JEOPARDY AND TERMINATION ASSESSMENTS AND ADMINISTRATIVE SUMMONSES

HEARING

BEFORE THE

SUBCOMMITTEE ON ADMINISTRATION OF THE INTERNAL REVENUE CODE

OF THE

COMMITTEE ON FINANCE

UNITED STATES SENATE

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CONTENTS

PUBLIC WITNESSES

	Page
American Bankers Association, Robert Brubaker, vice president for operations, Equibank of Pittsburgh, Pa., accompanied by: James E. Merritt, counsel for Crocker National Bank; and John Rolph, Tax counsel for American Bankers Association	90
Brubaker, J. Robert, vice president for operations, Equibank of Pittsburgh, Pa., on behalf of American Bankers Association	90
Fink, Robert S	86
Lynn, Theodore S	79
McCanse, Edson R	37
Merritt, James E., counsel for Crocker National Bank, on behalf of American Bankers Association	90
Plumb, William T., Jr	47
Rolph, John, tax counsel, American Bankers Association	107
Silver, Stephen	6

COMMUNICATIONS

American Civil Liberties Union, Hope Eastman, associate director	225
Eastman, Hope, associate director, American Civil Liberties Union	225
Plumb, William T., Jr	236
Saltzman, Michael I	238
Schnepper, Jeff A., Rutgers College	235

ADDITIONAL INFORMATION

Fact sheet—Jeopardy assessments and termination of taxable year—Referred to by Senator Haskell	3
Committee on Finance press release relative to these hearings	4
Saltzman, Michael I	
Supreme Court opinion (*United States et al.* v. *Bisceglia*)	113

APPENDIX

Communications received by the Committee on Finance expressing an interest in these hearing	223

JEOPARDY AND TERMINATION ASSESSMENTS AND ADMINISTRATIVE SUMMONSES

WEDNESDAY, NOVEMBER 5, 1975

U.S. SENATE,
SUBCOMMITTEE ON ADMINISTRATION
OF THE INTERNAL REVENUE CODE,
OF THE COMMITTEE ON FINANCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:02 a.m., in room 2221, Dirksen Office Building, Senator Floyd K. Haskell presiding.

Present: Senator Haskell.

OPENING STATEMENT OF SENATOR HASKELL

Senator HASKELL. The hearing of the Subcommittee on Administration of the Internal Revenue Code will commence.

I should mention that this morning it is the intent of the committee to examine the very extraordinary powers that the Internal Revenue Service has in aid of the collection of taxes. And with the extraordinary powers, of course, comes the opportunity for abuse of citizenry. On the one hand, we want adequate powers in the Internal Revenue Service to enforce our tax laws.

On the other hand, we want to be sure that the citizens of this country are protected from unnecessary harassment.

This morning the subcommittee will review the extensive and extraordinary powers granted to the IRS for the purpose of vigorously enforcing our tax laws.

One such tool in the hands of the IRS is known as a termination assessment. Under this procedure (provided for in section 6851 of the Code) the Commissioner may determine that the collection of income tax is in jeopardy prior to the expiration of the taxpayer's normal tax year or prior to the statutory date for the filing of the required tax return and payment of tax. Where such a determination is made, the IRS serves notice of the termination of the taxpayer's taxable year and demands immediate payment of any tax determined to be due for the terminated period. If payment is not forthcoming all of the taxpayer's property is subject to seizure and possible sale by the IRS. The taxpayer, under IRS' view of existing law can only contest this kind of action by paying the taxes alleged to be due, filing a claim for refund with the IRS, and after 6 months, unless the refund claim is denied sooner, filing a refund petition with a Federal district court or U.S. Court of Claims.

Another procedure which the IRS may employ under existing law (section 6861 of the Code) is a jeopardy assessment. Where the Commissioner determines a deficiency in income, estate or gift taxes is in jeopardy, he may immediately assess the tax, send a notice and demand for payment and levy on all the property of the taxpayer so that collection of the deficiency will not be jeopardized by delay. If no statutory notice of deficiency has been previously provided to the taxpayer, the IRS must, within 60 days of the making of the jeopardy assessment, provide the taxpayer with such a statutory notice. Upon receipt of this notice, the taxpayer may then file a petition with the Tax Court for a redetermination of the alleged deficiency in tax. Unlike the ordinary taxpayer, the taxpayer against whom a jeopardy assessment has been made, may be subject to collection action while his case is pending before the Tax Court. The IRS can seize the property of such a taxpayer but cannot sell it during the pendency of the Tax Court litigation. Nevertheless, such a taxpayer is deprived of any benefit of the use of such property while release is sought in the Tax Court.

Where a taxpayer is the subject of a jeopardy assessment under section 6862 of the Code, relating to taxes other than income, estate, and gift taxes (i.e., withholding taxes, employment taxes, excise taxes, et cetera), the IRS may immediately assess any taxes determined to be due, seize all the taxpayer's property where it believes collection would be jeopardized by delay, and can sell any property seized before the taxpayer has any right to contest the alleged tax liability. A taxpayer subject to this type of jeopardy assessment has only the right to pay the tax and then commence action for a refund of the taxes paid. If the IRS fails to deny the claim for refund before the expiration of 6 months from the date of payment, this taxpayer cannot even institute a refund action in the Federal courts before waiting 6 months.

The Internal Revenue Manual now provides that jeopardy and termination assessments shall be used sparingly and only if the taxpayer (1) is or appears to be designing quickly to depart from the United States or conceal himself; (2) is or appears to be designing quickly to place his property beyond the reach of the Government by removing it from the United States, or by concealing it, or by transferring it to other persons, or by dissipating it; (3) his financial solvency is or appears to be imperiled.

These extraordinary remedies were adopted by the Congress to insure that the IRS was provided with all the tools necessary to prevent those individuals bent on circumventing the tax laws from taking various measures to avoid the payment of their legitimate tax obligations. Congress is now warranted in reviewing these powers to insure that there are adequate safeguards to prevent those who are charged with the responsibility of administering these provisions from depriving people of their property without observing the basic constitutional requirements of due process.

We will also focus on another problem this morning involving the issuance of administrative summonses by the IRS. Of particular concern is whether taxpayers should be advised of the summons for their records on third parties. Also, under consideration is the appropriate latitude which ought to be provided to the IRS for the issuance of so-called "John Doe" summonses. Such a summons was recently approved in the case of *United States* v. *Bisceglia* by the Supreme Court

to permit the IRS to develop information concerning a particularly unusual transaction which raised a strong suspicion of a possible Federal tax liability. The restriction on the use of such a procedure will be discussed in detail by our witnesses this morning.

Senator HASKELL. The IRS has made public the following information concerning jeopardy assessments and termination of taxable year:

[The information referred to by Senator Haskell and Committee on Finance press release announcing these hearings follow:]

FACT SHEET

JEOPARDY ASSESSMENTS AND TERMINATION OF TAXABLE YEAR

Authority

Sections 6861, 6862 and 6851 of the Internal Revenue Code provide the basis for jeopardy assessments and termination of taxable periods. These actions are authorized upon a determination that the collection of tax will be jeopardized unless such proceedings are brought without delay.

Background

The Service has been concerned as to the possible misuse of our termination and jeopardy assessment procedures, particularly in the Narcotics Traffickers Program. The question was raised whether emphasis was being placed upon depriving traffickers of their working capital, as opposed to directing our attention to enforcement of the tax laws.

Jeopardy assessment and termination of taxable periods are serious and powerful tools. They have been a part of the tax laws for many years. These procedures are to be employed in instances where an individual designs quickly to depart from the United States, or to remove or conceal his property, or do any other act tending to prejudice collection of the tax.

Controls

Service procedures provide for personal approval of these assessments by District Directors, and review by Regional Offices in addition to a sampling in the National Office. We have repeatedly instructed our field offices that jeopardy-type assessments must conform to the law regardless of the background or criminal history of taxpayers against whom such assessments are recommended.

Statistics

The number and amounts of jeopardy and termination assessments in 1972, 1973, and 1974 (partial year) appears below. Although such assessments relating to the Narcotics Program reflect an increase from 1972 and 1973, a turnaround in 1974 is indicated.

JEOPARDY AND TERMINATION ASSESSMENTS

[Fiscal year]

	1972	1973	1974 (9 mo)
Narcotics:			
Taxpayers—Jeopardy	81	133	116
Amount assessed—Jeopardy (thousands)	$11,231	$24,325	$5,631
Taxpayers—Terminations	758	2,446	1,519
Amount assessed—Terminations (thousands)	$31,125	$63,083	$36,322
Total, taxpayers	839	2,579	1,635
Total, assessments (thousands)	$42,356	$87,408	$42,953
Other than narcotics:			
Taxpayers—Jeopardy	924	392	363
Amount assessed—Jeopardy (thousands)	$111,691	$80,310	$57,560
Taxpayers—Terminations	79	135	102
Amount assessed—Terminations (thousands)	$10,358	$8,001	$4,572
Total, taxpayers	373	527	465
Total, assessments (thousands)	$122,049	$88,311	$62,092
Summary:			
Number of taxpayers	1,212	3,106	2,100
Amount assessed (thousands)	$164,405	$175,719	$105,045

New instructions

The decline in FY 1974 assessments reflects the results of our efforts for cautious use of these procedures. We recently issued an Information Notice (Termination of Taxable Periods) expressing Service concern regarding present use of termination assessments and audit guidelines for spontaneous assessments. (See attached copy)

In addition, Manual revisions are in process to clarify any doubt as to the use of the authority under IRC 6861, 6862 and 6851.

[Press release]

U.S. SENATE COMMITTEE ON FINANCE,
October 31, 1975.

SUBCOMMITTEE ON ADMINISTRATION OF THE INTERNAL REVENUE CODE ANNOUNCES HEARINGS ON JEOPARDY AND TERMINATION ASSESSMENTS, ADMINISTRATIVE SUMMONSES, AND PUBLIC INSPECTION OF IRS PRIVATE LETTER RULINGS

The Honroable Floyd K. Haskell (D.-Colorado) announced today that the Subcommittee on Administration of the Internal Revenue Code will hold hearings November 5 and 6 on jeopardy and termination assessments, administrative summonses, and public inspection of Internal Revenue Service private letter rulings.

The hearings will begin at *10:00 A. M. in Room 2221, Dirksen Senate Office Building.*

Senator Haskell said the subcommittee is interested in reviewing certain portions of existing tax laws which provide the IRS with extraordinary powers but give taxpayers only limited rights of redress.

He pointed out that jeopardy and termination assessments may be made whenever the IRS determines the collection of income tax is in jeopardy. Such action may be taken suddenly and requires that the taxpayer first pay any taxes alleged to be due, file a claim for refund, and then wait six months before a suit for refund can be filed.

In certain circumstances, under a jeopardy assessment made pursuant to section 6861, Haskell said, the taxpayer may petition the Tax Court for a judicial determination of the proper tax liability without first having to pay the tax and then file a suit for refund.

Haskell also noted that after property is seized under a jeopardy assessment, such property often can be sold before the taxpayer ever has the right to contest the underlying tax liability. The subcommittee plans to look into these procedures, he said, to see if taxpayers should have an expanded and speedier right of review.

Haskell also said the IRS has the right to examine taxpayers' records, records relating to the taxpayer's business which might be in anyone else's custody, or to take testimony of any such persons under oath. In addition, when the IRS believes that transactions have occurred which may affect the tax liability of a taxpayer it cannot identify, it may issue a so-called "John Doe" summons for the books and records relating to certain transactions without specifying the taxpayer involved. Under existing law such summonses may be issued without informing the taxpayer of their issuance, Haskell said. Although he noted that the administrative summons is an important investigative tool for the IRS, Haskell said the subcommittee will look into whether taxpayers should have the right to participate in and be informed of as investigation into their affairs. In the case of "John Doe" summonses the subcommttee is interested in developing appropriate ground rules for their issuance.

"The subcommittee will also examine the area of private letter rulings, in which the IRS states, at the request of the taxpayer, whether or not a proposed transaction will receive favorable tax treatment," Haskell said. "Other taxpayers are denied access to the estimated half-million such rulings that have been made—making it possible for separate requests to result in different rulings, even under similar circumstances.

"We will consider procedures for the possible disclosure of these rulings, disclosure of the identity of taxpayers seeking such rulings and other pertinent information."

The following witnesses have been scheduled to testify before the subcommittee on November 5, concerning jeopardy and termination assessments:

Stephen Silver, Esq., Phoenix, Ariz. and William T. Plumb, Esq., Washington, D.C.

The following witnesses have been scheduled to testify before the subcommittee on November 5, concerning IRS issuance of administrative summonses: Theodore S. Lynn, Esq., New York, N.Y.; Robert S. Fink, Esq., New York, N.Y.; and John Fletcher Rolph III, Esq., Tax Counsel, American Bankers Association, accompanied by Mr. J. Robert Brubaker, Vice President—Operations, Equibank, N.A., Pittsburgh, Pa.

The following witnesses have been scheduled to testify before the subcommittee on November 6, concerning public inspection of IRS private letter rulings: Martin D. Ginsburg, Esq., Chairman Tax Section, New York Bar Association; Mr. William C. Penick, Chairman, Division of Federal Taxation, American Institute of Certified Public Accountants, accompanied by Mr. Joel M. Forster, Director, Federal Tax Division; Sherwin P. Simmons, Esq., Chairman, Section of Taxation, American Bar Association, accompanied by Don V. Harris, Jr., Esq., Chairman-elect, Section of Taxation; Tom Field, Esq., Executive Director, Tax Analysts and Advocates, Washington, D.C.; K. Martin Worthy, Esq., former Chief Counsel, Internal Revenue Service; and Prof. Peter Weidenbruch, Georgetown University Law Center, Washington, D.C.

To facilitate the presentation of relevant information for consideration by the subcommittee and the full Finance Committee, witnesses who have been scheduled to appear concerning public inspection of IRS private letter rulings are requested to address the following questions in the course of their oral and written presentations:

1. Should private letter rulings be made available for public inspection?

a. Including all information contained in the ruling file?

b. The identity of the taxpayer, representatives of the taxpayer, third parties commenting on the rulings, IRS personnel responsible for the ruling and other relevant information, excluding all information exempt under the Freedom of Information Act?

c. All information necessary to adequately explain the result reached in the ruling, including the ruling request and relevant documentation, with the identity of the taxpayer and others as well as other information which would permit persons without intimate knowledge of the taxpayer's business to identify the taxpayer-ruling recipient deleted?

d. What additional limitations might also be considered?

2. What procedures should be established concerning information to be made available for public inspection?

a. Should the taxpayer be required to request deletion of information he believes to be exempt from disclosure by specifically requesting deletion or by proposing the form of the ruling for publication?

b. Should taxpayer suggestions be advisory only, with responsibility for publication of proposed rulings on the IRS, and the taxpayer retaining a right to object to specific information proposed to be disclosed?

c. Should disputes over information to be made public be resolved prior to consideration of the ruling on the merits or after the determination of the issues raised has been made?

d. Should disputes concerning information to be disclosed be resolved by simply refusing to rule where agreement can not be reached? Should a limited judicial proceeding to resolve such controversies be established providing for publication of the originally requested ruling even where the taxpayer, after judicial determination, disagrees concerning the disclosure of certain information and would choose to rescind the ruling request?

e. Should taxpayers have the right to request delay in the issuance of a ruling until the proposed transaction is completed?

f. Should the IRS be required to index and maintain ruling files and how long should such information be kept available for public inspection?

3. Should technical advice memoranda be made available for public inspection and should procedures be adopted for maintaining anonymity of the taxpayer who may be the subject of such memoranda?

4. What interim rules should be adopted for the processing and disclosure of rulings issued prior to the effective date of any publication procedure which may be finally adopted?

a. Should such rulings be exempt from disclosure?

b. Should they be fully disclosed, with information exempted under the Freedom of Information Act deleted, or with only the name of the recipient deleted?

c. Should ruling recipients be contacted if disclosure is to be made, apprising them of their right to object to the inclusion of information in the published ruling? If ruling recipients can not be located, how should the publication of such rulings be processed?

d. Should disputes concerning information to be disclosed be resolved by IRS personnel? Should a judicial proceeding be provided for making such determinations and in what way should that procedure be limited?

5. Once it is decided that private rulings should be open to public inspection, what kind of precedent should such rulings be accorded for the purposes of other ruling requests?

a. How should such rulings affect transactions similar to those involved in the ruling, but for which no ruling request has been made?

b. Should the IRS be provided with a statutory right to rescind or modify rulings subsequently determined to be misleading, inaccurate or incorrect?

6. What changes would be appropriate concerning the publication of revenue rulings if private letter rulings are held to be open for public inspection? Should there be greater reliance on guideline type revenue procedures?

7. Should third parties be granted a right to question the results reached in specific rulings? Should this right be exercised through a hearing procedure within the IRS or through a judicial proceeding? What parameters should be placed on persons authorized to so intervene?

8. What would be your assessment of the impact of public disclosure of private letter rulings under the procedures mentioned above on the existing IRS ruling system?

Legislative Reorganization Act.—Senator Haskell stated that the Legislative Reorganization Act of 1946, as amended, requires all witnesses appearing before the Committees of Congress "to file in advance written statements of their proposed testimony, and to limit their oral presentations to brief summaries of their argument."

Witnesses scheduled to testify must comply with the following rules:

(1) A copy of the statement must be filed by the close of business two days before the day the witness is scheduled to testify.

(2) All witnesses must include with their written statement *a summary of the principal points included in the statement.*

(3) The written statements must be typed on letter-size paper (not legal size) and at least *75 copies* must be submitted by the close of business the day before the witness is scheduled to testify.

(4) *Witnesses are not to read their written statements* to the Subcommittee, but are to confine their ten-minute oral presentations to a summary of the points included in the statement.

(5) Not more than ten minutes will be allowed for oral presentation.

Written statements.—Persons who desire to present their views to the Subcommittee are urged to prepare a written statement for submission and inclusion in the printed record of the hearings. These written statements should be submitted to Michael Stern, Staff Director, Committee on Finance, Room 2227, Dirksen Senate Office Building on or before November 14, 1975.

Senator HASKELL. We have a series of witnesses who I think are knowledgable on the subject and know the extent of the powers, have had experience and have opinions in the area. And for that reason we will commence and the first witness is Stephen Silver of Phoenix, Ariz.

Mr. Silver, it is a pleasure to have you here.

STATEMENT OF STEPHEN SILVER, ESQ., PHOENIX, ARIZ.

Mr. SILVER. Mr. Chairman, may it please this subcommittee, we have seen in the last 4 years what has been a confrontation with due process. And this has resulted through the use of what the Internal Revenue Service has called a spontaneous assessment.

It all began in June of 1971, in a pronouncement which emanated from then President Nixon, where he announced a new all-out offensive upon those engaged in illegal activities in this country and the Internal Revenue Service was to be an equal participant in this war.

It established at that time, as a high priority program, what has become known as the narcotic traffickers project. The arsenal of weapons included power of summary seizure, termination of taxable years, and the use of the jeopardy assessments.

In the Internal Revenue Manual, which is now in the public sector, the program was stated to have the following purpose; and if I may quote that to you:

> The purpose of IRS participation in the Narcotics Project is to disrupt the distribution of narcotics through the enforcement of all available tax statutes. Maximum use will be made of jeopardy, quick, and transferee assessments, and termination of taxable periods.

In another section of the Internal Revenue Manual, which was given to the revenue officer—those were the ones that were given the power to seize the assets—the following statement was made to them:

> The Collection activity's role is primarily to secure by levy and seizure action the trafficker's assets. When a trafficker has no money, he cannot buy drugs to sell on the streets. Accordingly, seizing money from traffickers is one of the most effective means of ridding the country of the menace of drug abuse.

In Arizona, where I am from, Mr. Chairman, in March of 1972, our District Director gave the following internal directive to his field personnel. This particular document then became a matter of public record in a trial that I was involved in. He states:

> The Phoenix District is fully committed to the narcotics traffickers project. An integral function to the success of the operation is the prompt termination of tax years, etc. When we are in possession of facts which warrant such action, procedures will be developed so that terminations, etc., can be made in less than two hours. Emergency situations may be handled orally and covered thereafter by written reports.

And in fact, the facts that they were in possession of which warranted such action, constituted merely the arrest based upon an alleged, illegal activity.

Now, the first question that I ask this committee—is that the proper use of a tax statute; not to raise revenue, but to complement or supplement some other criminal law?

For the next 3 years, we saw, in the street, the use of this spontaneous assessment in wholesale fashion and as authority for what many of us felt constituted a taking of property without due process, the IRS relied upon an old 1918 law, which was originally enacted to prevent aliens from departing this country with taxable funds.

Now, I assume this committee is familiar with the statutory framework.

Senator HASKELL. Now, Mr. Silver, if I may, I am familiar with terminations; that is, short taxable years. I am familiar with the jeopardy assessment. I am not familiar with what you refer to as summary seizure. Is that a separate statutory authorization? Or where does that fit in?

Mr. SILVER. No, Mr. Chairman, it is not. When I use the words "summary seizure" and the words "spontaneous assessment," these are seizures which are effectuated under the existing statutes, either section 6851, section 6861 or section 6862, which the proposed—the actual word "summary," this came from a news release issued by Commissioner Alexander recently, where he used the word "summary seizure." And so when I use "summary seizure" I am equating it with the use of these assessments under these three statutes.

Senator HASKELL. Under the statutory framework that I mentioned I was familiar with?

Mr. SILVER. Yes, Mr. Chairman.

Senator HASKELL. All right.

Mr. SILVER. Let us just refer to the statutes for a moment, because there is a glaring deficiency in the statutory framework. Originally, when section 6851 was enacted in 1918, its purpose was designed to prevent individuals, either citizens or noncitizens, from departing this country with taxable funds.

It permitted the Commissioner to terminate the taxable period prior to the close of the taxable year, or in some instances, after the close of the taxable year, but before the due date for the return, and commence immediate collection proceedings.

By contrast, a jeopardy assessment under section 6861 will result where a taxpayer has filed a return and the Commissioner determines that additional tax is due and owing and prior to the normal assessment, which would permit an issuance of the statutory notice, they determine it is in jeopardy. Or, where an individual does not file a return, but the due date has passed, the provisions of section 6861 can be used.

In connection with section 6861 and section 6851, these apply with reference to income, estate, and gift taxes. The jeopardy assessment provisions under section 6862 apply with respect to all other taxes; for example, excise taxes. This is a tax which we normally associate in the practice with being used against those suspected of accepting wages. For example, if a man takes a bet for $10, under the law he is required to pay a 10-percent wagering tax.

And apparently the law enforcement officials have used this section 6862 to make assessment, based upon what they alleged to have been wages accepted by people purportedly involved in this illegal activity.

Now it is somewhat central to this whole discussion, Mr. Chairman, that the income tax deficiency procedures, which permits you to go to tax court—to get your ticket of admission, vis-a-vis, your stautory notice applied to section 6861. The Internal Revenue Service has taken the position—and with varying success in courts—that you have no right to a statutory notice where you have a termination under section 6851. And that decision is currently being argued in the Supreme Court and the decision hopefully will be coming down this term.

In reference to 6862, there is no right to a statutory notice and the taxpayer's relief is to pay the tax and go to district court.

Now the most glaring deficiency in the whole statutory framework, at least as it is being applied, is that without a statutory notice the taxpayer has no right to stay the sale of seized property. As we know, under section 6861, the stay of sale of seized property comes about when you file your petition with the Tax Court. However, the terminated taxpayer does not have that right as presently being applied by the Internal Revenue Service.

This has resulted in the Service going out and seizing assets and selling these assets at deflated value.

Senator HASKELL. Let me interrupt you there. Let us say the IRS has this early termination. They seize my car. Do I have a right to post a bond?

Mr. SILVER. You have a right to post a bond, Mr. Chairman. The problem with a bond is that it is often an illusory remedy, in that the way the program has been applied, the taxpayer's assets have all been seized and his net worth as such, based upon the assessment which exceeds the net worth, that the bond remedy is illusory.

Senator HASKELL. Oh, all right. Let me see if I follow you. In other words, they seize all of my assets or whatever else I have got. So you mean I have nothing with which to pay the bond premiums. Is that what you mean?

Mr. SILVER. That is correct, Mr. Chairman. And dealing with bonding companies, as we do—I am in commercial practice—they want security.

Senator HASKELL. Sure, go ahead.

Mr. SILVER. Now let us turn to the other section, section 6862. There is no right to a stay of sale of seized property under that section. I think it is important for us to turn for a moment to the IRS guidelines. As I have stated before, the *Long* case was decided in the State of Washington and affirmed by the ninth circuit. Certain IRS pronouncements were not in the public sector. Now they are.

What does the IRS Manual say? Let us first bear in mind that the IRS Manual is not binding upon the IRS and we cannot use it as a precedent when we go into a courtroom. It does say that these types of assessments—and I am taking and putting all three together, 6861, 6862, and 6851—that they are to be used sparingly; that care should be taken to avoid excessive and unreasonable assessments.

I think, as applied, number one to the narcotics project, these provisions were never applied sparingly. Now the Internal Revenue Manual does state generally the guidelines that are followed in determining whether to make a spontaneous assessment. But rather than refer to them, I want to refer to the guidelines that are under what are referred to as prima facie cases.

These are cases where, if the conditions and facts exist, then the Internal Revenue Service, without any further review, can make the assessments. Let us review them for a moment.

A. Major operators in the criminal field, irrespective of present financial condition.

Now, if we look at that for a moment, one of the conditions to make a jeopardy assessment is that it appears that the taxpayer is or appears to be designing to quickly place his property beyond reach of the Government, or his financial solvency is or appears to be in peril. When we look at the first condition, then we do not see those conditions superimposed upon it. If you are a major operator in a criminal field, irrespective of present financial condition, this is prima facie evidence, that you make a spontaneous assessment.

B. An individual generally known to frequently wager large amounts.

C. Individuals engaged in taking wagers, irrespective of whether major, secondary, or minor.

D. Individuals engaged in other activities, generally regarded as illegal.

E. Individuals with a background and history of engaging in illegal activity, such as gambling, bootlegging, narcotics, and so forth, who are also engaged in so-called legitimate business ventures.

Now as I look over these guidelines, Mr. Chairman, it strikes me that there appears to be one standard for those believed to be engaged in some illegal activity as distinguished from those that perhaps are the normal, routine taxpayers. And it seems to me that we have a denial of equal protection question here.

Let us turn now to the actual use of the spontaneous assessment, as it originally began.

Senator HASKELL. I see here in your written testimony—and incidentally your written testimony will be included and reproduced in full in the record—that one of the guidelines is "individuals against whom large damage suits are pending or against whom such suits are threatened." Do you interpret that guideline as being sufficient in and of itself to permit an early termination?

Mr. SILVER. No, I don't, Mr. Chairman. It is my opinion that the fact that there is a large lawsuit pending against a taxpayer, it does not seem to me to justify the Internal Revenue Service ex parte to go out and seize the assets.

Senator HASKELL. I do not think it does either. But does the Internal Revenue? How does the Internal Revenue Service—I will ask them, they are coming up in a week or so—how do they interpret it?

Mr. SILVER. We have seen one example on the west coast involving C. Arnholdt Smith, where they made a jeopardy assessment against him, contrary to advice that they received from regional counsel's office, by the way. As the chairman knows, the district directors are not required to follow the advice of their lawyer, in-house lawyer, at that stage of the proceeding.

The point is that we have a law which is being administered by certain individuals in the field. We had an atmosphere that permitted what former Commissioner Johnny Walters referred to as the boxcar use of these jeopardies. And so the whole due process that was supposedly built into the IRS Manual to screen these carefully was set aside. And I think that we have witnessed the use of these in these situations which really blink at due process.

Turning to the narcotics project, Mr. Chairman, a representative pattern quickly emerged when someone was arrested on suspicion of trafficking in narcotics. And for narcotics I am going to give it the broad definition, including marihuana and what would be defined as a narcotic. At the time of his arrest, his cash was seized as evidence by the police. Usually at the jail a termination notice was served upon the individual, demanding that he pay immediately a sum of money.

Now the normal 10-day notice and demand period was waived, obviously, and because the taxpayer was unable to pay the amount asked for, an immediate assessment was made. His assets were seized. The cash was turned over to the Internal Revenue Service, pursuant to the assessment, and his property was shortly thereafter scheduled to be sold at public auction.

And by property I mean if the man had a home, if he had a boat—we saw businesses padlocked. In many of these instances, after the program got rolling, the Internal Revenue Service personnel were notified in advance of arrest and they were often present at the time that the individual was arrested. As a matter of fact, IRS officials were even invited or perhaps they invited themselves, to participate in certain searches which were authorized by local warrants. Although these warrants were generally limited to seizing paraphernalia relat-

ing to the criminal activity, the Internal Revenue Service officials participated in these searches. And I had one instance where I asked the special agent "Had you seen a copy of the search warrant before you entered the premises?" "No." "Did you know what was covered under it?" "No." "How did you know what to search for?" And there was still silence.

In any event, they participated in these searches and they asked local law enforcement officials to seize financial information they felt relevant. It was not uncommon for these IRS agents to tape record what they saw visually, what was not included on the inventory.

Now you can see that with all of the property of the taxpayer tied up by liens and levies and seizures, he was often unable to employ counsel of his choice, which in my opinion, raises certain sixth amendment rights to counsel.

It was not too soon after we saw the use of these spontaneous——

Senator HASKELL. Well, let me ask you this. I gather that no showing has to be made to a court prior to——

Mr. SILVER. That is correct, Mr. Chairman. There is no preseizure hearing, with reference to the jeopardy or termination assessment.

Senator HASKELL. When they seize everything, do they have to figure out what the deficiency might be, such as a normal deficiency notice?

Mr. SILVER. Let me give you the answer to that right now. I am not here to tell my war stories, but there is one that I think is pertinent, because it shows you the representative pattern that emerged with reference to computing the assessments. Bear in mind that these assessments were made sometimes in less than 2 hours. They were made before the attorney could get to the jail and get an oral assignment of the confiscated cash.

And this is basically what they did. They would go to the local law enforcement authority, and they would say, what do you know about this individual? And the police officer would say, he has been dealing in 2,000 pounds a month. Well, how many months? Three months. On nothing more than those statements, they would then compute what they consider the profit would be. For example, if it was 1,000 pounds a month net, then he had $100,000 of income.

The *Lisner* case—this individual was arrested on March 18, 1972. The Internal Revenue Service—they were notified shortly thereafter, and they made an assessment based upon—an assessment for tax of $100,620. When I asked them how they computed it, they informed me that the local law enforcement authorities had told them that he had sold 2,000 pounds for the months of July and August.

When I called the local law enforcement authorities on the witness stand, I asked the arresting officer, when did you actually learn about this particular individual? July 15.

Did you begin to conduct surveillance on him? Yes, I did.

Well, when did you actually conduct surveillance? Well, we actually began on August 15.

When was he arrested? On August 18.

How much marihuana did he have in his possession? Well, it was not in his possession; he was not in the automobile, and there was some question of the propriety of this search—150 pounds.

No evidence was offered at that trial with respect to the level of this individual's dealing.

Now, we have other instances where—wiretaps.

Senator HASKELL. Is this all in a court proceeding, under oath somewhere?

Mr. SILVER. Yes, Mr. Chairman. This is a case which is a recorded case, which has been appealed to the ninth circuit.

Senator HASKELL. What is the name of it for the record?

Mr. SILVER. Lisner, L-i-s-n-e-r. It is in the material I furnished the committee this morning.

Senator HASKELL. Thank you.

Mr. SILVER. We have had other instances where wiretaps were used, whether they were legal or illegal, by local law enforcement authorities. Let me give you the example. A wiretap would be conducted for a period of, let us say, 10 days. During the 10-day period, this individual was overheard accepting wagers in the amount of $1,000 a day. Under the excise tax laws, he is supposed to pay 10 percent on each wager accepted, so that would mean that $100 a day times 10 would equal $1,000.

The Internal Revenue Service would get this information turned over to them, and then they would interpolate it for the remainder of the month, coming up with wagers accepted of $30,000, and then interpolate it for a year, for a 12-month period, arriving at a large assessment. And these are all cases which are in court. They are referred to in my footnotes in the materials that I furnished to you.

Not only are there questions that are concerned with the propriety of the IRS using wiretap evidence, a position that I contend the IRS is not in a position to receive or use, but more often than not, these wiretaps were not conducted in accordance with the Federal wiretap statute, and therefore they were tainted, and therefore, in any event, would not be admissible in a court.

Now, shortly after this narcotics project began, the people who were applying it saw that it could be a very effective device to help stamp out crime in this country, which is a worthy objective. And so, they began what they called a special enforcement program.

This is another IRS Manual supplement dated June 30, 1971, and it is labeled "Racketeer Wagering and Coin-Operated Gaming Device Program, Organized Crime Drive and Strike Program." And in that particular document, the use of the spontaneous assessment was encouraged, so what we saw was the same thing that happened with respect to alleged narcotic individuals we saw applied to people who were suspected of engaging in gambling activities and other activities.

In point of fact, I had four different cases where wiretap evidence was used from gamblers, interpolated for a 12-month period, and immediately upon their arrest, the IRS was there to serve the termination notice—not the termination notice, this was a notice of demand, because the assessment was made under 6862 for excise taxes, and their assets were seized. We had boats seized, homes seized. Businesses were padlocked, legitimate businesses. All without a preevidentiary hearing.

Now, I have indicated to you the types of evidence that were relied upon. The Government also relied upon informants' statements. These were informants who never met the revenue agent, but had told some police officer that he knew so-and-so was dealing in x-amount of marijuana, or he knows that so-and-so was accepting wagers for x period of time. These informants were never produced at trial for us

to cross-examine, and therefore, their statements were hearsay and should not have been a basis for the computation of the spontaneous assessment.

At the beginning, when we walked into the courtrooms, the judges, of course, recognizing that there was an anti-injunction statute under 7421–A, were somewhat reluctant to even entertain jurisdiction, based upon the Government's motion to dismiss. But we are somewhat lucky in Arizona. We have two Federal judges there that got these cases, the Honorable Walter Craig, the Honorable William Copple. And they permitted us to have an evidentiary hearing, and they permitted us to call witnesses, and they permitted us to subpena documents. And the Government was required to produce. They were required to permit us to examine their agents, to look in their files. And it led those judges—in *Lisner*, that was Judge Copple's opinion. He held that they had to issue a statutory notice.

Judge Craig, in granting an injunction against an assessment made against a taxpayer whose house and automobile had been seized, based upon an assessment over $200,000, made a remark at the conclusion of the trial. And if I could just read it to this committee, I think it deserves scrutiny:

> It taxes the credulity of the court, and I suspect any reasonable court, to give any merit to the method of calculation and the computation worksheet. This court is certainly favorable to cooperation between State and Federal agencies, but I think it is a miscarriage of that principle to use the Internal Revenue Service as an arm for State enforcement of criminal proceedings. And I don't think Congress ever intended that the IRS be used for that purpose.

We have also seen counteractions by other courts, and I will invite your attention to the remarks of Judge Clark of the fifth circuit, where he also echoes Judge Craig's sentiments.

The weapon that we had to counter the immediate impact of a sale of seized property at a deflated value was the temporary restraining order. But as this subcommittee may know, in order to get under the exception to the anti-injunction statute, you have to show that (A) you will prevail on the merits; and (B) that there is no adequate remedy at law. And as a practical matter, it is very difficult to do this, because you may have an individual who may not have been engaged in the illegal activity to the extent, but to some lesser extent; a portion of the assessment may be valid.

The effects of the *Enochs* confrontation—this was a Supreme Court case, however—has permitted us to have the evidentiary hearing, and it has permitted us in some outrageous situations to crystallize the issue and prevent the sale of assets and to get a decision in favor of the taxpayer.

But in every one of these instances, the Justice Department has appealed these cases to the appellate court.

Senator HASKELL. Are they still undecided in the appellate courts?

Mr. SILVER. Yes, Mr. Chairman, they are. The appellate courts are waiting for the decision of the Supreme Court.

There are two separate issues before the appellate courts. You can attack the assessment on the grounds, under *Enochs*, which basically is a head-to-head confrontation. That is that you cannot prevail under any circumstances, and you have no adequate remedy at law. Or you can appeal on the grounds that no statutory notice has been issued, and the failure to issue it permits you to have an injunction.

As to the later cases, there are appeals across the country that are pending, that await the decision by the Supreme Court in cases called *Lang* and *Hall*. As to the other cases, the circuit courts have reviewed these matters. Two in particular, *Pizzarella* and *Willits*, may have decided these in favor of the taxpayers.

What happened is, we recognized the problems that we would have in showing that the Government—that we could not prevail on the merits as to the whole assessment, so what normally you would do is, you would wait for 6 months—rather, you would file a return at the end of the year, assume that you had an assessment of $200,000, assume that they seized $30,000 worth of assets, and you show $10,000 of tax liability. So your return would show $20,000 tax due back to you as a refund. You would commence your refund action after waiting 6 months from the filing of the return, and the Justice Department did not entertain—did not move to dismiss these, because they could not, because they had made the argument that the court had jurisdiction in the case called *Irving*.

Now, after you filed these refund lawsuits, though, something very peculiar happened. The Government would serve upon you interrogatories, or they would schedule to take the deposition of your client. Now, bear in mind, your client generally was awaiting trial for certain State charges or Federal charges, and the questions would be designed to elicit information concerning the extent of their involvement in some illegal activity. You obviously had to invoke the fifth amendment, and when you invoked the fifth amendment, the Government promptly moved forward and filed a motion to dismiss with prejudice.

