment at the higher underpayment rate and crediting the overpayment at the lower overpayment rate. This results in the taxpayer being assessed a net interest charge, even if the amounts of the overpayment and underpayment are the same.

The Secretary has the authority to credit the amount of any overpayment against any liability under the Code.[124] Congress has previously directed the Internal Revenue Service to consider procedures for "netting" overpayments and underpayments.[125]

Description of Proposal

The bill would provide that the rate of interest would be the same for both overpayments and underpayments of tax. The rate would be determined by the Secretary and would be the rate that would result in the same net revenue to the Government as would have resulted without regard to this provision.

Effective Date

The provision would be effective for purposes of determining interest for periods after the date of enactment.

J. Elimination of Application of Failure to Pay Penalty During Period of Installment Agreement (sec. 310 of the bill)

Present Law

Section 6159 of the Code authorizes the IRS to enter into written agreements with any taxpayer under which the taxpayer is allowed to pay taxes owed, as well as interest and penalties, in installment payments if the IRS determines that doing so will facilitate collection of the amounts owed. An installment agreement does not reduce the amount of taxes, interest, or penalties owed; it does, however, provide for a longer period during which payments may be made during which other IRS enforcement actions (such a levies or seizures) are held in abeyance. Many taxpayers can request an installment agreement by filing Form 9465. This form is relatively simple and does not require the submission of detailed financial statements. The IRS in most instances readily approves these requests if the amounts involved are not large and if the taxpayer has filed tax returns on time in the past. Some taxpayers are required to submit background information to the IRS substantiating their application. If the request for an installment agreement is approved by the IRS, a user fee of $43 is charged.[126] This user fee is in addition to the tax, interest, and penalties that are owed.

One penalty that may continue to apply during the period of an installment agreement is the penalty for failure to pay taxes (sec. 6651(a)). This penalty is a half percent per month of the amount owed, up to a maximum of 25 percent. If the failure to pay is fraudulent, the maximum penalty is 75 percent.

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[124] Code sec. 6402.

[125] Pursuant to TBOR2 (1996), the Secretary conducted a study of the manner in which the IRS has implemented the netting of interest on overpayments and underpayments and the policy and administrative implications of global netting. A *Report to the Congress on Netting of Interest on Tax Overpayments and Underpayments* was issued by the Office of Tax Policy, U.S. Treasury, in April, 1997. The legislative history to the General Agreement on Tariffs and Trade (GATT) (1994) stated that the Secretary should implement the most comprehensive crediting procedures that are consistent with sound administrative practice, and should do so as rapidly as is practicable. A similar statement was included in the Conference Report to the Omnibus Budget Reconciliation Act of 1990.

[126] This user fee is imposed pursuant to 31 U.S.C. sec. 9701. See T.D. 8589 (February 14, 1995).

Description of Proposal

The bill would provide that the penalty for failure to pay taxes would not apply for the period that an installment agreement is in effect.

Effective Date

The provision would apply to installment agreements entered into after the date of enactment.

K. Safe Harbor for Qualification for Installment Agreement (sec. 311 of the bill)

Present Law

Section 6159 of the Code authorizes the IRS to enter into written agreements with any taxpayer under which the taxpayer is allowed to pay taxes owed, as well as interest and penalties, in installment payments if the IRS determines that doing so will facilitate collection of the amounts owed. An installment agreement does not reduce the amount of taxes, interest, or penalties owed; it does, however, provide for a longer period during which payments may be made during which other IRS enforcement actions (such a levies or seizures) are held in abeyance. Many taxpayers can request an installment agreement by filing Form 9465. This form is relatively simple and does not require the submission of detailed financial statements. The IRS in most instances readily approves these requests if the amounts involved are not large and if the taxpayer has filed tax returns on time in the past. Some taxpayers are required to submit background information to the IRS substantiating their application.

Description of Proposal

The bill would require the IRS to enter into an installment agreement with a taxpayer provided that: (1) the amount of the tax liability is $10,000 or less; (2) the taxpayer has not failed to file any tax return or pay any tax during the preceding five years; and (3) the taxpayer has not previously entered into an automatic installment agreement as provided for in the bill.

Effective Date

The provision would apply to installment agreements entered into after the date of enactment.

L. Payment of Taxes (sec. 312 of the bill)

Present Law

The Code provides that it is lawful for the Secretary to accept checks or money orders as payment for taxes, to the extent and under the conditions provided in regulations prescribed by the Sec-

retary (sec. 6311). Those regulations[127] state that checks or money orders should be made payable to the Internal Revenue Service.

Description of Proposal

The bill would require the Secretary or his delegate to establish such rules, regulations, and procedures as are necessary to allow payment of taxes by check or money order to be made payable to the United States Treasury.

Effective Date

The provision would be effective on the date of enactment.

M. Low-Income Taxpayer Clinics (sec. 313 of the bill)

Present Law

There are no provisions in present law providing for assistance to clinics that assist low-income taxpayers.

Description of Proposal

The bill would require the Secretary to make matching grants for the development, expansion, or continuation of certain low-income taxpayer clinics. Eligible clinics are those that charge no more than a nominal fee to either represent low-income taxpayers in controversies with the IRS or provide tax information to individuals for whom English is a second language. The term "clinic" would include (1) a clinical program at an accredited law school in which students represent low-income taxpayers, and (2) an organization exempt from tax under Code section 501(c) which either represents low-income taxpayers or provides referral to qualified representatives.

A clinic would be treated as representing low-income taxpayers if at least 90 percent of the taxpayers represented by the clinic have incomes which do not exceed 250 percent of the poverty level and amounts in controversy of $25,000 or less.

The aggregate amount of grants to be awarded each year are limited to $3,000,000. No one taxpayer clinic would receive more than $100,000 per year. The clinic must provide matching funds on a dollar-for-dollar basis. Matching funds may include faculty and clinic administration salaries and clinic equipment costs, but not general institutional overhead.

The following criteria are to be considered in making awards: (1) number of taxpayers served by the clinic, including the number of taxpayers in the geographical area for whom English is a second language; (2) the existence of other taxpayer clinics serving the same population; (3) the quality of the program; and (4) alternative funding sources available to the clinic.

Effective Date

The provision would be effective on the date of enactment.

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[127] Treas. Reg. Sec. 301.6311–1(a)(1).

N. Jurisdiction of the Tax Court (sec. 314 of the bill)

Present Law

Taxpayers may choose to contest many tax disputes in the Tax Court. Special small case procedures apply to disputes involving $10,000 or less, if the taxpayer chooses to utilize these procedures (and the Tax Court concurs) (sec. 7463).

Description of Proposal

The bill would increase the cap for small case treatment from $10,000 to $25,000.[128]

Effective Date

The provision would apply to proceedings commenced after the date of enactment.

O. Cataloging Complaints (sec. 315 of the bill)

Present Law

The IRS is required to make an annual report to the Congress, beginning in 1997, on all categories of instances involving allegations of misconduct by IRS employees, arising either from internally identified cases or from taxpayer or third-party initiated complaints.[129] The report must identify the nature of the misconduct or complaint, the number of instances received by category, and the disposition of the complaint.

Description of Proposal

The bill would require that, in collecting data for this report, records of taxpayer complaints of misconduct by IRS employees shall be maintained on an individual employee basis.

Effective Date

The provision would be effective on the date of enactment.

P. Procedures Involving Taxpayer Interviews

(sec. 316 of the bill)

Present Law

Prior to or at initial in-person audit interviews, the IRS must explain to taxpayers the audit process and taxpayers' rights under that process (sec. 7521). In addition, prior to or at initial in-person collection interviews, the IRS must explain the collection process and taxpayers' rights under that process. If a taxpayer clearly states that during an interview with the IRS that the taxpayer wishes to consult with the taxpayer's representative, the interview

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[128] This section of the bill also contains two proposals the substance of which became present law after the date of introduction of S. 1096. See sections 505 and 1452 of the Taxpayer Relief Act of 1997 (Public Law 105–34; August 5, 1997).

[129] Section 1211 of the Taxpayer Bill of Rights 2 (Public Law 104–168; July 30, 1996).

must be suspended to afford the taxpayer a reasonable opportunity to consult with the representative.

Description of Proposal

The bill would require that, prior to initial in-person audit interviews, the IRS must do four additional things. First, the IRS must ask whether the taxpayer is represented by a representative. If the taxpayer is so represented, the interview may not proceed without the presence of the representative unless the taxpayer consents. Second, the IRS must also explain that the taxpayer has the right to have the interview take place in a reasonable place and that it does not have to take place in the taxpayer's home. Third, the IRS must explain to the taxpayer the reasons for the selection of the taxpayer's return for examination. Fourth, the IRS must provide to the taxpayer a written explanation of the applicable burdens of proof on taxpayers and on the IRS.

Effective Date

The provision would apply to interviews and examinations taking place after the date of enactment.

Q. Explanation of Joint and Several Liability (sec. 317 of the bill)

Present Law

In general, spouses who file a joint tax return are each fully responsible for the accuracy of the tax return and for the full liability. This is true even though only one spouse may have earned the wages or income which is shown on the return. This is "joint and several" liability. Spouses who wish to avoid joint and several liability may file as a married person filing separately. Special rules apply in the case of innocent spouses pursuant to section 6013(e).

Description of Proposal

The bill would require that, no later than 180 days after the date of enactment, the IRS must establish procedures clearly to alert married taxpayers of their joint and several liability on all appropriate tax publications and instructions. It is anticipated that the IRS will make an appropriate cross-reference to these statements near the signature line on appropriate tax forms. Drafts of the statements would be required to be submitted to the House Committee on Ways and Means, the Senate Committee on Finance, and the Joint Committee on Taxation.

Effective Date

The bill would require that the procedures be established as soon as practicable, but no later than 180 days after the date of enactment.

R. Procedures Relating to Extensions of Statute of Limitations by Agreement (sec. 318 of the bill)

Present Law

The statute of limitations within which the IRS may assess additional taxes is generally three years from the date a return is filed (sec. 6501).[130] Prior to the expiration of the statute of limitations, both the taxpayer and the IRS may agree in writing to extend the statute, using Form 872 or 872–A. An extension may be for either a specified period or an indefinite period. The statute of limitations within which a tax may be collected after assessment is 10 years after assessment (sec. 6502). Prior to the expiration of the statute of limitations, both the taxpayer and the IRS may agree in writing to extend the statute, using Form 900.

Description of Proposal

The bill would require that, on each occasion on which the taxpayer is requested by the IRS to extend the statute of limitations, the IRS must notify the taxpayer of the taxpayer's right to refuse to extend the statute of limitations or to limit the extension to particular issues.

Effective Date

The provision would apply to requests to extend the statute of limitations made after the date of enactment.

S. Studies

1. Study of penalty administration (sec. 319 of the bill)

Present Law

The last major revision of the overall penalty structure in the Internal Revenue Code was the Improved Penalty Administration and Compliance Tax Act, part of the Omnibus Budget Reconciliation Act of 1989.[131]

Description of Proposal

The bill would require the Taxpayer Advocate to prepare a study and to provide an independent report to the Congress reviewing the administration and implementation of the "penalty reform recommendations" made in the Omnibus Budget Reconciliation Act of 1989, including legislative and administrative recommendations to simplify penalty administration and reduce taxpayer burden.

Effective Date

The report must be provided not later than nine months after the date of enactment.

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[130] For this purpose, a return filed before the due date is considered to be filed on the due date.

[131] Subtitle G of Title 7 of the Omnibus Budget Reconciliation act of 1989 (Public Law 101–239).

2. Study of treatment of all taxpayers as separate filing units (sec. 320 of the bill)

Present Law

The Code enumerates four filing statuses for individuals: (1) married individuals filing joint returns and surviving spouses; (2) heads of households; (3) unmarried individuals; and (4) married individuals filing separate returns (sec. 1).

Description of Proposal

The bill would require the Secretary or his delegate and, in addition, the General Accounting Office ("GAO"), to conduct separate studies on the feasibility of treating each individual separately for all purposes of the Code. The studies would be required to include recommendations for eliminating the marriage penalty, addressing community property issues, and reducing the burden for divorced and separated taxpayers.

Effective Date

The studies would be required to be provided to the Congress no later than 180 days after the date of enactment.

3. Study of burden of proof (sec. 321 of the bill)

Present Law

Under present law, a rebuttable presumption exists that the Commissioner's determination of tax liability is correct."[132] This presumption in favor of the Commissioner is a procedural device that requires the plaintiff to go forward with prima facie evidence to support a finding contrary to the Commissioner's determination. Once this procedural burden is satisfied, the taxpayer must still carry the ultimate burden of proof or persuasion on the merits. Thus, the plaintiff not only has the burden of proof of establishing that the Commissioner's determination was incorrect, but also of establishing the merit of its claims by a preponderance of the evidence".[133]

The general rebuttable presumption that the Commissioner's determination of tax liability is correct is a fundamental element of the structure of the Federal income tax system. Although this presumption is judicially based, rather than legislatively based, there is considerable evidence that the presumption has been repeatedly considered and approved by the Congress. This is the case because the Internal Revenue Code contains a number of civil provisions that explicitly place the burden of proof on the Commissioner in specifically designated circumstances. The Congress would have enacted these provisions only if it recognized and approved of the general rule of presumptive correctness of the Commissioner's determination. A list of these civil provisions follows.

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[132] *Welch* v. *Helvering*, 290 U.S. 111, 115 (1933).

[133] *Danville Plywood Corp* v. *U.S.*, U.S. Cl. Ct., 63 AFTR 2d 89–1036, 1043 (1989); citations omitted.