Their contention was that you are the plaintiff. You brought this action. You refused to submit to discovery, and we have a right to dismiss the case with prejudice.

And by the way, they also filed a counterclaim for the extent of the assessment, so if you were suing for $20,000 back and there was a $110,000 assessment on the books, and they had collected $20,000, they would counterclaim for $90,000, and they would move forward in their counterclaim and say, let us dismiss this complaint and give us judgment on our counterclaim, because he is invoking the fifth amendment.

Now, at the beginning, some courts began to accept this argument, the Justice Department lawyers being as well prepared as they were, and general counsel across the country not being very adept in these areas, but the seventh circuit reversed a lower court dismissal, and this is what the court said, in *Williamson*.

It said, normally, a plaintiff that seeks affirmative relief cannot rely upon his fifth amendment right. But the situation at hand was quite different, for the Internal Revenue Service, in actuality, triggered the series of events that led up to this individual being a plaintiff, only in a technical sense.

I also invite this committee's attention to the case of *U.S. Coin and Currency* v, *The United States*, concerning a civil forfeiture of property, which the Supreme Court said you cannot have. After losing these motions to dismiss, the Government attorneys recognized that they were not going to win the cases when they went to trial, on the basis of the assessments, and so, we began to see the motion to stay filed by the Government.

And what they did is, in essence, they said, well, your honor, we want this case held in abeyance until the criminal statute of limitations

expires. Normally, that was 6 years. Although these were quasi-criminal cases, some judges across the country said, fine. I am going to stay the proceeding until the relevant statute of limitations expires.

Meanwhile, what happens—the assessment remains on the books. All of the taxpayer's property is tied up. And he has to wait for 6 years until he has a right to litigate the removal of those assessments.

Now, the pivotal legal issue, in terms of the Tax Court, has been whether a taxpayer has a right to a statutory notice of deficency, which otherwise is known as the ticket of admission. The Tax Court has said, in the *Jones* case, that without a statutory notice, they do not have jurisdiction, and they refused to take sides in this controversy.

I think the conclusion we can draw from the whole area of litigation, which has been substantial, and of course, generally free to the taxpayers involved, since all of their money was normally tied up, is that the resort is too often the temptation of Government. They have a larger pursestring than any taxpayer, and they have more endurance than any taxpayer. We have seen, as a consequence, that we have not had the prompt judicial review of the arbitrary action of the Internal Revenue Service, and in all but one of my cases, no statutory notice has ever been issued in any of my cases, and these have been pending for several years, including the *Lisner* case. And I can go on and name others.

I think, in conclusion, that we can say that there have been substantial abuses, and they have been rampant. Little regard, I believe, has been given to individual rights, because properties have been sold at deflated values. We have seen deprivation not only of due process but of equal protection. And we have also seen an unintentional waiver of some fifth amendment rights against compulsory self-incrimination in those cases where a taxpayer attempts to go forward and protect his property, believing that if he does not waive his fifth amendment, the court will dismiss the action against him.

And we have also seen a denial of the right to counsel, under the sixth amendment, where, in many cases, these individuals have not had moneys to retain a lawyer of their choice.

Finally, I believe commonsense has returned to some of those at the Commissioner's Office, as witnessed by Mr. Alexander's most recent pronouncement. But what will be done in those thousands of cases across the country where no statutory notice has been issued? What can be done to assure that the wrongs will be righted? What will be done to assure that the recorded tax liens based upon spurious assessments will be removed? What can be done to compensate those individuals whose assets have been sold at deflated value, based upon assessments which perhaps are illegal in the first instance? What will be done to assure that these spontaneous assessments will not be used again for some political or personal reason of the one who wields this awesome power?

Now, I have heard, and it has been said, that the narcotics project and the special enforcement project were isolated war parties, that they were aberrations, and that most IRS officials were well-meaning officials, and I would agree, as a former IRS official. But the fact that these programs, Mr. Chairman, have gone on unchecked shows a latent, frightening mentality in some officials at the Internal Revenue Service that the end justifies the means.

Upon reflection, was not the cure worse than the disease? Does it not show that in this country at least, based upon the present state of the law, that this Government has the means to rationalize confiscation of one's property under the guise of tax administration?

My recommendations are basically as follows. I have reviewed your proposed legislation, and I believe that the show cause order should be available to all taxpayers who are faced with a spontaneous assessment, whether it is under section 6861, 6851, and 6862. The present statute does not provide for a show cause order, under 6862.

Tax Court review, in the form of a statutory notice, should be made available to all taxpayers who are faced with a spontaneous assessment. I know that a bill is pending now before the House on this, and I would expand the right to a statutory notice to those that are jeopardy assessed under 6862.

Most important is the question on the presumption of correctness. Now, when we go into a courtroom, and the Commissioner has a presumption of correctness, even though he has an assessment which was computed in the fashion which I just described, I think that a show cause hearing should be a true show cause hearing, and that is that the presumption of correctness should be nullified, and the burden of proving reasonableness should be on the Commissioner. The basis of evidence relied upon should likewise meet the test of admissibility.

Wiretap evidence should not be permitted to be included. Hearsay statements of informants should not be permitted to show reasonableness. And this comes up in the context of, was he a reliable informant? And I say, "Yes, he was." I lose.

The Government should not be permitted to stay the show cause hearing by attempting to show my client, the taxpayer, where he tries to elicit testimony, which will incriminate that individual. The Government should have the burden of proving the deficiency, the amount. It should not be incumbent upon the taxpayer to prove he owes no tax. He should be permitted to remain silent, and let the Government prove that they can substantiate the method that they used in the computation, and, therefore, his silence, the taxpayer's silence—he should not permit the Government to draw an adverse inference.

Otherwise, what you are going to see is an end run around your legislation. If you permit the Government lawyers to call the taxpayers and elicit incriminating statements from them, this statute will be hollow.

Finally, if the taxpayer prevails, I believe he should be entitled to recover his cost, plus reasonable attorney's fees. That is the end of my prepared text.

Senator HASKELL. Well, this whole area is news to me. What you are recommending is basically that the Government should make the same showing that a private party would make in getting a temporary restraining order. Is that basically what you are saying?

Mr. SILVER. I think it is a little more broad than that. I think if we go to our cases in the pregarnishment law where you cannot garnish unless you go forward and have a hearing——

Senator HASKELL. Right.

Mr. SILVER. I think we could probably say, yes, that is true, except that we should have the right to a confrontation; we should have a right to cross-examine their witnesses. Now, under the proposed legislation, they have the right to go ahead and jeopardy assess, but the

taxpayer has a right to go in within 10 days and make them show cause of why that assessment should remain on the books, and so that, perhaps, is a compromise.

The only other way that you would do it is to turn around and have, in essence, what we call a pregarnishment hearing, and that is not what your present legislation appears to do.

So, the assessment has already been made; then the taxpayer walks into court and says, ah-hah, Judge, I want a show cause hearing. Now it strikes a balance, and I think it is a reasonable balance, quite frankly, that in certain instances the Government should have a right to hold things in status quo where they believe someone is going to depart the country with taxable funds, whereas if you use your pregarnishment hearing device, you are going to lose the valuable time factor, and it would not be very effective. You may as well just wipe out your jeopardy assessment provisions.

Senator HASKELL. Well, one of the questions I was going to ask you, is, in your opinion, there are certain times when the Government should be able to just go ahead and seize. Is that what you were saying?

Mr. SILVER. I think if you look to the intent of the legislation, that there may be instances which are applied sparingly, which would justify a seizure to protect the tax revenue.

Senator HASKELL. How are you going to be sure? Do not forget we are dealing with humans. The rule would be just great if there were not humans who cause the troubles, and you give the Government authority to go in and seize if they think the man is going to depart the country. Well, if you have an official who is not doing his job—and I would say, some of the officials that you are talking about did not really do their job very well—you could easily write down, I think this guy is going to depart the country, boom.

Mr. SILVER. Well, quite frankly, Mr. Chairman, I am one who really believes if you want the true answer, that the rights to seizure should be limited and should not be given to the Internal Revenue Service at all, but I also recognize the reality of the situation and that is that the legislation originally was intended to be applied in a limited set of circumstances and, so, what I am suggesting is a compromise, and the compromise is your proposed legislation, vis-a-vis the show cause order, but make very clear that you have a right to go before an impartial judiciary and have the Government sustain the burden. This will put a dampening effect upon the Government, particularly when you add the attorney fee provision, because once they start losing these cases in these Federal courts across the country, you are going to see that these are not going to be used. They are not going to be used as much as they have in the past, but I do not know if I would agree with you. I do not know what your position is, but I would tell you——

Senator HASKELL. I do not know what my position is either because this is all news to me.

Mr. SILVER. I would prefer to see a limited form of a pregarnishment hearing before you go out and seize.

Senator HASKELL. I would think so. I would think that when you are talking about this type of extraordinary power, you would at least have to have a pregarnishment hearing even if it was an ex parte hearing, for a court to issue a temporary restraining order, possibly even the posting of bond, I do not know.

Mr. SILVER. Well, the procedure, for example, you go before an impartial magistrate and you obtain a search warrant. There is some showing at that point to someone independent of the Service.

Senator HASKELL. And, if I were going in for that kind of order, I would be pretty careful what I told the judge. Now, do you think this would slow down or hamper the Internal Revenue Service's ability to enforce the tax laws?

Mr. SILVER. No; I do not, Mr. Chairman.

Senator HASKELL. Now, I do not think it is in the record but, as I understand it, you were a lawyer with the Internal Revenue Service at one time. Am I correct?

Mr. SILVER. Yes; that is correct.

Senator HASKELL. How many years were you there?

Mr. SILVER. I was 4 years with the Internal Revenue Service as a trial lawyer.

Senator HASKELL. Now you are in private practice?

Mr. SILVER. Yes.

Senator HASKELL. How long have you been in private practice?

Mr. SILVER. I have been in private practice a little over 4 years.

Senator HASKELL. So that is equally balanced then.

Well, you have given me your opinion. Let me ask you again, do you feel that making the Government go in and get some kind of ex parte order, comparable to a temporary restraining order situation, would inhibit the Government's rights?

Mr. SILVER. I do not think it would inhibit the Government's rights. I think it would permit the Government to apply this law with a better review procedure in mind because, as I stated to you, this law has been applied by the district directors' offices across the country without prior review by a lawyer.

It has been my experience when lawyers from regional counsel review proposed jeopardy assessments, that they have normally culled the bad ones out. Now, if you have that same procedure where they can be notified, and they can cull the bad ones out, and then they walk it across the street to the U.S. attorney, who in turn presents it to a judge ex parte, with a judicial procedure there, I think that you are going to find that only those that are reasonable, or at least have a semblance of reasonableness based upon what is presented, will be made.

So, I think, yes, I think it may be a good idea to do that. But, what I am trying to get here——

Senator HASKELL. Let me ask counsel if he has any other questions.

Well, thank you, Mr. Silver. Did I interrupt you? Were you in the middle of saying something?

Mr. SILVER. No, sir.

Senator HASKELL. Thank you very much for coming here. You have presented very clearly and very well that something has got to be done. Thank you very much.

Mr. SILVER. Thank you, Mr. Chairman.

[The prepared statement of Mr. Silver follows. Oral testimony continues on p. 37.]

PREPARED STATEMENT OF STEPHEN E. SILVER[1]

SUMMARY

I. INTRODUCTION

The use of spontaneous assessments as a tool of law enforcement is of recent origin. On June 17, 1971, in a pronouncement emanating from then President Nixon, a "new, all-out offensive" upon those engaged in alleged illegal activities was launched and the Internal Revenue Service, as an equal participant in the war, established as a high priority program, its now infamous Narcotics Traffickers Project. The arsenal of weapons included power of summary seizure, termination of taxable years and jeopardy assessments. In the Internal Revenue Manual, the program was stated to be as follows:

"The purpose of IRS participation in the Narcotics Project is to disrupt the distribution of narcotics through the enforcement of all available tax statutes. Therefore, there may be cases where civil enforcement actions may be an extremely effective and timely means of accomplishing the objectives of the project. . . . Maximum use will be made of jeopardy, quick, and transferee assessments, and termination of taxable period."

In another section of the Internal Revenue Manual, the following statement is made:

"The Collection activity's role is primarily to secure by levy and seizure action the trafficker's assets. When a trafficker has no money, he cannot buy drugs to sell on the streets. Accordingly, seizing money from traffickers is one of the most effective means of ridding the country of the menace of drug abuse."

In Arizona, A. W. McCanless, who was then district director, in an internal directive dated March 8, 1972, gave the following instructions to his field personnel:

"The Phoenix District is fully committed to the narcotics traffickers project. An integral function to the success of the operation is the prompt termination of tax years, etc. When we are in possession of facts which warrant such action . . . procedures will be developed so that terminations, etc., can be made in less than two hours . . . Emergency situations may be handled orally and covered thereafter by written reports."

For the next three years, the IRS used the spontaneous assessment in wholesale fashion and as its authority, to justify what amounted to confiscation of property without due process, relied upon an old 1918 law, originally designed to prevent aliens from departing the United States with taxable funds.

II. STATUTORY FRAMEWORK

To assure that individuals, either citizens of the United States or aliens, do not depart from the United States owing taxes, section 6851 was initially enacted in 1918. Under its provisions, the Commissioner of Internal Revenue, under certain prescribed conditions, may declare the taxable year terminated and start immediate proceedings to collect the taxes believed due and owing for the terminated period. A termination may result before or after the taxable year has ended, but before the due date for filing the return.

By contrast, a jeopardy assessment made under the provisions of section 6861 normally results prior to normal assessment, when it is determined either that the tax reported on a return is understated and the taxpayer, in the opinion of the Commissioner, will owe additional taxes or deficiencies, or in the case of a nonfiler, delinquent taxes. The spontaneous assessment provisions under sections 6851 and 6861 apply only to income, estate and gift taxes, whereas the jeopardy assessment provision of section 6862 applies to any other tax, such as excise taxes.

The income tax deficiency procedures provided under section 6213(a), including the right to judicial review in Tax Court, applies to all assessments made

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under section 6861, whereas tax assessed under section 6862 requires payment before the taxpayer has the right to litigate and tax Court review is not available, and the Internal Revenue Service takes the position that the terminated taxpayer has no right to judicial review in the Tax Court.

Although the terminated taxpayer may stay collection and prevent forced sale by posting bond, this remedy is often illusory, for the taxpayer's assets are generally insufficient to guarantee collection of the liability. However, property interests of section 6861 jeopardy assessment taxpayers are protected against forced sale if a petition is filed with the Tax Court, but the stay of the sale of seized assets is not applicable to assessments made under section 6862.

III. IRS GUIDELINES

The Internal Revenue Manual sets forth intended guidelines that are supposed to be followed in making spontaneous assessments. Common to these guidelines is the stated admonition that the spontaneous assessment should be used "sparingly" and care should be taken to avoid excessive and unreasonable assessments. As applied to the narcotics project, this stated provision was not applicable.

The review procedures relating to spontaneous assessments made under sections 6861, 6862 and 6851 are, for all essential purposes, the same, except with respect to departing aliens. For example, in determining whether an assessment should be made, the Internal Revenue Manual requires that at least one of three conditions exist:

(a) The taxpayer is or appears to be designing quickly to depart from the United States;

(b) The taxpayer is or appears to be designing quickly to place his property beyond the reach of the government; and/or

(c) The taxpayer's financial solvency is or appears to be imperiled.

In what are referred to as "prima facie cases," certain conditions and circumstances can properly be considered as establishing facts sufficient to make the assessment. Some examples of cases considered to be prima facie are:

(a) Major operators in the criminal field, irrespective of present financial condition.

(b) Individuals generally known to frequently wager large amounts.

(c) Individuals engaged in taking wagers, irrespective of whether major, secondary or minor operators.

(d) Individuals engaged in other activities generally regarded as illegal.

(e) Individuals with a background and history of engaging in illegal activity, such as gambling, bootlegging, narcotics, etc., who are engaged in so-called legitimate business ventures.

(f) Individuals engaged in a legitimate business but who are consistently suffering business or personal losses.

(g) Individuals against whom large damage suits are pending or against whom such suits are threatened.

Based upon delineated guidelines, in general, a different standard has been used for those believed to be engaged in illegal activity, and basic questions concerning denial of equal protection become evident.

IV. USE OF SPONTANEOUS ASSESSMENT

A. Narcotics project

After then President Nixon announced the new all-out offensive upon drug abuse, a representative pattern quickly emerged. Contemporaneous with a taxpayer's arrest on suspicion of trafficking in narcotics, his available cash was confiscated by the police as "evidence" and Internal Revenue Service personnel were notified immediately. Shortly after the arrest, usually at the jail, a termination notice, in letter form, was given to the taxpayer. This formal notice and demand for payment of the spontaneous assessment waived the normal ten-day payment period. Because the taxpayer was unable to pay the amount demanded, a spontaneous termination assessment was made, followed by the seizure of all property, including the confiscated cash being held by the police as "evidence."

In many of these instances, Internal Revenue Service personnel were notified in advance of the arrest and were therefore present at the time of arrest. IRS officials were also invited to participate in searches authorized by warrants executed by the local law enforcement authorities. Although the warrants were limited to seizing paraphenalia related to alleged illegal activity, IRS agents participated in the search and as a result, often asked the local enforcement

officials to seize financial information they felt relevant, which was done. It was not uncommon for the IRS officials to tape record what they saw visually as it related to documents observed during the search which were not described in the search warrant or included in the inventory of the search.

With all the property of a taxpayer seized or tied up by liens and levies, the taxpayer was often unable to employ counsel of his choice, which singularly raises serious Sixth Amendment questions.

B. Special enforcement program

The use of the spontaneous assessment was promptly expanded to gamblers and others believed to be involved in certain illegal activities. When the IRS initiated its "Special Enforcement Program" (SEP) on June 30, 1971, and in particular, what was labeled the "Racketeer, Wagering and Coin-operated Gaming Device Program, Organized Crime Drive and Strike Program," the use of spontaneous assessments was encouraged. This soon led to a practice routine under the Narcotic Traffickers Project.

C. Type of evidence relied upon

The IRS teams relied upon various types of evidence in computing the amount of the assessment. The evidence included information received directly from wiretaps as well as the items seized by local law enforcement authorities at the time of arrest. Reliance upon the hearsay statements of informants also provided a basis for making a spontaneous assessment computation.

In most instances, the evidence was then interpolated for a 12 month period. For example, if an alleged gambler was overheard taking $100 in wagers in one day, this was interpolated for a 365 day period. Similarily, if an individual who was arrested had 5 pounds of marijuana on his person, it was assumed that this person sold 5 pounds a day for a certain period at a certain profit margin.

D. Type of property seized

Cars, houses, businesses, boats, and bank accounts were all seized and shortly thereafter, scheduled for public auction.

V. JUDICIAL REMEDIES

A. Introduction

Although it began somewhat slowly, counteractions by the courts did begin. Perhaps best representative of judicial commentary at the appellate level are the remarks by Judge Clark of the Fifth Circuit in *Willits* v. *Richardson*:

"The IRS has been given broad power to take possession of the property of citizens by summary means that ignore many basic tenets of pre-seizure due process in order to prevent the loss of tax revenues. Courts cannot allow these expedients to be turned on citizens suspected of wrongdoing—not as tax collection devices but as summary punishment to supplement or complement regular criminal procedures. The fact that they are cloaked in the garb of a tax collection and applied only by the Narcotics Project to those believed to be engaged in or associated with the narcotics trade must not bootstrap judicial approval of such use."

Trial judges observed the absurdity of what were found to be patently arbitrary and capricious assessments. In the forefront was federal district court judge Walter E. Craig of Phoenix, who granted an injunction against an assessment made against a taxpayer whose house and automobile had been seized based upon a spontaneous assessment of $244,314. In remarks made at the conclusion of trial, Judge Craig observed:

"It taxes the credulity of the Court, and I suspect any reasonable court, to give any merit to the method of calculation and the computation worksheet.

"This court is certainly favorable to cooperation between state and federal agencies, but I think it is a miscarriage of that principle to use the Internal Revenue Service as an arm for state enforcement of criminal proceedings. And I don't think Congress ever intended that the IRS be used for that purpose."

B. Injunctive relief

One of the taxpayer's principal weapons to counter the effect and immediate impact of a spontaneous assessment has been the temporary restraining order. Although section 7421(a) provides in general that no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court, a judicial exception was carved out by the Supreme Court in *Enochs* v. *Williams Packing & Navigation Co., Inc.*

The taxpayer who files such a lawsuit must show not only that he will prevail on the merits, but also, that he will suffer irreparable harm if an injunction is not granted, which is just another way of saying there is no adequate remedy at law.

The practical effect of the Enochs confrontation has been to entitle taxpayers to a temporary restraining order and an evidentiary hearing. In some outrageous instances, the courts have permitted the injunction lawsuit to crystallize the issue without the necessity of further litigation.

C. Refund lawsuit

The Second Circuit, in affirming the lower court in *Irving*, found that the terminated taxpayer has the right to have the assessment reviewed in the district court without paying the full amount of the tax. This led to the practice of the taxpayer filing a return and after waiting six months, commencing a refund lawsuit.

Shortly after the taxpayer filed the plenary refund suit, the Government would usually serve interrogatories upon or take the deposition of the taxpayer. Generally, the taxpayer has vulnerability as it relates to alleged violations of state and/or federal criminal statutes for which the statutes of limitation have not run. The questions are directed toward obtaining admissions from the taxpayer concerning the volume of the individual's participation in the alleged illegal activity. When the taxpayer invoked the Fifth Amendment, the Government routinely moved to dismiss the complaint with prejudice on the grounds that the taxpayer as plaintiff has the burden of proof and his failure to submit to discovery is grounds to dismiss as a sanction.

Although, at the beginning, some courts accepted the Government's argument, the Seventh Circuit in *Williamson* rejected it. The Seventh Circuit reversed the lower court's dismissal by pointing out that although normally a plaintiff seeking affirmative relief cannot rely upon the Fifth Amendment, the situation at hand was quite different, for the IRS in actuality triggered the series of procedures that resulted in the taxpayer being the plaintiff, only in the technical sense.

After losing motions to dismiss, and recognizing that the basis of the assessments would not win the day for them in court on the merits, the Government began to use the motion to stay as a means of holding the case in abeyance until the expiration of the applicable criminal statutes of limitation. Although these refund lawsuits are in essence quasi-criminal, some district court judges have been granting stays, which have the effect in some cases of tying up a taxpayer's property for a substantial period of time.

D. Tax court

The pivotal issue is whether a terminated taxpayer is entitled to a statutory notice of deficiency, otherwise known as the ticket of admission to the Tax Court. Without a statutory notice, the Tax Court does not have jurisdiction, and the Tax Court refuses to take sides in the legal controversy.

E. Conclusion

Resort to litigation is all too often the temptation of government, which has a larger purse and more endurance than any taxpayer. As a consequence, litigation in the courts has not provided the taxpayer prompt judicial review of the arbitrary actions of the IRS, and in all but one of my cases, no statutory notice has ever been issued, notwithstanding the fact that the assessments have been on the books for several years.

VI. CONCLUSIONS

There has been substantial abuse of power by the IRS since President Nixon's mandate was given in June 1971. Since that time, the use of the spontaneons assessment has been rampant, with little regard given to the rights of the individual whose properties were summarily seized and sold at deflated values. These spontaneous assessments have resulted not only in deprivations of the individuals rights to due process and equal protection, but also, some unintentional waivers of one's Fifth Amendment rights against compulsory self-incrimination in order to preserve property rights, as well as denying some taxpayers their Sixth Amendment right to counsel of their choice because their property was not available to pay legal fees.

Finally, common sense has returned to some of those who have wielded this awesome power, as reflected by Commissioner Alexander's most recent pronouncement. But what will be done in those thousands of cases across the country where

the IRS has still not issued a statutory notice of deficiency? What can be done to assure that the wrongs already done will be righted by removing recorded tax liens based upon these spurious assessments? What can be done to assure that the use of the spontaneous assessment will not be used for political or personal purposes of the one who wields this awesome power?

Although some will say that the NTP or SEP war parties were isolated aberrations, and most IRS officials are well meaning public officials, the fact that programs like these were permitted to go unchecked shows a latent frightening mentality in government that the end may justify the means. Upon reflections, was not the cure far worse than the disease, for it violated the very tenets this nation cherished when it began the great adventure toward individual rights almost two hundred years ago? Does it now show that, in this land, government has the means to rationalize confiscation of a citizen's property under the guise of tax administration?

VII. RECOMMENDATIONS

Upon review, two areas of your proposed bill need further clarification.

1. The Show Cause Order should be available to taxpayers who are jeopardy assessed under section 6862 as well as sections 6861 and 6851.

2. Tax Court review, in the form of a statutory notice, should be made available to taxpayers who are jeopardy assessed under section 6862.

3. The normal presumption of correctness that attaches to a jeopardy assessment should be nullified and the burden of proof to prove reasonableness should be placed upon the government. The basis of the evidence relied upon should likewise be required to meet the evidentiary standards of admissibility.

4. The government should not be permitted to stay the show cause by attempting to elicit testimony from the taxpayer which may be incriminating, but rather, the government should have the burden of providing whether any deficiency exists and if so, that amount. It should not be incumbent upon the taxpayer to prove he owes no tax or the amount of the tax.

5. If the taxpayer prevails, he should be entitled to recover costs plus reasonable attorney fees.

STATEMENT

I. INTRODUCTION: CONSTITUTIONAL ISSUES

Considerable attention has recently been focused on the lack of pre-seizure due process [1] and denial of equal protection [2] associated with the use and abuse of spontaneous assessments by the Internal Revenue Service. Spontaneous assessments have permitted the Internal Revenue Service to effectuate immediate and swift collection of what is assessed as a tax without opportunity for prior judicial review [3].

The use of spontaneous assessments as a tool of law enforcement is of recent origin [4]. On June 17, 1971, in a pronouncement emanating from then President Nixon, a "new, all-out offensive" upon those engaged in alleged illegal activities was launched and concordantly, the Internal Revenue Service established as a high priority program [5], its now infamous Narcotics Traffickers Project [6]. The arsenal of weapons included power of summary seizure, termination of taxable years and jeopardy assessments.

Those engaged in the war were not inclined to delay the testing of their new weapon until the propriety of its use could be fully debated [7]. Instead, its use was promptly implemented and even expanded to gamblers and others believed to be involved in any alleged illegal activities other than just narcotics [8].

The swiftness and range of its application was felt across the nation and soon, scholars, judges and lawyers alike began to question the propriety of its use. Effective internal examination by the Government began only after the use of the spontaneous assessment began to receive critical headlines in the press [9] and other media.

Perhaps reacting to a critical Wall Street Journal article, on May 31, 1974, almost three years to the day after the program began, IRS agents were cautioned to be more selective in its use [10].

Finally, the reality of forfeiture that could result from the use of this spontaneous assessment was acknowledged and the use of the summary seizure has all but stopped since May 31, 1974, except in those instance that were within the original contemplation of the legislators [11].

II. STATUTORY FRAMEWORK

To assure that individuals (either citizens of the United States or aliens) do not depart from the United States owing taxes, section 6851 was initially enacted in 1918. [12] Under its provisions, the Commissioner of Internal Revenue under certain prescribed conditions may declare the taxable year terminated and start immediate proceedings to collect the taxes believed due and owing for the terminated period. A termination may result before or after the taxable year has ended, but before the due date for filing the return. [13]

By contrast, a jeopardy assessment made under the provisions of section 6861 normally results prior to normal assessment, when it is determined either that the tax reported on a return is understated and the taxpayer, in the opinion of the Commissioner, will owe additional taxes or deficiencies, or in the case of a nonfiler, delinquent taxes. [14] The termination provision may apply to taxes owed by both corporations and individuals which would include liability for income, estate, gift, excise and all other taxes. The jeopardy assessment provision under section 6861 applies only to income, estate and gift taxes, whereas section 6862 applies to any other tax, such as excise taxes. [15]

The income tax deficiency procedures provided under section 6213(a), including the right to judicial review in Tax Court, applies to all assessments made under section 6861, whereas tax assessed under section 6862 requires payment before the taxpayer has the right to litigate and Tax Court review is not available. [16]

Although the terminated taxpayer may stay collection and prevent forced sale by posting a bond, this remedy is often illusory for the taxpayer's assets are generally insufficient to guarantee collection of the liability. [17] However, section 6861 jeopardy taxpayers' property interest are protected against forced sale if a petition is filed with the Tax Court, but the stay of the sale of seized assets is not applicable to assessments made under section 6862. [18]

III. IRS GUIDELINES

The Internal Revenue Manual sets forth intended guidelines that are supposed to be followed in making spontaneous assessments. Common to these guidelines is the stated admonition that the spontaneous assessment should be used "sparingly" and care should be taken to avoid excessive and unreasonable assessments which are subject to high level administrative review both before and after their imposition. [19] Although the Internal Revenue Manual states that assessments made under the termination provisions of section 6851 "are not in a technical sense jeopardy assessment," [20] the review procedures relating to jeopardy assessments made under sections 6861, 6862 or 6851 are for all essential purposes the same, except with respect to departing aliens. For example, in determining whether an assessment should be made, the Internal Revenue Manual requires that at least one of three conditions exist:

(a) The taxpayer is or appears to be designing quickly to depart from the United States;

(b) The taxpayer is or appears to be designing quickly to place his property beyond the reach of the Government; and/or

(c) The taxpayer's financial solvency is or appears to be imperiled. [21]

In what are referred to as "prima facie cases," [22] certain conditions and circumstances can properly be considered as establishing facts sufficient to make the assessment. Some examples of cases considered to be prima facie are:

(a) Major operators in the criminal field, irrespective of present financial condition.

(b) Individuals generally known to frequently wager large amounts.

(c) Individuals engaged in taking wagers, irrespective of whether major, secondary or minor operators.

(d) Individuals engaged in other activities generally regarded as illegal.

(e) Individuals with a background and history of engaging in illegal activity such as gambling, bootlegging, narcotics, etc., who are engaged in so-called legitimate business ventures.

(f) Individuals engaged in a legitimate business but who are consistently suffering business or personal losses.

(g) Individuals against whom large damage suits are pending or against whom such suits are threatened.

In the situations covered by examples (a) through (e), prior approval by the District Director is required. However, such approval can be given orally and in fact, many district directors formalized this policy by permitting the assessments to be made in less than two hours and thereafter supported by written reports prepared after the spontaneous assessment was made. [23]

Based upon the delineated guidelines, in general a different standard has been used for those believed to be engaged in illegal activity. [24]

IV. USE OF SPONTANEOUS ASSESSMENT

A. Narcotics project

After then President Nixon announced the new all-out offensive upon drug abuse, "America's public enemy No. 1," the rapidity, zest and zeal with which the program was implemented makes one wonder if indeed, Internal Revenue Service line employees are the unthinking and blindly loyal amanuenses of their supervisors' dictates.

A representative pattern quickly emerged. Contemporaneous with a taxpayer's arrest on suspicion of trafficking in narcotics, his available cash was confiscated by the police as "evidence" and Internal Revenue Service personnel notified immediately. Shortly after the arrest, usually at the jail, a termination notice, in letter form, was given the taxpayer. If the taxpayer either refused or was unable to pay the amount demanded, a spontaneous termination assessment was made, followed by the seizure of all property, including the confiscated cash that was being held by the police as "evidence." In many of these instances, Internal Revenue Service personnel were notified in advance of the arrest and were therefore present at the time of arrest. [25]

With all the property of a taxpayer seized or tied up by liens and levies, the taxpayer was often unable to employ counsel of his choice, which singularly raises serious Sixth Amendment questions. [26]

Although it began somewhat slowly, counteractions by the courts did begin and perhaps best representative of judicial commentary at the appellate level are the remarks by Judge Clark of the Fifth Circuit in *Willits* v. *Richardson*: [27]

"The IRS has been given broad power to take possession of the property of citizens by summary means that ignore many basic tenets of pre-seizure due process in order to prevent the loss of tax revenues. Courts cannot allow these expedients to be turned on citizens suspected of wrongdoing—not as tax collection devices but as summary punishment to supplement or complement regular criminal procedures. The fact that they are cloaked in the garb of a tax collection and applied only by the Narcotics Project to those believed to be engaged in or associated with the narcotics trade must not bootstrap judicial approval of such use." [28]

Trial judges observed the absurdity of what were found to be patently arbitrary and capricious assessments. For example, in the forefront was federal district court Judge Walter E. Craig of Phoenix who granted an injunction against an assessment made against a taxpayer whose house and automobile had been seized based upon a spontaneous assessment of $244,314. [29] In remarks made at the conclusion of trial, Judge Craig observed:

"It taxes the credulity of the Court, and I suspect any reasonable court, to give any merit to the method of calculation and the computation worksheet.

"This Court is certainly favorable to cooperation between state and federal agencies, but I think it is a miscarriage of that principle to use the Internal Revenue Service as an arm for state enforcement of criminal proceedings. And I don't think Congress ever intended that the IRS be used for the purpose. . . ." [30]

Apparently, Judge Craig was not alone in his conclusion for now, even Commissioner Alexander has recognized that the IRS was engaged in an adventure which was directed "to achieve ends other than those of tax administration and tax enforcement" and reevaluation of that program is now underway. [31]

B. Special enforcement program

In 1968, the Supreme Court dealt a temporary blow to Government efforts to tax gamblers 10 percent on the gross amount of wagers accepted when it held, in the companion cases of *Marchetti* v. *United States* [32] and *Grosso* v. *United States* [33] that gamblers were not required to register and pay the federal occupational tax on wagering or to to file Form 730, Wagering Tax Return.

In *Marchetti*, the taxpayer was convicted of failing to pay the federal occupational tax on wagering. The conviction was reversed by the Court on the basis that the filing and registration requirements would incriminate him. The Court specifically found that the statutory obligation to register and pay the occupational tax would necessitate the filing of a return that would violate the taxpayer's Fifth Amendment privileges against compulsory self-incrimination. However, the Court made clear that their decision did not address itself to the question of whether the United States may tax activities which the states or Congress have declared unlawful. The Court stated that the unlawfulness of the activity did not prevent its taxation, but it refused to subscribe the theory that the method which Congress chose to collect the tax, the filing of these returns, was required if their filing might tend to incriminate these individuals.

The underlying rationale of the *Marchetti* and *Grosso* decisions was premised upon the simple fact that there were various federal statutes which imposed criminal penalties upon interstate transmission of wagering information, as well as state and local enactments which were even more comprehensive. The Court accordingly concluded that due to the reciprocal exchange of information between the states and the federal government, information from these federal returns could and would be used by law enforcement authorities, other than the tax collector, in pursuit of their ongoing criminal investigations. [34]

The defeat for the Government in *Marchetti* and *Grosso* proved only temporary, for IRS efforts to collect the wagering tax due from gamblers shifted from emphasis on sanctions associated with failure to register and file to the use of the jeopardy assessment under section 6862 as a means to collect the tax.

Under what designated "Special Enforcement Program" (SEP) by the IRS on June 30, 1971, [35] directed against those involved in illegal activities and in particular, what was labeled "Racketeer, Wagering and Coin-operated Gaming Device Program, Organized Crime Drive and Strike Program," the use of spontaneous assessments was encouraged. This soon led to a practice that was routine under the Narcotic Traffickers Project. Local law enforcement officials, working closely with IRS special agents who headed SEP teams which included as its members, revenue agents and revenue officers, were usually notified in advance of an arrest. The team members would often accompany local law enforcement officials at the time of the arrest and immediately after the arrest, generally at the jail, prior to when the arrested person could see his attorney, personally serve the formal notice and demand for payment of the jeopardy assessment which waived the normal ten-day payment period. Because the taxpayer either refused or was unable to pay the amount demanded, the spontaneous jeopardy assessment was made followed closely by the seizure of all of the taxpayer's known property. [36]

The SEP teams relied upon various types of evidence in computing the amount of the assessment. The evidence included information received directly from wiretaps as well as the items seized by local law enforcement authorities at the time of arrest. Reliance upon the hearsay statements of informants also provided a basis for making a jeopardy assessment computation.

One garden variety case where the IRS based the assessment solely on wiretap evidence was *James* v. *McKeever*. [37] The taxpayer's telephone had been tapped by officers of the Phoenix Police Department pursuant to a court order for a period of ten days in October of 1971. The information obtained from this wiretap was voluntarily furnished to the IRS. The IRS initially interpolated the information for the whole month of October and for the preceding 11 months, but then decided to make the assessment only for the month of October 1971, in the amount of $21,019.00. Based upon this assessment, which was made contemporaneously with the taxpayer's arrest for alleged illegal activities, the IRS quickly moved in and levied upon the taxpayer's bank account, and subsequently seized his home and car which were scheduled to be sold at public auction. The taxpayer obtained a temporary restraining order prohibiting the sale of his car and residence, for in his verified petition, it was alleged that the Government based its assessment solely upon evidence obtained through a wiretap, which evidence was obtained illegally and, therefore, could not be used as a basis of a tax assessment.

The Government followed its standard procedure in such cases and filed a motion to dismiss, citing the so-called anti-injunction provisions of section 7421 (a), which was denied. Thereafter, the taxpayer filed a motion to suppress, requesting the suppression of all tapes of intercepted oral telephone communications recorded at his residence and place of business and all evidence derived therefrom.

The court granted the motion to suppress for three reasons. First and most important in the context of the tax proceeding, it found that the IRS was not au-

thorized to receive or use wiretap evidence. The court found that 18 U.S.C. Section 2517(1), which permits an investigative or law enforcement officer who receives a wiretap to disclose the information gained from a tap to other such officers to the extent that such disclosure is appropriate to the proper performance of the official duties of the officer making or receiving the disclosure, did not apply to Internal Revenue Service personnel. Under 18 U.S.C. Section 2510(7) entitled "Definitions," an investigative or law enforcement officer is defined as ". . . any officer of the United States or of a state or political subdivision thereof, who is empowered by law to conduct investigations of or to make arrests for offenses enumerated in this chapter."

Those offenses referred to are specifically enumerated by title and section number in 18 U.S.C. Section 2516(1). The court found that nowhere in that section is any violation of the internal revenue laws, Title 26 U.S.C., listed. The Government, however, argued that the Internal Revenue Service agents are indeed allowed to investigate certain crimes similar to those enumerated, albeit under a separate title, Title 26. As a result, the Government contended that the Internal Revenue Service should be permitted to receive information acquired through wiretaps. The court found that it was clear that 18 U.S.C. Section 2516(1) should be given a strict construction. [38] The court further found that nowhere in Title 26 was the Internal Revenue Service given any authority to perform wiretaps and, again, nowhere is Title 26 mentioned in the wiretap statute. Thus, the court concluded that the great specificity with which 18 U.S.C. Section 2516(1) catalogs those offenses for which wiretap authorization may be granted would indicate a clear congressional intent not to permit wiretaps for revenue law violations. The court, therefore, held that there was an unauthorized disclosure of the intercepted communications by the Phoenix Police Department to the Internal Revenue Service and such disclosure was prohibited under the federal wiretap statute. [39]

Reliance upon wiretap evidence may lead the IRS to reexamine its position, [40] and its recent dismissal of its appeal in *James* [41] could indicate that it would rather present the issue to another circuit court [42] or back away entirely from the use of wiretap evidence. [43]

A second and apparently fruitful basis for jeopardy assessments has been evidence seized by local law enforcement officials. This was what occurred in *Pizzarello* v. *United States* [44] as well as *Janis* v. *United States*, [45] and both the Second and Ninth Circuits have agreed that, in the context of a tax proceeding, whether it is a proceeding brought under *Enochs* jurisdiction as was *Pizzarello* or a plenary tax refund as was *Janis*, illegally obtained evidence, including the fruits thereof, may be suppressed. [46]

V. JUDICIAL REMEDIES

A. Statutory notice and tax court

The pivotal issue of whether a terminated taxpayer is entitled to a statutory notice of deficiency is before the Supreme Court. A decision is expected this coming term. Without a statutory notice, the Tax Court does not have jurisdiction. [47]

The two leading district court cases supporting the proposition that a statutory notice must be issued to a taxpayer whose taxable year has been terminated are *Schreck* v. *United States* [48] and *Lisner* v. *McCanless*. [49] Both the Fifth Circuit in *Clark* v. *Campbell* [50] and Sixth Circuit in *Hall* v. *United States* [51] have now held that a tax assessed under section 6851 is a deficiency within the ambit of sections 6211 and 6861. Accordingly, failure to issue a deficiency notice within 60 days from assessment under section 6861(b) is grounds for an injunction under section 6213(a) and the anti-injunction provisions of section 7421(a) are not applicable.

Support for the Government's position that a section 6851 liability is not a deficiency is found in the district court case *Irving* v. *Grey* [52] and both the Second Circuit in *Laing* v. *United States* [53] and Seventh Circuit in *Williamson* v. *United States* [54] have held that an assessment made under section 6851 and section 6201 is not a deficiency within the purview of section 6211 for which section 6212(a) requires issuance of a statutory notice of deficiency. Suffice it to say that the issue will be resolved when the Supreme Court rules on the issue this term. [55]

The opinion in *Schreck* deals exhaustively with the legislative history and the effectiveness of using legislative history as an analytical tool in determining whether the proper assessment authority is section 6201 or section 6861. [56]

Similar to the legislative history analysis is the "code structure" concept authored by the Federal District Court of Arizona in *Lisner*. [57] The *Lisner* court found three separate sources of assessment authority: "ordinary" assessments, authorized by section 6201; "deficiency" assessments, authorized by section 6213; and "jeopardy" assessments, authorized by section 6861. The court reasoned that an assessment after a section 6851 termination was either authorized by one of these three sections or was implicitly authorized by section 6851 itself. [58] Noting that section 6861 follows section 6851 and that both sections were enacted under the general title "Subchapter A—Jeopardy," the Arizona District Court concluded that assessments after section 6851 terminations were authorized by section 6861. To adopt any other construction of the Internal Revenue Code, the court explained, would be to "ignore plain English."

The Sixth Circuit in *Rambo* v. *United States*. [59] adopted the *Lisner* rationale by finding the fact that section 6861 was the next succeeding section in the same subchapter persuasive of congressional intent that section 6861 should provide the needed authority for assessments after section 6851 terminations. [60] Both *Rambo* and *Lisner* found the inference reasonable because of the proximity of the sections and because section 6861 was the only section designated as the "jeopardy" assessment authority. [61]

The *Irving* district court held that no statutory notice of deficiency had to be issued in conjunction with the termination of taxable year pursuant to 6851 because the assessment was made under section 6201(a). The underlying rationale was that since section 6201(a) and section 6851 existed prior to section 6861, there was obvious authority under section 6201(a) to make an assessment for a terminated year. [62] The Second Circuit in *Irving* [63] in affirming the lower court found that the terminated taxpayer has the right to have the assessment reviewed in the district court without paying the full amount of the tax assessed notwithstanding the Supreme Court full payment rule of *Flora* v. *United* States. [64] In concluding that the full payment rule was inapplicable to the terminated taxpayer, the Second Circuit reasoned that in *Flora*, "a deficiency had been determined and the taxpayer had paid only a portion of it before seeking his refund claim in a federal district court [whereas] [h]ere, . . . no deficiencies has yet been determined." [65] The rationale of *Irving* lacks merit for it is fairly evident that the Supreme Court in *Flora* viewed the question of full payment in terms of an assessment when it said:

"The question presented is whether a Federal District Court has jurisdiction . . . for the refund of income tax payments which did not discharge the entire amount of his assessment.

". . . [F]ull payment of the assessment is a jurisdictional prerequisite to suit." [66]

The Tax Court has refused to take sides in the controversy, having held that the form letter of termination is not a deficiency notice within the meaning of section 6212 and therefore, the Tax Court is without jurisdiction. [67]

The question, when further refined, requires analysis as to the reasons a taxpayer would prefer to have a statutory notice issued before proceeding to court.

Somewhat obvious is the fact that if a termination is construed as a jeopardy assessment, the Government cannot sell seized assets if a petition is filed in Tax Court. [68] But somewhat more central to the issue is the realization that once the matter gets in docketed status before the Tax Court, there exists a good possibility that the burden of proof normally on the taxpayer to prove the deficiency is erroneous, may be shifted to the Government [69] if it can be shown that the assessment was computed in an arbitrary and capricious manner. Such a determination could be made by the Tax Court prior to trial if an appropriate motion was filed. [70]

The Government, to counter the obvious due process arguments made by the taxpayer in *Irving* [71] that the terminated taxpayer had no available forum, argued that either the United States District Court or the Court of Claims has jurisdiction. [72] The Government specifically contended in *Irving* that the full payment rule of *Flora* was not applicable to a terminated taxpayer for his tax return would be treated equivalent to an informal claim for refund and after the requisite six months, he could file a plenary refund lawsuit.

The argument apparently won the day for the Government in *Irving*, but in refund cases filed by terminated taxpayers since *Irving*, the Government in its answer has raised as an affirmative defense, lack of jurisdiction on the grounds that the taxpayer has not made full payment of the assessment under the rule of *Flora* [73]

The taxpayer who is assessed under section 6862 for taxes other than income, estate and gift taxes does not have the right to proceed to Tax Court. However, full payment of the tax is avoided since this is a divisible tax and a judicial determination of the assessment is therefore available.[74] However, there is no comparable provision concerning the stay from sale of seized property which applies to the taxpayer who has a jeopardiy assessment imposed upon him under section 6861. This has lead to the practice of filing an injunctive lawsuit in order to preserve the status quo during the pendency of the refund suit where the Government refuses to administratively stay collection action. [75]

B. Refund action

The Government in the refund actions, perhaps reflecting a mirror image of the intent of then President Nixon when instituting the NTP and SEP adventures, has attempted to work a civil forfeiture of the taxpayer's property.

Shortly after the taxpayer files the plenary refund suit, the Government will usually serve interrogatories upon or take the deposition of the taxpayer. Generally, the taxpayer has vulnerability as it relates to alleged violations of state and/or federal criminal statutes for which the statute of limitations has not run. The questions are directed toward obtaining admissions from the taxpayer concerning the volume of the individual's participation in the alleged illegal activity. When the taxpayer either refuses to answer the question or invokes the Fifth Amendment, the Government routinely moves to dismiss the complaint with prejudice on the grounds that the taxpayer as plaintiff has the burden of proof and his failure to submit to discovery is grounds to dismiss as a sanction. [76]

Although some courts at the beginning accepted the Government's argument, the Seventh Circuit in *Williamson* v. *United States* [77] rejected it. Williamson had been arrested by the FBI after indictment for conspiracy and sale of narcotics. The Internal Revenue Service relying upon information obtained from the FBI, terminated Williamson's taxable year. The taxpayer filed a return and also a claim which was rejected. After waiting for the requisite six months, a refund lawsuit was commenced. The taxpayer, in refusing to answer questions concerning the extent and volume of his alleged narcotics dealings, invoked the Fifth Amendment. The Seventh Circuit reversed the lower court's dismissal by pointing out that although normally a plaintiff seeking affirmative relief cannot rely upon the Fifth Amendment, [78] the situation at hand was quite different for the IRS in actuality triggered the series of procedures that resulted in the taxpayer being the plaintiff, only in the technical sense. [79]

After the Government began to lose motions to dismiss, and recognizing that the basis of the assessments would not win the day for them in court on the merits, began to use the motion to stay as a means of holding the case in abeyance until the expiration of the applicable criminal statutes of limitations. Although these refund lawsuits are in essence quasi criminal, some district court judges have been granting stays, which have the effect in some cases of tying up a taxpayer's property for a substantial period of time. [80]

C. Injunctive relief

One of the principal weapons the taxpayer has had to counter the effect and immediate impact of a spontaneous assessment is the temporary restraining order. Although section 7421(a) provides in general that no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court, a judicial exception was carved out by the Supreme Court and such is the exception set forth in the Court's leading decision of *Enochs* v. *Williams Packing & Navigation Co., Inc.* [81]

The taxpayer who files such a lawsuit must show not only that he will prevail on the merits but also, that he will suffer irreparable harm if an injunction is not granted, which is just another way of saying there is no adequate remedy at law. [82]

The practical effect of the *Enochs* confrontation has been to entitle taxpayers to a temporary restraining order and an evidentiary hearings. In some outrageous instances, the courts have permitted the injunction lawsuit to crystalize the issue without the necessity of further litigation such as was done by the Second Circuit in *Pizzarello* and the Fifth Circuit in *Willits*. [83]

Since federal district court judges have wide latitude in controlling these cases, the status quo can be maintained as it relates to further seizures and the forced sale of seized assets while permitting the case to be appealed to the appellate court.

CONCLUSION

There has been substantial abuse of power by the IRS since then President Nixon's mandate was given in June 1971. Since that time, the use of the spontaneous assessment has been rampant, with little regard given to the rights of the individual whose properties were summarily seized and sold at deflated value at forced sales. Not only have there been deprivations of the individual's rights to due process and equal protection, but the effect of spontaneous assessment involved some unintentional waivers of one's Fifth Amendment rights in order to preserve property rights as well as denying some taxpayers their Sixth Amendment right to counsel of their choice because their property was unavailable to pay legal fees.

Common sense may have returned to some of those who have wielded this awesome power, as reflected by Commissioner Alexander's most recent pronouncement. [84] But what will be done in those thousands of cases across the country where the IRS has still not issued a statutory notice of deficiency? What can be done to assure that the wrongs will be righted by removing recorded tax liens based upon these spurious assessments?

Although some will say that the NTP or SEP war parties were isolated aberrations, and most IRS officials are well meaning public officials, the fact that programs like these were permitted to go unchecked shows a latent frightening mentality in government that the end may justify the means. Upon reflection, was not the cure far worse than the disease, for it violated the very tenets this nation cherished when it began the great adventure toward individual rights almost two hundred years ago? Does it not show that in this land, government has the means to rationalize confiscation of a citizen's property under the guise of tax administration?

Although the taking of property was usually limited to those believed to be, although not convicted of partaking in an illegal activity, the programs show the urgency of legislation to permit those who have been wronged to recover in court not only compensatory damages but attorney fees. Hopefully, Senator Warren Magnuson's bill will become reality and the abuses witnessed, curbed, thereby permitting the aggrieved individual the right to immediate judicial review by an impartial judiciary.[85]

REFERENCES

1. U.S. Const. Amend. V provides that: "[N]o person shall . . . be deprived of life, liberty, or property, without due process of law. . . ." The issue is whether the Government's taking of property and possible sale pursuant to an assessment made under the provision of section 6851 without a prior hearing is a denial of due process. In *Phillips* v. *Commissioner*, 283 U.S. 589, 595–597 (1931), the Supreme Court distinguished between personal and property rights and in so doing, recognized in some instances that "[p]roperty rights must yield provisionally to governmental need." The Court further said that "mere postponement of the judicial inquiry is not a denial of due process, in the opportunity given for the ultimate judicial determination of the liability is adequate." In a recent Supreme Court decision, *Fuentes* v. *Shevin*, 407 U.S. 67, 90–93 (1971), the Court, in addressing itself to the question of whether a summary pre-hearing seizure of a taxpayer's assets is consonant with due process, recognized that there were "extraordinary situations" that would justify such pre-hearing seizure, but that they were limited. *See also, North Georgia Finishing Inc.* v. *Di-Chem, Inc.*, 419 U.S. 601 (1975).

2. U.S. Const. Amend. XIV, § 1 provides that: "No State shall . . . deny to any person within its jurisdiction the equal protection of the laws." The Equal Protection clause has been determined by the Supreme Court as being operative against the federal government. *Bolling* v. *Sharpe*, 347 U.S. 497, 500 (1954). It can be argued that the revenue laws discriminate against section 6851 short year termination taxpayers because they are not accorded the same rights as the section 6861 jeopardy taxpayers who have the right to litigate the validity and the amount of their assessment within 60 days of the assessment under section 6861(b) for a notice of deficiency must be issued. *Schreck* v. *United States*, 301 F. Supp. 1265, 1281–84 (D. Md. 1969). Moreover, in the interim, section 6861 jeopardy taxpayers' property interests are protected against forced sale under section 6863(b)(3)(A). Finally, the use of the spontaneous assessment is being directed against a select group of individuals for a purpose that is not directed to a goal normally considered associated with tax administration. The issue of

civil forfeiture of property versus waiver of one's rights against compulsory self incrimination may also be raised. *cf. US* v. *U.S. Coin & Currency*, 401 U.S. 715 (1971).

3. Recent criticism has lead Commissioner of Internal Revenue Donald C. Alexander to reexamine the propriety of the IRS participating in certain law enforcement programs. Alexander, *The Role of the Internal Revenue Service in The Law Enforcement Community*, IRS News Release, IR-1488, June 10, 1975 [hereinafter cited as *The Role of the IRS*].

4. In *Schreck* v. *United States*, 301 F. Supp. 1265, 1276, the court found only eight cases for the period from 1926 to 1969 dealing with spontaneous assessments made under section 6851. The rarity of its use finds its genesis in the guideline set forth in Internal Revenue Manual.

5. *The Role of the IRS; IRS Narcotics Project-Intelligence Division*, Int. Rev. Man. Supp. 93G-112 § 17 (November 10, 1971). The purpose of the program was stated to be as follows:

"The purpose of IRS participation in the Narcotics Project is to disrupt the distribution of narcotics through the enforcement of all available tax statutes. Therefore, there may be cases where civil enforcement actions may be an extremely effective and timely means of accomplishing the objectives of the project. . . . Maximum use will be made of jeopardy, quick, and transferee assessments, and termination of taxable periods."

6. Hereinafter referred to as NTP.

7. It is an historic concept of government derived from Aristotle and Montesquieu that "men entrusted with power tend to abuse it." *See* Locke, *The Second Treatise on Civil Government*, Section 141; Duff and Whiteside, *4 Selected Essays on Constitutional Law*, 291-316 (1938).

8. *The Role of the IRS. See* note 3 supra and accompanying text.

9. *The IRS Swiftly Grabs Drug Suspects Assets in Crackdown Effort*, Wall Street Journal, April 10, 1974, at 1, col. 1.

10. I.R. Information Notice # 74-10, May 31, 1974, captioned "Termination of Taxable Periods," contained the following instructions to all field personnel: "We are concerned about the emphasis being placed upon depriving the narcotics traffickers of their working capital as opposed to the emphasis that should be placed on enforcing the tax laws against them." Attached to this Information Notice was a document, captioned, "Audit Guidelines for Spontaneous Assessments," that contained extracts from a memorandum to the Regional Commissioner, Southwest Region, dated March 21, 1972, from Mr. W. B. Riley, Regional Counsel, Southwest Region.

11. The predecessor of section 6851 was first enacted into law in the Internal Revenue Act of 1918 and has been a part of the tax laws in substantially the same form since that time. Until the passage of the 1926 Internal Revenue Act, no taxpayer was allowed to litigate in court before payment of the taxes. The only option was to post a bond or pay the tax and then commence a plenary refund suit. In 1924, the Board of Tax Appeals—now the United States Tax Court—was created in response to the "inherent harshness of the pay first—litigate later scheme." H.R. Rep. No. 179, 68th Cong., 1st Sess. 7 (1924) in 1939-1 Cum. Bull, 246. Its jurisdiction was limited to normal taxpayers thereby leaving jeopardy taxpayers in the same position as they had been prior to the 1924 Act. But then in 1926, the Revenue Act of 1926 changed the rights of jeopardy taxpayers by enacting the predecessor of section 6861 and this included the "absolute right" to litigate the validity of a jeopardy assessment before the Board of Tax Appeals. *Schreck* v. *United States*, 301 F. Supp. 1265, 1268-75 (D. Md. 1969) *aff'd on recon.* 375 F. Supp. 742 (D. Md. 1973), appeal docketed, No. 74-1566, (4th Cir. May 16, 1974).

12. *See* note 11, *supra*.

13. In *Irving* v. *Gray*, 479 F.2d 20 (2d Cir. 1973), the taxable year of novelist Clifford Irving, the author of the Howard Hughes book hoax, was terminated after the close of the taxable year but before the due date of his return.

14. The ostensible test is if "the Secretary or his delegate [i.e., the local District Director] believes that assessment or collection of a deficiency . . . will be jeopardized by delay." Int. Rev. Code of 1954, § 6861(a). While the making of a jeopardy assessment does not preclude Tax Court review of the merits of the deficiency, *Id.* § 6861(b) collection efforts may proceed concurrently and independently, *United States* v. *O'Connor*, 291 F.2d 520, 525 (2d Cir. 1969), *Cohen* v. *United States*, 297 F.2d 760, 773-74 (9th Cir. 1962); unless the taxpayer is able to post a bond. Int. Rev. Code of 1954, § 6863. In many jeopardy assessment cases, where the taxpayer's assets are insufficient to assure collection of the assessed

liability, the right to stay collection by posting a bond is illusory. *Shelton* v. *Gill*, 202 F.2d 503, 507 (4th Cir. 1953); *Macejko* v. *United States*, 174 F. Supp. 87, 89 (N.D. Ohio 1959); *Kimmel* v. *Tomlinson*, 151 F. Supp. 901, 902 (S.D. Fla. 1957); *see* Note, *Jeopardy Assessment: The Sovereign's Stranglehold*, 55 Geo. L.J. 701, 705–06 (1967). Congress has mitigated one of the hardships occasioned by a jeopardy assessment made under section 6861 by providing that, with certain exceptions, the sale of the taxpayer's property (but not its seizure, which may be as destructive of its value) may be stayed until the taxpayer has had an opportunity to litigate the assessment in the Tax Court. Int. Rev. Code of 1954, § 6863(b)(3). Bank accounts, wages and other claims may nevertheless be appropriated by levy, pending contest of the merits.

15. *See* text acompanying note 16, *infra*.

16. The Tax Court has no jurisdiction over liabilities for employment and other excise taxes. In actuality, the jurisdictional dichotomy between "prepayment" and "post-payment" litigation can be circumvented. Except for income, estate and gift taxes, for which Congress has failed to provide an alternative tribunal for prepayment litigation, the courts have jettisoned the jurisdictional prerequisite of prepayment of the assessment by devising a theory that such other liabilities are "divisible," so that the amount attributable to a single transaction may be paid and its refund sued for, in order to test the validity of the entire assessment covering all transactions in the period, year or quarter. *Flora* v. *United States*, 362 U.S. 145, 175 n. 38; *Steele* v. *United States*, 280 F.2d 89, 90 (8th Cir. 1960), *rev'g* 172 F. Supp. 793 (W.D. Ark. 1959).

17. *See* note 14, *supra*.

18. *See* note 14, *supra*.

19. Int. Rev. Man. Supp. 4584.2(1) (9–26–74); Int. Rev. Man. Supp. 4585.2(1) (7–26–74). *See* Plumb, *Federal Liens and Priorities—Agenda for the Next Decade III*, 77 Yale L.J. 1104, 1134 (1968). The policy limitations appearing in the Internal Revenue Manual are not always keyed to the Government's potentiality of losing revenue. For example, in section 6851 cases, if the taxpayer against whom the Service is about to move is a bank, insurance company, newspaper or some other taxpayer in a situation in which termination and subsequent assessment might "cause serious inconvenience to the general public," a termination will not be made without the prior approval of the Director of the Audit Division in the national office. Int. Rev. Man. § 5214.21(3) (1973). In the case of the individual taxpayer or even small to medium business taxpayer, and specifically in the context of the Narcotics Traffickers Program, this limitation is inapposite. *See* Rev. Proc. 60–4, 1960–1 Cum. Bull. 877.

20. Int. Rev. Man. 4585.1(1).

21. *Id.* at 4584.1.

22. *Id.* at 4584.5(2) and 4585.3(2).

23. In the Arizona District, A. W. McCanless who was then district director in an internal directive dated March 8, 1972, gave the following instructions to his field personnel:

"The Phoenix District is fully committed to the narcotics traffickers project. An integral function to the success of the operation is the prompt termination of tax years, etc. When we are in possession of facts which warrant such action . . . procedures will be developed so that terminations, etc., can be made in less than two hours. . . . Emergency situations may be handled orally and covered thereafter by written reports."

24. Obvious equal protection arguments become apparent. *See* note 2, *supra*, and accompanying text. Before 1971, the termination of taxable year provision was used primarily against aliens who were departing the country. *See*, e.g., *Rogan* v. *Mertens*, 153 F. 2d 937 (9th Cir. 1946). See notes 4 and 5, *supra*, and accompanying text.

25. *See generally*, Silver, Terminating the Taxpayer's Taxable Year: How IRS Uses It Against Narcotics Suspects. 40 J. Taxation 110 (1974).

26. *Illinois Redi-Mix Corp.* v. *Coyle*, 360 F. 2d 848 (7th Cir. 1966); *United States* v. *Rinieri*, 304 F. 2d 885 (2d Cir. 1962); *Lloyd* v. *Patterson*, 242 F. 2d 742, 744 (5th Cir. 1957).

27. 497 F. 2d 240 (5th Cir. 1974).

28. *Id.* at 246.

29. *Woods* v. *McKeever*, 32 Am. Fed. Tax R. 2d 73–5967 (D. Ariz. 1973), appeal docketed No. 74–1133 (9th Cir. Jan. 25, 1974).

30. *Id.*, Transcript of Hearing pursuant to Order that Respondent Appear to Show Cause, at Vol. 2 p. 386–387.

31. *The Role of the IRS.* In section 147.31(a) of the IR Manual, MT 5(17)00–53, the following statement is made: "The Collection activity's role is primarily to secure by levy and seizure action the trafficker's assets. When a trafficker has no money, he cannot buy drugs to sell on the street. Accordingly, seizing money from traffickers is one of the most effective means of ridding the country of the menace of drug abuse." *See* text accompanying notes 4–11, *supra.*

32. 390 U.S. 39 (1968).

33. 390 U.S. 62 (1968).

34. In Internal Revenue Manual, MT 94000–19, (3–14–69) ¶9423.(10) captioned "Coordination with the Federal Bureau of Investigation in Investigations of Gambling Operations" the following pertinent statement appears:

"Cooperation by the Internal Revenue Service is not just limited to state authorities for these has always been full cooperation between the IRS and other select federal law enforcement authorities. For example, the Federal Bureau of Investigation and the Internal Revenue Service will continue to exchange current information regarding gambling operations which have come to the attention of each agency.

* * * * * * *

"Where statutory violations within the jurisdiction of the other agency become apparent in the middle or later stages of an investigation being conducted by either the Internal Revenue Service or the Federal Bureau of Investigation, the agency conducting the investigation will immediately notify the other agency of the relevant facts. Responsibility for further investigation of the individual violations of law will be determined after discussion between representatives of the two agencies. . . ."

Less fortunate than the taxpayers in *Marchetti* and *Grosso* was the taxpayer in *Pauldino* v. *United States*, 500 F. 2d 1369 (10th Cir. 1974). Pauldino filed a return which disclosed that he was a gambler. The taxpayer did not invoke his Fifth Amendment rights in connection with the filing of the return as it related to the source of his income. Much to the taxpayer's chagrin, the return was later received in evidence in an unrelated federal criminal gambling charge which was pending in a United States District Court. *Accord, Garner* v. *United States, en banc*, 501 F. 2d 228 (9th Cir. 1974) cert. granted, 420 U.S. 923 (1975).

35. I.R. Manual Supplement 94G–45 (June 30, 1971) Sec. 10.

36. I.R.S. team members were also invited to participate in searches which were authorized by warrants that were executed by the local law enforcement authorities. Although the warrants were limited to seizing paraphenalia related to wagering, IRS agents participated in the search and as a result, asked the local enforcement officials to seize financial information felt relevant which was done. *Schildcrout* v. *United States*, CIV 74–94 PHX WEC (D. Ariz. filed 2/12/74), (Motion to Suppress Hearing, Tr., p. 9). It was not uncommon for the IRS officials to tape record what they saw visually as it related to documents observed during the search which were not described in the search warrant or included in the inventory of the search. *Id.*

37. 73–2 U.S. Tax Cas. ¶16. 119 (D. Ariz. 1973). The action was filed under *Enochs* v. *Williams Packing Co.*, 370 U.S. 1 (1962), which allows a taxpayer to obtain an injunction, provided there is no adequate remedy at law and the Government could not sustain the tax assessment under any circumstances. In the Arizona district, the taxpayers have been permitted an evidentiary hearing in an *Enochs* confrontation to test the validity of the assessment. In order to prepare for an evidentiary hearing, taxpayers have been permitted to utilize extensive pretrial discovery, including the use of depositions, interrogatories and requests for production of documents and things. *See* text accompanying note 83, *infra.*

38. The Supreme Court in *United States* v. *Giordano*, 416 U.S. 505 (1974), which was decided subsequent to when the motion to suppress order was granted in *James*, held that the wiretap statute had to be construed strictly.

39. The Arizona District Court also found that the authority for the state-authorized wiretap was based upon a statute which was substantially identical to the New York statute that was declared unconstitutional by the Supreme Court in *Berger* v. *New York*, 388 U.S. 41 (1967), and, therefore the Arizona statute under which the instant wiretap was authorized was likewise unconstitutional. Lastly, the Court found that of 872 interceptions which were made, because only 430 were catalogued as incriminating, the manner of monitoring the conversations violated the court order authorizing the taps because no at-

tempt was made to minimize interceptions of non-incriminating communications made to the taxpayer, a requirement of the federal wiretap statute.

40. In Information Notice, No. 74–16 dated May 31, 1974, the IRS field personnel were cautioned about the use of tainted wiretap evidence when making a spontaneous assessment: "Exclude unlawful wiretap evidence entirely and other tainted or illegally obtained evidence if possible. Consult [Regional] Counsel if in doubt as to legality."

41. A final judgment was never entered in the first *James* case for after waiting six months, a plenary refund action was filed which was addressed solely to the merits of the case and not the issue of irreparable harm, a factual finding necessary to come within *Enochs* jurisdiction. In the refund lawsuit, *James* v. *United States*, CIV 73–733 PHX WEC (D. Ariz., filed Nov. 20, 1973), appeal dismissed, Docket No. 75–1779 (9th Cir. 8/29/75), the Arizona District Court granted summary judgment in favor of the taxpayer and in so doing, followed the recently decided Ninth Circuit opinion, *James* v. *United States*, No. 73–2226 (9th Cir. 7/22/74), *cert. granted* 43 U.S. Law Week 3480 (4/4/75), affirming an unreported District Court case, 73–1 U.S. Tax Cas. ¶16,083 (C. D. Cal. 1973), which held that the suppression of illegally seized evidence could be raised in the context of a civil tax refund proceeding.

42. In *Ianelli* v. *Long*, 487 F. 2d 317 (3rd. Cir. 1973), the Third Circuit in dicta without any analysis stated that IRS personnel were law enforcement officials within the meaning of Title 18 U.S.C. § 2510(7) and therefore could receive and use wiretap evidence. Since this is dicta and based upon the most recent strict construction analysis of the wiretap statutes in *Giordano* by the Supreme Court coupled with the Government's dismissal of its appeal in *James*, the *Ianelli* opinion is of dubious vitality.

43. In the motion to suppress the use by the IRS of wiretap evidence, care should be taken to distinguish between evidence obtained illegally from evidence obtained in violation of the wiretap statute which does not otherwise constitute a Fourth Amendment violation. Section 2525 deserves close scrutiny. It provides in pertinent part:

"§ 2525. Prohibition of use as evidence of intercepted wire or oral communications.

"Whenever any wire or oral communication has been intercepted, no part of the contents of such communication and no evidence derived therefrom may be received in evidence in any trial, hearing, or other proceeding in or before any court, grand jury, department, officer, agency, regulatory body legislative committee or other authority of the United States a State, or a political subdivision thereof if the disclosure of that information would be in violation of this chapter.

The other pertinent section of the wiretap statute is contained in section 2518 (10) (a). It states in pertinent part:

"Any aggrieved person in any trial, hearing, or proceeding in or before any court, department, officer, agency, regulatory body, or other authority of the United States, a State, or a political subdivision thereof, may move to suppress the contents of any intercepted wire or oral communication, or evidence derived therefrom, on the grounds that: (i) the communication was unlawfully intercepted; (ii) the order of authorization or approval, under which it was intercepted is insufficient on its face; or (iii) the interception was not made in conformity with the order of authorization or approval."

The interrelationship, if any, of section 2515 and section 2518(10(a) must be analyzed.

In the now controlling case of *United States* v. *Giordano*, 416 U.S. 505 (1974), the Supreme Court, in a unanimous opinion, held, *inter alia*, that under section 2518(19) (a) (i), the words "unlawfully intercepted" are not limited to constitutional violations, but the statute was intended to require suppression where there is a failure to satisfy any of those requirements that directly and substantially implement the congressional intention to limit the use of intercept procedures to those situations clearly calling for the employment of this extraordinary investigative device. 416 U.S. at 524–528. Accordingly, the motion to suppress was granted because the Justice Department officer approving the application was not properly delegated to authorize the wiretap in the first instance.

The Court's observations at 524 are particularly relevant:

"The issue does not turn on the judicially fashioned exclusionary rule aimed at deterring violations of Fourth Amendment rights, but upon the provisions of Title III;

* * * * * * *

"Section 2515 provides that no part of the contents of any wire or oral communication, and no evidence derived therefrom, may be received at certain proceedings, including trials, "if disclosure of that information would be in violation of this chapter." What disclosures are forbidden, and are subject to motions to suppress, is in turn governed by section 2518(10)(a), . . ."

The Court did not say that the stated grounds under section 2518(10)(a) must first be met if an objection is made at a trial under section 2515, for this question was not before the Court. The Court only said that if the grounds for a motion under section 2518(10)(a) asking for suppression of evidence is present, then the granting of the motion under that section is proper. Those grounds are: (i) the communication was unlawfully intercepted; (ii) the order of authorization or approval under which it was intercepted is insufficient on its face; or (iii) the interception was not made in conformity with the order of authorization or approval.

Support for the conclusion that suppression as distinguished from an evidentiary objection is limited to these three grounds has its genesis in the Senate Report which accompanied Title III to Congress.

It states: "Section 2515 . . . imposes an evidentiary sanction to compel compliance with the other prohibitions of the chapter and that section 2518(10)(a) together with section 2515 'applies to suppress evidence directly . . . or indirectly . . .' S. Rep. No. 1097, 90th Cong. 2d Sess. 96 (1968)."

In a recent District Court case, *Schildcrout* v. *United States*, CIV 74-94 PHX WEC (D. Ariz. filed Feb. 12, 1974), the Arizona District Court acknowledged this distinction in denying a motion to suppress where the basis of the motion was not directed to what could be construed as an unlawful interception but rather only as an unauthorized use. The court's ruling appears to be a correct application of *Giordano* because the taxpayer was not contending that there had been either an "unlawfully intercepted" communication within the strict meaning of 18 U.S.C. § 2518(10)(a)(1) or a constitutional violation. If there had been a constitutional violation which infringed upon this taxpayer's Fourth Amendment rights, then a motion to suppress would be proper in the context of the civil tax proceeding under the authority of *Janis*. Similarly, if there had been an "unlawful interception" which did not otherwise involve a constitutional violation, then the motion to suppress would be proper and mandated under 18 U.S.C. § 2518(10)(a). *See generally*, Silver, Use of Motion to Suppress Wiretap Evidence Successful in Recent Tax Case, 40 J. Taxation 340 (1974).

44. 408 F.2d 579 (2nd Cir. 1969).

45. No. 73-2226 (9th Cir. 7/22/74), *cert. granted*, U.S. Law Week 3480 (4/4/75), affirming an unreported District Court case, 73-1 U.S. Tax Cas. ¶ 16,083 (C.D. Col. 1973).

46. Such principles were recognized and accepted in the leading case of *Pizzarello* v. *United States*, 408 F.2d 579, 585 (2d Cir. 1969), which involved an injunctive lawsuit against a jeopardy assessment for excise taxes concerning alleged wagers accepted by the taxpayer. In *Pizzarello*, the Second Circuit restated the rule espoused by the Supreme Court in *Helvering* v. *Taylor*, 293 U.S. 507, 513-516 (1935), that a tax assessment is only presumptively valid and the burden is on the taxpayer to prove its invalidity, but such a presumption is not evidence itself and disappears upon the introduction of evidence to overcome it. The taxpayer in *Pizzarello* overcame the burden by showing that the assessment was excessive and arbitrary for it was based upon evidence seized illegally. The Government had calculated the assessment by using a three-day average and then under the interpolation method, extended it over a five-year period.

47. See note 67, *supra*, and accompanying text.

48. 301 F. Supp. 1265, 1284 (D. Md. 1969).

49. 356 F. Supp. 398, 401 (D. Ariz. 1973).

50. 501 F.2d 108, 116-120 (5th Cir. 1974).

51. 493 F.2d 1211, 1212 (6th Cir. 1974), *cert. granted*, 419 U.S., 1087 (1974).

52. 344 F. Supp. 567, 572 (S.D. N.Y. 1972), *aff'd.* 479 F.2d 20 (2d Cir. 1973).

53. 496 F.2d 853, 854, (2d Cir. 1974) *cert. granted*, 419 U.S. 824 (1974).

54. 31 Am. Fed. Tax R.2d 73-800 (7th Cir. 1971).

55. *Hall* and *Laing* are set for oral argument this term. Appeals pending in the Third, Fourth and Ninth Circuits have been removed from the calendars of the respective circuit courts pending these decisions.

56. 301 F. Supp. at 1268-1275.

57. 356 F. Supp. at 402.

58. *Id.*

59. 492 F.2d 1960 (6th Cir. 1974).

60. *Id.* at 1064.

61. The contrary argument presented by the Government in *Lisner* was dismissed as being premised on "convolutions and strained interpretations." 356 F. Supp. at 403.

62. *Irving* overlooked the fact that prior to the district court case of *Clark* v. *Campbell*, 341 F. Supp. 171 (N.D. Tex. 1972), it was presumed by the Internal Revenue Service that section 6851 contained its own assessment authority.

63. 479 F.2d 20 (2d Cir. 1973).

64. 362 U.S. 145 (1960).

65. 479 F.2d at 25, n. 6 (Emphasis deleted).

66. 362 U.S. at 146.

67. *William Jones* v. *Comm'r.* 62 T.C. 1 (1974). In an earlier case, *Ludwig Littauer & Co.* v *Commissioner*, 37 B.T.A. 840 (1938), the Board of Tax Appeals said in dicta that no statutory notice of deficiency was required.

68. See note 2, *supra*, and accompanying text.

69. In a suit to contest the correctness of a tax assessment, the burden of disproving the assessment rests upon the taxpayer. *Hoffman* v. *Commissioner*, 298 F.2d 784, 788 (3d Cir. 1962). But if the taxpayer demonstrates that the Commissioner's determination was arbitrary, he is not required to assume the burden of disproving it. *Helvering* v. *Taylor*, 293 U.S. 507, 515 (1935). Therefore, when a taxpayer establishes that an arbitrary, and capricious assessment has been made, the Commissioner then has the burden of going forward with the evidence. *Herbert* v. *Commissioner*, 377 F.2d 65, 69 (9th Cir. 1966); *Merritt v. Commissioner*, 301 F.2d 484, 487 (5th Cir. 1962). After a taxpayer has overcome the presumption of correctness of the Commissioner's determination, the presumption thereafter disappears and the Commissioner then has the burden of proving whether any deficiency exists and, if so, the amount, and it is not incumbent upon the taxpayer to prove he owed no tax or the amount of tax which he does owe, or which he did owe.