(1) *Fraud.*—Any proceeding involving the issue of whether the taxpayer has been guilty of fraud with intent to evade tax (secs. 7454(a) and 7422(e)).

(2) *Required reasonable verification of information returns.*—In any court proceeding, if a taxpayer asserts a reasonable dispute with respect to any item of income reported on an information returned filed with the Secretary by a third party and the taxpayer has fully cooperated with the Secretary (including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer as reasonably requested by the Secretary), the Secretary has the burden of producing reasonable and probative information concerning such deficiency in addition to such information return (sec. 6201(d)).

(3) *Foundation managers.*—Any proceeding involving the issue of whether a foundation manager has knowingly participated in a prohibited transaction (sec. 7454(b)).

(4) *Transferee liability.*—Any proceeding in the Tax Court to show that a petitioner is liable as a transferee of property of a taxpayer (sec. 6902(a)).

(5) *Review of jeopardy levy or assessment procedures.*—Any proceeding to review the reasonableness of a jeopardy levy or jeopardy assessment (sec. 7429(g)(1)).

(6) *Property transferred in connection with performance of services.*—In the case of property subject to a restriction that by its terms will never lapse and that allows the transferee to sell only at a price determined under a formula, the price is deemed to be fair market value unless established to the contrary by the Secretary (sec. 83(d)(1)).

(7) *Illegal bribes, kickbacks, and other payments.*—As to whether a payment constitutes an illegal bribe, illegal kickback, or other illegal payment (sec. 162(c)(1) and (2)).

(8) *Golden parachute payments.*—As to whether a payment is a parachute payment on account of a violation of any generally enforced securities laws or regulations (sec. 280G(b)(2)(B)).

(9) *Unreasonable accumulation of earnings and profits.*—In any Tax Court proceeding as to whether earnings and profits have been permitted to accumulate beyond the reasonable needs of the business, provided that the Commissioner has not fulfilled specified procedural requirements (sec. 534).

(10) *Expatriation.*—As to whether it is reasonable to believe that an individual's loss of citizenship would result in a substantial reduction in the individual's income taxes or transfer taxes (secs. 877(e), 2107(e), 2501(a)(4)).

(11) *Public inspection of written determinations.*—In any proceeding seeking additional disclosure of information (sec. 6110(f)(4)(A)).

(12) *Penalties for promoting abusive tax shelters, aiding and abetting the understatement of tax liability, and filing a frivolous income return.*—As to whether the person is liable for the penalty (sec. 6703(a)).

(13) *Income tax return preparers' penalty.*—As to whether a preparer has willfully attempted to understate tax liability (sec. 7427).

(14) *Status as employees.*—As to whether individuals are employees for purposes of employment taxes (pursuant to the safe harbor provisions of section 530 of the Revenue Act of 1978).[134]

Description of Proposal

The bill would require GAO to prepare a report on the burdens of proof for taxpayers and the IRS in tax controversies. The report would be required to highlight the differences between these burdens and the burdens imposed in other disputes with the Federal Government. The report would also be required to comment on the impact of changing these burdens on tax administration and taxpayer rights.

Effective Date

The report would be required to be provided to the Congress no later than 180 days after the date of enactment.

[134] Public Law 95–600; November 6, 1978, as amended by section 1122 of the Small Business Job Protection Act of 1996 (Public Law 104–188; August 20, 1996).

II. PROVISIONS OF H.R. 2676

A. Burden of Proof (sec. 301 of the bill)

Present Law

Under present law, a rebuttable presumption exists that the Commissioner's determination of tax liability is correct.[135] "This presumption in favor of the Commissioner is a procedural device that requires the plaintiff to go forward with prima facie evidence to support a finding contrary to the Commissioner's determination. Once this procedural burden is satisfied, the taxpayer must still carry the ultimate burden of proof or persuasion on the merits. Thus, the plaintiff not only has the burden of proof of establishing that the Commissioner's determination was incorrect, but also of establishing the merit of its claims by a preponderance of the evidence".[136]

The general rebuttable presumption that the Commissioner's determination of tax liability is correct is a fundamental element of the structure of the Federal income tax system. Although this presumption is judicially based, rather than legislatively based, there is considerable evidence that the presumption has been repeatedly considered and approved by the Congress. This is the case because the Internal Revenue Code contains a number of civil provisions that explicitly place the burden of proof on the Commissioner in specifically designated circumstances. The Congress would have enacted these provisions only if it recognized and approved of the general rule of presumptive correctness of the Commissioner's determination. A list of these civil provisions follows.

(1) *Fraud.*—Any proceeding involving the issue of whether the taxpayer has been guilty of fraud with intent to evade tax (secs. 7454(a) and 7422(e)).

(2) *Required reasonable verification of information returns.*—In any court proceeding, if a taxpayer asserts a reasonable dispute with respect to any item of income reported on an information returned filed with the Secretary by a third party and the taxpayer has fully cooperated with the Secretary (including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer as reasonably requested by the Secretary), the Secretary has the burden of producing reasonable and probative information concerning such deficiency in addition to such information return (sec. 6201(d)).

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[135] *Welch* v. *Helvering,* 290 U.S. 111, 115 (1933).

[136] *Danville Plywood Corp.* v. *U.S.,* U.S. Cl. Ct., 63 AFTR 2d 89–1036, 1043 (1989); citations omitted.

(3) *Foundation managers.*—Any proceeding involving the issue of whether a foundation manager has knowingly participated in a prohibited transaction (sec. 7454(b)).

(4) *Transferee liability.*—Any proceeding in the Tax Court to show that a petitioner is liable as a transferee of property of a taxpayer (sec. 6902(a)).

(5) *Review of jeopardy levy or assessment procedures.*—Any proceeding to review the reasonableness of a jeopardy levy or jeopardy assessment (sec. 7429(g)(1)).

(6) *Property transferred in connection with performance of services.*—In the case of property subject to a restriction that by its terms will never lapse and that allows the transferee to sell only at a price determined under a formula, the price is deemed to be fair market value unless established to the contrary by the Secretary (sec. 83(d)(1)).

(7) *Illegal bribes, kickbacks, and other payments.*—As to whether a payment constitutes an illegal bribe, illegal kickback, or other illegal payment (sec. 162(c)(1) and (2)).

(8) *Golden parachute payments.*—As to whether a payment is a parachute payment on account of a violation of any generally enforced securities laws or regulations (sec. 280G(b)(2)(B)).

(9) *Unreasonable accumulation of earnings and profits.*—In any Tax Court proceeding as to whether earnings and profits have been permitted to accumulate beyond the reasonable needs of the business, provided that the Commissioner has not fulfilled specified procedural requirements (sec. 534).

(10) *Expatriation.*—As to whether it is reasonable to believe that an individual's loss of citizenship would result in a substantial reduction in the individual's income taxes or transfer taxes (secs. 877(e), 2107(e), 2501(a)(4)).

(11) *Public inspection of written determinations.*—In any proceeding seeking additional disclosure of information (sec. 6110(f)(4)(A)).

(12) *Penalties for promoting abusive tax shelters, aiding and abetting the understatement of tax liability, and filing a frivolous income return.*—As to whether the person is liable for the penalty (sec. 6703(a)).

(13) *Income tax return preparers' penalty.*—As to whether a preparer has willfully attempted to understate tax liability (sec. 7427).

(14) *Status as employees.*—As to whether individuals are employees for purposes of employment taxes (pursuant to the safe harbor provisions of section 530 of the Revenue Act of 1978).[137]

Description of Proposal

The bill would provide that the Secretary shall have the burden of proof in any court proceeding with respect to a factual issue if the taxpayer asserts a reasonable dispute with respect to any such issue relevant to ascertaining the taxpayer's income tax liability. Two conditions apply. First, the taxpayer must fully cooperate at all times with the Secretary (including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer, as rea-

[137] Public Law 95–600 (November 6, 1978), as amended by section 1122 of the Small Business Job Protection Act of 1996 (Public Law 104–188; August 20, 1996).

sonably requested by the Secretary).[138] Full cooperation also includes providing reasonable assistance to the Secretary in obtaining access to and inspection of witnesses, information, or documents not within the control of the taxpayer (including any witnesses, information, or documents located in foreign countries).[139] A necessary element of fully cooperating with the Secretary is that the taxpayer must exhaust his or her administrative remedies (including any appeal rights provided by the IRS). The taxpayer is not required to agree to extend the statute of limitations to be considered to have fully cooperated with the Secretary. Second, certain taxpayers must meet the net worth limitations that apply for awarding attorney's fees. In general, corporations, trusts, and partnerships whose net worth exceeds $7 million are not eligible for the benefits of the provision. The taxpayer has the burden of proving that it meets each of these conditions, because they are necessary prerequisites to establishing that the burden of proof is on the Secretary.

The provision explicitly states that nothing in the provision shall be construed to override any requirement under the Code or regulations to substantiate any item. Accordingly, taxpayers must meet all applicable substantiation requirements, whether generally imposed[140] or imposed with respect to specific items, such as charitable contributions[141] or meals, entertainment, travel, and certain other expenses.[142] Substantiation requirements include any requirement of the Code or regulations that the taxpayer establish an item to the satisfaction of the Secretary.[143] Taxpayers who fail to substantiate any item in accordance with the legal requirement of substantiation will not have satisfied all of the legal conditions that are prerequisite to claiming the item on the taxpayer's tax return and will accordingly be unable to avail themselves of this provision regarding the burden of proof. Thus, if a taxpayer required to substantiate an item fails to do so in the manner required (or destroys the substantiation), this burden of proof provision is inapplicable.[144]

Effective Date

The provision would apply to court proceedings arising in connection with examinations commencing after the date of enactment.

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[138] This requirement parallels the present-law provision relating to reasonable verification of information returns (sec. 6201(d)).

[139] Full cooperation also includes providing English translations, as reasonably requested by the Secretary.

[140] See e.g., Sec. 6001 and Treas. Reg. sec. 1.6001–1 requiring every person liable for any tax imposed by this Title to keep such records as the Secretary may from time to time prescribe, and secs. 6038 and 6038A requiring United States persons to furnish certain information the Secretary may prescribe with respect to foreign businesses controlled by the U.S. person.

[141] Sec. 170(a)(1) and (f)(8) and Treas. Reg. sec. 1.170A–13.

[142] Sec. 274(d) and Treas. Reg. sec. 1.274(d)–1, 1.274–5T, and 1.274–5A.

[143] For example, sec. 905(b) of the Code provides that foreign tax credits shall be allowed only if the taxpayer establishes to the satisfaction of the Secretary all information necessary for the verification and computation of the credit. Instructions for meeting that requirement are set forth in Treas. Reg. sec. 1.905–2.

[144] If, however, the taxpayer can demonstrate that he had maintained the required substantiation but that it was destroyed or lost through no fault of the taxpayer, such as by fire or flood, existing tax rules regarding reconstruction of those records would continue to apply.

B. Proceedings by Taxpayers

1. Expansion of authority to award costs and certain fees (sec. 311 of the bill)

Present Law

Any person who substantially prevails in any action by or against the United States in connection with the determination, collection, or refund of any tax, interest, or penalty may be awarded reasonable administrative costs incurred before the IRS and reasonable litigation costs incurred in connection with any court proceeding. In general, only an individual whose net worth does not exceed $2 million is eligible for an award, and only a corporation or partnership whose net worth does not exceed $7 million is eligible for an award.

Reasonable litigation costs include reasonable fees paid or incurred for the services of attorneys, except that the attorney's fees will not be reimbursed at a rate in excess of $110 per hour (indexed for inflation) unless the court determines that a special factor, such as the limited availability of qualified attorneys for the proceeding, justifies a higher rate. Awards of reasonable litigation costs and reasonable administrative costs cannot exceed amounts paid or incurred.

Once a taxpayer has substantially prevailed over the IRS in a tax dispute, the IRS has the burden of proof to establish that it was substantially justified in maintaining its position against the taxpayer. A rebuttable presumption exists that provides that the position of the United States is not considered to be substantially justified if the IRS did not follow in the administrative proceeding (1) its published regulations, revenue rulings, revenue procedures, information releases, notices, or announcements, or (2) a private letter ruling, determination letter, or technical advice memorandum issued to the taxpayer.

Description of Proposal

The bill would: (1) provide that the difficulty of the issues presented or the unavailability of local tax expertise can be used to justify an award of attorney's fees of more than the statutory limit of $110 per hour; (2) move the point in time after which reasonable administrative costs can be awarded to the date on which the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the IRS Office of Appeals is sent; (3) permit the award of attorney's fees (in amounts up to the statutory limit determined to be appropriate) to specified persons who represent for no more than a nominal fee a taxpayer who is a prevailing party; and (4) provide that in determining whether the position of the United States was substantially justified, the court shall take into account whether the United States has lost in courts of appeal for other circuits on substantially similar issues. The court may also take into account whether the United States has won in courts of appeal for other circuits on substantially similar issues.

Effective Date

The provision would apply to costs incurred and services performed more than 180 days after the date of enactment.

2. Civil damages for negligence in collection actions (sec. 312 of the bill)

Present Law

A taxpayer may sue the United States for up to $1 million of civil damages caused by an officer or employee of the IRS who recklessly or intentionally disregards provisions of the Internal Revenue Code or Treasury regulations in connection with the collection of Federal tax with respect to the taxpayer.

Description of Proposal

The bill would provide for up to $100,000 in civil damages caused by an officer or employee of the IRS who negligently disregards provisions of the Internal Revenue Code or Treasury regulations in connection with the collection of Federal tax with respect to the taxpayer. Inadvertent errors in IRS functions, such as in computer programming, do not trigger the application of this provision. No person is entitled to seek civil damages for negligent, reckless, or intentional disregard of the Code or regulations in a court of law unless he first exhausts his administrative remedies.