70. Prior to the promulgation of Rule 142(e) of the Tax Court's Rules of Practice which now permits the taxpayer to have a hearing prior to the trial on the sufficiency of a statement which is claimed to satisfy the requirements of Code section 534(c), the Tax Court would, upon timely motion filed, hold a bifurcated hearing to determine the burden of proof issue. Under the new Tax Court's Rules of Practice, the same procedure could be applied to determine if the assessment is arbitrary and capricious, and in essence the matter could be treated as a motion for partial summary judgment.

71. 479 F.2d at 22–23.

72. *See* notes 64–66, *supra*, and accompanying text.

73. See, for example, *Reese* v. *United States*, CIV 75–70 PHX WEC (D. Ariz., filed Feb. 6, 1975) which was a plenary refund lawsuit filed by a terminated taxpayer. Reese filed a return showing a refund of $18,037.65, which was the balance of the sum of $25,105 that had been seized from him by Phoenix police at the time of his arrest for suspected marijuana trafficking activities. The Government as an affirmative defense alleged that the "grounds for refund," prepayment of the assessment, as "required by law" had not been met and accordingly, the lawsuit should be dismissed, with prejudice. Such a contention is irreconcilable with the position espoused by the Government in *Irving*.

74. *See* note 16, *supra*, and accompanying text.

75. In SEP cases, stay of collection normally accorded most other taxpayers administratively when a refund action is pending does not apply. Accordingly, a preventative injunction action has been effective to maintain the status quo while the taxpayer waits for the requiste six months to expire before filing the refund action. Thereafter, the other issues that normally require resolution in the context of an *Enochs* action are mooted and the emphasis can be directed only toward the merits of the assessment.

76. The Government routinely cites the following cases in support of their motion to dismiss: *Florio* v. *United States*, 33 Am. Fed. Tax R.2d 74–1342 (N.D. W. Va. 1974); *McNatt* v. *United States*, 32 Am. Fed. Tax R.2d 73–5733 (N.D. Tex. 1973).

77. An unreported case, cited unofficially at 31 Am. Fed. Tax R.2d 73–800 (7th Cir. 1971).

78. *Kisting* v. *Westchester Fire Insurance Co.*, 290 F. Sup. 141, 149 (W.D. Wis. 1968), *aff'd*, 416 F.2d 967 (7th Cir. 1969).

79. *See Aliota* v. *Holtzman*, 320 F. Sup. 256 (E.D. Wis. 1970).

80. *Iannelli* v. *Long*, 487 F.2d 317 (3rd Cir. 1973); *Lisner* v. *United States*, CIV. 73-680 PHX-WEC (Order dated October 7, 1974). Courts granting the stay have recognized that the Fifth Amendment privilege against self-incrimination applies as well to a civil proceeding as to a criminal case. *McCarthy* v. *Arndstein*, 266 U.S. 34, 40 (1924). The Courts reason that a plaintiff should not be put to the election of foregoing either their civil suit or their rights under the Fifth Amendment and accordingly, all further discovery is deferred until plaintiff is able to participate in a two-way discovery.

81. 370 U.S. 1 (1962).

82. What is required to show irreparable harm may vary but financial detriment is one aspect. *Lucia* v. *United States*, 474 F.2d 565, 577 (5th Cir. 1973); *Bauer* v. *Foley*, 404 F.2d 1215, 1221 (2d Cir. 1968).

83. *See* note 27, *supra*, and accompanying text.

84. IRS officials are subject to the courts' supervisory as well as disciplinary power. *Meier* v. *Keller*, No. 74-1182 (9th Cir. 6/27/75).

85. Senator Warren Magnuson, from the State of Washington, introduced Senate Bill S. 2342 which provides sanctions against some of the abuses witnessed during the heyday of the various programs referred to in this article. S. 2342, 94th Cong., 1st Sess. Con. Rec. S15962-S15966 (1975). When introducing Senate Bill 2342, Senator Magnuson observed that in fiscal year 1973, there were 3,090 jeopardy terminations of assessments whereas in fiscal year ending 1975, the number of assesments declined to about 500. Notwithstanding the decline of its use, Senator Magnuson concluded: "But we cannot rely solely upon the discretion of administrators for restraint of the totally arbitrary powers currently residing in the Internal Revenue Service." 121 Cong. Rec. S15964 (daily ed. Sept. 16, 1975).

Senator HASKELL. Our next witness is Mr. Edson R. McCanse. Is Mr. McCanse here? Would you come forward, sir.

If you could just sit right down there, sir. Would you just go ahead, Mr. McCanse, and tell us whatever you want to say. We are talking about jeopardy assessments. I know from some material that I have been provided that you have had a particular problem involving jeopardy assessments and, perhaps, in your own words, you could just tell us about it.

STATEMENT OF EDSON R. McCANSE, LA GRANDE, OREG.

Mr. MCCANSE. Well, in my case, I had no warning that there was any question about my tax at all. There was some sort of a routine audit taking place. I was out of the country a good part of the time and could not be reached. My records have been kept by an accounting firm in Salem, Oreg., for, I guess 30 years. I do not even get my canceled checks. They are sent directly to the accountants by the bank, and the IRS apparently did not want to look at my records.

They say that they had set up several hearings through the Pendleton Regional IRS Office to inspect my records, but I was scattered around all over the country. I was up in the North Slope in Alaska, 300 miles from, well, Kasigluk was the nearest spot, and that was 500 miles from any road. I just could not be reached, and my accountant, Liphold, Brennan & Bingingheimer of Salem, Oreg., had all of my records, and they contacted this accounting firm, the IRS accountant, and wanted one of the representatives of the accounting firm to come to Pendleton, Oreg., to present my records. And, Bob Gufner, the man who has personally taken care of my business for the last 20, 30 years, told them that I was unavailable and that I kept no records at all of my own. He had all of my records, and it was a 300-mile drive for him to go to Pendleton, and he wondered if it would not be way more convenient for everyone concerned, if he could—they had plenty of agents in Salem, Oreg.—if he could not present my records to them, my books, in Salem, and that is as far as it ever went.

My books were there available and opened for their inspection at any time, and I had no notice of this, either written or verbal, of this jeopardy assessment until the thing was placed on me, and at that time I was a half-owner in the Round Valley Lumber Co., and we had—I do not remember the exact figures—but $2 million or $3 million worth of bonds in effect at the time, and they were taken through a local insurance and bonding company, and I, when the Commissioner, Pattison, the field man, I guess, for the Pendelton Branch Office, came by and notified me of what had happened, that they had placed this jeopardy assessment on me, told me I had the choice of paying it or putting up a bond.

Well, my accountant and my attorney both told me that I owed no part of it; that I owed no tax; in fact, I had a small refund due me at the time, and so, I thought at the time, well, the simplest thing is just simply to put up a bond to cover the amount that they claimed I owed in jeopardy assessment, and I went to the bonding company which had handled all of the mill business and explained my problems to them and told the Commissioner, Dave Baum, who ran the outfit, that I would like to get a bond and would be glad to put up all of my stock in the lumber company, which at that time was probably worth 10 or 12 times the amount of the assessment against me.

Mr. Baum's father at that time had had a serious heart attack and was expected to die at most any hour, and he was not around the office, and I kept going by, but he was never there, and not until the time given me by the regional agent of the IRS Office in Pendleton was due to expire, did Mr. Baum ever tell me that he could not get the bond. I had no idea in the world that the simplest possible would be to get that bond because we had maybe 20, 30 times that many bonds for the company. We were logging on national forest ground and we wanted protection in case of fire breaking out from our logging operations and doing a lot of damage to standing timber. Some of those things can get real bad. And we wanted to be thoroughly covered, and it never occurred to me that I could not get a bond. And, then, I called my accountant in Salem and he told me that with this jeopardy assessment, I needed the best legal advice possible to get, and he told me who he thought would be the proper man to contact, Mr. Leo Mysing, in Portland, Oreg., a tax attorney, and I went to Mr. Mysing and explained the whole thing, and he thought about it quite a little while. He kind of puzzled, and he said, IRS does not usually operate in this manner. He said, there is something funny about this deal. I do not understand it, and then he made the comment, he says, who stands to gain, and I think that is probably the basis of the whole action against me.

But that is another story. I cannot prove anything. I do not dare say anything that I cannot prove.

Senator HASKELL. Well, thank you. Now let me just ask a couple of questions because I want the hearing record to reflect exactly what happened to you. Now, see if I am correct. It is my understanding that in 1964, you and your daughter sold certain properties for about $960,000.

Mr. MCCANSE. That is correct.

Senator HASKELL. And it is further my understanding that you reported this sale as an installment sale.

Mr. McCANSE. That is right.

Senator HASKELL. Then it is also my understanding that on December 5, 1965, a jeopardy assessment was made against you in the amount of $119,000.

Mr. McCANSE. Right.

Senator HASKELL. It is further my understanding that after extensive litigation and discussion with the Internal Revenue Service, that they finally agreed that your reporting again on the installment basis was correct and that, therefore, you did not owe the $119,000. Am I right on that?

Mr. McCANSE. That is right.

Senator HASKELL. Now, it is only my understanding that when they put the jeopardy assessment on, they seized your property and you went to this Ronde Valley Lumber Co. and you borrowed money on your 50-percent interest so that you could satisfy the jeopardy assessment.

Mr. McCANE. That is correct.

Senator HASKELL. And that, as a result of borrowing the money as you thought from your partner in the business, you got into litigation because later on he claimed you sold your stock.

Mr. McCANSE. That is correct.

Senator HASKELL. And it is further my understanding that this has caused you a great deal of expense in litigation, attorney's fees, and the like. Is that correct?

Mr. McCANSE. Correct.

Senator HASKELL. So, the upshot is that the sole issue is whether or not you were entitled to take the installment gain treatment on the sale, and you prevailed, but ultimately you were successful. Is that correct?

Mr. McCANSE. That is correct.

Senator HASKELL. I think the record here is very important, Mr. McCanse, because the gentleman who preceded you in his testimony was by-and-large talking about people against whom certain criminal acts had been alleged.

There was no allegation of criminal act in your case, merely a civil suit. The Internal Revenue Service was later proven wrong, so I think you have added a great deal to this hearing record that, had you not come, we would not have, and I appreciate it very much.

Now, if you would stay there just a second, I want to ask counsel if he has any questions.

Mr. McCANSE. I asked my attorney, Mr. Leo Mysing, when my case was put on the ABC TV program, they had a question of power. I put a little notice in the LaGrande Observer to the effect—I had a lot of friends that wanted to know when this thing was coming up and I put a little notice in the LaGrande Observer in the effect that it would be on a certain date, and they sent a reporter around to interview me, and before he put a writeup in the paper on the thing, he consulted with the IRS regional office in Portland, and the man who was Director at the time, a Mr. Doss, I believe was the name, told the reporter that there had been a change in the law which changed the status of these installment payments, and this change had been made since my case came up, and that was the basis for my refund.

I asked my attorney about that, and he said, it was absolutely untrue. He said that clause under which I took the installment payment

method of reporting my income had been in effect, I think he said, since 1964. It was previous, at any rate, to the time of the sale, and he said that was not true at all.

Senator HASKELL. Well, thank you. Now, Mr. McCanse, when you were in Alaska on the North Slope, did you have a residence in Oregon?

Mr. MCCANSE. Yes, I have lived in the same house in LaGrande, Oreg., for 30–35 years, and I have been a resident of Oregon for almost 60 years.

Senator HASKELL. Did the Internal Revenue Service at any time say that they were scared you were going to flee the country?

Mr. MCCANSE. Well, the basis that I got was, well, Mr. Alexander, on that TV program, who presented my case, said that they had reviewed the case and they were satisfied that they took proper methods, and he said that I had been uncooperative.

Senator HASKELL. But you did have a house in Oregon?

Mr. MCCANSE. I have been farming in Oregon for over 50 years. I have quite a large ranch, which we sold, which apparently set off this problem, and I have lived there in that same house for about, well, at that time, almost 30 years, and I am still living in the same house.

Senator HASKELL. That sounds very permanent to me. Now, let me ask you one more question, Mr. McCanse. Had you been taking any property out of the country?

Mr. MCCANSE. I have four children, and two of them are farming in the United States. One boy has a ranch—he does not have a ranch, he has farming leased ground, out of Oregon, Illinois. He is farming about 900 acres in corn. I have another daughter and son-in-law that are farming at North Powder, Oreg. I have two daughters and sons-in-law who are in the cattle business in British Columbia, and when we sold the ranch, we were operating it as a joint venture partnership, and they wanted to go to British Columbia and get set up in the cattle business up there, and we took considerable equipment up there, but, at the same time, I owned a half-interest in the Round Valley Lumber Co., which is worth probably in excess of $2 million at that time. It was subject to a buy or sell agreement with my partner. I could not possibly have moved the thing to British Columbia. I had no intentions of selling it or of moving it, and that may be one of their contentions, that I was going to pick that sawmill up and take it to British Columbia; I do not know.

Senator HASKELL. One last question. Did you have a bank account in Oregon?

Mr. MCCANSE. I had a bank account until the IRS took it.

Senator HASKELL. Well, again, thank you very much, Mr. McCanse. You have added a great deal, and I appreciate it very much indeed.

Mr. MCCANSE. We had a little trouble in Frisco on the plane. We had to change planes. I do not know what we were going with, a flat tire or something. I should have had a little over 2 hours to get up here from the airport. As it was I got here 15 minutes after the time I was supposed to show up.

Senator HASKELL. Thank you very much, sir. I appreciate it.

[The following material was submitted by Mr. McCanse:]

DEAR SENATOR HASKELL: I have had more than my share of I.R.S. problems and all one gets out of them is statements as to how fair and just they are in their dealings, when actually they are not at all above plain flagrant violation of the laws set up to regulate their actions, as two instances in particular in my case. You cannot even take a deposition from one of their agents. If the regional

director sees fit to do so, you or your attorney may question said agent in the presence of him (the regional director) and said agent can lie all he pleases. You haven't a chance in the world of doing a thing about it. They are totally free of any responsibility for their actions or mistakes or liability for any loss they may cause their victims. They don't even need to check one's records which in my case were available for their inspection at any time, before levying a jeopardy assessment. Their claims that I was uncooperative were just as false as we proved in over 3½ years all their charges listed against me in their jeopardy assessment to be.

I've been through about seven years of plain hell on this deal and I would sure like to cause them to accept some responsibility for their mistakes and the years of worry and misery they have caused me. It was all so uncalled for and unnecessary, if they had only bothered to take the trouble to examine my records which were open and available to their agents at my accounting office at any time had they cared to inspect them.

I would very much like to carry this thing on and exhaust every possible chance to pin the blame on them for all the loss and misery they have caused the wife and I and get some actual recompense for the harm they have done me. Don't you feel that I should be entitled to more than just an "I'm sorry" for the lost years and misery they have caused me? Our case was put on A.B.C. T.V. program "A Question of I.R.S. Power" and I hope to get it publicized nation wide in every possible way. Can you help me? I've been warned by people in a position to know, not to irritate the I.R.S. or suffer the consequences. I just can't suffer any more than I already have.

When our case was put on the A.B.C. T.V. program there was an article printed in our local paper, the "LaGrande Observer". They, like everyone else, are scared to death of the I.R.S. and are not about to print anything that concerns the I.R.S. unless they are absolutely sure of the accuracy of all statements made. They consulted with the Portland office of the I.R.S. to verify my statements and as usual the I.R.S. men explain how they are so fair, just and within the law in all their actions. In their answer to my charges they intimated that there had been a ruling since the filing of the jeopardy assessment against me which caused a change in their treatment of the sale of our ranch as an installment sale. That, like many of their statements is just not true; simply more lies to try to justify their actions. Am enclosing said clipping and my attorney, Mr. Leo Meysings commented on same, that this ruling was made prior to their consideration of my case and had been for several years.

Over the years of worry this thing has become an obsession with me and I'm willing and anxious to go to any length to see that I get more than just a qualified "I'm sorry" for the years of plain hell they have caused me. I don't know how I can get this story spread widely enough across the country to get some semblance of justice for the wrongs done me by the I.R.S. but I'm sure going to try to the best of my ability to do so. The N.B.C. T.V. program by David Brinkley called a spade a spade and I sure hope will produce a decided change for the better in I.R.S. methods of extortion they now commonly use to enforce their totally unfair and brutal collection methods on their victims.

In the N.B.C. program by David Brinkley the I.R.S. representative Mr. Donald Alexander came down off his high horse he was so smugly on, through the A.B.C. program and was literally mumbling through his beard before the end of the program. More power to David Brinkley for being unafraid to call a spade a spade. Such a program I'm hopefully thinking will cause some radical changes in I.R.S. methods.

A detailed chronical of our case enclosed.

Very truly yours,

ED MCCANSE.

In 1964 my two daughters, Audrey Cummings and Bonnie Graham, and I were the owners of certain ranch and farming properties located near North Powder, Oregon. In the latter part of 1964 we sold these properties on an installment sales contract for the sum of $960,000.00. Less than thirty per cent of the sales price was in the form of cash and the balance was to be paid according to the terms of the installment contract executed between ourselves as sellers and the buyer as purchaser. Prior to the sales my daughters and their husbands and I had operated the ranch as a three-way family partnership. The real properties, however, were owned by my daughters, their husband and me as tenants in common. The aforementioned sale occurred in July of 1964.

In reporting the sale transaction for Federal and State of Oregon income tax purposes appropriate elections were made to report the gain from the sale according to the installment method as permitted under Section 453 of the Internal Revenue Code. During the latter part of the subsequent year 1965, the partnership and the personal income tax returns of my two daughters and their husbands and those of my wife and I were subjected to an audit which appeared to be a routine Internal Revenue Service field audit. On December 5, 1965, without prior warning the Internal Revenue Service and the State of Oregon Department of Revenue issued a jeopardy assessment against my two daughters and their husbands and me and my wife. The amount of the jeopardy assessment issued against my wife and I was in the amount of $119,000.00. At the time of the audit and for a number of years prior thereto my wife and I were also the owners of a fifty per cent stock interest in Ronde Valley Lumber Company, an Oregon corporation. At that time I was President of such corporation, which was engaged in the manufacture and sale of lumber and other forest products. The remaining fifty per cent of the stock of such corporation was owned by a Mr. C. W. Hoffman and members of his family.

The issuance of the jeopardy assessment referred to was without either written or verbal warnings from the Internal Revenue Service or the State of Oregon as to the reason for such assessment and without explanation of any kind as to why jeopardy assessment procedures were invoked against my family and I. Coincident with the issuance of the jeopardy assessment by the State of Oregon Department of Revenue the latter caused to be filed against my personal residence an income tax lien and on December 23, 1965, the Internal Revenue Service caused to be issued against my stock ownership in the Ronde Valley Lumber Company a levy thereon as well as a seizure of my personal bank account. Similar levies and seizures of my salary and other amounts due me from the lumber company were also made.

Upon being notified of the levy upon my fifty per cent capital stock interest in Ronde Valley Lumber Company and the seizure by the Internal Revenue Service of my bank account balances, I conferred with Mr. Leo Meysing of Portland, Oregon, an attorney, who advised that while the Internal Revenue Service had the power to issue a jeopardy assessment, they possessed no statutory authority to sell assets or properties to collect the tax unless I gave consent to such sale or unless the property was of a perishable nature. He advised me, however, that after a lapse of thirty days following the issuance of the jeopardy assessment the Internal Revenue Service could continue to seize liquid assets in the form of salary, bank accounts and other cash credits unless I was able to post a bond with the Internal Revenue Service in an amount equal to the amount of the jeopardy assessment to provide the Internal Revenue Service with security in the event the taxes were subsequently found to be justly owing.

In follow up of the advice I had received from Mr. Meysing, I attempted to procure through the services of the Baum Insurance Agency in LaGrande, Oregon, a bond in the amount of $119,000.00 to cover the levy. In connection with such application I tendered as security my capital stock in Ronde Valley Lumber Company which had a value at such time in excess of $950,000.00. In electing to utilize the services of Baum Insurance Agency I felt that this would be a likely source for the acquisition of the bond in question because this firm handled all of the casualty and broad underwriting of the Ronde Valley Lumber Company and was therefore well aware of the financial net worth of the corporation and of its financial circumstances in the community.

Toward the end of February, 1966, the collection agent for the Internal Revenue Service, operating out of their office in Pendleton, Oregon, advised me that unless the bond was forthcoming within ten days further collection action would be taken in pursuit of the jeopardy assessment. At the end of this ten-day period, the collection agent from the Internal Revenue Service, a Mr. Pattison, and I met with Mr. Baum, at which time Mr. Baum informed me that he was unable to procure the bond. This meeting occurred on the afternoon of March 4, 1966.

On Monday, March 7, 1966, I was advised by Agent Pattison that unless I paid in full the jeopardy assessment in the amount of $119,000.000 the Internal Revenue Service was going to sell my fifty per cent capital stock interest in Ronde Valley Lumber Company to certain unnamed and unidentified individuals who had tendered offers in undisclosed amounts for my said fifty per cent stock interest. Upon receipt of this information I immediately contacted my accountant, Mr. Robert Guthner, of Salem, Oregon, and Mr. Leo Meysing, of Portland, Oregon, to ask them to intercede for me on my behalf with the District Director of the Internal Revenue Service, Mr. O. Erickson, to ask for an extension of time

within which to procure the bond to cover the payment of the taxes which were the subject of the jeopardy assessment. Mr. Meysing and Mr. Guthner made an appointment with Mr. Erickson at his office and requested a 48 hour delay within which to procure the bond. Through sources of his own Mr. Meysing had been advised that such a bond was available through a Portland, Oregon, based insurance underwriter. Following a lengthy meeting with Mr. Erickson and the Chief of the Collection Division of the Internal Revenue Service, Mr. Rushford, Mr. Erickson advised Messrs. Meysing and Guthner that he would advise them as to their decision in regard to the extension. Mr. Erickson and Mr. Rushford confirmed to Messrs. Meysing and Guthner that the involuntary sale of our stock was in fact contemplated for the following day, namely March 8, 1966, but that they would take our request under advisement pending final decision. At 4:30 p.m. on the afternoon of March 7, 1966, Mr. Rushford called Mr. Meysing and advised him that the forced sale of my stock in Ronde Valley Lumber Company was to occur the following morning at 10:00. He claimed to have three unnamed and unidentified parties interested in effecting the purchase of the stock.

On the evening of March 7, 1966, after Mr. Meysing had advised me of the Internal Revenue Service's position, I, in desperation, contacted Mr. C. W. Hoffman, my partner in the lumber mill, and explained my problem. Mr. Hoffman and I had been on friendly terms as co-owners of the lumber mill and he assured me that the mill or he would help me in any way possible to raise the $119,000.00 by the March 8, 1966, 10:00 deadline set by the Collection Division of the Internal Revenue Service.

We had been on very friendly terms, and I had some $25,000.00 due my account from the mill. After telling me he was sure he could have the $119,000.00 the next day he asked me if I would be willing to put up three-fourths of my shares of mill stock as security for the loan, and I distinctly remember my reply. I said, "Hell, yes. I'll put it all up." The following day, March 8, 1966, I went over to the bank in LaGrande. Mr. Baum and the bank manager, Mr. Sullivan, were there and figured up what three-fourths of my stock amounted to in shares. It required the splitting of one certificate to come up with the proper number of shares. I got my wife to come down to the bank and sign, and I signed the stock powers, I believe they called them. After signing I told Mr. Sullivan I was very concerned as I had seen nothing stating I had the right to get my stock back on repayment of the loan. Both my accountant and attorney had assured me I did not owe any part of that $119,000.00 assessment. I had certainly not received over 29 per cent of the amount of the sale. The cattle, machinery, and irrigation equipment they claimed I had sold had all been taken to my daughters' ranches in British Columbia and were not sold. I have to admit at that time I was primarily worried about being able to get my stock back. The day after signing the stock powers I asked Mr. Hoffman if he wanted a note or how he wanted to handle the transaction. He replied that his attorney, Mr. Blaine Buchanan of Chattanooga, Tennessee, was tied up and unable to come out to Oregon at that time and to temporarily treat it as a sale. Being worried about it, I had my accountant try to get something in writing saying I could get my stock back on repayment of the loan. Mr. Hoffman assured him I could have it back any time I paid back the loan.

It took almost 3½ years to get the I.R.S. to admit they were wrong and that I owed no part of the $119,000.00. More months went by before the refund was made. Since the refund was in excess of the original assessment, it had to be reviewed and approved by a joint committee of Congress, which ultimately approved the refund action without exception.

The stock powers were signed on March 8, 1966. I received the refund in August of 1969. After receiving the refund I contacted Mr. Hoffman to find out what interest and expenses he might have incurred in getting the $119,000.00. His reply was that he was out some $300,000.00 and still had a tax problem to figure out and could not give me a figure at that time. In reply to a letter sent him by my attorney he said it was a sale, that I knew it was a sale, and he was not interested in returning my stock. In the time elapsed after I put up my stock as security for loan the mill cleared right at a million dollars.

My attorney advised me that due to the disproportionate amount of money advanced by Mr. Hoffman in relation to the total value of the stock and coercion imposed upon me by the Internal Revenue Service, my initial effort should be to attempt to recover the stock from Mr. Hoffman. My attorney further advised that the Federal Tort Claims Act exempts the Federal government from any liability in connection with assessment or collection of any tax and if redress were to be obtained against the government it would be necessary to obtain the

passage of a special act of Congress to confer jurisdiction upon the court of claims to hear my claim. Having subsequently brought an action against Mr. Hoffman for civil redress, I have had attorneys' fees, CPA fees and appraisers' fees in excess of $90,000,00, and other expenses. This ordeal has been going on for about six years and has just about left me a Welfare case. The six years plus have taken a terrific toll of worry, health and cash.

After a searchng evaluation of an offer made to me by Mr. Hoffman's attorneys for my remaining one-eighth interest in the mill, we decided our best course was to accept and put an end to the litigation expenses. Mr. Hess, Mr. Hoffman's attorney, assured me and I have no reason to doubt it, that in case I were to get a favorable verdict at the trial set for the 6th of November, 1972, they would appeal the case clear to the U.S. Supreme Court if necessary. I have been hiring attorneys and CPA's for going on the seventh year.

In this settlement with the Ronde Valley Lumber Co. and Mr. Hoffman they have agreed to pay me $335,000.00 spread over three taxable years. This pretty well sets a value on what the I.R.S. beat me out of. Three hundred thirty-five thousand dollars for one-eighth interest in the mill figures out that the stock I was forced to let go was worth three times that, or $1,000,000.00, when in fact I owed the Internal Revenue Service nothing. This does not take into account the attorneys' fees, accountants' fees, or in any way the terrific mental toll on my wife and me.

I have, in the last seven years, worried myself nearly into the grave and the Internal Revenue Service was dead wrong on every point. The whole mess could have been avoided if they had just been content to tie up all my assets, which were worth more than ten times the amount of the assessment.

My books were available for inspection to the state and federal income tax boys at any time at the office of Lippold, Brenner and Bingenheimer in Salem, Oregon. They quite evidently never examined them or they would have known that I did not owe anything. In fact, I believe I had a small refund due me at that time. When, in the first week of March, 1960, I first contacted my attorney, Mr. Leo Meysing, 414 Pittock Block, Portland, Oregon, and told him my problem he told me there was something queer about this case. He said the Internal Revenue Service does not usually impose jeopardy assessments and moreover are forbidden by law to sell property seized in connection therewith unless the same is of a perishable nature. He, like I, has never been able to ascertain why the Internal Revenue Service took the action it did except to wilfully use the full power of the Federal Government to destroy me financially.

Where is there any semblance of justice or constitutional right in this land of freedom? There just is no such thing when the I.R.S. decides to clean you out. You are guilty till proven innocent, and you can be 100 per cent innocent but still it is up to you to pay the expenses and prove your innocence in a country where you are supposed to be innocent till proven guilty. With the I.R.S. this just isn't the case. What protection does an honest taxpayer have against a totally wrong, vicious claim made against him by the I.R.S.?

One can shoot and kill a presidential candidate and it would seem that every segment of our legal process immediately goes all out to provide every means, including a tremendous amount of taxpayer money, to see that he gets all the help possible to protect him, be he a U.S. taxpayer or otherwise. The last I heard the so and so was still with us and the taxpayers were paying his keep (speaking of Sirhan Sirhan).

When the I.R.S. finally decided I owed them nothing, the IRS sat down and figured up what tax I should have paid on the sale of the ranch and came up with a figure that was within $5.00 of the amount my accountant had figured I owed at the time of the sale and which amount I had paid to the I.R.S.

It looks funny that they were so anxious to levy the jeopardy assessment when they surely knew I did not owe anything or would have known if they had done even a superficial search of my records. They would have been just as sure of obtaining their money with a lien on all my assets as they were in forcing the sale of my stock to get it.

Where does our vaunted justice for all, and constitutional rights, come into this picture? The I.R.S. can be completely wrong as they were in this case, vicious to the last degree, but are totally and completely immune from any responsibility for their mistakes (if indeed it was a mistake).

Who thinks the Gestapo of Germany or the Secret Service of Russia were tough? If so, they haven't dealt with our I.R.S. for it is just as arbitrary. What can a totally innocent taxpayer do to right the wrong done him by the I.R.S.?

My attorney has been a tax attorney for years and he tells me this is the most unjust case he has ever seen or heard of.

If you care to try to do something about this case I'll be glad to get all the data I have relative to it and meet with you at your convenience and go into all details. This letter is rather lacking in details but one thing speaks for itself The I.R.S. gave me back the $119,000.00 plus something like $24,000.00 in interest for the time it took us to convince them they were entirely wrong in their actions against me. The thing that bothers me is that I lost a lifetime of work through a false claim made against me by the I.R.S. My attorney tells me they had the authority to place the assessment against me if they thought they might be in danger of losing the tax monies due them, but they were absolutely wrong and acted in violation of the law in forcing the transfer of my stock. My mill stock was worth, at that time, nearly ten times the amount of their levy. I could not possibly have beat them out of it in any way. If they had levied against the stock pending the outcome of my efforts to prove I did not owe that amount they would not have had to pay interest on the $119,000.00 for the time they held it.

They were dead wrong all the way, but they cost me a lifetime of earnings and aren't even sorry for all the loss and expense they have caused me. The mill and its holdings in land, timber, cattle and machinery is probably worth twice what it was in March of 1966 and it was worth nearly $2,000,000.00 then.

One thing that could be done which I am sure would cause the I.R.S. to at least look at one's records before starting an action would be to hold them financially responsible for all costs when they are proven wrong. In my case that would have come to many thousands of dollars.

When they levy a jeopardy assessment against one and tie up all his assets his credit is gone completely. If I had not had friends who were willing to loan me the cash to fight for over six years I would have lost everything I had worked a lifetime for, including my home. It seems that the I.R.S. operates with that fact in mind. Most people are afraid to fight them, do not have the cash or credit to do so, and as in my case, everything one has accumulated goes by default.

I'll admit that in the over three years it took me to get that $119,000.00 returned to me there were many times when I seriously considered giving up trying to recover even though I knew I owed no part of the assessment against me.

Sincerely yours,

EDSON R. MCCANSE.

[From the Observer, LaGrande, Oreg., Mar. 21, 1975]

LOCAL MAN'S DISPUTE WITH IRS WILL BE SHOWN ON TV

(By Mike Revzin of the Observer)

Ed McCanse, 74, 1502 1st St., has fought a battle with the Internal Revenue Service (IRS) that he says has cost him heavily—financially and emotionally.

Details of McCanse's case, along with other taxpayers who have had disputes with the IRS, will be documented on ABC–TV's "Close-Up" program, shown locally on channel 2, (cable 2 and 6) at 10 tonight.

McCanse claims he lost $1 million worth of stock in his effort to raise money to pay $119,000 worth of taxes which the IRS later said he didn't owe.

McCanse's case began in July 1964 when he and his two daughters sold their ranch and farming property near North Powder for $960,000. Thirty per cent of the purchase price was paid in cash, with the rest being paid in installments.

During the latter part of 1965, McCanse and his daughters were audited by the IRS. As a result the IRS claimed McCanse owed $119,000 in taxes and placed a jeopardy assessment against him.

A jeopardy assessment is used by the IRS when it believes that, if it waited the usual 30-day appeal period, the taxes would be uncollectable, such as in a case when someone is taking his assets out of the country.

John Doss, who is currently chief of the IRS collection division in Oregon, says that jeopardy assessments are rare, that there have only been two in Oregon since 1968 and that they must be reviewed by people at three levels of the IRS, all of whom must agree it is necessary.

McCanse says that IRS claimed he did not report money he earned from the sale of property, livestock and machinery.

"Somebody had to have fed them a bunch of information that was entirely false," he said. "The cattle, machinery and irrigation equipment they claimed I had sold had all been taken to my daughters' ranches in British Columbia and were not sold."

Doss, who was not personally involved in this case but says he is familiar with it, explained the IRS reason for a jeopardy assessment.

"In this particular case, the investigation at the time indicated to the investigation officer that, in his opinion, the collection of tax would be in jeopardy if we waited to assess it," said Doss, adding that IRS officials at higher levels agreed with this opinion.

"In this case, I think the feeling was that the taxpayer (McCanse) was divesting himself of assets in Oregon and was planning to move to Canada to avoid the payment of taxes."

Doss said that, when a jeopardy assessment stops someone from doing something, it is difficult to prove that he would have done it if the assessment had not been made.

MONEY RETURNED

McCanse raised the money to pay the $119,000 in taxes, but three and a half years later the IRS returned the money, along with $24,000 interest, and said that he did not owe it.

McCanse feels the IRS made a mistake, but Doss says the refund to McCanse was the result of a court decision which changed the interpretation of tax laws regarding installment purchases.

At the time of the jeopardy assessment, McCanse owned 50 per cent of the stock of the Ronde Valley Lumber Company, Union. McCanse says that the IRS seized his personal bank account and threatened to sell his stock to raise money for the taxes that it said he owed.

Doss says that a lien was placed on his property and a notice of levy was served on his attorney. He adds that McCanse was given approximately 40 days in which to post a bond to insure payment of taxes or to pay the taxes.

McCanse says he asked the IRS for an extension of time, but that the IRS refused at the last minute. Doss contends that the IRS gave him an extension of "two or three days."

SEEK HELP

McCanse says he went to his partner, C. W. Hoffman, 1105 L Ave. and asked for help.

According to McCanse, Hoffman agreed to loan him $119,000 for the bond if McCanse would put up three-fourth of his stock as security for the loan.

McCanse says that Hoffman told him that this transaction would be temporarily treated as a sale. But, according to McCanse, "Mr. Hoffman assured him (my accountant) I could have it (the stock) back any time I paid back the loan."

In August 1969 McCanse received a refund for the $119,000 from the IRS. But, according to McCanse, when he contacted Hoffman about his stock, Hoffman reportedly told him, "He was not interested in returning my stock," and that "I (McCanse) knew it was a sale."

When contacted by The Observer, Hoffman said that the transaction involving McCane's stock was definitely a sale, not a loan. "It wasn't a loan at all," he said. "It was a sale."

"I bought three-fourths of his stock," Hoffman continued. "Then, two or three years after that, he claimed it was loan. We had it in black and white here where he signed paper after paper that it was a sale. It was not a loan. We never spoke of a loan."

McCanse sued Hoffman to recover his stock, but the case was settled before it came to trial with Hoffman and the company buying McCanse's remaining one-eighth interest in the company for $350,000. McCanse contends that, based on this price, he had been forced to let go of $1 million worth of stock for $119,000.

NO VICTORY

McCanse says that his success in getting his money returned by the IRS was not a victory. He estimates that he spent $70,000 in fighting the case, and said that the greatest loss was in having to give up his plans for travel, and suffering years of worry about whether or not he would be able to repay the thousands of dollars he borrowed from friends and relatives to fight the case.

McCanse says that the IRS would have been just as sure of collecting its money (if the IRS claim had proven true) by placing a lien on his assets, rather than on forcing the sale of his stock. "They had all my property tied up. They couldn't possibly lose anything," he said. It was just viciousness on their part.

"They (the IRS) are above the law. They're not responsible for their mistakes or any damage they may do to you."

Doss replied to this charge. "None of our employes are subject to personal suits for going about the performance of their duties in accordance with the law and procedure," he said, but added, "If they do it incorrectly or wrongfully, they can be held accountable."

He said that the public is safeguard against mistakes by the IRS through the constant scrutiny by Congress and the press as well as by self-scrutiny by the IRS.

"The type of situation with Mr. McCanse is a troubling matter for him, I know," said Doss. "And it is of concern to the IRS. I do want to stress one thing. At the time we're talking about, 1965 and 1966, the facts of the situation then indicate that our people proceeded in accordance with laws and regulations and all the safeguards that are built in."

Senator HASKELL. Our next witness is William T. Plumb of Washington, D.C.

STATEMENT OF WILLIAM T. PLUMB, JR., ESQ., HOGAN & HARTSON, WASHINGTON, D.C.

Mr. PLUMB. Thank you, Mr. Chairman.

Although it is in the power of Congress to insist that a taxpayer pay first and litigate later when a disputed tax is determined against him, it has been the policy for half a century, in the case of income, estate and gift taxes, to allow the taxpayer to have a proposed assessment reviewed by the Tax Court before he is compelled to pay. An exception was necessarily made, however, for the situation where collection of the tax would be jeopardized by delay.

Through the years, Congress has expanded the rights and protections enjoyed by one against whom a jeopardy assessment is made. The Commissioner is required to send a deficiency notice within 60 days after the assessment, so that the taxpayer may enjoy the same right of Tax Court review that others are entitled to. Until the Tax Court has decided the case, the tax collector is forbidden to sell the taxpayer's property, unless it is perishable or would be unduly expensive to retain.

Senator HASKELL. Mr. Plumb, it is a little hard to follow you when you read that fast. Your statement will be included in the record in full. I think it would facilitate matters if you could just talk to me.

Mr. PLUMB. I am afraid that my capacity to just talk—I am not a courtroom lawyer. I think I can do it better by reading. I will try to hold the speed down, but I have a tendency to let go. I will try to control it.

Senator HASKELL. All right, go ahead.

Mr. PLUMB. Unless the taxpayer can give a bond, which is impossible in the many cases where the assessment exceeds the taxpayer's assets, other collection measures may be taken even while the contest in the Tax Court continues. His bank accounts, receivables and wages may be seized under levy, automobiles and other movable assets may be seized and held in storage, but not sold. His business may be placed in the hands of a receiver, and tax liens may be filed against all his property.

In consequence, he will be unable to get business credit unless he is able to negotiate a subordination agreement with the tax collector;

which in the situation we have been talking about this morning, is not likely to happen. He may be unable to practice his trade, to pay his living expenses, to keep his property insured and in repair, or to pay the legal and accounting expenses of establishing that the tax is not owing or of defending related criminal charges.

The courts have almost uniformly held that there is no right of preliminary judicial review of the Service's belief that a jeopardy assessment is justified.

Termination assessments are similar in purpose and effect, but they presuppose a more urgent situation of jeopardy, usually involving some affirmative act of the taxpayer designed to avoid collection of the tax, and making it necessary to terminate the taxable year prematurely and compute a tax for the short period, which may be immediately collected.

I might say that in the Manual that the first witness spoke about, the guidelines, including the fact that you are engaged in criminal activity and so forth are the same. They do not require any affirmative act. But the law contemplates, I think, that there be some affirmative act that indicates you are either going to leave the country or conceal your assets or whatever in order to terminate the taxable year.

Although collection of termination assessments too may be stayed by giving bond, if the taxpayer is fortunate enough to be able to do so, this long neglected provision fails to provide expressly for Tax Court review or for delaying sale of the taxpayer's property until the liability has been judicially established.

The courts of appeals are divided on whether the termination assessment is really a form of jeopardy assessment, to which those protections apply by implication, and the issue is now pending before the Supreme Court.

Drastic as those remedies are, they are undeniably necessary in appropriate cases. But it is vital that such powerful weapons, which have been called "the sovereign's stranglehold on a taxpayer's assets," and which necessarily bear most heavily on those who are financially less secure, should be confined to their proper purpose.

Despite stringent internal administrative safeguards, there is some evidence that the termination and jeopardy procedures have been used against criminal suspects to inflict a form of punishment without trial, by seizing and selling all the taxpayer's property to satisfy a tax liability arbitrarily determined.

The first essential form of relief is to provide a speedy disinterested review of the question whether the tax is actually in jeopardy. Mistakes do occur, as well as plainly arbitrary actions, and it is contrary to our concept of fairness and justice that the only protection a person has against abuse of these extraordinary powers—whether he is a criminal suspect or an ordinary citizen—lies in the Service's own internal policy limitations and review.

Even if only a few of the publicized cases of alleged oppression have substance—and many of the reported cases arose on motions to dismiss, so the facts may or may not be true as presented by the taxpayer in the case—the Congress should be concerned that they occur at all, with no remedy afforded.

The American Bar Association, therefore, in 1958, urged legislation permitting the district courts, by declaratory judgment, to determine,

in advance of payment, whether collection of a tax is in fact in jeopardy. If it is not, the Service would be remitted to the customary procedures for determination of the tax. The reform is a highly desirable one, although I have called attention in my paper—that is the longer paper that I have filed—to a number of technical and substantive improvements that ought to be made in it.

The most significant modification I would urge is that, if the court does find that jeopardy exists, it should be empowered nevertheless to give the taxpayer partial relief if it finds the tax is arbitrary or excessive, by making a preliminary determination of the maximum amount that appears likely to be sustained in later litigation of the merits.

The court might then limit the lien of the jeopardy or termination assessment and the amount that may be collected or retained pending final disposition of the case, without prejudice, however, to the rights of the parties to establish a greater or lesser amount in the Tax Court.

I believe an earlier witness spoke of a bill that your committee had in draft. I have only seen the one that the Ways and Means Committee released a few days ago. That bill would provide a procedure for testing not only whether there is reasonable cause for making the jeopardy or termination assessment but also whether the amount assessed was "appropriate under the circumstances."

Since the finding is to be made within 20 days after the taxpayer petitions for relief, it is obvious that a final determination of the tax is not contemplated at that stage, but that the committee envisions the preliminary finding of unreasonableness that I have suggested. But the draft bill would place jurisdiction in the Tax Court, not the district court, necessitating that a commissioner of that court be instantly detached from his other duties and assigned to journey to the taxpayer's vicinity in time to hear and decide the matter within the 20-day period.

Even if only a few hundred jeopardy and termination assessments were made in a year, as was the case before the flood, the seven Tax Court commissioners would be kept jumping around the country and would have no time for their other duties. I wonder if it might not be more efficient and economical to vest the power to make the preliminary determination in the local district court, as the ABA proposed.

Another proposal of the American Bar Association, which is not reflected in the House bill, would empower the district court, even if jeopardy exists and the asserted tax exceeds the assets, to order release of funds to pay the necessary expenses of civil or criminal litigation relating to the tax liability, as well as the costs of necessary repair, maintenance, and preservation of the liened property and certain other tax liabilities. That too is desirable relief, although in my paper I have suggested some technical improvements.

One substantive suggestion is that some modest amount of the taxpayer's funds ought also to be allowed to be released by the court for the essential living expenses of one whose bank account, wages, and means of livelihood are frozen by the still unsettled tax assessment.

The recent litigation on termination assessments has brought to the fore the urgent need for expeditious determination of the merits of such exactions. Because if the tax is found to be in jeopardy, the taxpayers property is still going to be tied up for an indefinite period and it should be speeded up in some way that the merits can be reached.

The more concerned courts have therefore required that a deficiency notice be issued within 60 days after the termination assessment is made, so that the taxpayer may go at once to the Tax Court. While that may be the best that can be done within the framework of interpretation of existing law, I regard it as an exercise in futility. Long before the Tax Court can hear and decide such a case on the merits, the normal taxable year will have been completed and the determination for the short period will have become moot.

I suggest instead that a relatively short but not impossible time limit, following the filing of a return by the taxpayer for the full year, should be prescribed within which the Service should be required to make a definitive determination of a deficiency for the year as a whole, on pain of having the termination assessment vacated.

Meanwhile, of course, the taxpayer's property will have been in custody or tied up by a lien, but letting him petition the Tax Court before th full-year determination is made would afford little relief from that problem. Relief in that regard is better provided by empowering the district court or the Tax Court, in a preliminary summary proceeding, to determine the existence of jeopardy and to limit the lien to the maximum amount of tax that appears likely to be sustained.

There is need for protection also against forced sale of the taxpayer's property pending final determination of the merits of the tax. That is now provided in the case of ordinary jeopardy assessments of income, estate, and gift taxes, but whether it applies also to termination assessments is in dispute.

Such relief clearly is now unavailable in the case of miscellaneous taxes, which can be collected as soon as assessed, whether the regular or jeopardy procedure is used, there being no right in any case to prior Tax Court review. While the Service is often willing to hold off collection of miscellaneous taxes, if the taxpayer makes a test case by paying the tax on a single item or transaction, there is no compulsion on it to do so.

The Ways and Means draft bill would extend the protection from forced sale to income tax termination assessments, and also to jeopardy assessments of miscellaneous taxes, but the protection would last only until the preliminary determination, adverse to the taxpayer, is made that jeopardy actually exists.

Consistently with the present rule for jeopardy assessments of income taxes, the restraint on forced sale should extend for the duration of the contest of the merits of the tax, conditioned upon prompt pursuit of the appropriate remedies. In the case of miscellaneous taxes, the rule should be no less generous to one against whom a regular assessment is made than to the victim of a jeopardy assessment.

Senator HASKELL. Now, Mr. Plumb, you have practiced law for a considerable length of time. Have you personally dealt with these jeopardy or termination assessment matters?

Mr. PLUMB. Not to any significant extent. I am primarily a corporate tax man. I got into this through bar association activities about 20 years ago and became a writer on this subject, but I have not had a great deal of practical experience on it.

Senator HASKELL. You have been following the area for about 20 years though?

Mr. PLUMB. Yes.

Senator HASKELL. Then from your experience in being interested in the area, under what circumstances does the IRS usually make a termination assessment?

Mr. PLUMB. Until the recent drive on the narcotics suspects and so forth, I think it was primarily made when an alien wanted to leave the country. He was required to file a return up to the date of his departure. And they then assessed the tax. Now, of course, if one leaves without going through that procedure, then they would probably make an assessment against him when they hear he is going to leave.

It became a device used against criminal suspects just in the last few years, as Mr. Silver mentioned. I do not believe there was a great deal of it before. There were only, I think, seven or eight reported cases involving any mention that a termination assessment had been made up until a few years ago.

Senator HASKELL. Suppose the law was amended as you indicate and there would be some kind of a hearing ahead of time—where the Government would have to set forth a jurisdictional basis for making a termination assessment or jeopardy assessment as the case may be; and also as you suggest, make some kind of prima facie showing of the amount due—what would be your reaction as to whether or not that would hamper the Internal Revenue Service in its tax collection proceedings?

Mr. PLUMB. I think they ought to have at least something to show the court. Obviously, however, they are going to have cases where the tax is pretty much a guess, because if a man is caught at the border, for instance, they are going to have to guess at that tax then and there or the money is gone.

Now I think what we need is an immediate procedure to straighten out the facts. But I think the Service has to have the power to assess because, if you find a man leaving the country with $200,000 in the motor of his car—and there was one such case—there is a pretty good reason to believe—it may or not be—but the circumstances suggest that there is a tax due. It takes some time to find out what it is and the Service has to act fast.

I think the Service needs that procedure, but we also need very much the procedure to get the man an immediate hearing on the subject.

Senator HASKELL. And your suggestion for the immediate hearing is the local Federal district court, as opposed to the Tax Court for the reasons you gave?

Mr. PLUMB. Yes. I think that is a practical way, because that court is always there. The Tax Court visits the area periodically: in some areas, not very often. The Tax Court Commissioner, as I say, has other duties. So I do not think it is a practical—of course, the Tax Court can speak better to that than I can, but I do not think it is a practical course.

Senator HASKELL. Mr. Morris has suggested a question to me. Some people might feel that the Tax Court is the more appropriate place to determine that jeopardy exists. So, if Congress should decide that the Tax Court is more appropriate, would that, in your opinion, mean that we should decentralize the Tax Court as opposed to the present system of sitting in Washington and making periodic swings around the country?

Mr. PLUMB. I think it is helpful to have a full Tax Court available in one place. I mean, of course, many cases are in effect decided en

banc, the more important ones. I think, in the first place, 16 judges—assuming that remains the figure—would be spread pretty thin around the country. That is an independent question of how the Tax Court should operate. But I do not really think it would contribute to solution of this problem.

Incidentally, on the question of whether the Tax Court is better qualified to decide the resistance of jeopardy; the Tax Court has never had the question of deciding whether tax is in jeopardy. That is a question that never comes up. That has been an administrative question and there has been no judicial review at all. And I do not think the Tax Court's experience specially qualifies it to determine—and the judge on the scene perhaps is better able than the Tax Court judge to decide—whether the man is about to abscond or has assets that he is dissipating or taking out of the country.

That is the kind of question that district judges can handle.

Senator HASKELL. All right, sir, I thank you very much for appearing. Your testimony is very thoughtful and helpful.

Mr. PLUMB. Thank you.

[The prepared statement of Mr. Plumb follows. A subsequent letter received from Mr. Plumb appears at p. 236 of this volume. Oral testimony continues on p. 79.]

PREPARED STATEMENT OF WILLIAM T. PLUMB, JR., WASHINGTON, D.C.

JEOPARDY AND TERMINATION ASSESSMENTS

Historically, the only way a taxpayer could contest a federal tax assessment, if agreement could not be reached administratively, was to "pay first and litigate later." [1] If he failed to pay the disputed assessment voluntarily, his property became subject to an all-inclusive lien for the disputed tax liability, [2] and could be seized and sold under administrative levy. [3] Prior to payment or enforced collection, he could not obtain review of the assessment by injunction or otherwise, [4] except perhaps in extaordinary and exceptional circumstances. [5]

The controlling notion in the early years of our history was that "no government could exist that permitted the collection of its revenues to be delayed by every litigious man or every embarrassed man, to whom delay was more important than the payment of costs." [6] Over 50 years ago, however, rightly sensing that such fears were exaggerated and concluding that the "right of appeal after payment of the tax is an incomplete remedy, and does little to remove the hardship occasioned by an incorrect assessment," [7] Congress established the Board of Tax Appeals (now the Tax Court) as a forum in which proposed deficiency assessments of income, estate and gift taxes might be litigated before payment. [8] The statutory prohibition on injunctions was modified to permit the taxpayer generally to obtain an injunction against assessment or collection of any of those taxes until he had been given a notice of the deficiency and an opportunity to contest the validity of the tax before the Board. [9]

JEOPARDY ASSESSMENTS

It was recognized, nevertheless, that circumstances might exist in which the tax had to be collected quickly or it might not be collected at all. The 1924 Act provided, therefore, as does the law today, that those taxes might be immediately assessed and collected, without the delay occasioned by sending a deficiency notice and awaiting decision by the Board (or Tax Court), if the Commissioner "believes that the assessment or collection of a deficiency will be jeopardized by delay." [10] The general prohibition on injunctions applies in such cases, so the taxpayer cannot contest the merits before payment by bringing a suit to enjoin collection of a tax he considers to be excessive, even if he can show irreparable injury (such as the ruination of a business or the impoverishment of a family). [11] unless he is able to show in addition that the tax is so arbitrary, excessive, and without factual foundation that under no circumstances could the Government ultimately prevail. [12]

In 1926, Congress concluded that the taxpayer who suffers such a jeopardy assessment should not be denied the same opportunity as any other taxpayer to seek review of the tax liability by the Board (or Tax Court). Since a deficiency notice is the essential jurisdictional "ticket to the Tax Court," [13] it was prescribed that a deficiency notice be mailed within 60 days after the jeopardy notice if none had previously been sent. [14] Because of the exigencies of the jeopardy situation, however, certain collection efforts may go forward before and during such a contest of the merits. [15] Failure to send the deficiency notice in the time prescribed, however, may invalidate the jeopardy assessment, [16] although the Commissioner then may simply make another timely assessment and gain another 60 days in which to send the notice, [17] while the taxpayer's funds and property remain tied up and collection efforts continue. It is at least theoretically possible that the taxpayer's access to the Tax Court might be deferred indefinitely by the making of a series of jeopardy assessments within the period of limitations, with only the last being followed by a deficiency notice.

Congress, seeking to balance the interests of the taxpayer and the Government in cases where a disputable tax has been assessed by jeopardy procedures, has provided a number of ways in which undue hardship may be avoided.

From the outset, it was provided that collection of the assessment might be stayed until the outcome of a Board (or Tax Court) contest by filing a bond to secure payment of the amount determined to be due. [18] That remedy is likely to prove illusory, however, for the very financial circumstances that cause a jeopardy assessment to be resorted to will often make it impossible for the taxpayer to procure a bond. [19]

In 1953, Congress provided further that the jeopardy assessment might be abated, allowing the contest to proceed in the normal course like a regular deficiency case, without need for a bond, if upon review it was determined that the tax was not in jeopardy after all. [20] But that too may be a doubtful remedy, for it depends upon convincing the same official who found the tax to be in jeopardy that a mistake has been made. [21] No right to a formal administrative hearing is accorded the taxpayer, [22] and the right to judicial review of the finding is very doubtful. It is clear, at least, that the Tax Court is confined to consideration of the merits of the tax and may not examine into the existence of jeopardy; [23] and the absence of jeopardy is not a ground for a court to order refund of the tax collected under such an assessment. [24] That leaves the possibility of review of that issue by an injunction suit, since in the absence of jeopardy the general statute permitting assessment and collection to be enjoined until normal deficiency procedures have been followed is applicable. [25] One court has allowed such injunctive review, [26] but most have stated, with little or no analysis, that the determination of jeopardy rests solely in the tax collector's discretion, subject to no review by the courts. [27]

Prior to the 1954 Code, if no bond was filed and the jeopardy assessment was not otherwise abated, a taxpayer's property might be sold under levy before the merits of the jeopardy assessment could be adjudicated, causing substantial hardship for many taxpayers, who not only lost their businesses or other property beyond recall [28] but who, on ultimately vindicating their position in the courts, could recover only the proceeds derived from a forced sale, since that amount, rather than the true value of the property, was all that had been credited on the erroneous tax. [29] The 1954 Code provided significant relief from such hardships by forbidding the forced sale of the taxpayer's property under a jeopardy assessment until the expiration of the time within which he may appeal the deficiency to the Tax Court and thereafter, if a petition is filed, until the tax determined by the Tax Court would be assessable in the absence of jeopardy. [30] Prompt sale is permitted, however, if the expenses of conservation and maintenance will greatly reduce the net proceeds, or if the property is perishable. [31]

An amendment by the Federal Tax Lien Act of 1966, although not confined to jeopardy assessments, afforded relief from the practice of enforcing tax liens on life insurance policies by causing their surrender, which had often destroyed irreplaceable family protection without commensurate benefit to the Government [32] a practice that one court likened to "wrecking of seized tangible property in order to secure its junk value." [33] Now, in most cases, a levy on life insurance may be satisfied by paying the Government the loan value, without destroying the policy. [34]

In other respects, however, a jeopardy assessment can still be devastating to a taxpayer, if he is unable to provide a bond. Although a sacrifice sale of his property during the pendency of a contest may now generally be avoided, a lien

foreclosure suit may be instituted as a vehicle for placing his business in the hands of a receiver pending determination of the merit. [35] Other property which might readily be spirited away or disposed of, despite the filing of the lien, may be seized under levies and retained by the tax collector without sale, [36] thus depriving the taxpayer of the use of his automobile and other essential personal property until the contest is settled. The taxpayer's wages, bank accounts, and other claims, being reachable without sale, may be appropriated by levy while the contest continues, thus possibly rendering him "indigent overnight" [37]—unable to pay his living expenses, [38] to keep his property insured and in repair, or to employ counsel and pay the other expenses of establishing that the tax is not owing [39] or of defending related criminal charges. [40] Even if the tax collector is content merely to file notices of lien, without actual seizure, [41] the resulting priority over later extensions of credit [42] may cause the drying up of sources of borrowed funds, on which the operation of the taxpayer's business may depend, unless the Commissioner in his discretion agrees to subordination of the lien. [43]

It is vital, of course, that the use of such a powerful weapon, which has been called "the sovereign's stranglehold on a taxpayer's assets," [44] and which necessarily bears most heavily on those individuals and businesses that are financially less secure, [45] should be confined to its proper purpose. The Service appears to have made a determined effort to bring the possibility of abuse of the power under control, by insisting that every jeopardy assessment be personally approved by the District Director. [46] Further approval by the Director of the Audit Division in the National Office is required if jeopardy is claimed to exist for any *reason other than* the standard ones that (a) the taxpayer is or appears to be designing quickly to depart the United States or to conceal himself or (b) to place his property beyond the reach of the Government by removing it from the United States, concealing it, transferring it or dissipating it, or (c) his financial solvency or appears to be imperiled other than by reason of the proposed assessment itself. [47] Requests for abatement on the ground that jeopardy does not in fact exist are required to be given expedited considered by the District Director personally, subject to review by the Assistant Regional Commissioner (Audit). [48] Officials are admonished to use jeopardy assessments "sparingly", to take "care . . . to avoid excessive and unreasonable assessments," and to limit the assessment "to an amount which reasonably can be expected to protect the Government's interest." [49]

It is impossible for one on the outside to assess the overall effect of those efforts at self-regulation. Although the Service apparently publishes no statistics on the number of jeopardy assessments, figures furnished informally to writers and practitioners in the course of years indicate a decline in the number from about 2,500 in 1958 [50] to 279 in 1966 [51] and "very few" (whatever that may mean) in 1972. [52] Instances of overreaching reported in magazines and on television may need to be discounted somewhat for the less than disinterested character of the sources; and those in reported cases must be read in light of the fact that they have almost invariably arisen upon motions to dismiss the taxpayers' complaints, the allegations of which must be taken as true by the court for the purpose of the motions. The Government, on the basis of the reported cases alone, may be subject to criticism not so much for having done what it was alleged to have done (which stands unproved, at least judicially), [53] but for standing on the position that, even if it did those things, the taxpayer is entitled to no judicial relief from arbitrary administrative action.

Nevertheless, enough objective facts appear in the reported cases to suggest that sometimes jeopardy assessments have been tailored, not to the evidence, but to what was necessary to exhaust the discovered property of the taxpayer, [54] or have been based on extreme and unsupported assumptions of fact. [55] Most often, those instances have arisen when the awesome powers of tax collection have been, as Commissioner Alexander has acknowledged, misused as an adjunct to criminal law enforcement, affording a means of "summary punishment to supplement or complement regular criminal procedures," and they perhaps reflect the breakdown of the Service's system of internal controls as a result of the use of interdepartmental strike forces. [56] But the powers that have been turned against the criminal element can be, and allegedly at times have been, turned against those holding unpopular (or merely opposing) political, social, economic or religious views, [57] or against the ordinary citizen.

Another occasional source of complaint among tax practitioners is that the threat of a jeopardy assessment, not otherwise justified by the circumstances,

has sometimes been used as a club to extract from a taxpayer an agreement to extend the statute of limitations when an audit is incomplete. [58] Actually, a normal notice of deficiency will protect the Government as fully against the running of the statute as will the making of a jeopardy assessment. [59] What the Government would gain by using a jeopardy assessment in these circumstances is a burden of proof advantage, since it has the burden of proving any new issues it injects into the case after the mailing of the deficiency notice, [60] and the jeopardy procedure allows it 60 more days in which to complete its investigation and perfect a deficiency notice raising all the issues it expects to rely on. But that is hardly a sufficient excuse for subjecting the taxpayer to the consequences of a jeopardy assessment. The Service maintains that it has put out stringent prohibitions against such use of jeopardy assessments, and that control is maintained since that ground is not one of those on which a jeopardy assessment could be made without National Office approval. [61] That defense may not be wholly responsive to the charge, however, since the threat of a jeopardy assessment might be made by the auditing agent even though he lacks the power to execute it; and the complaints of such threats do recur despite the Service's assurances.

TERMINATION ASSESSMENTS

Ever since 1918, the law has provided, with minor variations, that, if the Commissioner "finds that a taxpayer designs quickly to depart from the United States or to remove his property therefrom, or to conceal himself or his property therein, or to do any other act tending to prejudice or to render wholly or partly ineffectual proceedings to collect the income tax for the current or the preceding year," or if he finds that collection of the tax of a corporation will be jeopardized by a distribution in complete or partial liquidation, he shall declare the current taxable year immediately terminated. The tax for the short period and for the preceding taxable year, whether or not the time for filing a return and paying the tax has expired, then becomes immediately due and payable unless the taxpayer puts up a bond.[62] In all but name, the assessments made under this provision are jeopardy assessments,[63] although the law here "presupposes a more exigent situation of jeopardy" than that covered by the general jeopardy assessment provision.[64] However, although the provision is found in the subchapter of the Code headed "Jeopardy," it does not expressly label them jeopardy assessments, and it will help to distinguish the two procedures if I follow the Service's terminology and refer to them as "termination assessments." [65]

The Service's internal policy guidelines on termination assessments closely parallel those applicable to jeopardy assessments, as already described. Termination assessments must be personally approved by the District Director, and further approval by the National Office is required if none of the three standard grounds heretofore enumerated [66] are present; termination assessments are to be made "sparingly," using "care ... to avoid excessive and unreasonable assessments." [67] It is expressly stated that assessments arbitrarily made to equal the amount of assets available for distraint, or found on the taxpayer at his arrest, are not acceptable as constituting reasonable computations of tax liability.[68]

For the first 40 years the law was in effect, so far as the reported cases indicate, termination assessments appear to have been used very "sparingly" indeed,[69] except in connection with the short period returns required of aliens as a condition to their departure from the country.[70] But in recent years the termination device was discovered as an instrument of criminal law enforcement, particularly in connection with the Narcotics Traffickers Program instituted by President Nixon in 1971.[71] What had been a trickle of cases became a flood, with 600 termination assessments reportedly made in 1972 and 1,800 in 1973.[72] Although the Internal Revenue Manual mandates that its general requirements are to be "followed strictly in recommending and processing jeopardy assessments" under the narcotics program,[73] the reported cases—discounted, as they must be, for the fact that the Government, in moving to dismiss, never presented its side of the facts [74]—suggest that arbitrary assessments at least equal to the funds and property found on a suspect have not infrequently been used, on tenuous supporting evidence, to maintain control of what might otherwise have had to be returned on constitutional grounds.[75]

I have mentioned earlier several ways in which the adverse effects of regular jeopardy assessments may be relieved.[76] But, because termination assessments have existed so long in a little noticed backwater of the law, those reforms have not generally been expressly extended to termination cases. Provi-

sion is made, it is true, for stay of collection upon giving bond, [77] but that remedy in the typical case will be no more efficacious than the right to give bond in regular jeopardy cases. There is no statutory provisions for abatement of the termination assessment when the tax collector finds that jeopardy does not exist after all, as there is in regular jeopardy assessment cases; but the Service's procedural ruling may be interpreted as permitting it to take such action in termination cases as well. [78] On the other hand, the vitally important restraint on forced sales of seized property, pending a judicial determination of the liability, has not been expressly made applicable to termination assessments, and the Service has made or attempted sales in some such cases, [79] contending that such relief is unavailable to the taxpayer because it is provided only in the section relating to regular jeopardy assessments. [80]

Controversy has centered on the availability in termination cases of the right to have the liability promptly determined by the Tax Court, a right that Congress nearly 50 years ago deemed it equitable and proper to afford to the victims of jeopardy assessments. Whether this right exists depends on the source of the power to *assess* the tax in termination cases. The section permitting termination is silent on the power to assess the short-period tax, and the Government has acknowledged that the power must be found elsewhere in the law. [81] The debate in the courts has been over whether the power must be derived from the jeopardy assessment provision [82] (which imposes the condition of following the assessment with a deficiency notice and an opportunity for Tax Court review), or may be found in a general provision authorizing, without condition, the assessment of taxes other than "deficiencies" in income, estate and gift taxes. [83] That in turn raises the question whether the tax determined for the terminated period, before a return has been or could be filed, is a "deficiency", which the law defines, in substance, as the excess of the tax imposed by law over the sum of the amount shown on the return (if a return was made by the taxpayer) and amounts previously assesed as deficiencies. [84] The Seventh Circuit has held that the termination assessment was not an "imposed tax" but "merely an amount which the I.R.S. believed justified the termination of the taxable year," and that no "deficiency" was determinable since no return had been filed at the date of assessment. [85]

The Second Circuit further projected that holding by declaring that even when such an assessment was made for the full year, after the year had ended but before the return was due, it could not be a "deficiency" since there had been no return fied. [86] The fifth and Sixth Circuits reached the contrary conclusion, observing that the Commissioner's own regulations contemplate the determination of a deficiency in the absence of a return, treating the "amount shown as tax . . . upon his return" in such a case as zero and the full amount of tax determined as the "deficiency." [87] Although the amount determined may be tentative, it is referred to in the law as a "tax" for a "taxable period" that has been terminated, [88] and one for which the law prescribes that a short period return shall be filed, [89] a return which the Tax Court has held to be as effective as a full-year return to commence the running of the period of limitations on further assessments. [90] It is no less a return for a taxable period for the fact that the law permits the taxable period to be reopened by the Commissioner if he finds additional income to have been subsequently received, or by the taxpayer if he files a return for the full year. [91] And the amount found owing for a period for which a return is thus required to be filed is no less a tax merely because the taxpayer may in fact not file.

The disagreement among the courts concerning the right to Tax Court review is paralleled by a conflict over what alternative remedies the taxpayer may have. The courts that would grant access to the Tax Court point out that the Service would otherwise be enabled to wait as long as three years after the filing of a return for the full year (and, in one reported case did so), before providing the taxpayer with the deficiency notice that is his "ticket to Tax Court," and that meanwhile his money is tied up and his property may have been sold. [92] The courts on the other side point out that he can expedite matters by timely filing a return for the full year, asking refund of an overpayment if the amount collected under the termination assessment exceeds the tax shown on his return, and that after six months he may sue in the district court of the Court of Claims for a refund of the difference; or, if the Service believes he owes more than he shows on his final return (whether more or less than the amount of the termination assessment), it can then send him a deficiency notice from which he may appeal to the Tax Court. [93]

The courts that view the termination assessment itself as a statutory deficiency foresee an impediment to the taxpayer's obtaining prompt relief by suit for refund, if the termination assessment, as is often the case, exceeds the amount collected thereunder: [94] The Supreme Court held in *Flora* v. *United States* [95] that a taxpayer who claims he owes less than has been collected from him is powerless to sue for refund unless he first pays the full balance of the amount assessed against him, and the magnitude of some termination assessments may make this impossible. [96] On the other hand, the courts that view the termination assessment and collection as in the nature of an enforced deposit of estimated tax, rather than as a deficiency, insist that the *Flora* rule would be no impediment to a refund suit, despite the existence of an unpaid balance, unless the Service meanwhile makes a regular or jeopardy assessment for the full year, exceeding what has been paid (in which event the Tax Court would be open to the taxpayer). [97] Whatever the rule may be in that regard, there will be a delay, at the very least, from the time of the termination assessment (which could be quite early in the taxable year) until at least six months after the year ends before the taxpayer can even commence the action to recover his money and his property or its proceeds, if earlier access to the Tax Court is denied. [98]

The Supreme Court heard reargument in October on two cases that should resolve those questions. [99]

I have noted that, in ordinary jeopardy assessment cases, the courts have generally denied their power to review the Commissioner's belief that the collection of the tax is in jeopardy. [100] In contrast, in termination, the statute clearly contemplates some limited judicial review of that question, not only by prescribing that the Commissioner "find" certain facts, but also by stating that "In any proceeding in court brought to enforce payment of taxes made due and payable by virtue of the provisions of this section, the finding of the Secretary or his delegate, made as herein provided, whether made after notice to the taxpayer or not, shall be *presumptive evidence* of jeopardy." [101] As a practical matter, however, most termination assessments will be enforced by seizure and not by proceedings in court; and most of those that do require court action will probably ripen into ordinary jeopardy assessments for the full taxable year before they are reached for trial, [102] so actual court review of the existence of jeopardy issue is likely to be rare. Nothing in the termination statute permits the taxpayer himself to initiate by injunction suit an inquiry into the existence of jeopardy; those cases that have allowed injunctions have turned not on the absence of jeopardy but on the Commissioner's failure to follow deficiency notice procedures which those courts deemed applicable.

OTHER TAXES

The foregoing discussion has focused on jeopardy assessments of income, estate and gift taxes, and on termination assessments of income taxes. Since 1932, however, with an amendment in 1934, there has also been a provision for immediate assessment of taxes other than income, estate and gift taxes, if the Commissioner believes that the collection of such other tax would be jeopardized by delay. [103] Since such an assessment may be made whether or not the time otherwise prescribed by law for making a return and paying the tax has arrived, it combines the features of both the jeopardy and termination assessments heretofore discussed, although it goes by the name of jeopardy assessment.

Since none of these other taxes can in any event be litigated in the Tax Court prior to payment, there is naturally no provision for a deficiency notice to follow the assessment, and the provision restricting sale of the property pending such review is not made applicable. [104] The effect of such an assessment is to require payment in advance of the normal due date, and even immediately after a taxable transaction, without awaiting the end of the period for which the tax is normally computed. Where the due date of the tax has passed, the only effect of such an assessment is to deprive the taxpayer of the ten days of grace normally allowed the taxpayer between the date of notice and demand and the time when he must pay or be subjected to levy. [105] As in the case of normal assessments of these taxes (and jeopardy assessments of income, estate and gift taxes), collection cannot be enjoined except in extreme circumstances. [106] However, collection may be stayed by giving bond. [107]

There is an unexplained gap between this provision for immediate assessments of miscellaneous taxes and the provisions previously discussed. In the case of ordinary jeopardy assessments made after the due date, there is no gap, since the provision I first discussed (§ 6861) covers income, estate and gift taxes, which

are excluded from the section now under discussion (§ 6862). But the provision for closing the taxable period and for accelerating the due date of the tax for a completed period (§ 6851) is confined to income taxes, and the terms of § 6862 do not fill the gap—although the original 1932 version of that provision [108] did cover all taxes other than the income tax. Even though gift taxes are now payable on a quarterly basis, it is still possible that as much as 4½ months may elapse between a taxable gift and the time when a return is due. And 9 months after death are allowed for filing and paying tax on an estate tax return. Without some provision for terminating the taxable period in the case of gift taxes and advancing the time for filing a return in the case of both taxes, if jeopardy exists, it is doubtful that a technical "deficiency", on which an ordinary jeopardy assessment could be based, would exist.

SUGGESTIONS FOR LEGISLATION

Jeopardy and termination assessments are important tools in the tax collection process, and some accommodation of individual rights to the necessities of tax collection may be justified when the circumstances calling for their use exist. But I submit that those necessities can be accommodated without denying the citizen an independent review of the circumstances requiring such actions, and without impoverishing the less fortunate citizen for many months before he is enabled to obtain the determination of his liability that all others can obtain before payment. Since there are no more than a few hundred cases a year in which even the Service believes that the use of such extraordinary procedures is necessary, it can hardly be claimed that some further relief from their rigors would "dry up the sources of revenue or stop the Government in its tracks."[109] It is no answer to say (even if it is true) that the great majority of those against whom such weapons have been used are suspected criminals; for the injury is inflicted at a time when they are merely accused, not convicted, and continues irrespective of the outcome of their trial.

1. *Review of finding of jeopardy*

The first essential form of relief is to provide a speedy disinterested review of the question whether tax is actually in jeopardy. Although the power to make these assessments is currently exercised with restraint (except, until very recently, in the case of criminal suspects, mistakes, oversights, and arbitrary determinations do inevitably occur, and it is contrary to the ordinary citizen's concept of fairness and justice that the only protection he has against abuse of these exceptional procedures lies in the Service's internal policy limitations, and that his only remedy is a plea addressed to the same officials who made the determination. Internal review, even on a centralized basis, is meaningless when, as appears to have been the case in the recent alleged abuses by the interagency "strike forces," the departures from established standards are rooted in administration (not necessarily Internal Revenue policy.

The Commission's talk reported in 1975–9 C.C.H. Fed. Tax Serv. ¶6656 suggests that the manner of operation of the strike forces "decreases the control and supervision that IRS employees assigned to the team." That statement explains but it does not excuse. However desirable such cooperation with other agencies may be, it should not be permitted to involve the arming of lower echelon employees with power to use procedures based on the "imperious need" of the Government for revenue, for purposes foreign to the collection of taxes. What has occurred before can occur again, and "[i]t is repugnant to the values of a free society to leave citizens at the mercy of the bureaucracy solely on the faith that the bureaucracy will not act arbitrarily."[110] Even if only a few of the publicized instances of alleged oppression have substance, the Congress should be concerned that they can exist at all, with no effective external remedy afforded.