Effective Date

The provision would be effective with respect to actions of officers or employees of the IRS occurring after the date of enactment.

3. Increase in size of cases permitted on small case calendar (sec. 313 of the bill)

Present Law

Taxpayers may choose to contest many tax disputes in the Tax Court. Special small case procedures apply to disputes involving $10,000 or less, if the taxpayer chooses to utilize these procedures (and the Tax Court concurs).

Description of Proposal

The bill would increase the cap for small case treatment from $10,000 to $25,000.

Effective Date

The provision would apply to proceedings commenced after the date of enactment.

C. Relief for Innocent Spouses and Persons With Disabilities

1. Innocent spouse relief (sec. 321 of the bill)

Present law

Spouses who file a joint tax return are each fully responsible for the accuracy of the return and for the full tax liability. This is true even though only one spouse may have earned the wages or income which is shown on the return. This is "joint and several" liability. A spouse who wishes to avoid joint liability may file as a "married person filing separately."

Relief from liability for tax, interest and penalties is available for "innocent spouses" in certain limited circumstances. To qualify for such relief, the innocent spouse must establish: (1) that a joint return was made; (2) that an understatement of tax, which exceeds the greater of $500 or a specified percentage of the innocent spouse's adjusted gross income for the preadjustment (most recent) year, is attributable to a grossly erroneous item[145] of the other spouse; (3) that in signing the return, the innocent spouse did not know, and had no reason to know, that there was an understatement of tax; and (4) that taking into account all the facts and circumstances, it is inequitable to hold the innocent spouse liable for the deficiency in tax. The specified percentage of adjusted gross income is 10 percent if adjusted gross income is $20,000 or less. Otherwise, the specified percentage is 25 percent.

It is unclear under present law whether a court may grant partial innocent spouse relief. The Ninth Circuit Court of Appeals in *Wiksell* v. *Commissioner*[146] has allowed partial innocent spouse relief where the spouse did not know, and had no reason to know, the magnitude of the understatement of tax, even though the spouse knew that the return may have included some understatement.

The proper forum for contesting a denial by the Secretary of innocent spouse relief is determined by whether an underpayment is asserted or the taxpayer is seeking a refund of overpaid taxes. Accordingly, the Tax Court may not have jurisdiction to review all denials of innocent spouse relief.

No form is currently provided to assist taxpayers in applying for innocent spouse relief.

Description of Proposal

The bill would generally make innocent spouse status easier to obtain. The bill eliminates all of the understatement thresholds and requires only that the understatement of tax be attributable to an erroneous (and not just a grossly erroneous) item of the other spouse.

The bill would provide that innocent spouse relief may be provided on an apportioned basis. That is, the spouse may be relieved of liability as an innocent spouse to the extent the liability is at-

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[145] Grossly erroneous items include items of gross income that are omitted from reported and claims of deductions, credits, or basis in an amount for which there is no basis in fact or law (Code sec. 6013(e)(2)).

[146] 90 F.3d 1459 (9th Cir. 1997).

tributable to the portion of an understatement of tax which such spouse did not know of and had no reason to know of.

The bill would specifically provide that the Tax Court has jurisdiction to review any denial (or failure to rule) by the Secretary regarding an application for innocent spouse relief. The Tax Court may order refunds as appropriate where it determines the spouse qualifies for relief and an overpayment exists as a result of the innocent spouse qualifying for such relief. The taxpayer must file his or her petition for review with the Tax Court during the 90-day period that begins on the earlier of (1) 6 months after the date the taxpayer filed his or her claim for innocent spouse relief with the Secretary or (2) the date a notice denying innocent spouse relief was mailed by the Secretary. Except for termination and jeopardy assessments (secs. 6851, 6861), the Secretary may not levy or proceed in court to collect any tax from a taxpayer claiming innocent spouse status with regard to such tax until the expiration of the 90-day period in which such taxpayer may petition the Tax Court or, if the Tax Court considers such petition, before the decision of the Tax Court has become final. The running of the statute of limitations is suspended in such situations with respect to the spouse claiming innocent spouse status.

The bill would also require the Secretary of the Treasury to develop a separate form with instructions for taxpayers to use in applying for innocent spouse relief within 180 days from the date of enactment. An innocent spouse seeking relief under this provision must claim innocent spouse status with regard to any assessment not later than two years after the date of such assessment.

Effective Date

The provision would be effective for understatements with respect to taxable years beginning after the date of enactment.

2. Suspension of statute of limitations on filing refund claims during periods of disability (sec. 322 of the bill)

Present Law

In general, a taxpayer must file a refund claim within three years of the filing of the return or within two years of the payment of the tax, whichever period expires later (if no return is filed, the two-year limit applies) (sec. 6511(a)). A refund claim that is not filed within these time periods is rejected as untimely.

There is no explicit statutory rule providing for equitable tolling of the statute of limitations. Several courts have considered whether equitable tolling implicitly exists. The First, Third, Fourth, and Eleventh Circuits have rejected equitable tolling with respect to tax refund claims. The Ninth Circuit has permitted equitable tolling. However, the U.S. Supreme Court has reversed the Ninth Circuit in *U.S.* v. *Brockamp*,[147] holding that Congress did not intend the equitable tolling doctrine to apply to the statutory limitations of section 6511 on the filing of tax refund claims.

[147] 117 S. Ct. 849 (1997), reversing 67 F. 3d 260 and 70 F. 3d 120.

Description of Proposal

The bill would permit equitable tolling of the statute of limitations for refund claims of an individual taxpayer during any period of the individual's life in which he or she is unable to manage his or her financial affairs by reason of a medically determinable physical or mental impairment that can be expected to result in death or to last for a continuous period of not less than 12 months. Proof of the existence of the impairment must be furnished in the form and manner required by the Secretary. It is anticipated that, in applying the medically determinable test, the Secretary will evaluate whether a medical opinion that a physical or mental impairment exists has been offered by a person qualified to do so with respect to that particular type of impairment. Tolling does not apply during periods in which the taxpayer's spouse or another person is authorized to act on the taxpayer's behalf in financial matters.

Effective Date

The provision would apply to periods of disability before, on, or after the date of enactment but would not apply to any claim for refund or credit which (without regard to the provision) is barred by the statute of limitations as of January 1, 1998.

D. Provisions Relating to Interest

1. Elimination of interest differential on overlapping periods of interest on income tax overpayments and underpayments (sec. 331 of the bill)

Present Law

A taxpayer that underpays its taxes is required to pay interest on the underpayment at a rate equal to the Federal short term interest rate plus three percentage points. A special "hot interest" rate equal to the Federal short term interest rate plus five percentage points applies in the case of certain large corporate underpayments.

A taxpayer that overpays its taxes receives interest on the overpayment at a rate equal to the Federal short term interest rate plus two percentage points. In the case of corporate overpayments in excess of $10,000, this is reduced to the Federal short term interest rate plus one-half of a percentage point.

If a taxpayer has an underpayment of tax from one year and an overpayment of tax from a different year that are outstanding at the same time, the IRS will typically offset the overpayment against the underpayment and apply the appropriate interest to the resulting net underpayment or overpayment. However, if either the underpayment or overpayment has been satisfied, the IRS will not typically offset the two amounts, but rather will assess or credit interest on the full underpayment or overpayment at the underpayment or overpayment rate. This has the effect of assessing the underpayment at the higher underpayment rate and crediting the overpayment at the lower overpayment rate. This results in the taxpayer being assessed a net interest charge, even if the amounts of the overpayment and underpayment are the same.

The Secretary has the authority to credit the amount of any overpayment against any liability under the Code.[148] Congress has previously directed the Internal Revenue Service to consider procedures for "netting" overpayments and underpayments.[149]

Description of Proposal

The bill would establish a net interest rate of zero on equivalent amounts of overpayment and underpayment that exist for any period. Each overpayment and underpayment would be considered only once in determining whether equivalent amounts of overpayment and underpayment exist. The special rules that increase the interest rate paid on large corporate underpayments and decrease the interest rate received on corporate underpayments in excess of $10,000 would not prevent the application of the net zero rate. The bill would apply to income taxes and self-employment taxes.

For example, following an examination of its 1998 return, a corporate taxpayer is determined to have overpaid its 1998 taxes by $5,000. Previously, the taxpayer established by an amended return that it had underpaid its 1999 taxes by $7,000. The taxpayer has paid the 1999 underpayment, plus interest determined at the underpayment rate. The statute of limitations has not run with respect to either 1998 or 1999. In determining the amount of the refund owed the taxpayer with regard to the 1998 overpayment, the period for which the 1999 underpayment was outstanding must be taken into account. For all periods in which the underpayment and overpayment run concurrently (i.e., from the due date of the 1999 return until the underpayment was paid), the interest rate on the $5,000 overpayment and $5,000 of the underpayment must be the same so that the net interest rate of zero applies.[150] The interest rate on the remaining $2,000 of the underpayment that was originally calculated at the short term Federal rate plus three percent would not be affected.

Effective Date

The provision would apply to interest for calendar quarters beginning after the date of enactment. Until such time as procedures are implemented that allow for the automatic application of this provision by the IRS, the House bill intends that the Secretary will promptly and carefully consider any taxpayer's request to have interest charges recalculated in accordance with this provision and that the Secretary will extend the statute of limitations where necessary to allow for the consideration of such requests.

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[148] Code sec. 6402.

[149] Pursuant to TBOR2 (1996), the Secretary conducted a study of the manner in which the IRS has implemented the netting on overpayments and underpayments and the policy and administrative implications of global netting. A *Report to the Congress on Netting of Interest on Tax Overpayments and Underpayments* was issued by the Office of Tax Policy, U.S. Treasury, in April, 1997. The legislative history to the General Agreement on Tariffs and Trade (GATT) (1994) stated that the Secretary should implement the most comprehensive crediting procedures that are consistent with sound administrative practice, and should do so as rapidly as is practicable. A similar statement was included in the Conference Report to the Omnibus Budget Reconciliation Act of 1990.

[150] In this case, it is assumed that the interest rate on $5,000 of overpayment will be set equal to the underpayment rate for the period that both the underpayment and overpayment are outstanding in order to achieve the required net interest rate of zero. However, the Secretary may use other procedures or methodologies that he deems appropriate, so long as a zero net interest rate is achieved.

2. Increase in overpayment rate payable to taxpayers other than corporations (sec. 332 of the bill)

Present Law

A taxpayer that underpays its taxes is required to pay interest on the underpayment at a rate equal to the Federal short-term interest rate (AFR) plus three percentage points. A special "hot interest" rate equal to the Federal short term interest rate plus five percentage points applies in the case of certain large corporate underpayments.

A taxpayer that overpays its taxes receives interest on the overpayment at a rate equal to the Federal short-term interest rate (AFR) plus two percentage points. In the case of corporate overpayments in excess of $10,000, this is reduced to the Federal short term interest rate plus one-half of a percentage point.

Description of Proposal

The bill would provide that the overpayment interest rate is the AFR plus three percentage points, except that for corporations, the rate is to remain at AFR plus two percentage points. The special "hot interest" rate (AFR plus five points) on certain large corporate underpayments and the reduced rate (AFR plus one-half point) on corporate underpayments in excess of $10,000 would continue to apply.

Effective Date

The provision would apply to interest for calendar quarters beginning after the date of enactment.

E. Protections for Taxpayers Subject to Audit or Collection

1. Privilege of confidentiality extended to taxpayer's dealings with non-attorneys authorized to practice before the IRS (sec. 341 of the bill)

Present Law

A common law privilege of confidentiality exists for communications between an attorney and client with respect to the legal advice the attorney gives the client. Communications protected by the attorney-client privilege must be based on facts of which the attorney is informed by the taxpayer, without the presence of strangers, for the purpose of securing the advice of the attorney. The privilege may not be claimed where the purpose of the communication is the commission of a crime or tort. The taxpayer must be, or be seeking to become, a client of the attorney.

The privilege of confidentiality applies only where the attorney is advising the client on legal matters. It does not apply in situations where the attorney is acting in other capacities. Thus, a taxpayer may not claim the benefits of the attorney-client privilege simply by hiring an attorney to perform some other function. For example, if an attorney is retained to prepare a tax return, the attorney-client privilege will not automatically apply to communications and documents generated in the course of preparing the re-

turn. The privilege of confidentiality also does not apply where an attorney that is licensed to practice another profession is performing such other profession. For example, if a taxpayer retains an attorney who is also licensed as a certified public accountant (CPA), the taxpayer may not assert the attorney-client privilege with regard to communications made and documents prepared by the attorney in his role as a CPA.

The attorney-client privilege is limited to communications between taxpayers and attorneys. No equivalent privilege is provided for communications between taxpayers and other professionals authorized to practice before the Internal Revenue Service, such as accountants or enrolled agents.

Description of Proposal

The bill would provide that, in any noncriminal proceeding before the Internal Revenue Service, a taxpayer would be entitled to the same common law protections of confidentiality with respect to tax advice furnished by a qualified individual as the taxpayer would have if the tax advice were furnished by an attorney. For this purpose, a qualified individual is any individual other than an attorney who is authorized to practice before the Internal Revenue Service and who is acting in a manner consistent with State law for such individual's profession.

The bill would allow taxpayers to consult with other qualified tax advisors in the same manner they currently may consult with tax advisors that are licensed to practice law. The provision does not modify the attorney-client privilege. Accordingly, except for criminal proceedings, the privilege of confidentiality under this provision applies in the same manner and with the same limitations as the attorney-client privilege of present law. The provision does not extend the privilege of confidentiality to communications that would not be eligible for the privilege if prepared by an attorney.