In 1958, after a two-year study, the American Bar Association recommended amendments to the Internal Revenue Code and the Declaratory Judgments Act, whereby the federal district courts would be permitted to determine, in advance of payment of a jeopardy assessment, the single question whether "the taxpayer has, upon a fair preponderance of the evidence, proved that the assessment or collection of the deficiency will not be jeopardized by delay." The court would be empowered to stay any further proceedings for collection pending determination of the action and, if jeopardy was not found to exist, to declare the assessment void and of no effect. The proposal provides that such actions be given calendar preference, in order to minimize delay in the collection of the tax where

jeopardy in fact exists. The court, however, would not be empowered in such a proceeding to determine the merits of the tax, which would be left to be determined by regular procedures. [111]

While the substance of that proposal, which is attached as an exhibit [112] deserves serious and sympathetic consideration, I would like to suggest several modifications that may make it better achieve its purposes:

a. As has been so often the case with reforms in this area, the proposal is limited to ordinary jeopardy assessments, under §§ 6861 and 6862, and overlooks the equally pressing need for a judicial hearing on the existence of jeopardy in the case of termination assessments under § 6851. The effects of either form of emergency assessment can be equally devastating to the taxpayer, and his right to independent review of the justification therefor should not depend upon whether the tax collector acted before or after the tax became due.

b. As the A.B.A. proposed, the stay of collection action should be in the discretion of the court, since an automatic stay could enable defeat the very purpose of the jeopardy or termination proceeding while the court is considering the existence of jeopardy. The court should be empowered to condition a stay upon appropriate protective measures, such as impoundment of funds or of readily concealable or disposable property.

c. The relief permitted under the proposal seems too narrow, being limited to a stay of collection pending the court's determination and ultimately a nullification and voiding of the assessment (and the resulting lien) if jeopardy if found not to exist. Levy under a jeopardy or termination assessment may be made with no waiting period at all. [113] In many cases, the taxpayer's money will have been seized before he can get to the courthouse, and nullification of the assessment will not automatically entitle him to its return, without resort to a refund suit in which the merits of the tax may be raised by the Government as a defense. [114] If the taxpayer who disproves the existence of jeopardy is to be restored to status quo, enabled to litigate his liability before parting with his money or property, the court which passes on the jeopardy issue should be empowered to order return of what has been seized under the assessment (without itself passing on the merits).

d. The relief provided for may also be inappropriate in the case of certain jeopardy assessments made pursuant to § 6862, relating to taxes *other than* income, estate and gift taxes. When such taxes are assessed before the normal due date of the return and payment of the tax, a nullification of the assessment may be appropriate. But § 6862 also provides for jeopardy assessments of such taxes *after* the time for payment is past. In those circumstances, the Service is within its rights in assessing, without opportunity for prior contest, even where jeopardy does not exist, so it appears inappropriate for the court to hold the assessment void. [115] If, as the draft report of the General Accounting Office to the Joint Committee on Internal Revenue Taxation is said to have recommended, [116] sale of property seized under a jeopardy assessment of miscellaneous taxes under § 6862 is to be precluded pending expedited judicial review of the liability, the same relief should be extended to regular assessments of such taxes, since (after the 10 day wait prescribed by § 6331(a)) the situation of the taxpayer is the same in either case.

e. The proposed provision for calendar preference may fail its purpose to assure a speedy determination of whether there is real justification for departing from normal procedures and denying the taxpayer the protections enjoyed by others. Under Rule 57 of the Federal Rules of Civil Procedure, [117] it has been held that, when the Government or an officer thereof is a defendant, the provision for calendar preference and a speedy hearing in declaratory judgment cases operates only after the case is at issue and cannot override the governmental defendant's right under Rule 12 to have 60 days in which to file an answer. [118] Of course, if the Government has not already collected from available assets of the taxpayer, it will have an incentive to answer quickly and establish its right to proceed with collection. But, in many cases, it will already have made seizure of as much as it is likely to get, and it can afford to wait the full 60 days before answering, while the taxpayer's opportunity to regain his property by proving the absence of jeopardy is deferred. What is really needed, in my judgment, is a proceeding as summary in nature as the writ of habeas corpus, [119] in which, without the delay of formal pleadings, [120] the court would determine the right to hold, not the person, but the money and property of the taxpayer pending determination of the merits in another forum.

f. The proposal provides no standards by which the courts may measure the existence of jeopardy; in fact, it fails even to change the present subjective

language of §§ 6861 and 6862, by which the right to assess depends merely on whether the Commissioner "believes" that collection will be jeopardized by delay. [121] Judicial review may thus be ineffective since, without standards, the courts may be inclined in most cases simply to defer to the judgment of the collection officers. [122] It has been suggested that "standards similar to those in section 6851 on the propriety of closing the taxable year should be included to guide the Service and the courts." [123] Those standards, however, contemplate affirmative actions by the taxpayer that threaten to defeat collection if the taxable year is permitted to run its normal course, [124] and should not be regarded as exhausting the situations, including what may be called "passive" jeopardy, in which immediate assessment of deficiencies for past periods may be justified.

The Internal Revenue Manual contains an extensive list of conditions and circumstances that are viewed as establishing a prima facie case for making a jeopardy or termination assessments, such as criminal activities, engaging in gambling and other transactions that might result in sudden losses, having a past record of resisting or avoiding payment of taxes, and having known or suspected plans to leave the United States without providing for taxes. [125] That listing might be examined for suitability as statutory guides for judicial review, at least to the extent of giving presumptive weight to the Commissioner's findings when such circumstances exist. There is a danger, however, that such statutory particularization may result in converting what are now only indicators of possible jeopardy into mandates that assessments should be made when such circumstances exist.

g. One of the Service's internal standards for establishing jeopardy ought, I believe, to be re-examined. The Manual states that there exists a prima facie case for making a jeopardy or termination assessment if the facts and circumstances indicate that the taxpayer's present financial condition or future possibilities are such as to make collection of the tax doubtful. [126] Elsewhere, however, the Manual prescribes that such an assessment is not to be made where it is the proposed tax itself that would make the taxpayer insolvent. [127] I submit that, even with that restriction, the standard is too broad. The only really relevant fact in this regard is not the taxpayer's existing financial condition, but whether a delay, pending administrative and normal judicial consideration of the merits, is likely to *reduce* the fund available to satisfy the Government's claim, through concealment or disposition of assets, intervention of judgment liens, anticipated continuing losses, or the like. The fact that the taxpayer is insolvent now and will probably still be insolvent to about the same extent when the contest is over is not a good reason to impoverish him by collecting a still disputed liability that one in better financial shape would be permitted to contest before payment.

h. The insolvency test of jeopardy seems peculiarly inappropriate as a standard for whether to make a *termination* assessment, since the law and regulations contemplate that termination assessments be triggered, not by the mere existence of a condition (or even by the possibility that such condition will get worse) but by affirmative actions and contemplated actions designed to avoid payment of tax. [128] If the mere existence of insolvency were sufficient, the taxable year of an insolvent (who is making money for a change, in excess of available carryovers, or whose insolvency reflects high living or market losses rather than deductible expenditures) could be terminated, and immediate payment of an amount determined by the Service could be demanded and enforced, each time the insolvent received or was thought to have received significant income. It may be responded that such treatment would be consistent with the requirement of current payments of estimated tax, [129] although it differs in that the "estimate" is made by the Service without opportunity even for the review provided for jeopardy assessments and without restraint on the sacrifice sale of the taxpayer's property to satisfy the still disputed tax. Perhaps some such device is needed to deal with those who are not faithfully meeting their obligations to declare and pay estimated tax and whose financial condition makes the statutory penalties an inadequate remedy.

If it is thought appropriate, however, to put the Government's protection on a more current basis in the case of passive jeopardy (insolvency), it should be done by statutory standard, limited to cases where the insolvency appears likely to get worse, and accompanied by the amendments hereafter urged to restrict sacrifice sales [130] and to provide prompt judicial review [131] in termination cases.

i. It was mentioned at the Ways and Means hearing on this matter that a witness before Senator Montoya's Subcommittee on Appropriations in 1974 had recommended that jeopardy assessments be limited to taxpayers fleeing the United

States, since there exist other remedies against those who, with intent to defraud the Government, transfer or conceal their assets. I submit that the witness took on unduly narrow view of what can make collection more difficult or impossible. As Patty Hearst and thousands of runways have demonstrated, a person can disappear without leaving the United States. Money can be secreted within as well as without the United States even though the owner never leaves the country. Remedies are available, it is true, against transferees of property, but the Government must assume the burden of proving fraud or the absence of consideration. The witness' proposal takes no account of situations in which the taxpayer is simply sinking deeper into insolvency as time goes by.

j. The one statutory standard that would be expressed in the American Bar Association proposal (Exhibit A) is a negative one, that "The fact that the period of limitation for the collection of the tax is about to expire shall not be considered in the determination that the assessment or collection of a deficiency will be jeopardized by delay." The Service represents that it does not rely on that ground in any event, but expressing the restriction in the statute might help to remove whatever credibility an examining agent's threat of a jeopardy assessments in such circumstances might otherwise have (at least if the amendment is coupled with a right of quick judicial review of the grounds for jeopardy). Legislative consideration might be given, however, to alleviating the practical problem that has at times given rise to such threats by Service personnel—the difficulty of framing a sufficient deficiency notice to fix the normal burden of proof on the taxpayer when, for whatever reason, the notice must be prepared from available information when the statute of limitations is about to expire. [132]

The problem is a real one, even though the only heretofore available remedy was an excessive and inappropriate action that exposes the taxpayer to liens and collection action not warranted by the facts. To deal directly with that problem, it might be provided that, notwithstanding § 6212(c) (restricting further deficiency notices if the first one is taken to the Tax Court) and Tax Court Rule 142(a) (relating to the burden of proof on new issues), a supplemental deficiency notice sent within 60 days of the first shall be permitted and shall be considered, for burden of proof purposes, a part of the original notice. That is the same period of time the Service would have had in which to frame a sufficient deficiency notice if it had made a jeopardy assessment on the date the original notice was sent, and it is a short enough period so that the taxpayer would not be prejudiced in preparing his affirmative case.

k. If a court finds jeopardy not to exist and, as the proposal provides, declares the assessment null and void, a problem will arise where the period of limitations for sending a normal deficiency notice has meanwhile expired. The making of a timely assessment that is subsequently voided does not ordinarly suspend the running of the statute of limitations for making a new assessment.[133] An exception to that rule is provided in § 6861(g), suspending the running of limitations from the date of a jeopardy assessment until 10 days after it is abated by the Commissioner upon a finding that jeopardy does not exist. That provision should be broadened to embrace cases where the jeopardy assessment is voided by court action under the proposed law.

l. Under the proposal, if the court is unable to find the absence of jeopardy, it will have no choice but to dismiss the proceeding. I suggest that the court should in such cases be given some leeway in protecting the assets of a going business pending a final tax determination [134] and should be empowered to grant conditional relief from the jeopardy assessment if the taxpayer can tender less burdensome alternative arrangements that would preserve the status quo and prevent or control the encumbrance or dissipation of assets. The statutory bond, in the full amount of the tax, is obviously impossible for the taxpayer to furnish where the assessment exceeds the equity in his property; but giving a security interest in such assets as do exist might serve the purpose of preserving everything the Government could realistically expect to collect, and might be ordered by the court as a condition to letting the business continue without foreclosure until the merits of the tax can be determined. If even such an encumbrance would unduly hamper the operations of a business, some supervision by a court appointee might protect the Government without putting the taxpayer out of business or depriving him of possession and general control while the tax liability remains in doubt.[135]

m. In many cases, particularly those involving criminal suspects, the known propensities of the taxpayers may fully justify the conclusion that the collection of whatever tax is owing may be jeopardized by delay, and yet it may be clear to the court that the amount of the tax was arbitrarily determined in an amount

expressly designed to freeze all the suspect's property. Even though it may be thought inappropriate to have the merits of the tax determined in such a summary proceeding, consideration might be given to permitting the court to require the Government to make a prima facie showing of the manner in which the tax was determined, so that the court may make a preliminary determination of the maximum amount which is likely to be sustained in later litigation of the merits. The court might then be permitted to limit accordingly the lien of the jeopardy assessment and the amount that may be collected or retained pending final disposition of the case, without prejudice to the rights of the parties to establish a greater or lesser amount in the Tax Court or in a suit for refund. It should be made clear that the district court's jurisdiction may be invoked *either* on an allegation that the tax is not in jeopardy or that, even if in jeopardy, the assessment is arbitrary and unreasonable in amount.

n. It seems preferable to have this preliminary relief provided in the district court rather than the Tax Court. Speedy relief is essential at this stage, and the local district judge is always available, while the 16 Tax Court judges and a few commissioners riding circuit may reach some areas only at long intervals. A district court, even with a crowded docket, can act quickly if the issues are narrowed as above and if the court is directed to give the case top priority and to act summarily.

o. Although Congress has provided that the taxpayer's property, with some necessary exceptions, shall not be sold under a jeopardy assessment without his consent while the merits remain undetermined. [136] it has provided no express remedy by which the taxpayer may vindicate his right if the Service persists in holding a sale. The Government has argued, although unsuccessfully, that § 7421 of the Code, prohibiting injunctions restraining the collection of taxes, precludes relief in such a situation. [137] I suggest that, in addition to the jurisdiction which the Bar proposal would confer on the district courts, they should also be expressly empowered to protect the taxpayer from unauthorized sale of his property if that should be threatened.

p. The district court should be authorized to retain jurisdiction, once acquired, so that it can make such further orders as changes in the situation may require, such as one reinstating a jeopardy assessment that had initially been set aside or making any necessary modification in protective provisions it may have imposed as conditions to relief.

q. The suggested procedure encounters the century-old prejudice against injunctive or declaratory relief in tax matters. But Congress has recently recognized, with respect to pension plans, that irreparable harm may result unless declaratory relief is granted even in advance of the incurring of a tax; and a similar proposal for advance declaratory relief for exempt organizations is expected to be reported favorably in the pending tax reform legislation. Surely the need is no less for one whose property has been seized and threatened with sale, without being accorded the usual right of prelitigation of the liability, to have an immediate determination of whether the circumstances really require such drastic action pending appropriate judicial consideration of the merits of the tax.

r. It was mentioned at the House hearings on this matter that Senator Montoya had introduced a bill (S. 137) that would shift the burden to the Service to obtain judicial approval of a jeopardy assessment within five days after the assessment is made. I do not know the details of the bill, but apparently it would have an effect similar to that of the American Bar Association proposal except that the moving party in court would be the Service. This has the obvious advantage that the taxpayer, who may be unable to hire a lawyer (even to obtain the release of funds for legal expenses), is relieved of having to take the initiative, and the pressure is on the tax collector to avoid delay. Its disadvantage may be that affirmative action in court may be required of the Government even in cases that are so clear that the taxpayer would not have instituted a proceeding if the initiative rested with him. Such clear cases, however, should be quickly disposable by the court, and it does not disturb me that the Service, in making drastic departure from normal procedures and taxpayer protections, would have to support its action before a disinterested umpire in every case.

s. The question of which party should take the initiative in bringing the issue of jeopardy before the court also raises the question of burden of proof. It seems to me that, since the facts concerning the taxpayer's financial circumstances and intentions are entirely within his knowledge, the ultimate burden of negating jeopardy by a preponderance of the evidence should be on him, although the Service should be required to specify its grounds so that the taxpayer may know to what he should address his proofs.

2. Release of funds for counsel fees and other necessary expenses

A coordinate proposal by the American Bar Association would empower a district court, even where jeopardy exists and the assessment exceeds the taxpayer's assets, to order the release of funds or other assets to pay the legal and other "necessary" expenses of contesting both the civil and criminal aspects of the tax liability asserted in the jeopardy assessment. [138] Whatever the limits of the constitutional requirements [139] (and there appear to be none on the civil side), [140] common fairness would seem to require that the Government not prosecute the taxpayer and perhaps strip him of all he owns, while depriving him of the means of defending himself—which one district court described as "holding and hitting." [141] Although the majority of the appellate court in the case referred to raised the question whether the person who had property and was not able to get at it was entitled to more consideration than the one who was too poor in the first place to afford an adequate defense, Chief Judge Duffy, in dissent, saw a vast difference:

> Here the Government, by its deliberate act, by jeopardy assessment, captured the defendant's assets and thus denied him the use of his own funds to defend himself; the tools of defense were taken from him; the Government pauperized him by placing him in a financial straight-jacket. [142]

On the criminal side, it is true that court-appointed counsel are available, and Congress has, since the Bar proposal was made, provided for payment out of appropriated funds for "investigative, expert, or other services necessary for an adequate defense." [143] Tax litigation, however, is complex and expensive, and it is argued that "regardless of the quality of court-appointed counsel and of the amount of time which they can afford to donate, it is still repugnant to our concepts of justice to prevent a defendant from using his own property to hire counsel of his choice to represent him." [144] From the purely selfish standpoint of the Government, incidentally, there may be an advantage in relieving appropriated funds of the burden of the taxpayer's defense, enabling him to spend a possibly larger amount out of funds that would in any event be returned to him if he wins the civil case, and resulting in a smaller credit on his tax liability (and possible eventual collection from his later assets) if he loses.

The proposal would also permit release of funds necessary to repair, maintain and preserve the liened property, and to satisfy superior liens thereon (expenditures which ordinarily will be as beneficial to the Government as to the taxpayer), [145] and also to pay other taxes owed by the taxpayer "whether due before or after the making of [the] jeopardy assessment."

The release of the funds would be in the discretion of the court, which would be expected to impose reasonable safeguards against unwarranted expenditures. The release could be ordered irrespective of the adequacy of the taxpayer's remaining property to cover the jeopardy assessment or the probable amount that can be sustained. The Service would be authorized voluntarily to release funds for the same purposes without court order, but only after the taxpayer has filed a petition therefor in the court.

The substance of that proposal, which is attached as an exhibit, [146] deserves serious consideration, but I would like to suggest a few modifications that may make it better achieve its purpose.

a. Like the principal proposal, this one is confined to regular jeopardy assessments and ignores the equally pressing need for such relief when all a taxpayer's property has been tied up or seized under a termination assessment. This second proposal, in fact, fails also to deal with the like problem that may arise in the case of jeopardy assessment of miscellaneous taxes, such as gambling taxes, alcohol taxes, employment taxes, and others, under § 6862. [147]

b. The proposal would afford relief only when a notice of lien for the jeopardy assessment has been filed. No relief is afforded if, having already seized all or most of the taxpayer's funds and assets, the tax collector refrains from filing notice of the lien. Even if such notice is filed, only the lien may be released, and there is no provision for return to the taxpayer of funds actually seized from him or from his bank account and applied on the tax, before or after filing of the lien. If there is merit in the proposal to make funds available to the taxpayer for these essential purposes, it should not be defeated by the prior seizure of funds under the jeopardy or termination assessment.

c. The proposal permits release of the lien in order to pay litigation expenses only if the litigation relates to the very tax liability giving rise to the lien. Since civil tax liability, especially in cases where fraud is asserted, may relate to periods for which prosecution is barred by the statute of limitations. [148]

it is possible that a lien exceeding the taxpayer's assets might exist (or a seizure of his entire property might occur) with respect to a tax liability for which he is not prosecuted, leaving him unable to pay for the defense of a criminal prosecution for the later years. Such restriction on the relief ought to be reconsidered.

d. It ought to be made clear that the expenses of repair, maintenance, and preservation of property, for which release is authorized, include premiums on fire and other insurance on the property.

e. There is obvious justification in letting the taxpayer's funds and property be used to pay real estate taxes, which give rise to liens superior to even antecedent federal tax liens (§ 6323(b)(6)); and a reasonable argument can be made for letting current federal, state, and local income taxes be paid out of current funds, despite some resulting inversion of priorities. But I have difficulty seeing why the lien of the jeopardy assessment should yield place to other tax deficiencies and delinquencies for prior years if they are otherwise junior in rank.

f. Consideration should be given to permitting the court also to release moderate amounts for the taxpayer's essential living expenses where his entire assets, including in some cases the means by which he has made his living, have been seized under a jeopardy or termination assessment, the merits of which remain in doubt. [149] Without a jeopardy assessment, he would have been enabled to support himself out of the property while the tax liability remained in controversy, and it is unlikely as a practical matter that the possibility of consumption of assets for that purpose would *in itself* have been viewed as justification for making a jeopardy assessment; so it is not unreasonable to let the victim of a jeopardy assessment support himself from his property pending resolution of the tax controversy, if other sources of support are unavailable. It should be made clear, however, that the level of support to be provided out of the seized or liened property and funds is not necessarily that to which the taxpayer has been or would like to become accustomed. [150]

g. The taxpayer should be required to show the unavailability of funds for the foregoing purposes from sources united in interest with him (but not subject to the jeopardy lien), such as from stockholders or affiliates of a corporate taxpayer, or from a spouse if living together, [151] although the mere hope for the largess of friends should not be a factor for consideration. [152] The law of the committee reports should set such standards.

h. The taxpayer should be required to justify the necessity and reasonableness of the expenditures, with safeguards provided to prevent the disclosure of privileged information (other than perhaps for *in camera* inspection by the court) in the course of justifying a legal fee. The fees should not be limited, however, to what would be allowed to assigned counsel in a criminal case (which involve a *pro bono* element not present in the typical tax case where the taxpayer has funds, although beyond his reach), but should be related to what the attorney or accountant normally charges for the grade of work required. To set lower fees may result in making the services unavailable to the taxpayer, in circumstances where the court is not empowered to "draft" the attorney or accountant.

i. To assure the application of the funds to the prescribed purposes, the court might pay the approved amounts (from funds ordered to be paid into court) directly to the payees on vouchers submitted by the payees and approved by the parties or, in case of disagreement, by the court.

j. Under the Bar proposal, the Service itself may voluntarily release funds or property for any of the purposes contemplated by its terms. For some reason not clear, such voluntary relief is permitted only "subsequent to the mailing of [the] notice" to the Service of the filing with the court of a petition for release. Since no judicial approval of a voluntary release is prescribed, and the court will not become involved unless the taxpayer is dissatisfied with the amount granted, why should either the taxpayer or the court be burdened with the filing of a petition if the Service is willing to grant the desired release voluntarily?

3. *Prompt adjudication of the tax liability*

The foregoing suggested procedures may be regarded as in the nature of first aid. The first of the Bar proposals affords a prompt determination of whether the victim is in such good shape that he should be returned to the mainstream of tax litigation. For those who are not, the second proposal lessens the injury they may suffer through the application of emergency procedures. Ultimately, however, for those to whom it is found that the emergency procedures must be

applied, the need is to get them over with as promptly as possible. Even more than taxpayers generally, the victim of a jeopardy or termination assessment needs prompt resolution because he is virtually immobilized until judicial consideration of the tax liability is completed. As the Fifth Circuit has said, "Where the taxpayer's assets have been frozen, the only meaningful remedy is to obtain an adjudication as promptly as possible." [153]

For ordinary jeopardy assessments, Congress has sought to provide that prompt review by requiring that a deficiency notice be mailed within 60 days, on the basis of which the taxpayer may petition the Tax Court. The Supreme Court will decide next term whether a similar right exists in the case of termination assessments. [154] But the Supreme Court is limited by the nature of the statutory materials it must work with, provisions enacted and amended at different times and without reference to each other, leaving unanswered many questions concerning the scope and nature of that review, which will not be resolved in the pending cases. If the Supreme Court denies the right of Tax Court review, it may mean only that the existing law is inadequate, and not that the right of review of termination assessments is necessarily undesirable. Either way the Court goes, Congress ought to consider what the law *should* be, and then fill in the missing procedural details.

In opposition to granting a right of review, it may be argued that the payment exacted is merely a provisional estimate of the amount necessary to protect the Government's interest, [155] and that the taxpayer "is, in effect in the same position as one who has made payments of estimated tax throughout the year, except that by necessity the Government, rather than the taxpayer, has estimated the amount of the tax." [156] The analogy fails, however, because one who pays estimated tax makes his own determination of his probable liability, relying on his own books and records, and there is no occasion to permit him, before the end of the year, to seek a court determination that his own estimate was too high. In contrast, the "estimate" made by the Service, often arbitrary and in any event disputable, forcibly deprives the taxpayer of his funds and property, and it may be many months before a definitive determination of the tax liability for the year can be made and the taxpayer can even commence the requisite administrative and judicial proceedings to contest it. There is as much need and justification for prompt judicial consideration of such an assessment and seizure as there is in the case of a jeopardy assessment for a past period.

A more troublesome argument, based on judicial economy, is that the amount of the termination assessment is incapable of precise judicial determination and will in any event be mooted as soon as the normal taxable year is ended and a correct tax liability for the full year becomes determinable. [157] In fact, whenever additional income is realized during the remainder of the year, the short period may be reopened and again terminated. [158] Although there is then only one taxable year in the 12-month period, [159] there would be separate assessments and separate deficiency notices (if required at all), each mooting the one before. Ultimately, allowing for the time required for deficiency notices, petitions, answers, trial, briefing and decision, it would inevitably be the full year's tax and not the termination assessment or assessments on which the Tax Court would pass. The process might be speeded a little by legislation treating the subsequent deficiencies as amendments of the first, not requiring a new petition; but it should then me made clear that the increase in the deficiency resulting from covering the whole year or a larger portion of it is not the kind of increased deficiency that shifts the burden of proof to the Commissioner. [160] Even under the most streamlined procedure, however, it is very doubtful that Tax Court review of any but the final assessment for the year would ever be achieved in practice.

It seems futile, therefore, to require that a formal deficiency notice and an opportunity to file a petition with the Tax Court be afforded before the close of the normal taxable year. At most, an early petition could achieve a higher place in line for hearing, but it may be meaningless since the issues cannot really be shaped until the year is over. The taxpayer, however, having had his property seized or subjected to lien under a termination assessment, should not have to wait for up to three years for his "ticket to the Tax Court" (deficiency notice), [161] nor should he be confined (unlike all other taxpayers) to the remedy by suit for refund. [162] He ought to have the same right to prompt Tax Court consideration as taxpayers subjected to ordinary jeopardy assessments. On the other hand, the Service should be permitted a reasonable time in which to audit the tax and prepare a deficiency notice, after having in hand a return for the full year. Although 60 days after the assessment is all that it is allowed in the case of

jeopardy assessments, those are cases where it may have already had an opportunity for audit before making the assessment. Even measured from the return, 60 days would not be enough where the entire audit (apart from whatever consideration had previously been given to the partial year) must occur between the return date and the notice. Some reasonable but limited period, measured from the filing of the return, should be prescribed within which a deficiency notice for the full year must issue.

Meanwhile, of course, the taxpayer's property will have been tied up for months, and will continue to be so during the pendency of the Tax Court case. But that would not be significantly relieved by letting him petition the Tax Court before the full-year determination, for the reasons I have indicated. It seems to me that the only meaningful relief that can be provided in that intervening period is that which I have previously suggested be allowed, in both jeopardy and termination cases, by summary proceeding in the district court. Either in connection with an unsuccessful challenge to the finding of jeopardy, or as an independent matter if jeopardy is not disputed, the taxpayer and the Government could be required to present evidence of his taxable income to the date of termination. The court would not make a final determination of the amount of tax then owed, since that is more properly dealt with when the year as a whole is presented for determination. But the evidence would affect the district court's summary determination of the maximum amount of the termination assessment that would be allowed to stand until the tax for the year is determined. [163]

One may ask why, if the district court makes the preliminary determination, it should not retain jurisdiction and make a prompt definitive determination of the merits of a jeopardy assessment or, in the case of a termination assessment, a finding as to the full year's tax as soon after the end of the year as the Service has had a reasonable opportunity to audit a return filed for the year. No objection will be heard from me if that is the solution adopted. I hesitate, however, in recommending specific relief from the inequities resulting from jeopardy assessments, to risk all on a challenge to the dogma with which two generations have been indoctrinated, which was elevated to Holy Writ by the Supreme Court in the *Flora* case, [164] that only those who can afford to part with the full amount of tax asserted against them should be permitted the option to litigate the merits in the federal court for their home district. If it should be determined that the district court may give complete relief, the remedy (in the case of a termination assessment) should in any event be in two stages, with the definitive determination of the amount of the tax reserved until the year is completed and can reasonably be audited. And, even if the taxpayer is to have the right to remain in the district court for the second stage, he should not be denied the option that others have to take the final determination to the Tax Court if he prefers.

4. *Miscellaneous suggestions concerning termination assessments*

A number of possible amendments to the termination provision, in addition to those mentioned in the general discussion above, ought to be considered.

a. Although the Service instructs its personnel that termination assessments "should be limited to amounts which can reasonably be expected to equal the ultimate tax liability for the terminated period" (Internal Revenue Manual § 4585.2(1)), it belies its good intentions by instructing that the taxpayer be given "no further explanation in the Notice and a written report will not be given to the taxpayer," except that, if the taxpayer or his counsel demands "information as to the basis for computation of income and tax, the examining agent may explain his report but he should not give taxpayer a copy." [165] The most elemental requirements of due process surely require that the taxpayer whose property is taken from him be promptly advised of how it is that he is thought to owe the tax asserted. In normal audits a copy of the examination report is always furnished to the taxpayer. [166] While it may not be feasible to provide a deficiency notice at that tentative stage, the taxpayer should be entitled to know, with the least possible delay, how the Government arrived at his liability; and he will need such information if the summary court procedure suggested in 1.m, above, is to be effective.

b. The rule of § 6863(b)(3), restricting forced sale of the taxpayer's property until review of a jeopardy assessment has been completed is "very important to a taxpayer," [167] and the law should expressly extend it to termination assessments.

c. Any doubt there may be that the Service has power to abate a termination assessment upon finding that jeopardy does not exist, just as it may abate a regular jeopardy assessment on that ground under § 6861(g), should be removed. [168]

d. Consideration should be given to whether there is a need to fill the gap between § 6851, which allows assessments before the due date in income tax cases, and § 6862, which similarly allows such assessment before the due date of taxes other than income, estate and gift taxes. If it is anticipated that the need for such immediate assessments could arise in estate or gift tax cases, amendment may be required. [169]

The tax system has been used in many ways as an aid in combatting crime, and it is not clear that the results have been worth the social cost. Congress in Public Law 91–513 (1970) substantially ended a 56-year experiment with attempting to suppress evil by taxing it. That the fruits of crime and the practice of the occupation of crime may be taxed is well established. [170] The courts have gone very far in sustaining such taxes under the taxing power, despite minimal production of revenue, [171] and have sustained a panoply of other requirements if they had "any relation to the raising of revenue." [172] By applying information-gathering techniques appropriate to the determination and collection of taxes, information might be extracted that could not be obtained by the constitutional process of the criminal law, [173] until the Supreme Court finally applied the brakes in the *Marchetti* case. [174] An outgrowth of those practices is the apparently more recent discovery of the law enforcement utility of the arsenal of collection weapons with which Congress has armed the tax collector and which the courts have sustained in the name of the "imperious need" for the revenue that is the "lifeblood" of the Government, [175] including the power in some circumstances to make summary collection before hearing. [176] By making arbitrary assessments in unsustainable amounts, and seizing all the suspected wrongdoer's assets, selling some at a sacrifice and withholding the rest indefinitely, the tax collector for all practical purposes effects a forfeiture without trial, which the Constitution forbids as surely as it precludes fine and imprisonment without due process. [177]

The *procedure* for jeopardy and termination assessments, appropriate and necessary in proper cases (no doubt including those in which one who has in fact incurred a tax is engaged in criminal activity and may be expected to conceal himself or his property), has been brought into disrepute by being applied to assessments having (allegedly) no basis in fact, and by being defended, not on the merits, but on the ground that, even if the asserted abuse occurred, the citizen has no remedy.

Taxes, like rain, must fall alike on the just and the unjust. But when tax procedures are used to enforce the criminal law, the need for expeditious determination of the validity of the imposition, with such interim safeguards as will protect both the revenue and the victim, is apparent. And, if the criminal suspect is entitled to such protection, so also is the ordinary citizen (even if, as the Service claims, his numbers in the statistics of jeopardy assessments are "very few").

REFERENCES

1. *Cheatham* v. *United State*, 92 U.S. 85, 86 (1876).
2. Now Int. Rev. Code of 1954, § 6323.
3. Now Int. Rev. Code of 1954, § 6331.
4. Act of March 2, 1867, 14 Stat. 475, now Int Rev. Code of 1954, § 7421.
5. The ebb and flow of judicially implied exceptions to the prohibition on injunctions is reviewed in *Bob Jones University* v. *Simon*, 416 U.S. 725, 742–46 (1974).
6. See *Tennessee* v. *Sneed*, 96 U.S. 69, 75 (1877).
7. H.R. Rep. No. 179, 68th Cong., 1st Sess. 7 (1924).
8. Revenue Act of 1924, § 900.
9. Revenue Act of 1926, § 274(a), now Int. Rev. Code of 1954, § 6213(a).
10. Revenue Act of 1924, §§ 274(d), 308(d), 324, now Int. Rev. Code of 1954, §§ 6861–63.
11. *E.g.*, *Enochs* v. *William Packing & Navig. Co.*, 370 U.S. 1, 6 (1962); *Westgate-California Corp.* v. *United States*, 496 F.2d 839, 843 (9th Cir. 1974); *Johnson* v. *Wall*, 329 F.2d 149 (4th Cir. 1964); *La Londe* v. *United States*, 350 F. Supp. 976 (D. Minn. 1972), aff'd, 478 F.2d 700 (8th Cir. 1973).
12. *Shapiro* v. *Secretary of State*, 499 F.2d 527, 533–35 (D.C. Cir. 1974), cert. granted; *Lucia* v. *United States*, 474 F.2d 565, 573–75 (5th Cir. 1973);

Pizzarello v. *United States*, 408 F.2d 579, 582–86 (2d Cir. 1969). The determination is to be made, not by full consideration of the law and the evidence in the injunction suit, but by applying the legal position most favorable to the Government to the facts that were available to it at the time of the suit. *Trent* v. *United States*, 442 F.2d 405, 406 (6th Cir. 1971); *Johnson* v. *Coppinger*, 320 F. Supp. 716 (N.D. Ala.), aff'd, 443 F.2d 71 (5th Cir. 1971); *cf. Bauer* v. *Foley*, 404 F.2d 1215, 1221 (2d Cir. 1968); See *Enochs* v. *Williams Packing Co.*, 370 U.S. 1, 7 (1962). Some courts appear to hold that it is not enough to show the tax to be arbitrary and excessive if it appears that the Government will be entitled to *some* recovery, since the assessment cannot then be viewed as an illegal exaction in the guise of a tax. *Iannelli* v. *Long*, 487 F.2d 317 (3d Cir.), cert. denied, 414 U.S. 1040 (1973); *Vuin* v. *Burton*, 327 F.2d 967, 970 (6th Cir. 1964); *Homan Mfg. Co.* v. *Long*, 264 F.2d 158 (7th Cir. 1959); *Patrick* v. *United States*, 74–2 U.S. Tax Cas. ¶ 9658 (N.D. Ill. 1974); see *Lucia* v. *United States*, *supra*, at 575.

13. *Mason* v. *Commissioner*, 210 F.2d 388 (5th Cir. 1954).

14. Revenue Act of 1926, §§ 279(b), 312(b), now Int. Rev. Code of 1954, § 6861(b).

15. *Westgate-California Corp.* v. *United States*, 496 F.2d 839 (9th Cir. 1974); *Cohen* v. *United States*, 297 F.2d 760, 773–74 (9th Cir.), cert. denied, 369 U.S. 865 (1962); *United States* v. *O'Connor*, 291 F.2d 520, 525 (2d Cir. 1961); *United States* v. *Stone*, 59 F.R.D. 260, 166 (D. Del. 1973).

16. *United States* v. *Ball*, 326 F.2d 898, 901 (4th Cir. 1964).

17. *Williams* v. *United States*, 373 F. Supp. 71, 81 (D. Nev. 1973); *Berry* v. *Westover*, 70 F. Supp. 527 (S.D. Cal. 1947).

18. Revenue Act of 1924, §§ 279(a), 312(a), 324. See Int. Rev. Code of 1954, § 6863(a).

19. See *Clark* v. *Campbell*, 501 F.2d 108, 123, (5th Cir. 1974), cert. pending; *Shelton* v. *Gill*, 202 F.2d 503, 507 (4th Cir. 1953); *Kimel* v. *Tomlinson*, 151 F. Supp. 901, 902 (S.D. Fla. 1957); *Macejko* v. *United States*, 174 F. Supp. 87 (N.D. Ohio 1959). See Note, Jeopardy Assessment: The Sovereign's Strangehold, 55 Georgetown L.J. 701, 705 (1967).

20. Public Law 274, 83d Cong., 1st Sess., 67 Stat. 583 (1953), now Int. Rev. Code of 1954, § 6861(g).

21. See *Clark* v. *Campbell*, 501 F.2d 108, 124 (5th Cir. 1974), cert. pending. Jeopardy assesments must be personally approved in the first instance by the District Director, subject to review in special circumstances by the National Office. Internal Revenue Manual § 4584.2. (See *infra* at note 48.) The District Director is required also to "give personal consideration on an expedite basis" to a request for abatement on the ground that jeopardy does not exist, and his statement of reasons is then reviewed by the Assistant Regional Commissioner (Audit). *Id.* § 4584.10.

22. See *Schreck* v. *United States*, 301 F. Supp. 1265, 1280 (D. Md. 1969).

23. H.R. Rep. No. 356, 69th Cong., 1st Sess. 42 (1925). See *Durovic* v. *Commissioner*, 487 F.2d 36, 40 (7th Cir. 1973); James Couzens, 11 B.T.A. 1040, 1158 (1928).

24. Foundation Co., 15 F. Supp. 229, 246–47 (Ct. Cl. 1936).

25. See Kaminsky, Administrative Law and Judicial Review of Jeopardy of Assessments Under the Internal Revenue Code, 14 Tax L. Rev. 545. The jeopardy assessment provision, Int. Rev. Code of 1954, § 6861(a), when satisfied, is an exception to the provision of § 6213(a) permitting such an injunction.

26. *Philanthropic Institute of America* v. *Wise*, 65–2 U.S. Tax Cas. § 9492 (D. Ariz. 1965).