The bill would apply to individuals authorized to practice before the Internal Revenue Service, regardless of the method pursuant to which they are so authorized. Some, such as accountants, are authorized to practice by fulfilling State licensing requirements. Others, such as enrolled agents and enrolled actuaries, are authorized to practice by passing a Treasury Department examination.

Effective Date

The provision would be effective on the date of enactment.

2. Expansion of authority to issue Taxpayer Assistance Orders (sec. 342 of the bill)

Present Law

Taxpayers can request that the Taxpayer Advocate in the Internal Revenue Service ("IRS") issue a taxpayer assistance order ("TAO") if they are suffering or about to suffer a significant hardship as a result of the manner in which the internal revenue laws are being administered (sec. 7811). A TAO may require the IRS to release property of the taxpayer that has been levied upon, or to

cease any action, take any action as permitted by law, or refrain from taking any action with respect to the taxpayer.

Description of Proposal

The bill would provide that in determining whether to issue a TAO, the Taxpayer Advocate shall consider, among others, the following four factors: (1) whether there is an immediate threat of adverse action; (2) whether there has been an unreasonable delay in resolving the taxpayer's account problems; (3) whether the taxpayer will have to pay significant costs (including fees for professional representation) if relief is not granted; and (4) whether the taxpayer will suffer irreparable injury, or a long-term adverse impact, if relief is not granted. In addition, in cases where an IRS employee to whom the order would be issued is not following applicable published administrative guidance, including the Internal Revenue Manual ("IRM"), the Taxpayer Advocate shall construe the factors taken into account in determining whether to issue a TAO in the manner most favorable to the taxpayer.

Effective Date

The provision would be effective on the date of enactment.

3. Limitation on financial status audit techniques (sec. 343 of the bill)

Present Law

The IRS examines Federal tax returns to determine the correct liability of taxpayers. The IRS selects returns to be audited in a number of ways, such as through a computerized classification system (the discriminant function ("DIF") system).

Description of Proposal

The bill would prohibit the IRS from using financial status or economic reality examination techniques to determine the existence of unreported income of any taxpayer unless the IRS has a reasonable indication that there is a likelihood of unreported income.

Effective Date

The provision would be effective on the date of enactment.

4. Limitation on authority to require production of computer source code (sec. 344 of the bill)

Present Law

The Secretary of the Treasury is authorized to examine any books, papers, records, or other data that may be relevant or material to an inquiry into the correctness of any Federal tax return. The Secretary may issue and serve summonses necessary to obtain such data, including summonses on certain third-party record keepers. There are no specific statutory restrictions on the ability of the Secretary to demand the production of computer records, programs, code or similar materials.

Description of Proposal

Under the bill, the Secretary would be generally prohibited from issuing (or beginning an action to enforce) a summons in a civil action for any portion of any third-party tax-related computer source code unless (1) the Secretary is unable to otherwise reasonably ascertain the correctness of an item on a return from the taxpayer's other books, papers, records, other data, or the computer software program and associated data itself and (2) the Secretary first identifies with reasonable specificity the portion of the computer source code to be used to verify the correctness of the item.

The Secretary would be considered to have satisfied these requirements with regard to the identified portion of the source code if the Secretary makes a formal request for such materials to both the taxpayer and the owner or developer of the software that is not satisfied within 90 days. Such formal request must clearly state that one of the consequences of failure to respond to the request will be the waiver of any prohibition on the summons of tax-related computer source code that might otherwise apply.

The Secretary's determination that the identified portion of the third-party tax-related computer source code may be summoned may be contested in any proceeding to enforce the summons, by any person to whom the summons is addressed. For this purpose, the special procedures for third-party summonses[151] will apply. In any such proceeding, the court may issue any order that is necessary to prevent the disclosure of trade secrets or other confidential information.

For these purposes, tax-related computer source code includes the human readable instructions for any computer software program that is used for accounting, tax return preparation, tax compliance or tax planning, along with the design and development materials related to such software program, including any relevant program notes and memoranda.

The prohibition on issuing summons for tax-related computer source code does not apply in connection with any inquiry into any offense connected with the administration or enforcement of the internal revenue laws. A computer software program will not be treated as tax advice for the purpose of the professional-client privilege contained in section 341 of this bill.

The prohibition applies only in the case of tax-related computer software that is intended for commercial distribution. Source code related to computer software that was developed by, or primarily for the benefit of, the taxpayer or a related person (within the meaning of section 267 or 707(b)) for the internal use of the taxpayer or such related person may continue to be summoned by the Secretary to the extent allowed under present law.

Effective Date

The provision would be effective for summonses issued more than 90 days after the date of enactment. The House bill intends that the Secretary will not use the 90 day period between the date of

[151] Sec. 7609.

enactment and the effective date in a manner that would circumvent the intent of the provision.

5. Procedures relating to extensions of statute of limitations by agreement (sec. 345 of the bill)

Present Law

The statute of limitations within which the IRS may assess additional taxes is generally three years from the date a return is filed (sec. 6501).[152] Prior to the expiration of the statute of limitations, both the taxpayer and the IRS may agree in writing to extend the statute, using Form 872 or 872–A. An extension may be for either a specified period or an indefinite period. The statute of limitations within which a tax may be collected after assessment is 10 years after assessment (sec. 6502). Prior to the expiration of the statute of limitations, both the taxpayer and the IRS may agree in writing to extend the statute, using Form 900.

Description of Proposal

The bill would require that, on each occasion on which the taxpayer is requested by the IRS to extend the statute of limitations, the IRS must notify the taxpayer of the taxpayer's right to refuse to extend the statute of limitations or to limit the extension to particular issues.

Effective Date

The provision would apply to requests to extend the statute of limitations made after the date of enactment.

6. Offers-in-compromise (sec. 346 of the bill)

Present Law

Section 7122 of the Code permits the IRS to compromise a taxpayer's tax liability. In general, this occurs when a taxpayer submits an offer-in-compromise to the IRS. An offer-in-compromise is a proposal to settle unpaid tax accounts for less than the full amount of the assessed balance due. An offer-in-compromise may be submitted for all types of taxes, as well as interest and penalties, arising under the Internal Revenue Code.

Taxpayers submit an offer-in-compromise on Form 656. There are two bases on which an offer can be made. The first is doubt as to the liability for the amount owed. The second is doubt as to the taxpayer's ability fully to pay the amount owed. An application can be made on either or both of these grounds. Taxpayers are required to submit background information to the IRS substantiating their application. If they are applying on the basis of doubt as to the taxpayer's ability fully to pay the amount owed, the taxpayer must complete a financial disclosure form enumerating assets and liabilities.

As part of an offer-in-compromise made on the basis of doubt as to ability fully to pay, taxpayers must agree to comply with all pro-

[152] For this purpose, a return filed before the due date is considered to be filed on the due date.

visions of the Internal Revenue Code relating to filing returns and paying taxes for five years from the date the IRS accepts the offer. Failure to observe this requirement permits the IRS to begin immediate collection actions for the original amount of the liability.

Description of Proposal

The bill would require the IRS to develop and publish schedules of national and local allowances designed to provide taxpayers entering into an offer-in-compromise with adequate means to provide for basic living expenses. The bill also would provide that, in the case of a compromise agreement that is terminated due to the actions of one spouse or former spouse, the spouse or former spouse remaining in compliance with the agreement may obtain reinstatement of such agreement on application. All payments required under the offer-in-compromise must be current for either spouse or former spouse to be in compliance with the agreement. Further, the bill would require the IRS to prepare a publication or statement providing guidance to taxpayers on the rights and obligations of taxpayers and the IRS relating to offers in compromise. This statement is intended to include materials explaining to married taxpayers their responsibilities should their marital status change and instructions for applying to have an offer-in-compromise reinstated under the circumstances discussed above. The House bill intends that this publication or statement will be provided to taxpayers considering an offer in compromise at appropriate times.

Effective Date

The provision would be effective on the date of enactment. The House bill intends that the materials required by this provision will be published as soon as practicable, but no later than 180 days after the date of enactment. Further, the House bill intends that offers-in-compromise based on this provision will be available as of the date of enactment.

7. Notice of deficiency to specify deadlines for filing Tax Court petition (sec. 347 of the bill)

Present Law

Taxpayers must file a petition with the Tax Court within 90 days after the deficiency notice is mailed (150 days if the person is outside the United States) (sec. 6213). If the petition is not filed within that time period, the Tax Court does not have jurisdiction to consider the petition.

Description of Proposal

The bill would require that the IRS include on each deficiency notice the date determined by the IRS as the last day on which the taxpayer may file a petition with the Tax Court. The House bill intends that the last day on which a taxpayer who is outside the United States may file a petition with the Tax Court will be shown as an alternative. The bill provides that a petition filed with the Tax Court by this date shall be treated as timely filed.

Effective Date

The provision would apply to notices mailed after December 31, 1998.

8. Refund or credit of overpayments before final determination (sec. 348 of the bill)

Present Law

A taxpayer may petition the Tax Court for a redetermination of a deficiency within 90 days (150 days if the notice is addressed to a person outside the United States) from the date the notice of deficiency is mailed by the IRS. Generally, the Secretary may not make any assessment or commence any levy or other proceeding to collect the deficiency during such period or, if the taxpayer petitions the Tax Court, until the decision of the Tax Court has become final. The making of any such assessment, or the commencing of any proceeding or levy, during the prohibited period may be enjoined by a proceeding in the proper court (including the Tax Court). However, no authority is provided for ordering the refund of any amount collected within the prohibited period.

If a taxpayer contests a deficiency in the Tax Court, no credit or refund of income tax for the contested taxable year generally may be made, except in accordance with a decision of the Tax Court that has become final. Where the Tax Court determines that an overpayment has been made and a refund is due the taxpayer, and a party appeals a portion of the decision of the Tax Court, no provision exists for the refund of any portion of any overpayment that is not contested in the appeal.

Description of Proposal

The bill would provide that where a timely petition in respect of a deficiency is filed in the Tax Court, the proper court (including the Tax Court) may order a refund of any amount that was collected within the period during which the Secretary is prohibited from collecting the deficiency by levy or other proceeding.

The bill also would allow the refund of that portion of any overpayment determined by the Tax Court to the extent the overpayment is not contested on appeal.

Effective Date

The provision would apply on the date of enactment.

9. Threat of audit prohibited to coerce tip reporting alternative commitment agreements (sec. 349 of the bill)

Present Law

Restaurants may enter into Tip Reporting Alternative Commitment (TRAC) agreements. A restaurant entering into a TRAC agreement is obligated to educate its employees on their tip reporting obligations, to institute formal tip reporting procedures, to fulfill all filing and record keeping requirements, and to pay and deposit taxes. In return, the IRS agrees to base the restaurant's li-

ability for employment taxes solely on reported tips and any unreported tips discovered during an IRS audit of an employee.

Description of Proposal

The bill would require the IRS to instruct its employees that they may not threaten to audit any taxpayer in an attempt to coerce the taxpayer to enter into a TRAC agreement.

Effective Date

The provision would be effective on the date of enactment.

F. Disclosures to Taxpayers

1. Explanation of joint and several liability (sec. 351 of the bill)

Present Law

In general, spouses who file a joint tax return are each fully responsible for the accuracy of the tax return and for the full liability. This is true even though only one spouse may have earned the wages or income which is shown on the return. This is "joint and several" liability. Spouses who wish to avoid joint and several liability may file as a married person filing separately. Special rules apply in the case of innocent spouses pursuant to section 6013(e).

Description of Proposal

The bill would require that, no later than 180 days after the date of enactment, the IRS must establish procedures clearly to alert married taxpayers of their joint and several liability on all appropriate tax publications and instructions. The House bill intends that the IRS will make an appropriate cross-reference to these statements near the signature line on appropriate tax forms.

Effective Date

The bill requires that the procedures be established as soon as practicable, but no later than 180 days after the date of enactment.

2. Explanation of taxpayers' rights in interviews with the IRS (sec. 352 of the bill)

Present Law

Prior to or at initial in-person audit interviews, the IRS must explain to taxpayers the audit process and taxpayers' rights under that process (sec. 7521). In addition, prior to or at initial in-person collection interviews, the IRS must explain the collection process and taxpayers' rights under that process. If a taxpayer clearly states during an interview with the IRS that the taxpayer wishes to consult with the taxpayer's representative, the interview must be suspended to afford the taxpayer a reasonable opportunity to consult with the representative.

Description of Proposal

The bill would require that the IRS rewrite Publication 1 ("Your Rights as a Taxpayer") to more clearly inform taxpayers of their rights (1) to be represented by a representative and (2) if the taxpayer is so represented, that the interview may not proceed without the presence of the representative unless the taxpayer consents.

Effective Date

The addition to Publication 1 must be made not later than 180 days after the date of enactment.

3. Disclosure of criteria for examination selection (sec. 353 of the bill)

Present Law

The IRS examines Federal tax returns to determine the correct liability of taxpayers. The IRS selects returns to be audited in a number of ways, such as through a computerized classification system (the discriminant function ("DIF") system).

Description of Proposal

The bill would require that the IRS add to Publication 1 ("Your Rights as a Taxpayer") a statement which sets forth in simple and nontechnical terms the criteria and procedures for selecting taxpayers for examination. The statement must not include any information the disclosure of which would be detrimental to law enforcement. The statement must specify the general procedures used by the IRS, including whether taxpayers are selected for examination on the basis of information in the media or from informants. Drafts of the statement or proposed revisions to the statement are required to be submitted to the House Committee on Ways and Means, the Senate Committee on Finance, and the Joint Committee on Taxation.

Effective Date

The addition to Publication 1 must be made not later than 180 days after the date of enactment.

4. Explanations of appeals and collection process (sec. 354 of the bill)

Present Law

There is no statutory requirement that specific notices be given to taxpayers along with the first letter of proposed deficiency that allows the taxpayer an opportunity for administrative review in the IRS Office of Appeals.

Description of Proposal

The bill would require that, no later than 180 days after the date of enactment, an explanation of the appeals process and the collection process be provided with the first letter of proposed deficiency

that allows the taxpayer an opportunity for administrative review in the IRS Office of Appeals.

Effective Date

The bill would require that the explanation be included as soon as practicable, but no later than 180 days after the date of enactment.

G. Low-Income Taxpayer Clinics (sec. 361 of the bill)

Present Law

There are no provisions in present law providing for assistance to clinics that assist low-income taxpayers.

Description of Proposal

Under the bill, the Secretary would be required to make matching grants for the development, expansion, or continuation of certain low-income taxpayer clinics. Eligible clinics are those that charge no more than a nominal fee to either represent low-income taxpayers in controversies with the IRS or provide tax information to individuals for whom English is a second language. The term "clinic" includes (1) a clinical program at an accredited law school in which students represent low-income taxpayers, and (2) an organization exempt from tax under Code section 501(c) which either represents low-income taxpayers or provides referral to qualified representatives.

A clinic is treated as representing low-income taxpayers if at least 90 percent of the taxpayers represented by the clinic have incomes which do not exceed 250 percent of the poverty level and amounts in controversy of $25,000 or less.

The aggregate amount of grants to be awarded each year is limited to $3,000,000. No taxpayer clinic could receive more than $100,000 per year. The clinic must provide matching funds on a dollar-for-dollar basis. Matching funds may include the allocable portion of both the salary (including fringe benefits) of individuals performing services for the clinic and clinic equipment costs, but not general institutional overhead.

The following criteria are to be considered in making awards: (1) number of taxpayers served by the clinic, including the number of taxpayers in the geographical area for whom English is a second language; (2) the existence of other taxpayer clinics serving the same population; (3) the quality of the program; and (4) alternative funding sources available to the clinic.

Effective Date

The provision would be effective on the date of enactment.

H. Other Taxpayer Rights Provisions

1. Actions for refund with respect to certain estates which have elected the installment method of payment (sec. 371 of the bill)

Present Law

In general, the U.S. Court of Federal Claims and the U.S. district courts have jurisdiction over suits for the refund of taxes, as long as full payment of the assessed tax liability has been made. *Flora* v. *United States,* 357 U.S. 63 (1958), aff'd on reh'g, 362 U.S. 145 (1960). Under Code section 6166, if certain conditions are met, the executor of a decedent's estate may elect to pay the estate tax attributable to certain closely-held businesses over a 14-year period. Courts have held that U.S. district courts and the U.S. Court of Federal Claims do not have jurisdiction over claims for refunds by taxpayers deferring estate tax payments pursuant to section 6166 unless the entire estate tax liability has been paid (i.e., timely payment of the installments due prior to the bringing of an action is not sufficient to invoke jurisdiction). See, e.g., *Rocovich* v. *United States,* 933 F.2d 991 (Fed. Cir. 1991), *Abruzzo* v. *United States,* 24 Ct. Cl. 668 (1991).

Description of Proposal

The bill would grant the U.S. Court of Federal Claims and the U.S. district courts jurisdiction to determine the correct amount of estate tax liability (or for any refund) in actions brought by taxpayers deferring estate tax payments under section 6166, as long certain conditions are met. In order to qualify for the provision, the estate must have made an election pursuant to section 6166, fully paid each installment of principal and/or interest due before the date the suit is filed (as long as one or more installments are not yet due), and no portion of the payments due may have been accelerated. The bill further provides that once a final judgment has been entered by a district court or the U.S. Court of Federal Claims, the IRS would not be permitted to collect any amount disallowed by the court, and any amounts paid by the taxpayer in excess of the amount the court finds to be currently due and payable would be refunded to the taxpayer. In addition, the bill would provide that the 2-year statute of limitations for filing a refund action would be suspended during the pendency of any action brought by a taxpayer pursuant to section 7479 for a declaratory judgment as to an estate's eligibility for section 6166.

Effective Date

The provision would be effective for claims for refunds filed after the date of enactment.

2. Cataloging complaints (sec. 372 of the bill)

Present Law

The IRS is required to make an annual report to the Congress, beginning in 1997, on all categories of instances involving allega-

tions of misconduct by IRS employees, arising either from internally identified cases or from taxpayer or third-party initiated complaints.[153] The report must identify the nature of the misconduct or complaint, the number of instances received by category, and the disposition of the complaints.

Description of Proposal

The bill would require that, in collecting data for this report, records of taxpayer complaints of misconduct by IRS employees shall be maintained on an individual employee basis. These individual records are not to be listed in the report, but they will be useful in preparing the report. The House bill intends that these records be used in evaluating individual employees.

Effective Date

The requirement would be effective on the date of enactment.

3. Archive of records of the IRS (sec. 373 of the bill)

Present Law

The IRS is obligated to transfer agency records to the National Archives and Records Administration ("NARA") for retention or disposal. The IRS is also obligated to protect confidential taxpayer records from disclosure. These two obligations have created conflict between NARA and the IRS. Under present law, the IRS determines whether records contain taxpayer information. Once the IRS has made that determination, NARA is not permitted to examine those records. NARA has expressed concern that the IRS may be using the disclosure prohibition to improperly conceal agency records with historical significance.

IRS obligation to archive records

The IRS, like all other Federal agencies, must create, maintain, and preserve agency records in accordance with section 3101 of title 44 of the United States Code. NARA is the Government agency responsible for overseeing the management of the records of the Federal government.[154] Federal agencies are required to deposit significant and historical records with NARA.[155] The head of each Federal agency must also establish safeguards against the removal or loss of records.[156]

Authority of NARA

NARA is authorized, under the Federal Records Act, to establish standards for the selective retention of records of continuing value.[157] NARA has the statutory authority to inspect records management practices of Federal agencies and to make recommendations for improvement.[158] The head of each Federal agency must submit to NARA a list of records to be destroyed and a schedule

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[153] Section 1211 of the Taxpayer Bill of Rights 2 (Public Law 104–168; July 30, 1996).
[154] 44 U.S.C. sec. 2904.
[155] 5 U.S.C. sec. 552a(b)(6).
[156] 44 U.S.C. sec. 3105.
[157] 44 U.S.C. sec. 2905.
[158] 44 U.S.C. sec. 2904(c)(7).

for such destruction.[159] NARA examines the list to determine if any of the records on the list have sufficient administrative, legal research, or other value to warrant their continued preservation. In many cases, the description of the record on the list is sufficient for NARA to make the determination. For example, NARA does not need to inspect Presidential tax returns to determine that they have historical value and should be retained. In some cases, NARA may find it helpful to examine a particular record. NARA has general authority to inspect records solely for the purpose of making recommendations for the improvement of records management practices.[160] However, tax returns and return information can only be disclosed under the authority provided in section 6103 of the Internal Revenue Code. There is no exception to the disclosure prohibition for records management inspection by NARA.[161]

In connection with its evaluation of the records management system of the IRS, NARA noted several instances where the disclosure prohibitions of Code section 6103 complicated their review of many IRS records.

NARA is also responsible for the custody, use and withdrawal of records transferred to it.[162] Statutory provisions that restrict public access to the records in the hands of the agency from which the records were transferred also apply to NARA. Thus, if a confidential record, such as a Presidential tax return, is transferred to NARA for archival storage, NARA is not permitted to disclose it. In general, the application of such restrictions to records in the hands of NARA expire after the records have been in existence for 30 years.[163] The issue of whether the specific disclosure prohibition of section 6103 takes precedence over the general 30–year expiration of restrictions generally applicable to records in the hands of NARA has not been addressed by a court, but an informal advisory opinion from the Office of Legal Counsel of the Attorney General concluded that the 30-year expiration provision would not reach records subject to section 6103.[164]

Confidentiality requirements

The IRS must preserve the confidentiality of taxpayer information contained in Federal income tax returns. Such information may not be disclosed except as authorized under Code section 6103. Section 6103 was substantially revised in 1976 to address Congress' concern that tax information was being used by Federal agencies in pursuit of objectives unrelated to administration and enforcement of the tax laws. Congress believed that the widespread use of tax information by agencies other than the IRS could adversely affect the willingness of taxpayers to comply voluntarily with the tax laws and could undermine the country's self-assessment tax system.[165] Section 6103 does not authorize the disclosure of confidential return information to NARA.

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[159] 44 U.S.C. sec. 3303.
[160] 44 U.S.C. sec. 2906.
[161] *American Friends Service Committee* v. *Webster*, 720 F.2d 29 (D.C. Cir. 1983).
[162] 44 U.S.C. sec. 2108.
[163] 44 U.S.C. sec. 2108.
[164] Department of Justice, Office of Legal Counsel, Memorandum to Richard K. Willard, Assistant Attorney General (Civil Division) (February 27, 1986).
[165] S. Rept. 94–938, p. 317 (1976).

Section 6103 restricts the disclosure of returns and return information only. Return means any tax or information return, declaration of estimated tax, or claim for refund, including schedules and attachments thereto, filed with the IRS. Return information includes the taxpayer's name; nature and source or amount of income; and whether the taxpayer's return is under investigation. Section 6103(b)(2) provides that "nothing in any other provision of law shall be construed to require the disclosure of standards used or to be used for the selection of returns for examination, or data used or to be used for determining such standards, if the Secretary determines that such disclosure will seriously impair assessment, collection, or enforcement under the internal revenue laws." Section 6103 does not restrict the disclosure of other records required to be maintained by the IRS, such as records documenting agency policy, programs and activities, and agency histories. Such records are required to be made available to the public under the Freedom of Information Act ("FOIA").[166]

The Internal Revenue Code prohibits disclosure of tax returns and return information, except to the extent specifically authorized by the Internal Revenue Code (sec. 6103). Unauthorized disclosure is a felony punishable by a fine not exceeding $5,000 or imprisonment of not more than five years, or both (sec. 7213). An action for civil damages also may be brought for unauthorized disclosure (sec. 7431).

Description of Proposal

The bill would provide an exception to the disclosure rules to require IRS to disclose IRS records to officers or employees of NARA, upon written request from the Archivist, for purposes of the appraisal of such records for destruction or retention. The present-law prohibitions on and penalties for disclosure of tax information would generally apply to NARA.

Effective Date

The provision would be effective for requests made by the Archivist after the date of enactment.

4. Payment of taxes (sec. 374 of the bill)

Present Law

The Code provides that it is lawful for the Secretary to accept checks or money orders as payment for taxes, to the extent and under the conditions provided in regulations prescribed by the Secretary (sec. 6311). Those regulations[167] state that checks or money orders should be made payable to the Internal Revenue Service.

Description of Proposal

The bill would require the Secretary or his delegate to establish such rules, regulations, and procedures as are necessary to allow

[166] FOIA does not require disclosure of records or information that would frustrate law enforcement efforts. 5 U.S.C. sec. 552(b)(7).
[167] Treas. Reg. Sec. 301.6311–1(a)(1).

payment of taxes by check or money order to be made payable to the United States Treasury.

Effective Date

The provision would be effective on the date of enactment.

5. Clarification of authority of secretary relating to the making of elections (sec. 375 of the bill)

Present Law

Except as otherwise provided, elections provided by the Code are to be made in such manner as the Secretary shall by regulations or forms prescribe.

Description of Proposal

The bill would clarify that, except as otherwise provided, the Secretary may prescribe the manner of making of any election by any reasonable means.

Effective Date

The provision would be effective as of the date of enactment.

6. Limitation on penalty on individual's failure to pay for months during period of installment agreement (sec. 376 of the bill)

Present Law

Taxpayers who fail to pay their taxes are subject to a penalty of one-half percent per month on the unpaid amount, up to a maximum of 25 percent (sec. 6651(a)). Taxpayers who make installment payments pursuant to an agreement with the IRS (under sec. 6159) are also subject to this penalty.

Description of Proposal

The bill would provide that the penalty for failure to pay taxes is not imposed with respect to the tax liability of an individual with respect to any month in which an installment payment agreement with the IRS (under sec. 6159) is in effect to the extent that doing so would result in the cumulative penalty percentage exceeding 9.5 percent (instead of 25 percent).

Effective Date

The provision would be effective for installment agreement payments made after the date of enactment.

I. Studies

1. Study of penalty administration (sec. 381 of the bill)

Present Law

The last major revision of the overall penalty structure in the Internal Revenue Code was the Improved Penalty Administration

and Compliance Tax Act, part of the Omnibus Budget Reconciliation Act of 1989.[168]

Description of Proposal

The bill would require the Joint Committee on Taxation to conduct a study reviewing the administration and implementation of the penalty reform provisions of the Omnibus Budget Reconciliation Act of 1989, and to make any legislative and administrative recommendations it deems appropriate to simplify penalty administration and reduce taxpayer burden.

Effective Date

The report must be provided not later than nine months after the date of enactment.

2. Study of confidentiality of tax return information (sec. 382 of the bill)

Present Law

The Internal Revenue Code prohibits disclosure of tax returns and return information, except to the extent specifically authorized by the Internal Revenue Code (sec. 6103). Unauthorized disclosure is a felony punishable by a fine not exceeding $5,000 or imprisonment of not more than five years, or both (sec. 7213). An action for civil damages also may be brought for unauthorized disclosure (sec. 7431). No tax information may be furnished by the IRS to another agency unless the other agency establishes procedures satisfactory to the IRS for safeguarding the tax information it receives (sec. 6103(p)).