27. *Transport Mfg. & Equip. Co.* v. *Trainor*, 382 F.2d 793 (8th Cir. 1967); *Lloyd* v. *Patterson*, 242 F.2d 742, 744 (5th Cir. 1957); *Communist Party* v. *Moyse*y, 141 F. Supp. 332, 336 (S.D. N.Y. 1956). *Cf. Homan Mfg. Co.* v. *Long*, 242 F.2d 645, 649–50 (7th Cir. 1957). Although the statutory test is whether "the Secretary or his delegate *believes* that the assessment or collection of a deficiency . . . will be jeopardized by delay," the fact which he must "believe" exists is an objective fact which the courts are capable of ascertaining. Comparable language, requiring that the Secretary must be "satisfied" that a fact exists, has recurred frequently in the tax laws (*e.g.*, Int. Rev. Code of 1954, §§ 166(a)(2), 355(a)(1)(D), 911(a)(1)), and has generally been deemed "largely admonitive and [to mean] that the additional element is not lightly to be inferred but to be established by proof which convinces in the sense of inducing belief." *United States* v. *Jefferson Elec. Co.*, 291 U.S. 386, 397–98 (1934); see *Stranahan* v. *Commissioner*, 42 F.2d 729, 731 (6th Cir. 1930), cert. denied, 283

U.S. 822 (1931). But cf. *Bush Terminal Bldgs. Corp.* v. *Commissioner*, 204 F.2d 575, 578 (3d Cir. 1953). A similar phrase ("found by the Secretary," in Int. Rev. Code of 1954, § 401 (a)(3)) has been construed as not precluding meaningful judicial review but merely suggesting that the finding be "given a shade more than its usual substantial weight." *Cornell-Young* v. *United States*, 469 F.2d 1318, 1323–24 (5th Cir. 1972); *Commissioner* v. *Pepsi-Cola Niagara Corp.*, 399 F.2d 390, 393 (2d Cir. 1968).

28. *E.g.*, *Darnell* v. *Tomplinson*, 220 F.2d 894 (5th Cir. 1955) (small printing business and automobile of a cripple).

29. *Kjar* v. *United States*, 108 Ct. Cl. 119, 140–41 (rehearing), cert. denied, 332 U.S. 768 (1947).

30. Int. Rev. Code of 1954, § 6863(b)(3); *Smith* v. *Flinn*, 261 F.2d 781 (8th Cir. 1958), modified, 264 F.2d 523 (8th Cir. 1959). To the extent that the Tax Court sustains the tax, the pendency of an appeal therefrom does not defer enforcement of either a jeopardy or non-jeopardy deficiency, by sale or otherwise, unless the taxpayer can file a *supersedeas* bond. Int. Rev. Code of 1954, § 7485; Treas. Reg. § 301. 6863–2(a)(2).

31. Int. Rev. Code of 1954, § 6863 (b)(3)(B).

32. H.R. Rep. No. 1884, 89th Cong., 2d Sess. 16 (1966).

33. *Mutual Life Ins. Co.* v. *United States*, 343 F.2d 71, 74 (9th Cir. 1955).

34. Public Law 89–719, § 104(b) (1966), adding Int. Rev. Code of 1954, § 6332(b).

35. Internal Revenue Manual § 5213.24(2). Although sale would not occur until the merits are determined, either by the Tax Court or in the foreclosure suit, a receiver may be appointed upon or after institution of such suit. Int. Rev. Code of 1954, § 7403(d); *United States* v. *O'Connor*, 291 F.2d 520 (2d Cir. 1961).

36. Rev. Proc. 60–4, § 4, 1960–1 Cum. Bull. 877, 878; Internal Revenue Manual § 5213.24(1).

37. See *Clark* v. *Campbell*, 501 F.2d 108, 122 (5th Cir. 1974), cert. pending.

38. See *Stanton* v. *Machiz*, 183 F. Supp. 719, 726 (D. Md. 1960). If seizure of the taxpayer's cash assest leaves him without funds to live on, a sacrifice sale of his property (which § 6863(b)(3) was designed to avoid) may be necessary in order to provide for such expenses. *Cf. Darnell* v. *Tomlinson*, 220 F.2d 894, 896 (5th Cir. 1955).

39. *Avco Delta Corp. Canada Ltd.* v. *United States*, 484 F.2d 692, 706–07 (7th Cir. 1973); *Illinois Redi-Mix Corp.* v. *Coyle*, 360 F.2d 848 (7th Cir. 1966); *Lebanon Woolen Mills, Inc.* v. *United States*, 311 F.2d 364 (1st Cir. 1962); *Lloyd* v. *Patterson*, 242 F.2d 742, 744 (5th Cir. 1957); Human Engineering Institute, 61 T.C. 61 (1973). No relief is obtainable if financial pressures caused by the jeopardy assessment force the taxpayer, to settle a tax liability that he might have successfully defended. *Funkhouser* v. *Commissioner*, 226 F.2d 910 (4th Cir. 1955).

40. The courts will neither enjoin the assessment on that ground (*Licavoli* v. *Nixon*, 312 F.2d 200, 202 (6th Cir. 1963)) nor release funds from the lien in order to pay counsel and accountants (*United States* v. *Rinieri*, 304 F.2d 885 (2d Cir. 1962); *United States* v. *Brodson*, 241 F.2d 107 (7th Cir.), cert. denied, 354 U.S. 911 (1957), rev'g 136 F. Supp. 158 (E.D. Wis. 1955), leaving for post-trial determination the question whether "effective" assistance of counsel (*e.g.*, by inability to employ an accountant to help in preparation) was in fact denied. *Summers* v. *United States*, 250 F.2d 132 (9th Cir. 1957). See *United States* v. *Brodson*, *supra*, at 110. In the Brodson case, the district court, having been overruled in its effort to release liened funds for the criminal deefnse, ordered delay of the criminal trial until after determination of the civil liability, so that if the ultimate determination left a surplus of assets for the taxpayer, they migh be available for expenses of the criminal case. *United States* v. *Brodson*, 155 F. Supp. 407 (E.D. Wis. 1957).

41. Internal Revenue Manual § 5213.24(1).

42. Int. Rev. Code of 1954, § 6323(c).

43. Int. Rev. Code of 1954, § 6325(d); Proposed Treas. Reg. § 301.6325–1(d).

44. See *Homan Mfg. Co.* v. *Long*, 242 F.2d 645, 651 (7th Cir. 1957).

45. See *Ginsburg* v. *United States*, 278 F. 2d 470 (1st Cir. 1960), cert. denied, 364 U.S. 878 (1960).

46. Rev. Proc. 60–4, § 2.03, 1960–1 Cum. Bull. 877, 878; Internal Revenue Manual §§ 4584.2(1), 5213.21(6).

47. Internal Revenue Manual §§ 4584.1(1), 4584.2(1), 5213.21(2). Consultation with the Regional or National Office is encouraged even in cases involving the standard grounds (*id.* § 4584.2(1)), and all jeopardy assessments are forwarded

to the Regional Office for post-review, with selected samples being post-reviewed also in the National Office. Rev. Proc. 60–4, § 3, 1960–1 Cum. Bull. 877, 878; Internal Revenue Manual §§ 4584.8, 5213.23.

48. Internal Revenue Manual § 4584.10. It is unclear whether the views which the Assistant Regional Commissioner is directed to "communicate" to the District Director are binding on the latter, or whether the ultimate decision whether to abate the assessment rests with the one who made it in the first place. See note 21 *supra*.

49. Internal Revenue Manual §§ 4584.2(1), 5213.21(6). See also Rev. Proc. 60–4, § 2.03, 1960–Cum. Bull. 377, 378.

50. Gould, Jeopardy Assessments: When They May Be Levied and What To Do About Them, 18 N.Y.U. Inst. on Fed. Tax. 937, 937 (1960).

51. Note, Jeopardy Assessments: The Sovereign's Stranglehold, 55 Georgetown L. J. 701, 705 (1967).

52. 134 J. of Accountancy, Dec. 1972, p. 74. The above figures do not include so-called termination assessments, hereafter discussed. The number may have increased with the policy of using jeopardy assesments as instruments of criminal law enforcement. *Infra* at notes 56 and 71–74.

53. See *Aguilar* v. *United States*, 501 F. 2d 127, 129 n. 3 (5th Cir. 1974); *Lucia* v. *United States*, 474 F. 2d 565, 575, 577 (5th Cir. 1973).

54. *Aguilar* v. *United States*, 501 F. 2d 127, 130 (5th Cir. 1974); *United States* v. *Bonaguro*, 294 F. Supp. 750, 754 (E.D. N.Y. 1968); *Rinieri* v. *Scanlon*, 254 F. Supp. 469, 472 (S.D. N.Y. 1966). Although those cases involved termination assessments (hereafter discussed), rather than strictly jeopardy assessments, they differ principally in that the former are determined before, rather than after, the tax would normally become due.

55. *Willits* v. *Richardson*, 497 F. 2d 240, 244–46 (5th Cir. 1974) (termination assessment); *Lucia* v. *United States*, 474 F. 2d 565, 573–75 (5th Cir. 1973); *Pizzarello v. United States*, 408 F. 2d 579, 583–84 (2d Cir. 1969); *Homan Mfg. Co.* v. *Long*, 264 F. 2d 158, 160–61 (7th Cir. 1959); *Williams* v. *United States*, 373 F. Supp. 71, 72–73 (D. Nev. 1973) (termination assessment). See *Shapiro* v. *Secretary of State*, 499 F. 2d 527, 533–35 (D.C. Cir. 1974), cert. granted; *Clark* v. *Campbell*, 501 F. 2d 108, 117 n. 28 (5th Cir. 1974), cert. pending.

56. See the speech of Commissioner Donald C. Alexander on The Role of the Internal Revenue Service in the Law Enforcement Community, June 10, 1975, in 1975–9 C.C.H. Std. Fed. Tax Rep. § 6656, quoting *Willits* v. *Richardson*, 497 F. 2d 240, 246 (5th Cir. 1974) ("Courts cannot allow these expedients to be turned on citizens suspected of wrongdoing—not as tax collection devices but as summary punishment to supplement or complement regular criminal procedures.")

57. Note, Jeopardy Assessment: The Sovereign's Stranglehold, 55 Georgetown L.J. 701, 732–33 (1967). Instances in which such motivations were alleged (but not passed on factually in dismissing the injunction suits) include *La Londe* v. *United States*, 350 F. Supp. 976 (D. Minn. 1972), aff'd. 478 F. 2d 700 (8th Cir. 1973); *Communist Party* v. *Moysey*, 141 F. Supp. 332 (S.D. N.Y. 1956); *Publishers New Press* v. *Moysey*, 141 F. Supp. 340 (S.D. N.Y. 1956). Commissioner Alexander, *supra* note 56, has said in this connection, "A subsidiary issue is how, and whether, one can distinguish between the use of the tax system to investigate political corruption and the use of the tax system to investigate political opponents."

58. See Note, *supra* note 57, at 719–21. See also 134 J. Accountancy, Dec. 1972, p. 74.

59. A finding of jeopardy may have been more supportable years ago, when the sending of a deficiency notice suspended the statute only for the time during which an appeal to the Board of Tax Appeals could be filed, and until final decision if an appeal was filed, so that, if only a few days remained for assessment when the notice was sent, the same few days would be all the time for getting the assessment machinery moving after the restraint on assessment was removed. *Veeder* v. *Commissioner*, 36 F. 2d 342, 343 (7th Cir. 1929); *Foundation Co.* v. *United States*, 15 F. Supp. 229, 247 (Ct. Cl. 1936); James Couzens, 11 B.T.A. 1040, 1157–58 (1928). That mechanical problem, however, has long since been resolved by adding 60 days to the suspension period. Now Int. Rev. Code of 1954, § 6503(a)(1).

60. Tax Court Rule 142(a).

61. See 134 J. Accountancy, Dec. 1972, p. 74. The permitted grounds, not requiring National Office approved, are listed at note 47 *supra*. In *La Londe* v.

United States, 350 F. Supp. 976, 977 (D. Minn. 1972), aff'd, 478 F. 2d 700 (8th Cir. 1973), the district court stated that, when the taxpayer declined to sign a waiver of the statute, "the Government followed its customary practice of notifying the taxpayer of a 'jeopardy assessment' which had been calculated by the use of its current third party sources." Since the decision was one granting a motion to dismiss an injunction suit, however, it cannot be viewed as a factual finding that such is the "customary practice."

62. Revenue Act of 1918, § 250(g), now Int. Rev. Code of 1954, § 6851.

63. See *Clark* v. *Campbell*, 501 F. 2d 108, 121 (5th Cir. 1974), cert. pending.

64. See Ludwig Littauer & Co., 37 B.T.A. 840, 842 (1938).

65. Internal Revenue Manuel §§ 4585.1(2), 5213.3.

66. *Supra* at note 47.

67. Internal Revenue Manuel § 4585.2(1).

68. Internal Revenue Manual §§ 4585.2(3), 5213.3(4).

69. See *Clark* v. *Campbell*, 501 F. 2d 108, 114–15 (5th Cir. 1974), cert. pending. In 1969, a court found only eight previous decided cases in which such assessments may have been involved. *Schreck* v. *United States*, 301 F. Supp. 1265, 1276 (D. Md. 1969).

70. Treas. Reg. § 1.6851–2.

71. The use of termination assessments in that program is provided in Internal Revenue Manual § 4567.15. See Silver, Terminating the Taxpayer's Taxable Year: How IRS Uses It Against Narcotics Suspects, 40 Taxation 110 (1974).

72. So stated in Government's petition for certiorari in *Hall* v. *United States*, 493 F. 2d 1211 (6th Cir. 1974), cert. granted.

73. Internal Revenue Manual § 4567.15(1).

74. *Supra* at note 53.

75. *Supra* at notes 54–55.

76. *Supra* at notes 18–31.

77. Int. Rev. Code of 1954, § 6851(e).

78. Rev. Proc. 60–5, 1960–1 Cum. Bull. 879, deals in § 5 with such abatements of "jeopardy assessments," and § 2.02 thereof states that, while termination assessments under § 6851 "are not in a technical sense jeopardy assessments, the procedure set forth herein shall also apply to assessments made under that section." Although the legislative history of the 1953 amendment permitting such abatement of jeopardy assessments indicated doubt that the power existed in the absence of such amendment (S. Rep. No. 730, 83d Cong., 1st Sess. 1953), perhaps the more tentative nature of the termination assessment is thought by the Service to afford more flexibility in altering it, without need for special legislation.

79. *Aguilar* v. *United States*, 501 F. 2d 127, 129 (5th Cir. 1974); *Hall* v. *United States*, 493 F.2d 1211, 1212 (6th Cir., 1974), cert. granted; *Rambo* v. *United States*, 353 F. Supp. 1021, 1022 (W.D. Ky. 1972), aff'd, 492 F. 2d 1060 (6th Cir. 1974), cert. pending; *Lisner* v. *McCanless*, 356 F. Supp. 398, 403 n. 11 (D. Ariz. 1973).

80. See *Schreck* v. *United States*, 301 F. Supp. 1265, 1280 n. 29 (D. Md. 1969).

81. Int. Rev. Code of 1954, § 6851. See *Clark* v. *Campbell*, 501 F.2d 108, 120 (5th Cir. 1974), cert. pending; *Rambo* v. *United States*, 492 F.2d 1060, 1061 (6th Cir. 1974), cert. pending.

82. Int. Rev. Code of 1954, § 6861.

83. Int. Rev. Code of 1954, § 6201.

84. Int. Rev. Code of 1954, § 6211(a).

85. *Williamson* v. *United States*, reported only in 31 A.F.T.R. 2d 800 (7th Cir. 1971). See also *Laing* v. *United States*, 496 F.2d 853 (2d Cir. 1974), cert. granted.

86. *Irving* v. *Gray*, 479 F.2d 20 (2d Cir. 1973).

87. Treas. Reg. § 301.6211–1(a). See *Clark* v. *Campbell*, 501 F.2d 108, 116–17 (5th Cir. 1974), cert. pending; *Rambo* v. *United States*, 492 F.2d 1060, 1064 (6th Cir. 1974), cert. pending.

88. Int. Rev. Code of 1954, § 6851(a) (1) and (2). See *Clark* v. *Campbell*, *supra*, at 117–18; *Rambo* v. *United States*, *supra*, at 1064.

89. Int. Rev. Code of 1954, § 443(a)(3). See *Clark* v. *Campbell*, *supra*, at 118–19; *Rambo* v. *United States*, *supra*, at 1064. In Note, Termination of Taxable Year: Procedure in Jeopardy, 26 Tax L. Rev. 829, 834–38 (1971), an elaborate argument is constructed to the effect that a return is not in fact generally by the short period because the only return expressly referred to in the regulations under § 6851 is that which is required of departing aliens by Treas. Reg. § 1.6851–2(b)(1), and that Treas. Reg. § 1.6851–1, relating to terminations on account of jeopardy, refers only to the full-year return required for reopening the period. However, Treas. Reg. § 1.443–1(a)(3), under the statutory section which im-

poses the requirement, declares that "A" return must be filed for a short period resulting from the termination by the Commissioner of a taxpayer's taxable year for jeopardy," which should be clear enough not to require repetition. The courts have not doubted that a return is prescribed to be made for the short period. In addition to *Clark* and *Rambo, supra*, see *Lisner* v. *Canless*, 356 F. Supp. 398, 403 (D. Arfiz. 1973), on appeal to 9th Cir.; *Parrish* v. *Daly*, 350 F. Supp. 735, 737 (S.D. Ind. 1972).

90. Nino Sanzongo, 60 T.C. 321 (1973).

91. Int. Rev. Code of 1954, § 6851(b).

92. In *Schreck* v. *United States*, 375 F. Supp. 742 (D. Md. 1973), the Service waited until the day before the period of limitations would have expired, before sending a regular deficiency notice. In *Martinez* v. *United States*, 75–1 U.S. Tax Cas. ¶ 9108A (S.D. Fla. 1974), it was 21 months after the assessment and seizure (and then only in anticipation of trial of the taxpayer's suit for injunction), while the liens and levies meanwhile remained in effect.

93. *Laing* v. *United States*, 496 F.2d 853, 854 (2d Cir. 1974), cert. granted; *Boyd* v. *United States*, 74–1 U.S. Tax Cas. ¶ 9408 (E.D. Pa. 1974). The Internal Revenue Manual § 4585.5 establishes controls to prevent "premature processing" of the refund of any overpayment shown on the return (that would otherwise occur automatically soon after filing), but directs expedited examination of the return when filed. If the tax determined exceeds that shown on the return, if one is filed, a deficiency notice (giving access to the Tax Court) will be sent even if the amount has been fully collected pursuant to the termination assessment. *Id.* § 5485.6.

94. *Rambo* v. *United States*, 353 F. Supp. 1021, 1024 (W.D. Ky. 1972), aff'd, 492 F.2d 1060, 1062 (6th Cir. 1974), cert. pending; *Schreck* v. *United States*, 301 F. Supp. 1265, 1281 (D. Md. 1969), reaffirmed, 375 F. Supp. 742, 743 (D. Md. 1973).

95. 362 U.S. 145 (1960).

96. For example, if $20,000 was assessed and only $10,000 collected, of which the taxpayer claims only $4,000 is properly due, he cannot sue to get his $6,000 overpayment back unless he first pays the $10,000 balance of the assessment. Inability to pay the difference does not relieve him of the condition. See Plumb, The Tax Recommendations of the Commission on the Bankruptcy Laws—Tax Procedures, 88 Harvard L. Rev. 1360, 1409, n. 270 (1975).

97. *Irving* v. *Gray*, 479 F.2d 20, 24–25 n. 6 (2d Cir. 1973); *Boyd* v. *United States*, 74–1 U.S. Tax Cas. ¶ 9408 (E.D. Pa. 1974). See also *Lewis* v. *Sandler*, 498 F.2d 395, 400 (4th Cir. 1974).

98. See *Clark* v. *Campbell*, 501 F.2d 108, 125 n. 55 (2d Cir. 1974), cert. pending.

99. *United States* v. *Hall*, Dkt. 74–75; *Laing* v. *United States*, Dkt. 73–1808.

100. *Supra* at note 27.

101. Int. Rev. Code of 1954, § 6851(a)(1).

102. But see *United States* v. *Johansson*, 62–1 U.S. Tax Cas. ¶ 9130 (S.D. Fla. 1961), in which a suit for foreclosure of a tax lien based on a termination assessment made on March 14 was tried in September and decided on December 13 of the same year (although only the merits, not the existence of jeopardy, was determined).

103. Revenue Act of 1932, § 1105, amended by Revenue Act of 1934, § 510; now Int. Rev. Code of 1954, §§ 6862, 6331(a) (last sentence).

104. Int. Rev. Code of 1954, § 6863(b)(3).

105. Int. Rev. Code of 1954, § 6331(a).

106. *Supra* at notes 11–12. The *Enochs*, *Johnson*, *Lucia*, *Pizzarello*, *Trent*, *Iannelli*, *Vuin*, and *Patrick* cases, there cited, involved such miscellaneous taxes.

107. Int. Rev. Code of 1954, § 6863(a).

108. *Supra* note 103.

109. See *Clark* v. *Campbell*, 501 F.2d 108, 126 (5th Cir. 1974), cert. pending.

110. Note, "Jeopardy Assessment: The Sovereign's Stranglehold," 55 Georgetown L.J. 701, 721–22 (1967).

111. 83 A.B.A. Rep. 221–23 (1958). (Adoption of the proposal is reflected at page 197.) An explanation of the proposal is found in A.B.A. Section of Taxation, 1958 Program and Committee Reports 159–60.

112. The proposal and explanation are submitted herewith as Exhibit A.

113. Int. Rev. Code of 1954, § 6331(a).

114. *Cf. Foundation Co.* v. *United States*, 15 F. Supp. 229 (Ct. Cl. 1936).

115. *Delia* v. *Dath*, 74–2 U.S. Tax Cas.¶9803 (N.D. Ohio 1974), which set aside a termination assessment for failure to send a deficiency notice within 60 days

thereafter, notwithstanding that a formal deficiency notice for the full year had been sent before the court acted, is distinguishable in that the court viewed the 60-day notice as required by statute. Here, the most that could be said is that the taxpayer may have been denied an administrative hearing on the merits, a step that is prescribed not by the statute but by the Service's internal procedural rules. *Cf. Lühring* v. *Glotzbach*, 304 F.2d 560, 563 (4th Cir. 1962).

116. See House Ways and Means Committee Print on Jeopardy and Termination Assessments [etc.], Prepared by Staff of Joint Committee on Internal Revenue Taxation for Use in Markup Sessions on Tax Reform Legislation.

117. It is unclear why the proposal refers to local federal district court rules rather than to Federal Rule 57, which deals expressly with calendar preference for declaratory judgment cases.

118. *Drinan* v. *Nixon*, 364 F. Supp. 853 (D. Mass. 1973).

119. See Note, Jeopardy Assessment: The Sovereign's Stranglehold, 55 Georgetown L.J. 701, 728 (1967).

120. *Cf.* 28 U.S.C. § 2243.

121. At the very least, the word "believes" should be changed to "finds," to conform to the reference in the proposal to "A finding of the Secretary or his delegate."

122. See *Veeder* v. *Commissioner*, 36 F.2d 342, 345 (7th Cir. 1929), in which the court declined to interfere with a jeopardy assessment, in part because of "the absence of statutory standards by which any reviewing body may test the correctness of the belief of the Commissioner."

123. Note, Jeopardy Assessment: The Sovereign's Stranglehold, 55 Georgetown L. Rev. 701, 735 (1967).

124. *Supra* at note 62.

125. Internal Revenue Manual § 4584.5.

126. Internal Revenue Manual §§ 4584.5(2)(j), 4585.3(2)(h).

127. Internal Revenue Manual §§ 4584.1(1)(c), 4584.2(1)(c).

128. Int. Rev. Code of 1954 § 6851(a) directs termination of the taxable year when the taxpayer "designs" to do certain affirmative *acts*. See *supra* at note 62. Treas. Reg. § 1.6851-1(a) interprets that to refer to *a design to avoid payment of income tax* by doing one of those acts. See Note, Termination of Taxable Year: Procedures in Jeopardy, 26 Tax. L. Rev. 829, 831 (1971).

129. Courts have made this argument in denying judicial review of termination assessments. See *infra* at note 156.

130. See *infra* at note 168.

131. See *infra* at notes 153–64.

132. See *supra* at note 60.

133. *Cf.* Carney Coal Co., 10 B.T.A. 1397, 1403 (1928).

134. See *Kimmel* v. *Tomlinson*, 151 F. Supp. 901, 902 (S.D. Fla. 1937).

135. In *Melvin Bldg. Corp.* v. *Long*, 58-2 U.S. Tax Cas. ¶ 9792 (N.D. Ill. 1958), rev'd, 262 F.2d 920 (7th Cir. 1958), and *Homan Mfg. Co.* v. *Sauber*, 55-2 U.S. Tax Cas. ¶ 9666 (N.D. Ill. 1955), rev'd, 242 F.2d 645 (7th Cir. 1957), the district courts granted injunctions against jeopardy assessments conditioned upon supervision of the taxpayer's property by the court or by a receiver, but the appellate court held that an injunction was improper under existing law, even upon conditions.

136. *Supra* at notes 28–31.

137. *Smith* v. *Flinn*, 261 F.2d 781 (8th Cir. 1958), mod., 264 F.2d 523 (8th Cir. 1959).

138. 83 A.B.A. Rep. 223–24. (Adoption of the proposal is reflected at page 196.) An explanation of the proposal is found in A.B.A. Section of Taxation, 1958 Program and Committee Reports 161–62.

139. See *Gideon* v. *Wainwright*, 372 U.S. 335 (1963).

140. See Human Engineering Institute, 61 T.C. 61, 66–67 (1973), and authorities cited.

141. *United States* v. *Brodson*, 136 F. Supp. 158, 163 (E.D. Wis. 1955).

142. *United States* v. *Brodson*, 241 F.2d 107, 111 (7th Cir.), cert. denied, 354 U.S. 911 (1957).

143. Criminal Justice Act of 1964, as amended, 18 U.S.C. § 3006A. See Note, The Indigent's Right to an Adequate Defense: Expert and Investigatorial Assistance in Criminal Proceedings, 55 Cornell L. Rev. 632 (1970).

144. A.B.A. 1968 Program and Committee Reports 162 (Exhibit B).

145. Compare Int. Rev. Code of 1954, § 6325(d)(2), permitting the Service to agree to subordination of a tax lien to claims incurred for purposes which it is believed will increase the amount realizable by the Government and will facilitate

ultimate collection. Such purposes may include repair and maintenance of the property. Proposed Reg. § 301. 6325–1(d)(2)(ii), Example (2).

146. The proposal and explanation are submitted herewith as Exhibit B.

147. Furthermore, there being in any case no right of prepayment litigation in the case of these other taxes, the problem of a seizure of all one's assets leaving one with no funds to litigate the liability or to defend a related criminal case exists whether a regular or jeopardy assessment is made. *Cf. Enochs* v. *Williams Packing & Navig Co.*, 370 U.S. 1 (1962); *Lucia* v. *United States*, 474 F.2d 565, 577 (5th Cir. 1973).

148. Compare Int. Rev. Code of 1954, § 6531 (criminal) with § 6501(c)(1) and (2) (civil fraud).

149. Such relief was granted by the district court in the case from which the Government's appeal was dismissed in *United States* v. *Fauci*, 242 F.2d 237 (1st Cir. 1957). Although early cases allowed injunctions against assessments the enforcement of which would deprive the taxpayer of his livelihood and reduce his family to destitution (*Macejko* v. *United States*, 174 F. Supp. 87 (N.D. Ohio 1959); *Arnold* v. *Cobb*, 57–2 U.S. Tax Cas. ¶ 9711 (N.D. Ga. 1957); *Long* v. *United States*, 148 F. Supp. 758 (S.D. Ala. 1957), that result is no longer possible. *McClure* v. *Rountree*, 330 F.2d 954 (6th Cir. 1964); *Johnson* v. *Wall*, 329 F.2d 149 (4th Cir. 1964); *Botta* v. *Scanlon*, 314 F.2d 392 (2d Cir. 1963).

150. Under statutes permitting creditors to reach the income of spendthrift trusts in excess of what is necessary for support, the courts have adopted the view that the exemption extends to the amount required to maintain the debtor's station in life, extravagant though it may have been. See Plumb, The Recommendations of the Commission on the Bankruptcy Laws: Exempt and Immune Property, 61 Virginia L. Rev. 1, 81 (1975). It has never been thought, however, that one's *tax* obligations should be permitted to take second place to extravagant living. *Id.* 87–88, 92.

151. *Cf. Lebanon Woolen Mills* v. *United States*, 311 F. 2d 364 (1st Cir. 1962); *United States* v. *Allied Stevedoring Co.*, 138 F. Supp. 364 (S.D. N.Y. 1956).

152. *Cf. Willits* v. *Richardson*, 497 F.2d 240, 246 (5th Cir. 1974). But in *United States* v. *Brodson*, 241 F.2d 107, 109 (7th Cir. 1957), cert. denied, 354 U.S. 911 (1957), the court questionably gave weight to the possibility of such gratuitous assistance, in refusing to release funds for criminal defense.

153. *Clark* v. *Campbell*, 501 F.2d 108, 124 (5th Cir. 1974), cert. pending.

154. *Supra* at note 99.

155. *Supra* at notes 85–86.

156. See *Willits* v. *Richardson*, 362 F. Supp. 456, 461 (S.D. Fla. 1973), rev'd, 497 F.2d 240 (5th Cir. 1974); *Boyd* v. *United States*, 74–1 U.S. Tax Case ¶ 9408 (E.D. Pa. 1974).

157. See *United States* v. *Cooper*, 75–1 U.S. Tax Cas. ¶ 9234 (D. D.C. 1975), holding it futile and duplicative for the district court to consider the validity of the short-period deficiency once a jeopardy assessment for the full year had been made and appealed to the Tax Court.

158. See Note, Termination of Taxable Year: Procedures in Jeopardy, 26 Tax L. Rev. 829, 842 (1971).

159. Int. Rev. Code of 1954 § 6851(b); H.R. Rep. No. 1337, 83d Cong., 2d Sess. A421 (1954).

160. See Tax Court Rule 142(a).

161. Note 92 *supra*.

162. *Supra* at notes 93–98.

163. See legislative suggestion l.m, *supra*.

164. *Flora* v. *United States*, 362 U.S. 145 (1960).

165. Internal Revenue Manual Supplement 45G–204, § 4.05 (Feb. 8, 1973).

166. Statement of Procedural Rules § 601.105(c)(2)(i). See Silver, Terminating the Taxpayer's Taxable Year: How IRS Uses It Against Narcotics Suspects, 40 J. Taxation 110, 110 (1974).

167. See *Hall* v. *United States*, 492 F.2d 1211, 1212 (6th Cir. 1974), cert. granted.

168. *Supra* at note 78.

169. *Supra* at note 108.

170. *United States* v. *Sullivan*, 274 U.S. 259 (1927); *United States* v. *Yuginovich*, 256 U.S. 450, 462 (1921); *Washington* v. *United States*, 402 F.2d 3 (4th Cir. 1968), cert. denied, 402 U.S. 978 (1971).

171. *Sonzinski* v. *United States*, 300 U.S. 506, 514 (1937).

172. *United States* v. *Doremus*, 249 U.S. 86, 94 (1919).

173. *United States* v. *Kahriger*, 345 U.S. 22, 32–33 (1953); *United States* v. *Sullivan*, 274, U.S. 259 (1927).
174. *Marchetti* v. *United States* 390 U.S. 39 (1968).
175. See *Bull* v. *United States*, 295 U.S. 247, 259 (1935).
176. *Phillips* v. *Commissioner*, 283 U.S. 589, 595 (1931).
177. *Cf. United States* v. *United States Coin & Currency*, 401 U.S. 715 (1971).
I reiterate that I cannot know from the reported cases, in which the allegations are taken as true for the purposes of a motion to dismiss, whether such charges are true or the instances widespread.

EXHIBIT A

XXIII. JUDICIAL REVIEW OF THE EXISTENCE OF JEOPARDY WHERE A JEOPARDY ASSESSMENT HAS BEEN MADE

Resolved, That the American Bar Association recommends to the Congress that the Internal Revenue Code of 1954 and the Judicial Code be amended to permit the United States District Courts to review the finding of the Secretary of the Treasury that the assessment or collection of a deficiency would be jeopardized by delay; and

Be It further Resolved, That the Association proposes that this result be achieved by adding section 6865 to the 1954 Code and amending sections 6861(a) and 7421(a) of the 1954 Code and section 2201 of the Judicial Code; and

Be It Further Resolved, That the Section of Taxation is directed to urge the following amendments or their equivalent in purpose and effect upon the proper committees of Congress:

Sec. 1. Section 6861(a) of the Internal Revenue Code is amended to read as follows (insert new matter in italics):

(a) AUTHORITY FOR MAKING.—If the Secretary or his delegate believes that the assessment or collection of a deficiency, as defined in section 6211, will be jeopardized by delay, he shall, notwithstanding the provisions of section 6213(a), immediately assess such deficiency (together with all interest, additional amounts, and additions to the tax provided for by law), and notice and demand shall be made by the Secretary or his delegate for the payment thereof. *The fact that the period of limitation for the collection or assessment of the tax is about to expire shall not be considered in the determination that the assessment or collection of a deficiency will be jeopardized by delay.*

Sec. 2. Chapter 70, Subchapter A, Part II, of the Internal Revenue Code is amended by adding at the end thereof a new section as follows:

Sec. 6865. JUDICIAL REVIEW OF JEOPARDY ASSESSMENTS.

(a) REVIEW OF SECRETARY'S FINDING AND VACATION OF ASSESSMENT.—*A finding of the Secretary or his delegate that the assessment or collection of a deficiency would be jeopardized by delay shall be subject to review under section 2201 of Title 28, United States Code. Upon such review, if the court decides that the taxpayer has, by a fair preponderance of the evidence, proved that the assessment or collection of the deficiency will not be jeopardized by delay, the court shall vacate and annul the assessment made under section 6861(a) or section 6862(a), and it shall be void and of no effect.*

(b) STAY OF FURTHER PROCEEDINGS OF SECRETARY.—*In an action for such review, the court shall have the power to stay any further proceeding of the Secretary or his delegate for the collection of the deficiency pursuant to the assessment sought to be reviewed, pending the determination of such action.*

(c) PREFERENCE ON CALENDAR ACCORDED TO REVIEW OF SECRETARY'S FINDING.—*Any such review pursuant to the provisions hereof shall be entitled to a preference on the calendar pursuant to the rules of the district court having jurisdiction of the proceeding.*

Sec. 3. Title 28, Chapter 151, section 2201 of the United States Code is hereby amended to read as follows (insert new matter in italics):

Sec. 2201. In a case of actual controversy within its jurisdiction, except with respect to Federal taxes *other than a proceeding under section 6865 of Title 26, United States Code*, any court of the United States and the District Court for the Territory of Alaska, upon the filing of an appropriate pleading may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought. Any such declaration shall have the force and effect of a final judg-

ment or decree and shall be reviewable as such. *In a proceeding under section 6865 the sole issue before the court shall be whether the collection of the deficiency will be jeopardized by delay.*

SEC. 4. Section 7421(a) of the Internal Revenue Code is hereby amended to read as follows (eliminate the matter struck through and insert the new matter in italics):

(a) TAX.—Exempt as provided in sections 6212(a) and (c), *and* 6213(a), *and 6865(b)*, no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court.

EXPLANATION

Summary

The authority of the Secretary or his delegate to make a jeopardy assessment when he finds that assessment or collection of a tax will be jeopardized by delay is not, under present law, subject to judicial review. The absence of independent review permits the exercise of this authority in situations for which it was not intended. The proposed legislation enables the taxpayer to obtain a review in the district court of the question whether jeopardy exists, and authorizes the court to annul the jeopardy assessment if the taxpayer proves that delay will not jeopardize the assessment or collection of the tax.

Discussion

Under present law, jeopardy assessments are made by the Secretary or his delegate under § 6861. He is authorized to make them when he believes that the assessment or collection of a tax delinquency will be jeopardized by delay. A determination that jeopardy exists is not subject to judicial review (e.g. Lloyd v. Patterson, 242 F.2d 742 (5th Cir. 1957); Harcey v. Early, 66 F. Supp. 761 (W.D. Va. 1946), aff'd 160 F. 2d 836 (4th Cir. 1947); Veeder v. Commissioner, 36 F. 2d 342 (7th Cir. 1929); Foundation Co. v. United States. 15 F. Supp. 229 (Ct. Cl. 1936). The statute relegates the taxpayer to two avenues of relief: (1) abatement by the Treasury under § 6861(g), largely illusory because the decision to grant relief stems from the agency imposing the assessment in the first place, although there has been judicial admonition that this discretion should be exercised in proper cases (Darnell v. Tomlinson, 220 F. 2d 894 (5th Cir. 1955)); and (2) by posting a bond under § 6863 to stay collection of the assessment, nebulous, to say the least, when all of the taxpayer's assets are tied up (see Kimmel v. Tomlinson, 151 F. Supp. 901 (S.D. Fla. 1957), which characterized the right to post a bond in this situation as a "mockery").

Attempts at injunctive relief immediately run counter to § 7421 of the Code, prohibiting injunctions in tax cases. While it is true that unusual circumstances will justify an injunction (e.g. Communist Party, U.S.A. v. Moysey, 141 F. Supp. 332 (S.D.N.Y. 1956); Shelton v. Gill, 202 F. 2d 503 (4th Cir. 1953); Midwest Haulers v. Brady, 128 F. 2d 496 (6th Cir. 1942); Allen v. Regents, etc., 304 U.S. 439 (1938); Miller v. Standard Nut Margerine Co., 284 U.S. 498 (1932); Mitsu-Kiyo Yoshimura v. Alsup, 167 F. 2d 104 (9th Cir. 1948)), such relief is granted on a strictly case-by-case basis (Homan Mfg. Co. v. Long, 242 F. 2d 645 (7th Cir. 1957). In any event, exceptional and extraordinary circumstances must be shown to exist, and indigency is not such a showing (Lloyd v. Patterson, *supra;* but see Arnold v. Cobb, — F. Supp. —, 57-2 U.S.T.C. ¶ 9711, 1957 P-H Fed. ¶ 72,727 (N.D. Ga. 1957), where this relief was granted to prevent the taxpayer from becoming a public charge). Furthermore, in the light of § 7421, false jeopardy would not appear to be one of these exceptional circumstances. Lastly, the fact that the imposition of the assessment leaves the taxpayer wholly without means to contest the matter is, under the current state of the law, or no moment (United States 1. Brodson, 234 F. 2d 97 (7th Cir. 1965), cert. denied 354 U.S. 911).