Description of Proposal

The bill would require the Joint Committee on Taxation to conduct a study on provisions regarding taxpayer confidentiality. The study is to examine present-law protections of taxpayer privacy, the need for third parties to use tax return information, and the ability to achieve greater levels of voluntary compliance by allowing the public to know who is legally required to file tax returns but does not do so.

Effective Date

The findings of the study, along with any recommendations, are required to be reported to the Congress no later than one year after the date of enactment.

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[168] Subtitle G of Title 7 of the Omnibus Budget Reconciliation Act of 1989 (Public Law 101–239).

PART IV: ESTIMATED BUDGET EFFECTS OF H.R. 2676, THE "INTERNAL REVENUE SERVICE RESTRUCTURING AND REFORM ACT OF 1997," AS PASSED BY THE HOUSE OF REPRESENTATIVES

Fiscal Years 1998–2007

[Millions of dollars]

Provision	Effective	1998	1999	2000	2001	2002	1998–2002	1998–2007
Title I. Executive Branch Governance				*No Revenue Effect*				
Title II. Electronic Filing				*No Revenue Effect*				
Title III. Taxpayer Bill of Rights 3:								
1. Burden of proof	aca DOE	−80	−166	−174	−183	−192	−795	−1,912
2. Expansion of authority to award costs and certain fees	180da DOE	−8	−10	−11	−12	−13	−54	−134
3. Civil damages for negligence in collection actions	DOE	−2	−15	−25	−50	−30	−122	−247
4. Increase in size of cases permitted on small case calendar	pca DOE			*No Revenue Effect*				
5. Innocent spouse relief	tyba DOE			−5	−12	−14	−31	−131
6. Suspension of statute of limitations on filing refund claims during periods of disability	tyoea 1/1/98	−40	−50	−25	−15	−16	−146	−241
7. Elimination of interest rate differential on overlapping periods of interest on income tax overpayments and underpayments	cqba DOE	−1	−9	−28	−42	−54	−134	−449
8. Increase refund interest rate to Applicable Federal Rate ("AFR") + 3 for individual taxpayers	cqba DOE	−49	−51	−54	−56	−59	−269	−613
9. Privilege of confidentiality extended to taxpayer's dealings with non-attorneys authorized to practice before Internal Revenue Service	DOE	(1)	(1)	(1)	(1)	(1)	(2)	(3)
10. Expansion of authority to issue taxpayer assistance orders	DOE	(1)	(1)	(1)	(1)	(1)	(2)	(3)
11. Limitation on financial status audits	DOE			*Negligible Revenue Effect*				
12. Limitation on authority to require production of computer source code	si 90da DOE	(1)	(1)	(1)	(1)	(1)	(2)	(3)
13. Procedures relating to extensions of statute of limitations by agreement	DOE			*No Revenue Effect*				
14. Offers-in-compromise	DOE			*No Revenue Effect*				
15. Notice of deficiency to specify deadlines for filing Tax Court petition	12/31/98			*Negligible Revenue Effect*				

16. Refund or credit of overpayments before final determination	DOE			*Negligible Revenue Effect*				
17. Prohibition on improper threat of audit activity	DOE			*No Revenue Effect*				
18. Explanation of joint and several liability	180da DOE			*No Revenue Effect*				
19. Explanation of taxpayers' rights in interviews with the Internal Revenue Service	180da DOE	−13	(4)	(4)	(4)	(4)	−16	−20
20. Disclosure of criteria for examination selection	180da DOE			*No Revenue Effect*				
21. Explanations of appeals and collection process	180da DOE			*No Revenue Effect*				
22. Low-income taxpayer clinics	DOE			*No Revenue Effect*				
23. Estates holding closely-held businesses	DOE			*Negligible Revenue Effect*				
24. Cataloging complaints	DOE			*No Revenue Effect*				
25. Archive of records of Internal Revenue Service	DOE			*No Revenue Effect*				
26. Payment of taxes[5]	DOE			*No Revenue Effect*				
27. Clarification of authority of Secretary relating to the making of elections	DOE			*No Revenue Effect*				
28. Failure to pay penalty capped at 9.5% for individuals (installment agreements only)	DOE	−176	−198	−209	−220	−231	−1,034	−2,392
29. Study of penalty administration	9ma DOE			*No Revenue Effect*				
30. Study of confidentiality of tax return information	1ya DOE			*No Revenue Effect*				
Subtotal of Title III		**−378**	**−509**	**−541**	**−600**	**−619**	**−2,646**	**−6,229**
Title IV. Congressional Accountability for the Internal Revenue Service				***No Revenue Effect***				
Title V. Revenue Offset:								
1. Clarify deduction for accrued vacation pay	**tyea 10/8/97**	**705**	**1,111**	**584**	**120**	**126**	**2,646**	**3,377**
Net Total		**327**	**602**	**43**	**−480**	**−493**		**−2,852**

[1] Loss of less than $5 million.
[2] Loss of less than $25 million.
[3] Loss of less than $50 million.
[4] Loss of less than $1 million.
[5] Estimate provided by the Congressional Budget Office.

Legend for "Effective" column: aca = audits commencing after; cqba = calendar quarters beginning after; DOE = date of enactment; pca = proceedings commencing after; si = summaries issued; tyba = taxable years beginning after; tyea = taxable years ending after; tyoea = taxable years open or ending on or after; 1ya = 1 year after; 9ma = 9 months after; 90da = 90 days after; 180da = 180 days after.

Note.—Details may not add to totals due to rounding. Estimates prepared at time of Committee on Ways and Means action on H.R. 2676.

Source: Joint Committee on Taxation.

APPENDICES

APPENDIX A

Meetings Held With IRS Restructuring Commissioners and Other Interested Parties

To assist the Joint Committee staff in analyzing the Commission Report and related proposals, the Joint Committee staff invited the Commissioners and other interested parties to discuss significant issues raised by the Report and related proposals. The staffs of the House Ways and Means and Senate Finance Committees were also invited to attend. Following is a list of meetings that the Joint Committee staff held (or scheduled) with interested parties prior to the publication of this pamphlet. It is expected that additional meetings and discussions will occur as the legislative process on the restructuring proposals progresses.

Commissioners of the National Commission on Restructuring the Internal Revenue Service

Fred T. Goldberg, Jr.—Skadden, Arps, Slate, Meagher & Flom
Gerry Harkins—Southern Pan Services Company
David Keating, National Taxpayers Union
Edward S. Knight—General Counsel, U.S. Department of Treasury
J. Fred Kubik, Baird, Kurtz & Dobson
Mark McConaghy—Price Waterhouse
Robert Tobias—President, National Treasury Employees Union
Josh S. Weston—Automated Data Processing
James W. Wetzler—Deloitte & Touche

Other Interested Parties

Michael Dolan—Acting Commissioner, Internal Revenue Service
Donald C. Alexander—Akin, Gump, Strauss, Hauer & Feld, LLP (former IRS Commissioner)
Sheldon S. Cohen—Morgan, Lewis & Bockius (former IRS Commissioner)
Lawrence B. Gibbs—Miller & Chevalier (former IRS Commissioner)
Dr. Jay Lorsch, Harvard Business School
Dr. Robert Stubaugh, Harvard Business School
American Institute of Certified Public Accountants
National Association of Manufacturers
National Federation of Independent Businesses
Tax Section of the American Bar Association
Tax Section of the New York State Bar Association

APPENDIX B

Memorandum From the Congressional Research Service to the National Commission on Restructuring the Internal Revenue Service

Congressional Research Service,
The Library of Congress,
Washington, DC, June 4, 1997.

To: National Commission on Restructuring the Internal Revenue Service. Attention: Armando Gomez.
From: American Law Division.
Subject: Constitutionality of Vesting the Appointment of a Commissioner of the Internal Revenue Service in an Independent Board of Directors Located in the Treasury Department.

You have asked that we review the constitutional propriety of a proposed restructuring of the Internal Revenue Service (IRS). Under the proposal, Congress would establish as an independent entity within the Department of Treasury, a seven member Oversight Board of Directors whose mission would be to oversee the operational management of the IRS and provide guidance and direction with respect to the development and implementation of long-term strategic and business plans. The Board would be composed of five persons nominated by the President and confirmed by the Senate from the private sector who would serve for five year staggered terms; and two officials from the Executive Branch designated by the President. A chairman would be elected from among the Board members by the members for a two year term. The Board would have the authority to appoint, and remove at its will, a Commissioner who would serve as chief executive officer of IRS for a five year term and be responsible for the day-to-day management of IRS operations.

More particularly, it is conceived that the Board of Directors would have authority to:

1. Review and approve the Commissioner's recommendations regarding IRS strategic and business plans, and the IRS goals and measurements relative to those plans.
2. Review and approve the Commissioner's recommendations regarding major operational and organizational plans (*e.g.*, plans for modernizing technology systems; training; outsourcing; managed competition; reorganization of the Commissioner's office; reorganization of IRS business units).
3. Appoint and compensate the Commissioner and review and approve the Commissioner's recommendations regarding the appointment, performance, and compensation of senior IRS executives.
4. Review and approve the Commissioner's recommendations regarding the IRS Budget, with particular emphasis on the alignment of that budget with the IRS strategic and business plans. The board will send the budget to Treasury to incorporate with Treasury's budget, and send a copy of the board's budget request directly to Congress.
5. Review the IRS annual financial audits.

6. Provide annual stewardship reports to the President, the Congress and the American public regarding the matters under its jurisdiction.

Finally, the Treasury Department would continue to maintain full control of the establishment of tax policy. It is not clear from the proposal what other authority arrangements that now exist between Treasury and IRS (*e.g.,* litigation authority) will remain, be modified, or be abolished. It appears that IRS will determine its own annual budget request which would be transmitted through Treasury to Congress unchanged.

The proposal raises a substantial constitutional question with respect to the Board's power to appoint the Commissioner. While it is beyond a doubt that Congress can establish a presidentially appointed Oversight Board within Treasury, it is not yet a clearly settled matter whether such a Board can be vested with the authority to appoint such an official. The issue turns on the answer to two questions: Will the Commissioner be an "inferior officer"? If so, is the Oversight Board a "Head of Department" within the meaning of the Appointments Clause? We conclude that a reviewing court is like to answer both questions in the affirmative.

1. Congress' Power Over Offices and Officers

While the infrastructure of the Executive Branch and other entities charged with the execution of the law is not specified by the Constitution, it is clear that the Framers intended to vest the task of creating the governmental structure in the Congress alone. See, *e.g.,* Article II, sec. 2, cl. 2 (the President "shall nominate, and by and with the advice and consent of the Senate, shall appoint ambassadors, other public ministers and counsels, judges of the Supreme Court, and all other officers of the United States, whose appointments are not herein otherwise provided for and which shall be established by law.")(emphasis added). Thus it is well established that Congress, in exercising its powers to legislate under Article I, sec. 8, and other provisions of the Constitution, is empowered to provide for the execution of those laws by officers appointed pursuant to the Appointments Clause, and under the Necessary and Proper Clause, Art., sec. 8, cl. 18, it has authority to create and locate offices, determine the qualifications of officeholders, prescribe their appointments, and generally promulgate the standards for the conduct of the offices. *Myers* v. *United States,* 272 U.S. 52, 129 (1926) ("To Congress under its legislative power is given the establishment of offices, the determination of their functions and jurisdiction, the prescribing of reasonable and relevant qualifications and rules of eligibility of appointees, and the fixing of the term for which they are to be appointed, and their compensation—all except as otherwise provided by the Constitution."); *Buckley* v. *Valeo,* 424 U.S. 1, 134–35 (1976); *Morrison* v. *Olson,* 487 U.S. 654, 685–93 (1988); *Mistretta* v. *United States,* 488 U.S. 361 (1989).

Only where the object of the exercise of legislative power is clearly seen in the particular situation as an attempt at aggrandizement or encroachment have the court's felt constrained to intervene. See, *e.g., Buckley* v. *Valeo,* supra (Congress may not appoint executive officials performing substantial functions under the Law); *Bowsher* v. *Synar,* 478 U.S. 714, 732 (1986) (Congress may not retain re-

moval power over an officer performing executive functions); *INS* v. *Chadha,* 462 U.S. 919 (1983) (Congress may not exercise legislative power without conforming to the constitutionally prescribed lawmaking power); *Metropolitan Washington Airports Authority* v. *CAAN,* 501 U.S. 252 (1991) (Board of Review composed of Members of Congress could not exercise veto power over operational decisions of Airports Authority); *Hechinger* v. *Metropolitan Washington Airport Authority Board of Review,* 36 F.3d 97 (D.C. Cir. 1994), *cert. denied,* 115 S.Ct. 934 (1995) (Board of Review which could only recommend and delay, but not veto, the operational decisions of the Airports Authority held to be an unconstitutional direct exercise of congressional influence); *Federal Election Commission* v. *NRA Political Victory Fund,* 6 F.3d 821 (D.C. Cir. 1993), *cert. denied for want of jurisdiction,* 115 S.Ct. 537 (1994) (congressional appointment of two of its agents as non-voting members of the Commission who could attend all business meetings of the agency held unconstitutional).

But beyond such direct congressional intrusions on agency decisionmaking, the Supreme Court has been generous in broadly defining the legislative authority to structure the administrative bureaucracy. It has upheld congressional actions lengthening and shortening terms of office and abolishing offices altogether, *Crenshaw* v. *United States,* 134 U.S. 99, 105–6 (1890); *Lewis* v. *United States,* 244 U.S. 1345 (1917); limiting the removal power of the President, *Morrison* v. *Olson,* 487 U.S. 854 (1988); locating an independent agency performing executive functions in the judicial branch, *Mistretta* v. *United States,* supra; allowing an agency to assume jurisdiction over state-law counterclaims, *Commodity Futures Trading Commission* v. *Schor,* 473 U.S. 833 (1986); empowering the Attorney General to determine what substances would be criminal and to prosecute violations, *Touby* v. *United States,* 500 U.S. 160 (1991); and establishing the qualifications for holding office, *Myers* v. *United States,* 272 U.S. 52, 128, 129 (1926). In sum, the breadth of the congressional power is captured in the *Mistretta* court's admonishment that "our constitutional principles of separated powers are not violated . . . by mere anomally or innovation", 488 U.S. at 385, and an appeals court's more recent observation that the fact that Congress has not structured a governmental entity "like a traditional government agency need not imply that its structure is not constitutionally permissible. There is no one way to structure an agency nor one means to comply with the constitutional appointments process". *Silver* v. *U.S. Postal Service,* 951 F. 2d 1033, 1037 (9th Cir. 1991).

There can be little doubt that the proposal to establish a presidentially appointed Overnight Board as an independent establishment within the Treasury Department to oversee and guide the operational management of the IRS falls well within administrative structuring powers of the Congress. Nor is the placement of such multi-member, presidentially appointed independent entity within a cabinet department of either anomalous or unique. See, e.g., 18 U.S.C. 4201–4218 (1994) (Parole Commission established an independent agency within Department of Justice); 42 U.S.C. 7101 et seq. (1994) (Federal Energy Regulatory Commission established as

an independent regulatory agency within the Department of Energy).

Moreover, as proposed, there appear to be no issues of legislative aggrandizement or encroachment: Congress retains no power of appointment or removal over a agency officials nor does it maintain any direct or indirect control over its decision making processes. The requirement that IRS's annual budget requests be transmitted unchanged to Congress through Treasury's submission is well supported in law and practice. The Supreme Court has long, and uniformly recognized Congress' virtually plenary power to inform itself and the public as to the operations of the agencies it creates and oversees. The informing power has been deemed so essential to the legislative function as to be implied from the general vesting of legislative power in Congress, *Eastland* v. *United States Servicemen's Fund,* 421 U.S. 491, 505 (1975); *Barenblatt* v. *United States,* 360 U.S. 109, 116–23 (1959); *Watkins* v. *United States,* 354 U.S. 178, 187 (1957); *McGrain* v. *Daugherty,* 273 U.S. 135, 137 (1927).

With particular regard to the Congress' informing functions, the Supreme Court in *Nixon* v. *Administrator of General Services,* 433 U.S. 425 (1977), had occasion to note that "there is abundant statutory precedent for the regulation and mandatory disclosure of documents in the possession of the Executive Branch" and that "[s]uch regulation of material generated in the Executive Branch has never been considered invalid as an invasion of its autonomy." 433 U.S. at 447. There the Court cited with approval the Freedom of Information Act, the Privacy Act, the Government in the Sunshine Act, the Federal Records Management Act, and provisions concerned with census data and tax returns as appropriate instances of such regulations.

In *Nixon,* the Court upheld the Presidential Recordings and Materials Preservation Act, which protects, among other things, public access to former President Nixon's presidential papers from presidential claims of violation of the doctrine of separation of powers and executive privilege. In *INS* v. *Chadha, supra,* Court reaffirmed Congress's authority to legislate "report and wait" provisions, distinguishing them from otherwise unconstitutional legislative veto provisions there under review. 461 U.S. at 935 n.9;955 n. 19. More recently, the Court in *Morrison* v. *Olson, supra,* reaffirmed Congress's authority to require the submission of reports and other information to it from executive branch officials, as an exercise of oversight over agencies "that we have recognized generally as being incidental to the legislative function of Congress". 487 U.S. at 694.

Moreover, Congress has selectively required simultaneous or unaltered submission of budget requests and legislative proposals and comments that limit review by OMB of budget requests, legislative proposals, review of proposed agency rules, and other required reports and documents. Thus, since 1973, Congress has mandated that the budget requests of the U.S. Postal Service, see Act of June 30, 1974, Pub. Law No. 93–328, 23 88 Stat. 28 (codified at 39 U.S.C. 2009 (1994), and the U.S. International Trade Commission, see Trade Act of 1974, Pub. L. No. 93–618, 175(a)(1), 88 Stat. 1978 (1975)(codified at 19 U.S.C. 2232 (1994), be submitted to Congress without revision, and that the budget requests and legislative proposals of other agencies be submitted concurrently to

OMB and the Congress. See, *e.g.*, 7 U.S.C. 4a(h)(1)(2)(1994) (Commodity Futures Trading Commission); 31 U.S.C. 1107(b)(1994) (Interstate Commerce Commission).

Also, Congress has exempted the Securities and Exchange Commission, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Federal Home Loan Bank Board, and the National Credit Union Administration from OMB clearance of their legislative proposals and comments. Act of Oct. 28, 1974, Pub. L. No. 93–111, 88 Stat. 1500 (codified at 12 U.S.C. 250 (1994).

Since there is no direct prohibition on the President from presenting his views with respect to any recommendation or plan submitted by the IRS directly to the Congress, no constitutional difficulty could be raised with respect to his recommendatory duty under Article II, section 3. Indeed, the Article II duty to recommend, as with the duty to "take care" that the laws be faithfully executed, which appears in the same clause, is not a source of substantive presidential power and claims to that effect have consistently been rejected by the courts. See, *e.g.*, *Kendall ex rel Stokes* v. *United States*, 37 U.S. (12 Pat.) 522, 612–13 (1838) ("To contend that the obligation imposed on the President to see the laws faithfully executed, implies a power to forbid execution, is a novel construction of the Constitution, and entirely inadmissible.); *Youngstown Sheet and Tube Co.* v. *Sawyer*, 343 U.S. 579, 587 (1952) (". . . " [T]he President's power to see that the laws are faithfully executed refutes the idea he is to be a lawmaker. The Constitution limits his functions in the lawmaking process to the recommending of laws he thinks wise and the vetoing of laws he thinks bad".); *National Treasury Employee Union* v. *Nixon*, 492 F.2d 587, 604 (D.C. Cir. 1974) ("That constitutional duty does not permit the President to refrain from executing laws duly enacted by the Congress as those laws are construed by the judiciary").

Thus, the sole questions that remain are whether the proposed Commissioner of IRS is an "inferior officer" and, if so, whether he can be lawfully appointed by the Oversight Board.

2. Whether The Proposed Commissioner of IRS Is An Inferior Officer

In developing its separation of powers jurisprudence, the Supreme Court has acknowledged that it has been animated by its concern with "encroachment and aggrandizement" by one branch against the other, and that in adopting its "flexible understanding of separation of powers" it is recognizing "Madison's teaching that the greatest security against tyranny is the accumulation of excessive authority in a single Branch—lies not in a hermetic division among the Branches, but in a carefully crafted system of checked and balanced power within each Branch." *Mistretta* v. *United States*, *supra*, 488 U.S. at 380–81. The application of this teaching is abundantly evident in the appointments process established by Article II, sec. 2, cl. 2. The Court has made clear that "The principle of separation of powers is embedded in the Appointments Clause". *Freytag* v. *Commissioner of Internal Revenue*, 501 U.S. 868, 882 (1991). The Appointments Clause directs that all superior officers, such as ambassadors, judges and heads of departments,

must be appointed by the President with the advice and consent of the Senate. Congress may also subject any other officer of the United States ("inferior officers") to Senate confirmation but may, "as they think proper," vest the appointment of inferior officers in the President alone, in the courts or in the department heads. Thus the choice Congress makes with respect to mode of appointment of necessity reflects a decision to impose either a heightened or lesser degree of congressional scrutiny on a nominee, or perhaps to provide a degree of insulation of the officer from the President by having him appointed (and removable) by a department head. See *United States* v. *Perkins*, 116 U.S. 483 (1886). It also advances the concerns sought to be avoided by the Framers. The *Freytag* Court observed:

> The "manipulation of official appointments" had long been one of the American revolutionary generation's greatest grievances against executive power, see G. Wood, The Creation of the American Republic 1776–1787, p. 79 (1969) (Wood), because "the power of appointment to offices" was deemed "the most insidious and powerful weapon of eighteenth century despotism". Id, at 143. Those who framed our Constitution addressed these concerns by carefully husbanding the appointment power to limit its diffusion. Although the debate on the Appointments Clause was brief, the sparse record indicates the Framers' determination to limit the distribution of the power of appointment. The Constitutional Convention rejected Madison's complaint that the Appointments Clause did "not go far enough if it be necessary at all": Madison urged that "Superior Officers below Heads of Departments ought in some cases to have the appointment of the lesser offices." Records of the Federal Convention of 1787, pp. 627–628 (M. Farrand rev. 1966). The Framers understood, however, that by limiting the appointment power, they could ensure that those who wielded it were accountable to political force and the will of the people. Thus, the Clause bespeaks a principle of limitation by dividing the power to appoint the principal federal officers—ambassadors, ministers, heads of departments, and judges—between the Executive and Legislative Branches. *See Buckley*, 424 U.S., at 129–131. Even with respect to "inferior Officers," the Clause allows Congress only limited authority to devolve appointment power on the President, his heads of departments, and the courts of law.

501 U.S. 883–84. See also *Edmond* v. *United States*, 65 U.S.L.W. 4362, 4365 (S. Ct., May 19, 1997) ("[T]he Appointment Clause of Article II is more than a matter of 'etiquette or protocol'; it is among the significant structural safeguards of the constitutional scheme.) See also *Confederated Tribes of Siletz Indians of Oregon* v. *United States*, 110 F.3d 688, 696 (9th Cir. 1997) "Appointments Clause serves as a guard against one branch aggrandizing its power at the expense of another.").

Congress has a choice of requiring appointment with Senate advice and consent or by the President alone, by a department head

or by a court of law only with respect to inferior officers. Until very recently, Supreme Court decisions did "not set forth an exclusive criterion for distinguishing between principal and inferior officers for Appointment Clause purposes", *Edmond* v. *United States, supra*, 65 U.S.L.W. at 4865, preferring to deal with each officer on an ad hoc basis. In *Morrison* v. *Olson, supra*, the Court found the independent counsel created by the Ethics in Government Act to be an inferior officer because she met four criteria: she was subject to removal by a higher officer (the Attorney General), she performed only limited duties, her jurisdiction was narrow, and her tenure was limited. *Morrison*, 487 U.S. at 671–672. In *Edmonds* v. *United States, supra*, however, the Court revisited the principal/inferior officer distinction, establishing a test relying on the single criterion whether the officer has a superior:

> Generally speaking, the term "inferior officer" connotes a relationship with some higher ranking officer or officers below the President: whether one is an "inferior" officer depends on whether one has a superior. It is not enough that other officers may be identified who formally maintain a higher rank, or possess responsibilities of a greater magnitude. If that were the intention, the Constitution might have used the phrase "lesser officer." Rather, in the context of a clause designed to preserve political accountability relative to important government assignments, we think it evident that "inferior officers" are officers whose work is directed and supervised at some level by others who were appointed by presidential nomination with the advice and consent of the Senate.

65 U.S.L.W. at 4366. Moreover, the Court held that the fact that a person exercises "'significant authority pursuant to the laws of the United States" marks, not the line between principal and inferior officer for Appointments Clause purposes, but rather, as we said in *Buckley*, the line between officer and non-officer, 424 U.S., at 126". *Id.*

The *Edmond* ruling appears to answer the question whether the Commissioner in the proposed new scheme for IRS is an inferior officer. That the Commissioner has been a presidential appointee subject to Senate confirmation and only removable by the President for many years would be irrelevant. The new scheme would relegate the Commissioner to inferior officer status since he would be appointed and overseen by the Oversight Board, the members of which are presidentially appointed with Senate advice and consent, and is removable by that body at its pleasure. The only question, then, is whether the Board can lawfully appoint the Commissioner at all.

3. Whether The Oversight Board Is a "Head of Department" Capable of Appointing Inferior Officers

In order to vest appointment authority in the Oversight Board it must qualify as a "Head of Department" under the Appointments Clause. Our review of the pertinent case law, and in particular the Supreme Court's recent ruling in *Edmond* v. *United States*, persuades us that it is likely that a reviewing court will find that the

Board is a "Head of Department" capable of being vested with authority to appoint inferior officers.

Three judicial decisions need to be considered. In the first, *Freytag* v. *CIR*, 501 U.S. 868 (1991), the Supreme Court unanimously upheld the authority of the Chief Judge of the Tax Court to appoint "special trial judges" to hear certain classes of cases when its workload was heavy. The entire court agreed that the Tax Court had to be either a "department" or a "court of law" in order for the Chief Judge to exercise the appointing authority. Five of the Justices found it to be a court of law, four voted to sustain the authority on the ground that it was a department. The majority opinion appeared to take a rigid view of the nature of the term "department", seeking to limit it to those governmental entities specifically identified as cabinet departments, relying on statements in late 19th and early 20th century Appointments Clause rulings by the Court:

> Confining the term "Heads of Departments" in the Appointments Clause to executive divisions like the Cabinet-level departments constrains the distribution of the appointment power just as the Commissioner's interpretation, in contrast, would diffuse it. The Cabinet-level departments are limited in number and easily identified. Their heads are subject to the exercise of political oversight and share the President's accountability to the people.
>
> Such a limiting construction also ensures that we interpret that term in the Appointments Clause consistently with its interpretation in other constitutional provisions. In *Germaine*, see 99 U.S., at 511, this Court noted that the phrase "Heads of Departments" in the Appointments Clause must be read in conjunction with the Opinion Clause of Art. II, sec. 2, cl. 1. The Opinion Clause provides that the President "may require the Opinion, in writing, of the principal Officer in each of the Executive Departments," and *Germaine* limited the meaning of "Executive Departmen[t]" to the Cabinet members.

501 U.S. at 886. But at the same time the majority significantly qualified its broad holding by noting that: "We do not address here any question involving the appointment of an inferior officer by the head of one of the principal agencies, such as the Federal Trade Commission, the Securities and Exchange Commission, the Federal Energy Regulatory Commission, the Central Intelligence Agency, and the Federal Reserve Bank of St. Louis," *Id.* at 887 note 4.

The majority's qualification is likely a reaction to the strong opinion of the four concurring justices written by Justice Scalia, and is arguably meant to limit the court's decision to the rather unique circumstances of the Article 1 Tax Court situation. Justice Scalia contested the majority's view that the constitutional term department could be equated with "cabinet-level agency".

> There is no basis in text or precedent for this position. The term "Cabinet" does not appear in the Constitution, the Founders having rejected proposals to create a Cabinet-like entity. See H. Learned, The President's Cabinet

> 74–94 (1912); E. Corwin, The President 97, 238–240 (5th rev. ed. 1984). The existence of a Cabinet, its membership, and its prerogatives (except to the extent the Twenty-fifth Amendment speaks to them), are entirely matters of Presidential discretion. Nor does any of our cases hold that "the Heads of Departments" are Cabinet members. In *United States* v. *Germaine*, 99 U.S. 508 (1879), we merely held that the Commissioner of Pensions, an official within the Interior Department, was not the head of a department. And, in *Burnap, supra*, we held that the Bureau of Public Buildings and Grounds, a bureau *within* the War Department, was not a department.
>
> The Court's reliance on the Twenty-fifth Amendment is misplaced. I accept that the phrase "the principal officers of the executive departments" is limited to members of the Cabinet. It is the structural composition of the phrase, however, and not the single word "departments" which gives it that narrow meaning—"the principal officers" of the "executive departments" in gross, rather than (as in the Opinions Clause) "the principal Officer in each of the executive Departments" or (in the Appointments Clause) simply "the Heads" (not "principal Heads") "of Departments."

Id. at 916–917 (emphasis in original).

Scalia goes on to note that so confining the scope of the term department ignores the reality of the current structure of the federal administrative bureaucracy:

> Modern practice as well as original practice refutes the distinction between Cabinet and non-Cabinet agencies. Congress has empowered non-Cabinet agencies to appoint inferior officers for quite some time. See, *e.g.*, 47 U.S.C. § 155(f) (FCC—managing director); 15 U.S.C. § 78d(b) (Securities and Exchange Commission—"such officers . . . as may be necessary"); 15 U.S.C. § 42 (Federal Trade Commission—secretary); 7 U.S.C. § 4a(c) (Commodity Futures Trading Commission—general counsel). In fact, I know of very few inferior officers in the independent agencies who are appointed by the President, and of none who is appointed by the head of a Cabinet department. The Court's interpretation of "Heads of Departments" casts into doubt the validity of many appointments and a number of explicit statutory authorizations to appoint.
>
> A number of factors support the proposition that "Heads of Departments" includes the heads of all agencies immediately below the President in the organizational structure of the Executive Branch. It is quite likely that the "Departments" referred to in the Opinions Clause ("The President . . . may require the Opinion, in writing, of the principal Officer in each of the executive Departments," Art. II, § 2) are the same as the "Departments" in the Appointments Clause. See *Germaine, supra*, at 511. In the former context, it seems to me, the word must reasonably be thought to include all independent establishments. The purpose of

the Opinions Clause, presumably, was to assure the President's ability to get a written opinion on all important matters. But if the "Departments" it referred to were only Cabinet departments, it would not assure the current President the ability to receive a written opinion concerning the operations of the Central Intelligence Agency, an agency that is not within any department, and whose Director is not a member of the Cabinet.

This evident meaning—that the term "Departments" means all independent executive establishments—is also the only construction that makes sense of Article II, § 2's sharp distinction between principal officers and inferior officers. The letter, as we have seen, can by statute be made appointable by "the President alone, . . . the Courts of Law, or . . . the Heads of Departments." Officers that are not "inferior officers," however, must be appointed (unless the Constitution itself specifies otherwise, as it does, for example, with respect to officers of Congress) by the President, "by and with the Advice and Consent of the Senate." The obvious purposes of this scheme is to make sure that all the business of the Executive will be conducted under the supervision of officers appointed by the President with Senate approval; only officers "inferior," *i.e.*, subordinate, to those can be appointed in some other fashion. If the Appointments Clause is read as I read it, all inferior officers can be made appointable by their ultimate (sub-Presidential) supporters; as petitioners would read it, only those inferior officers whose ultimate superiors happen to be Cabinet members can be. All the other inferior officers, if they are to be appointed by an Executive official at all, must be appointed by the President himself or (assuming cross-department appointments are permissible) by a Cabinet officer who has no authority over the appointees. This seems to me a most implausible disposition, particularly since the makeup of the Cabinet is not specified in the Constitution, or indeed the concept even mentioned. It makes no sense to create a system in which the inferior officers of the Environmental Protection Agency, for example—which may include, *inter alias*, bureau chiefs, the general counsel, and administrative law judges—must be appointed by the President, the courts of law, or the "Secretary of Something Else."

In short, there is no reason, in text, judicial decision, history, or policy, to limit the phrase "the Heads of Departments" in the Appointments Clause to those officials who are members of the President's Cabinet. I would give the term its ordinary meaning, something which Congress has apparently been doing for decades without complaint. As an American dictionary roughly contemporaneous with adoption of the Appointments Clause provided, and as remains the case, a department is "[a] separate allotment or part of business, a distinct province, in which a class of duties are allotted to a particular person . . ." IN. Webster American Dictionary 58 (1828). I readily acknowledge that

> applying this word to an entity such as the Tax Court would have seemed strange to the Founders, as it continued to seem strange to modern ears. But that is only because the Founders did not envision that an independent establishment of such small size and specialized function would be created. The Constitution is clear, I think about the chain of appointment and supervision that it envisions: Principal officers could be permitted by law to appoint their subordinates. That should subsist, however much the nature of federal business or of federal organizational structure may alter.

Id. at 918–920.

This lengthy quotation from Justice Scalia's opinion is justified in light of its apparent impact on two subsequent decisions. In *Silver* v. *U.S. Postal Service,* 951 F.2d 1033 (9th Cir. 1991), the appeals court dealt with a challenge to the validity of the appointment of the Postmaster General by the Governors of the Postal Service. The nine Governors are appointed by the President, with Senate advice and consent, and are vested with the power to appoint (and remove) the Postmaster General and the Deputy Postmaster General who serve with the Governors on the Board of Governors. It was argued by the appellant that a collegial body cannot be a department capable of exercising appointment authority. The court disagreed. Finding that the Postal Service was an Executive Branch entity, it utilized the *Freytag* court's inexact suggestion that departments are "executive divisions like the Cabinet-level departments" to hold that since the Post Office prior to its reorganization in 1970 was in fact a cabinet department and the reorganization did not "fundamentally change the nature and purpose of the postal Service," Congress's action "did not render what was once a Cabinet level department into an entity that was not 'like a Cabinet-level department'." 951 F.2d at 1038. The appeals court concluded that the nine Governors constitutes the "head of department" since they are appointed by the President, can appoint and remove the Postmaster General, can revoke any authority delegated by the Board to the Postmaster General, and have the authority to designate mail classifications and to set postal rates. In view of the subordination of the Postmaster General to the Governors, and his statutory role as their managing agent, the court found him to be an inferior officer capable of being appointed by the Governor.

The *Silver* court appeared to reach a satisfactory and proper result but only by stretching Freytag's uncertain limitation on the scope of the definition of department. This uncertainty, however, appears to have been essentially dissipated by the Court's decision in *Edmond* v. *United States.*

Edmond involved the questions whether Congress authorized the Secretary of Transportation to appoint civilian members of the Coast Guard Court of Criminal Appeals and, if so, whether those judges are inferior officers. As previously detailed, Justice Scalia, for a unanimous court, effectively adopted his concurrence in *Freytag* with respect to the test for determining when an officer is "inferior" for constitutional purposes. "We think it evident that 'inferior officers" are officers whose work is directed and supervised

at some level by others who were appointed with the advice and consent of the Senate," *Edmond, supra* at 65 U.S.L.W. at 4366. Finding that the judges in question were supervised by the General Counsel of the Department of Transportation in his capacity as Judge Advocate General and by the Court of Appeals for the Armed Forces, and that the Secretary of Transportation was authorized by Congress to appoint the judges, the Court concluded that the appointments were valid.

But Justice Scalia's opinion also pointedly diminished the majority opinion in *Freytag* in two ways: First, it limited *Freytag* to its facts: "Petitioners contend that Court of Criminal Appeals judges more closely resemble Tax Court judges—who we implied (according to petitioners) were principal officers—than they do special trial judges. We note initially that *Freytag* does not hold that Tax Court Judges are principal officers; only the appointment of special trial judges was at issue in that case." Second, and more importantly, Scalia's opinion significantly altered the *Freytag* majority's statement of the rationale for the Appointments Clause. That opinion made it evident that it was their view that at the heart of the Framers' intent was the desire to limit abuse of the appointment power by limiting its diffusion: "Those who framed our Constitution addressed those concerns by carefully husbanding the appointment power to limit its diffusion." 501 U.S. at 883. And again, more clearly, the *Freytag* court stated:

> We cannot accept the Commissioner's assumption that every part of the Executive Branch is a department, the head of which is eligible to receive the appointment power. The Appointments Clause prevents Congress from distributing power too widely by limiting the actors in whom Congress may vest the power to appoint. The Clause reflects our Framers' conclusion that widely distributed appointment power subverts democratic government. Given the inexorable presence of the administrative state, a holding that every organ in the Executive Branch is a department would multiply indefinitely the number of actors eligible to appoint. The Framers recognized the dangers posed by an excessively diffuse appointment power and rejected efforts to expand that power. See Wood 79–80. So do we.

501 U.S. at 885. The *Freytag* Court closely linked the danger of diffusion to its limitation of the scope of term "department" to cabinet-level like entities.

The Edmond opinion abandons the notion of diffusion as a rationale for the Appointments Clause. Justice Scalia wrote:

> As we recognized in *Buckley* v. *Valeo*, 424 U.S. 1, 125 (1976), the Appointments Clause of Article II is more than a matter of "etiquette or protocol"; it is among the significant structural safeguards of the constitutional scheme. By vesting the President with the exclusive power to select the principal (noninferior) officers of the United States, the Appointments Clause prevents congressional encroachment upon the Executive and Judicial Branches. See *id.*, at 128–131; *Weiss, supra*, at 183–185 (Souter, J. concurring). This

> disposition was also designed to assure a higher quality of appointments: the Framers anticipated that the President would be less vulnerable to interest-group pressure and personal favoritism than would a collective body. "The sole and undivided responsibility of one man will naturally beget a livelier sense of duty, and a more exact regard to reputation." The Federalist No. 76, p. 387 (M. Beloff ed. 1987) (A. Hamilton); accord, 2 J. Story, Commentaries on the Constitution of the United States 374–375 (1888). The President's power to select principal officers of the United States was not left unguarded, however, as Article II further requires the "Advice and Consent of the Senate." This serves both to curb executive abuses of the appointment power, see 3 Story, at 376–377, and "to promote a judicious choice of [persons] for filing the offices of the union," The Federalist No. 76, at 386–387. By requiring the joint participation of the President and the Senate, the Appointments Clause was designed to ensure public accountability for both the making of a bad appointment and the rejection of a good one. Hamilton observed: "The blame of a bad nomination would fall upon the president singly and absolutely. The censure of rejecting a good one would lie entirely at the door of the senate; aggravated by the consideration of their having counteracted the good intentions of the executive. If an ill appointment should be made, the executive for nominating, and the senate for approving, would participate, though in different degrees, in the opprobrium and disgrace." *Id.*, No. 77, at 392.

See also 3 Story, *supra*, at 375 ("If [the President] should . . . surrender the public patronage into the hands of profligate men, or low adventurers, it will be impossible for him long to retain public favor." 65 U.S.L.W. at 4355.

While we normally eschew predictions of changes in direction of the Supreme Court, two strong indications that Justice Scalia's encompassing view of the term "department" in his *Freytag* concurrence has been adopted by the Court cannot be readily ignored. The first is the apparent abandonment of the diffusion rationale of *Freytag* as a basis for the Appointment Clause. The second is the substantial change in the composition of the Court since *Freytag* was decided. Three of the five justices making up the *Freytag* majority, Justice Blackmun, the author of the opinion, and Justices Marshall and White, have left the Court. Chief Justice Rehnquist and Justice Stevens remain, and they joined in Justice Scalia's *Edmond* opinion.

With due regard for the uncertainty of forecasting the outcome of Supreme Court rulings in separation of powers cases, and recognizing that the issue is not free from doubt, we believe, based upon the significant alteration in the Court's rationale for the basis of the Appointment Clause in *Edmond* from that of *Freytag*, and the changed composition of the Court since the *Freytag* ruling, that a reviewing court may well find that the IRS Oversight Board is

a "head of a department" capable of appointing an inferior officer, and that the proposed commissioner is an inferior officer.

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