Thus, the taxpayer who is subjected to a jeopardy assessment finds himself in a position where he cannot secure independent review of the correctness of the Treasury determination that jeopardy does in fact exist. Conversely, the Treasury is in a position to use its jeopardy powers in an unintended fashion.

While it is generally considered wrong to use the threat of a jeopardy assessment as a vehicle for extracting an extension of the statute of limitations from

a taxpayer, there appears to be some practice to the contrary. Section 6861 uses the words "assessment or collection" in the disjunctive. In Veeder v. Collector, *supra*, it was indicated that the fact that the statute of limitations is about to run constitutes jeopardy.

Amendment to the law should be sought to afford the taxpayer a right to review the Treasury's administrative determination as to the existence of jeopardy. Your committee feels that such a review should be made available to a taxpayer under the declaratory judgment procedure, because this would permit a speedy determination which might result in the release of needed funds to contest or defend the action. The courts also should be granted power to stay any further proceedings under the jeopardy assessment already made pending the outcome of the declaratory judgment suit.

Since this recommendation as well as recommendation 2 below, comprehends the fields in which the Committee on Court Procedure, the Committee on Administrative Practice and the Committee on Federal Tax Liens and Collection Proceedings are working, both recommendations have been referred to those committees.

While these recommendations cover situations involving criminal income tax evasion and civil fraud situations, the scope is considerably broader. They also cover cases in which, without either of these elements being present, a jeopardy assessment is made for one reason or another. Thus, they cover the whole field of tax administration.

EXHIBIT B

XXIV. RELEASE OF FUNDS FROM JEOPARDY ASSESSMENTS

Resolved, That the American Bar Association recommends to the Congress that the Internal Revenue Code of 1954 be amended to permit the United States District Court to order the release of the taxpayer's property from jeopardy assessment liens for certain purposes; and

Be It Further Resolved, That the Association proposes that this result be achieved by amending section 6861 of the 1954 Code; and

Be It Further Resolved, That the Section of Taxation is directed to urge the following amendment or its equivalent in purpose and effect upon the proper committees of Congress:

Sec. 1. Section 6861 of the Internal Revenue Code is amended by redesignating the present subsection (h) as subsection (j), and by adding new subsections (h) and (i) as follows:

(h) RELEASE OF FUNDS FROM JEOPARDY ASSESSMENTS.—*Where a jeopardy assessment has been made and notice of the lien or liens arising by virtue thereof has been filed, the United States District Court for the district in which the taxpayer resides, upon verified petition of the taxpayer, may in its discretion order released from said liens such funds or other assets as are sufficient to enable the taxpayer—*

(1) to retain the services of legal counsel and to provide for other necessary expenses in the representation of the taxpayer in all matters, civil, criminal, or both, relating to or affecting the tax liability asserted in the jeopardy assessment;

(2) to repair, maintain and preserve property against which a lien in favor of the United States exists by virtue of the jeopardy assessment, including the satisfaction of liens against such property which have priority over said lien; and

(3) to pay taxes (except taxes covered by the jeopardy assessment) owing by the taxpayer whether due before or after the making of said jeopardy assessment.

Upon releasing such funds from such liens, the said court shall impose such conditions, as in its discretion it shall deem advisable, to insure the application of such funds to the purposes for which they were released.

(i) NOTICE TO SECRETARY.—*The verified petition of taxpayer shall be served upon the Secretary or his delegate in triplicate at least twenty days before a hearing thereon. Subsequent to the mailing of such notice, the Secretary or his delegate shall have authority to release funds or other assets as requested in said petition without regard to the provisions of subsection (g) hereof.*

EXPLANATION

Summary

The freezing of the taxpayer's assets by a jeopardy assessment has harsh consequences which sometimes prejudice the interests of the Government as well as the taxpayer. One of the unfair results is the denial to the taxpayer of the use of his own property to defend himself against a criminal charge of tax evasion, or even to contest the jeopardy assessment in the Tax Court. Another is the legal inability to obtain a release of funds to pay for needed repairs, fire insurance premiums, and similar expenses necessary for the protection, preservation, and maintenance of the property. The proposed legislation empowers the district court, in its discretion, to release such funds as are necessary for the purposes specified in the statute. The supervision of the court will restrict the release of funds to proper purposes and protect the interests of the Government without the unfair results which the presently inflexible statute produces.

Discussion

The right to levy jeopardy assessments against taxpayers is one of the most drastic and far-reaching powers vested in the Secretary of the Treasury. This power is intended to be used sparingly, and only in situations in which there is good reason to believe that the taxpayer is planning to conceal his assets or otherwise place them beyond the reach of the collection officers of the Treasury Department. There have been many complaints that this power has been misused by the making of jeopardy assessments for reasons other than any real jeopardy to the assessment or collection of a deficiency, and that the amount of the assessment has been arbitrarily determined at a level far above what the facts warrant.

Whatever the reasons which prompt its issuance, a jeopardy assessment has far-reaching and often disastrous effects upon the taxpayer, and at times the interests of the Government are also jeopardized. For example, the freezing of the taxpayer's bank account may prevent him from paying fire insurance premiums on his property and from making necessary repairs, thus exposing the Government as well as the taxpayer to a risk of loss. The Government's interests as well as the taxpayer's require some means of relief in this situation. Similarly, the taxpayer should be permitted to make use of his property to pay his current income taxes, as well as deficiencies for years other than those involved in the jeopardy assessment.

Even more compelling than these considerations, however, is the necessity for safeguarding the right of the taxpayer to make an effective defense against a criminal charge of evading the alleged tax deficiency on which the jeopardy assessment is based, and to contest in the Tax Court the alleged liability for such taxes. It is manifestly unfair to prevent a taxpayer from using his own property in such situations; yet that is the inevitable and necessary result of a jeopardy assessment under the present law.

The problem is dramatically illustrated by the case of United States v. Brodson, pending in the United States District Court for the District of Wisconsin. The district court, after lengthy but futile efforts to obtain administrative release of funds from the jeopardy assessment, dismissed the tax evasion indictment on the ground that the Government's action in tying up the defendant's assets had made it possible for him to have a fair trial, particularly since the services of a qualified accountant were indispensable to a proper presentation of the taxpayer's defense in a complex net worth case. (136 F. Supp. 158.) This decision was reversed on appeal by a 3–2 decision, in which the majority concluded that the district court's conclusion was premature and that the question of whether the jeopardy assessment had in fact made a fair trial impossible should have been decided after, rather than before, the trial. (241 F. 2d 107.)

Following the remand, the district court made an order postponing the criminal trial until after the taxpayer's appeal to the Tax Court from the jeopardy assessment had been determined, notwithstanding the vigorous protest of the Government that under a longstanding and consistently-followed policy the Tax Court trial should be deferred until after the criminal charge had been disposed of. (58–1 U.S.T.C. ¶ 9183, 1958 P–H Fed. ¶ 58–352.)

The defense counsel in the Brodson case had been appointed by the court, but regardless of the quality of court-appointed counsel and of the amount of time which they can afford to donate, it is still repugnant to our concepts of justice to prevent a defendant from using his own property to hire counsel of his own

choice to represent him. Moreover, the courts have no authority to appoint accountants to work for a taxpayer, although their services are usually indispensable in tax fraud cases.

Since the release of funds would be under the supervision of a district court, there would be reasonable safeguards against unwarranted expenditure of funds.

Senator HASKELL. I am going to suspend here for about 5 minutes, but our next witness is Theodore S. Lynn of New York City.

[A brief recess was taken.]

Senator HASKELL. Mr. Lynn?

Mr. Lynn, I appreciate your being here.

STATEMENT OF THEODORE S. LYNN, ESQ., WEBSTER, SHEFFIELD, FLEISCHMANN, HITCHCOCK & BROOKFIELD

Mr. LYNN. Thank you, Senator.

My name is Theodore S. Lynn. I am a member of the New York City law firm of Webster, Sheffild, Fleischmann, Hitchcock, and Brookfield.

As a consultant to the IRS project of the Administrative Conference of the United States and a New York State Bar Association tax section subcommittee chairman, I have recently studied the Internal Revenue Service's summons powers. My comments are my own, however.

The IRS is widely using its administrative summons power to seek evidence of possible criminal and civil tax liability.

A summons may be freely issued by most any Internal Revenue Service agent demanding books, records, and testimony under oath. There is little, if any, review by an agent's superior and no application to a grand jury or any judicial body is required before a summons is issued.

I leave my prepared text for a minute to mention that there was inquiry at the Internal Revenue Service as to the number of summonses that had been issued; how many were contested; and how many were enforced in court. Apparently the Internal Revenue Service keeps no records on the subject. Summons forms are apparently available in a pile in an IRS office. An agent simply picks forms up and puts them in his briefcase. When appropriate, he pulls one out, fills it in, and hands it to the taxpayer or third party recipient. And apparently there are no records at all.

Thus, an IRS agent——

Senator HASKELL. Let me ask you, Mr. Lynn, I am really not familiar with this procedure. Would the agent be, for instance, auditing my return when he issues a summons, or might he be auditing your return and issue me the summons to see if you had had any transactions with me?

Mr. LYNN. It could be in either instance.

Senator HASKELL. Either instance? I see. OK. Thank you.

Mr. LYNN. Thus, an IRS agent may arrive at a person's office or home, pull out a blank summons form from his briefcase, fill it out, and serve it. The summons might demand that the person bring his personal or business records to, and be prepared to testify under oath at, an IRS office some days hence.

The summons form does not notify the recipient of his rights to a court hearing; indeed, it contains an in terrorem statement that:

"Failure to comply with this summons will render you liable to proceedings in the district court of the United States or before a United States Commissioner or magistrate to enforce obedience to the requirements of this summons, and to punish default or disobedience."

While the IRS is not empowered to punish refusal to obey a summons without applying to a court, recipients of summonses often are unaware of the technicalities. IRS agents, whether or not intentionally, frighten many people. Unlike other investigative agencies, the IRS is involved in everyone's life year after year. Taxpayers may comply with broad, unclear summonses through fear and lack of understanding.

Since the IRS is not empowered to enforce its summons without judicial application, the summons power has become a trap for the unwary. Sophisticated taxpayers know that they can have a day in court to determine to what extent they must comply with the summons; less educated taxpayers feel that they must comply.

If a summoned person wishes to contest a summons, he must appear at the time and place specified on the summons to object. Who is the hearing officer who hears the objection? It is usually the IRS agent who issued the summons. A sophisticated taxpayer knows that all he need do at this hearing is state his "good faith" objections; if the Service wishes to proceed, it must go to court.

For various administrative reasons, the Service often does not apply for judicial enforcement of these summones. This injects an unfortunate element of gamesmanship.

Now, what about third party summonses? These are summonses issued to financial institutions such as a bank or to the accountant of a taxpayer under investigation. Although the taxpayer who is under investigation may have grounds to object to enforcement of such a summons, many third parties readily comply. Thus, the taxpayer may wish to apply for judicial restraint of third party cooperation with the IRS. If the third party contests the summons, the taxpayer may wish to intervene in the enforcement hearing, that is, participate in the enforcement hearing.

The threshold problem for the taxpayer is that of discovering whether a summons has been served on a third party. The courts have held that, under the existing statutes, that the IRS is not required to notify the taxpayer in such a situation. I believe that notice should be given in order to make meaningful any right to intervene or apply for restraint. However, only Congress can change the statute. Indeed, an analagous problem exists under the Bank Secrecy Act of 1970.

Even if he knows of the third party summons, in order to intervene or restrain, a taxpayer must establish a valid reason, and even then permission to intervene or restrain is in the court's discretion. A court may refuse to enforce a summons if it violates constitutional rights or attorney-client or other applicable privilege; if it is deficient in describing the material requested, or the procedures for issuing or serving it have not been complied with; if the witness can establish that he is unable to comply with its demands because he does not have possession of the records summoned, or he is in ill health; if it is not issued for a legitimate purpose; or if it calls for material which is not relevant to the inquiry.

Now under each of these various tests, there are numerous cases. Suffice that taxpayers have great difficulty in being granted to be

heard on third party summonses and most summonses are enforced by the courts.

A major problem, in my judgment, is that the IRS uses its administrative summons power during the criminal tax fraud investigations. Special agents of the Intelligence Division of the IRS are a major source of issued summonses and they are charged—some say solely—with the duty of investigating for criminal tax fraud.

Is the obtaining of evidence to establish criminal tax law violations a proper use of the IRS administrative summons power? The consistent IRS assertion has been that each summons in question was motivated at least partially by civil tax investigation purposes. A recent district court decision has characterized this situation as one which "invites hypocrisy and dissimulation on the part of Government investigators."

The Supreme Court, however, with a few limitations, has supported the IRS position. The Court has stated that a summons may be issued in such an investigation "if it is issued in good faith and prior to a recommendation for criminal prosecution."

Thus, unless a witness can show that the summons was issued solely for criminal purposes or that there was a prior recommendation to prosecute, the summons will likely be enforced. Questions remain, such as when a criminal prosecution recommendation is deemed to occur.

Even if a summons is issued with the proper procedures and pursuant to a legitimate purpose—the legitimate purpose issue includes whether or not the summons has been used solely for criminal purposes—a summons may only be used to demand production of books and testimony "as may be relevant or material" to an authorized inquiry.

The test of materiality and relevancy has been liberally construed by the courts. Probable cause for the investigation need not be established. The Service is not required to show that the information sought will contradict a tax return. A summons will be enforced if the information sought might throw light upon the correctness of a tax return.

Finally, the problem of John Doe summonses. It had been thought that the IRS would use its administrative summons power only when it was investigating the tax liability of a particular person or group or when there was cause to believe that a specific tax liability was due.

However, the IRS has increasingly been using a summons which lists John Doe as the person whose tax liability is being considered. Such a summons may have proper use during a focused and limited audit. I believe it an improper use, however, if issued to a financial institution or other organization in the hope that some unsuspected tax liability might be discovered.

The gentlemen from the banking association will discuss the various judicial decisions with you. Suffice here that the judiciary has not yet settled the question.

The courts might not have permitted such apparent fishing expeditions under section 7602 of the Internal Revenue Code, the statutory authority granted to the Service for its usual summons power. Unfortunately, the existence of another section of the Code, 7601, which permits canvassing of districts for taxable persons and objects has been seen as statutory support for the John Doe summons. I believe this confuses an authority intended to permit canvasses for research and

review of IRS enforcement operations with authority for issuance of unfocused summonses.

Now, to his credit, Commissioner Alexander announced in a speech in May that he was tightening IRS internal controls over the issuance of John Doe summonses. The appropriate District Chief and IRS Regional Council's office must approve the issuance and they are to be issued "only in limited and justifiable circumstances," to use his words. In my judgment, the new procedure does not go far enough.

In any event, I believe that the potential for invasion of privacy and for fishing expeditions is sufficiently serious that your subcommittee should consider articulating legislative standards and limitations. Restrictions on the use of unfocused, wide gaged administrative summonses should not depend on possibly changing administrative policy.

I believe that your subcommittee should consider amending the code to assure that the administrative summons cannot be used to force third parties to cooperate in fishing expeditions which merely hope that some unknown person might be shown to have some unsuspected tax liability.

I understand that the House Ways and Means Committee is considering proposing a new Section 7609, entitled: "Limitations on Use of Administrative Summons." For all third party summonses, John Doe or otherwise, the taxpayer would have to receive notice from the IRS on or before the time the summons is issued and the taxpayer would have standing and 10 days to challenge the summons in the applicable District Court.

Further, in the case of a third party John Doe summons, the IRS would also have to satisfy a court that there is reasonable cause to believe that an unreported taxable transaction has occurred and that other sources for the information are not readily available.

I think this is a step in the right direction, although I still have concern with the use of an administrative summons during an investigation of criminal tax liability. Further, the current in terrorem statement on the summons form should be removed and, in its place, there should be a statement that a person has the right to contest enforcement in court. Also, the broad delegation to just about any IRS agent to issue a summons should be changed, with standards articulated and controls initiated.

If I may also add, in response to an earlier question to another speaker, as a former clerk to the U.S. Tax Court, I think it works quite well. I think it might have some concern about additional decentralization of its activities.

Senator HASKELL. Well, we were getting pretty far afield there.

You reviewed, I gather, the use of these administrative summonses. And what principal problems have you run into?

Mr. LYNN. Well, I think the first problem is the free ability of just about any agent to serve them—to fill them out with a pencil on a desk and to hand it to either the taxpayer, to his representative, or to a financial institution on a third party basis.

Senator HASKELL. Is this done very often?

Mr. LYNN. Yes.

Senator HASKELL. It is?

Mr. LYNN. I say yes from understanding because the second problem is the fact that the IRS apparently keeps no records on this entire subject.

Senator HASKELL. One of your basic concerns is that somebody who is not a lawyer or does not have ready access to a lawyer will think that is the equivalent of a court order. Is that basically it?

Mr. LYNN. Well, you get something very fancy from a government official that says in big type "Summons" and it says "failure to comply will subject you to proceedings in the district court," for punishment and what have you. And if you are not sophisticated, it is rather frightening and you would then open your books completely to someone who may well be really motivated by trying to put you in jail without telling you about your fifth amendment rights, contrary to the entire case law in the last 20 years.

Senator HASKELL. And you do find it is used rather frequently?

Mr. LYNN. I think so, yes. I think, of course, someone from the Service would be your best witness on this subject.

Senator HASKELL. I beg your pardon?

Mr. LYNN. I think someone from the IRS should be asked that very question.

Senator HASKELL. Well, we will.

Do you have any suggestions as to standards that might be set up in the use of administrative summonses or are you just against administrative summonses?

Mr. LYNN. I am not against administrative summonses. It seems to me that in the area of deductions, the IRS does not need it because it can always deny deductions and give you the burden of proving that they are proper. In the area of unreported income, however, the IRS has to investigate and sometimes witnesses are uncooperative and they have to go to court to get enforcement.

However, first I would have the summons form changed to make sure that the person receiving it understands that this is the first step merely and that he has a right to object and if the Government wishes to proceed, they have to go to court to enforce it. He does not have to go to court. All he has to do is attend—to visit with the agent at the time he is supposed to and say "I have good faith objections. The summons asks for the product of my attorney's work. I am claiming the fifth amendment privilege against self-incrimination. The summons asks for material which is not relevant to your inquiry. It is being used for an improper purpose. You are using it to harass me," or whatever. The form should disclose the recipient's rights.

And secondly, I am concerned about the use of administrative summonses by special agents of the IRS, whose sole purpose really in substance is to investigate for a criminal violation. For that purpose, it seems to me that the administrative summons altogether too casual a procedure. Theirs should obtain grand jury or court permission—it should not use a piece of paper from any agent's briefcase.

Thirdly, the "John Doe" summons is a problem.

Senator HASKELL. Yes. I was going to ask you about that. Tell me a little bit more. Do you know any specific instances, other than these I am aware of?

Mr. LYNN. Fortunately, I think, all of the gentlemen that follow me will be focusing mostly on the "John Doe" summonses, the Banking Association and the others. But the case law discloses, for example, the *Bisceglia* decision where a number of decrepit bills were deposited in a bank. After that fact was disclosed, an IRS agent served a summons to the bank in the liability of "John Doe" attempting to find out

the identity of the depositor. This was a broad summons issued for numerous bank records for a number of months and what have you. The district court limited it. As limited, it seems to me it was OK, and the Supreme Court so held. This was a united search while a transaction usually indicated that a tax on unreported income might be due. I do not know if the gentlemen who follow me would agree with this conclusion.

A "John Doe" summons which, in my judgment, was not proper was the one that was issued to the Humble Oil Co. The IRS said it was engaged in research and asked, basically, for all of their records on the termination of some oil leases. The IRS believed that there was general tax avoidance going on when oil leases were terminated.

So, without thinking of anybody in particular, they wanted to run through all of Humble Oil's records. The Firth Circuit Court said that the summons can be used "only when IRS scrutiny of a taxpayer or a group * * * becomes particularized or focused." The Supreme Court vacated and remanded that decision to the Fifth Circuit Court on the basis of the *Bisceglia* decision. The fifth circuit said again, even with that decision, it thought that the summons should not be enforced.

Other reported instances of "John Doe" summonses involved summonses issued to tax return preparers, to attorneys seeking identity of their clients, to a soybean supplier, and to financial institutions to obtain the identity of an operator's stockholders. In some cases, I agree they were appropriate; in others, I disagree. The test should be whether there is sufficient facts on a particular suspected tax liability.

It seems to me the House Ways and Means Committee is correct, in as far as it has gone. The taxpayer should get notice and standing when a third party is asked for this information. So, for example, if a client has some complaints, his accounting firm should not be put in the position of having to disclose all of the man's records without the man even knowing it.

There certainly should be notice and the ability to contest this in court. And the House Ways and Means Committee is correct also in giving the taxpayer standing. A lot of the courts will not even hear the taxpayer on this issue; saying that when the deficiency occurs, then you can be heard.

Senator HASKELL. This is to protest a third party summons?

Mr. LYNN. Yes. If the taxpayer says "well, I do not want you, my lawyer, to give material to——"

Senator HASKELL. That lawyer would be disbarred if he did that, would he not?

Mr. LYNN. Well, the lawyer might or might not. There are a number of cases that indicate that the lawyer, and indeed the taxpayer, may have to give up certain kinds of impersonal records. A taxpayer has material, such as his accountant's workpapers, which may or may not convict him of a crime. He gives them to his lawyer. Can a lawyer keep them when a summons is issued for them?

Senator HASKELL. I had always thought there was a privileged relationship.

Mr. LYNN. So do most lawyers. But unfortunately some of the courts may not agree. See the second circuit court of appeal's August decision in *Beattie*.

Senator HASKELL. On the "John Doe" summonses, do you know of any others, other than the two cases you mentioned, where they were used for fishing expeditions?

Mr. LYNN. There are a large number of reported cases on the very subject. I could give to the staff the report—well, I have prepared a report for the administrative conference. I have a copy with me. I could give it for use of the staff, if you like; if I could get it back.

Senator HASKELL. Yes, I think that would be helpful. And that lists the uses? I mean you are not meant to release it until a certain time?

Mr. LYNN. The administrative conference has it own procedures. I have the copyright and it should not really be printed. But if you are just reading and returning, I do not think there is any question.

Senator HASKELL. All right. If you could leave it, I would be interested in some additional examples of where they have been used, as I say, as a fishing expedition.

Mr. LYNN. Well, there will be a number of gentlemen following me.

Senator HASKELL. I have to go vote and come back. So I do not want to keep you. I just wanted to see if I had anymore questions of you.

It seems to me that it is a particular problem—the arbitrariness of summonses to the taxpayer can be pretty well cured by saying you can go to court, do not take this too seriously or something to that effect.

Mr. LYNN. I think so.

Senator HASKELL. The third-party summons would seem to me to present a more difficult problem. It would seem your suggestion there is that the taxpayer ought to be informed ahead of time and should have an opportunity to say to the third party, "Do not respond."

Mr. LYNN. There is a problem from the Government's point of view on ahead of time. It seems to me the notice may be simultaneous. For example, a summons to an accountant for the workpapers on an audit is a normal first step in a tax fraud audit. If the taxpayer was given the notice that they were going to go after the accountant and serve a summons on him, the accountant would sweep up all of his workpapers and give them to the taxpayer who could then claim his fifth amendment privilege. The taxpayer might not win in court, but this is an unsettled area.

It seems to me, simultaneously with the summons, and before the summons can be enforced, the taxpayer should be given notice.

I might say the accounting profession is up in arms about all of this because there is no accountant-client privilege as there is an attorney-client privilege, and they feel rather uncomfortable whenever they are corroborating with the IRS and in a sense assisting in either putting their clients either in jail or in establishing large tax liabilities for him. For example, an accountant might do an analysis of the tax implications of a transaction on a one hand, on the other hand basis, and the man engages in the transaction and reports it quite honestly. But an audit the Service can summon that document and then use it in preparing a court case against the taxpayer.

Senator HASKELL. But you would have the notification simultaneous. Of course, the third party might—if agents show up at two places, different agents at one time—hand over all of his records, and it might be a criminal investigation.

Mr. LYNN. That is a different problem. A summons is not returnable in less than 10 days by statute currently. If an agent just came

over and said, "Please, give it to me" and did it without the summons, there is not much that——

Senator HASKELL. I see. The summons now is 10 days.

Mr. LYNN. Oh, yes. There is a minimum 10-day return.

Senator HASKELL. So that would take care of that.

Well, thank you very much, Mr. Lynn. I appreciate your being here.

Mr. LYNN. Thank you.

Senator HASKELL. I will just go over and vote, I will say to the remaining witnesses, and be back in 5 minutes.

[A brief recess was taken.]

Senator HASKELL. Is Mr. Robert S. Fink of New York in the room?

Mr. FINK. Yes.

STATEMENT OF ROBERT S. FINK, ESQ.

Mr. FINK. Mr. Chairman, my name is Robert S. Fink. I am a partner in the New York firm of Kostelanitz, Ritholz & Mulderig. Our firm specializes in tax litigation, and as such, I have extensive experience in dealing with the subject of the Internal Revenue Service's summons power.

When applying for a home mortgage or for a personal loan, we reveal to our banker the intimate details of our financial circumstances to an extent often undisclosed to one's spouse. Indeed, in this age of computerized finances, we reveal to our banker more of our personal self than most of us would dream of revealing to our clergyman, doctor, or lawyer. A mere perusal of one's personal checks will disclose everything from one's political affiliations and club memberships to how one furnishes his home, what one eats for dinner, where one goes for the evening and often with whom.

In light of the foregoing, many countries, in one form or another, have established a privilege for the relationship between banker and customer. We, in America, evidently have determined that the necessity for regulation of our financial markets and the need for tax collection outweigh the values of personal privacy. An agent of the Internal Revenue Service has full access to all banking records through his summons power. In conferring this power under title 26, United States Code, section 7602, Congress carefully delineated the limited purposes for which the summons power may be used.

Until recently, it was believed that this powerful administrative tool could only be used during the course of an Internal Revenue Service investigation of a specifically ascertainable, identifiable taxpayer. This belief was supported by the restraint of the Internal Revenue Service in the use of its summons power only during the course of an investigation of a specific taxpayer. Moreover, section 7602 speaks in the singular. It refers to the "correctness of any return" and to "the liability of any person." This specific language of section 7602 stands in marked contrast to the broad language delineating the general duties of the Internal Revenue Service set forth in section 7601.

The Internal Revenue Service has recently expanded the breadth of its summons power through the "John Doe" summons.

Senator HASKELL. Now, Mr. Fink, one thing you do mention; you use the phrase, "an agent of the IRS has full access to all banking records through this summons power." This, of course, is a power only if

agreed to by the court. In other words, if you as a lawyer protest the issuance of a summons, the IRS has got to go to court to enforce the summons, is that not right?

Mr. FINK. I rarely, as an attorney representing a taxpayer, have noticed that the client's bank records have been taken, pursuant to summons by the Internal Revenue Service. The taxpayer may only learn at a later date. Often, the bank will inform——

Senator HASKELL. This is the question Mr. Lynn was addressing himself to.

Mr. FINK. Yes. A bank has no duty, and IRS has no obligation, to inform the taxpayer that his records are being seized by summons.

Senator HASKELL. I understand. All right, go ahead. Excuse me.

Mr. FINK. So indeed, the taxpayer often finds out after it is an accomplished fact.

Senator HASKELL. Sure, I understand.

Mr. FINK. The Internal Revenue Service has recently expanded the breadth of its summons power through the "John Doe" summons. By the use of such a summons, the Internal Revenue Service has subpenaed, from third parties, production of records of large numbers of unspecified and unidentified persons.

In the case of *United States* v. *Bisceglia*, the U.S. Supreme Court, on February 19 of this year, permitted, without guideline or limitation, this expanse of power. In *Bisceglia*, a branch of the Federal Reserve Bank received, within a 10-day period, from a commercial bank, two separate deposits, each of which included $20,000 comprised of 200 $100 bills. A special agent of the Internal Revenue Service issued a "John Doe" summons to the vice president of the commercial bank, demanding production of all books and records which would provide information as to the entity or entities which deposited the $100 bills to the commercial bank.

The bank officer, evidently believing that production of such documents would permit an unrestricted rummaging by the Internal Revenue Service into the personal financial affairs of an undetermined number of bank customers, refused to comply with the summons, and an enforcement proceeding was brought in the U.S. District Court for the Eastern District of Kentucky. The district court ordered the production of all the bank's deposit slips for a 1-month period, which showed either total cash deposits in the amount of $20,000 or more, or which showed cash deposits of $5,000 or more involving $100 bills.

It should be noted that this district court order did limit the original request by the Internal Revenue Service.

This enforcement order was appealed to the U.S. Court of Appeals for the Sixth Circuit. The court of appeals reversed the district court and held that section 7602 did not authorize the use of "John Doe" summonses for the purpose of examining the affairs of a particular group of persons when no identifiable taxpayer is under investigation, and denied enforcement of the summons. The Supreme Court, however, reversed the Sixth Circuit's Court of Appeals.

With the *Bisceglia* Supreme Court decision, all statutory restraints on the authority of the Internal Revenue Service to issue "Joe Doe" summonses appear to have dissipated. The Service is now empowered to monitor through its summons power any particular segment of our society or economy, on the theory that the information sought falls

within the legitimate interest of the Internal Revenue Service. Should the courts be called upon to limit claimed misconduct by the Internal Revenue Service, the courts will be faced with the fact that there does not exist any statutory standards protecting our citizens from the abuse of a particular tax investigator.

It is submitted that unrestrained use of the Internal Revenue Service's summons power raises fundamental questions as to the kind of government we wish to have control our lives and what hitherto we considered as inviolate privacies. Presently, such invasions into privacies, no matter how shocking, are rarely subject to challenge, since the Internal Revenue Service is not required and as a practice does not notify the taxpayer when it issues a summons to a third party for records of or concerning the taxpayer.

Thus, unless the summoned party voluntarily notifies the taxpayer that an Internal Revenue Service summons concerning him has been served, the taxpayer, who generally is the only aggrieved party, has no notice of the summons. Equally surprising is the fact that even if the aggrieved party has notice, our courts have held that the requisite legal standing to intervene is wanting. Thus, this leaves only the disinterested third party, at his own expense, to champion the rights of the individual against improper governmental activities, a course which is hardly likely.

This expansion of power, judge made, was not in response to a fiscal crisis, wartime condition or other emergency pressure. To legislate constraints on this power will not hinder the Internal Revenue Service's ability to collect taxes or ferret out tax improprieties, for our Federal tax system has operated efficiently for 200 years without the use of such summonses. Unlike a search warrant, the Internal Revenue Service need not show "probable cause" in order to issue a summons. The establishment of a legislative limitation is necessary in order to avoid further abusive infringements on the rights of our citizens to be free from governmental surveillance of such unparticularized breadth.

I must emphasize that fundamental concepts of liberty are at stake. The recent use of the "John Doe" summons by the Internal Revenue Service is not innocent, nor an isolated instance of abuse. Rather, it is a radical departure of prior administrative procedure. It is part of a growing trend of surveillance by the Internal Revenue Service, which includes dossiers on political activists and organizations compelled disclosure by banks under the Bank Secrecy Act of 1970, the increased use of midnight search warrants on the homes of taxpayers, and increased use of grand juries which deny procedures mandated by Congress and Treasury Department regulations.

This trend of continued surveillance reflects a concept of socialized government wherein the individual is subjected to continuous observation by the State. It was Mr. Justice Robert H. Jackson, in his opinion in the well-known case of *Shapiro* v. *United States*, who succinctly stated: "It would, no doubt, simplify enforcement of all criminal laws if each citizen were required to keep a diary that would show where he was at all times, with whom he was, and what he was up to."

It is a legislative responsibility to determine what kind of a relationship our citizens should have to their Government, and unless certain minimal safeguards are established as to the Internal Revenue

Service's administrative summons power, we may be inviting and facilitating the eventuality feared by Mr. Justice Jackson.

I propose that the following safeguards, which are minimal in nature, are necessary. One, upon serving a third party summons, the Internal Revenue Service be required to serve notice of the summons upon the subject taxpayer. Two, the concerned taxpayer be granted standing in court to challenge the propriety of a third party summons. And three, prior to issuing a "John Doe" summons, the Internal Revenue Service be required to establish to a U.S. district judge of magistrate that there is probable cause to believe that our tax laws have been violated, and that an unknown but specific individual or entity is the target of Internal Revenue Service's investigation.

Thank you, Mr. Chairman.

Senator HASKELL. Thank you, Mr. Fink.

You have cited this *Bisceglia* case, and also somebody else mentioned the *Humble Oil* case—are you aware of any widespread use of the "John Doe" summons?

Mr. FINK. I am aware of other use of the "John Doe" summons. I would not say it was widespread. It was not seen until the early mid-1970's. The cases in which it has been used, I would imagine, fall within two broad categories. The first is the Theodore Turner-type cases; and that is, the "John Doe" summons served upon tax preparers. The summons would ask for all records concerning all taxpayers' returns which this preparer had prepared. You can understand that when this is served upon a large accounting firm, that the records of literally thousands upon thousands of innocent taxpayers would be turned over to the Internal Revenue Service.

There was recently a case called Anderson-Clayton, in which the Internal Revenue Service wanted to investigate all soybean farmers in Mississippi, and "John Doe" summonses were used there. There is the *Armour* case, which arose out of the ITT merger. When the Internal Revenue Service revoked an earlier favorable ruling as to that merger, they then wanted the name and information as to all of Hartford Fire Insurance Company's stockholders who took part in that merger. The only way to obtain that information was through the bank that acted as transfer agents, and "John Doe" summonses were used there.

There is an increasing use of the "John Doe" summons, but I do not know if you would say it is widespread. Everything is a matter of degree.

Senator HASKELL. You have made a suggestion here on the "John Doe" summons that a showing of probable cause that tax laws are being violated, and that some unknown but specific person is the subject of an investigation. Now, how would that type of restriction on the use square, let us say, with the *Humble* case?

Mr. FINK. The *Humble* case is, I think, a case unto itself which will never arise again. In Humble Oil—by the way, I do not think it would be permitted, the "John Doe" summons would be permitted in Humble Oil under such a statutory amendment.

Senator HASKELL. You do not?

Mr. FINK. I do not. In Humble Oil, Humble was served with a "John Doe" summons for the records of oil lessors. This was relating to the mineral lessors of Humble Oil. The investigation—I should not use the word investigation—the IRS was looking into whether lessors

were taking lease bonuses into income in the year in which the lessee abandoned the lease without production.

The interesting thing in Humble Oil Co. was that the Internal Revenue Service made an admission that there was no investigation, that there was no intention of an investigation, and that it was merely part of a "data-gathering" research project. The reason why I say that would never occur again is, I do not think there will ever be such an admission again; and the court of appeals in Humble Oil did not permit the "John Doe" summons, and based its opinion on the fact that there was no investigation. The Internal Revenue Service admitted that it was a research project. You cannot use the summons powers for research projects, but I do not think we will see too many research projects any more.

Senator HASKELL. I think you are right.

I gather your suggestions on the restriction of the "John Doe" summons may not be too far off from the concurring opinions of Justices Blackman and Powell in the *Bisceglia* case. Would that be correct?

Mr. FINK. I think it would be very close to Justice Blackmun's opinion.

Senator HASKELL. Thank you, Mr. Fink. I appreciate very much your being here.

Mr. FINK. Thank you.

Senator HASKELL. Our last witness is James E. Merritt of San Francisco, accompanied by Mr. Robert Brubaker of Pennsylvania.

STATEMENTS OF J. ROBERT BRUBAKER, AMERICAN BANKERS ASSOCIATION; AND JAMES E. MERRITT, COUNSEL FOR CROCKER NATIONAL BANK

Mr. MERRITT. Thank you, Mr. Chairman. I would like Mr. Brubaker to go first. He is going to talk to us briefly about the bank procedures that are involved upon the receipt of administrative summons from the Internal Revenue Service.

Senator HASKELL. Fine. Proceed, sir.

Mr. BRUBAKER. Mr. Chairman, my name is Robert Brubaker. I am vice president of operations for Equibank in Pittsburgh, Pa. Originally, I was scheduled to be accompanied by Mr. John Rolph, tax counsel for the American Bankers Association, who is ill today and cannot attend. However, Mr. Merritt will cover some of the legal aspects of it.

We are here to testify for the American Bankers Association on behalf of its nearly 14,000 commercial bank members, and we wish to express our appreciation for this opportunity to testify on the procedures used by the Internal Revenue Service in conducting tax investigations through the use of administrative summonses to obtain bank customer records. The question of how and when the Internal Revenue Service may examine the financial records of bank customers involves the fundamental question of the individual rights of more than 125 million bank customers.

Our testimony today will outline the factual circumstances surrounding IRS summons of bank customer records, and discuss the legal implications of the current IRS summons practices, concluding with certain specified recommendations for legislative changes concerning the IRS administrative summons power.

My testimony will be directed toward the kinds of bank records which are subject to summons, the scope of the summonses for bank records, and how banks respond to IRS summonses.

Recently, there has been an extensive public debate on the concerns of many Americans over the quest of modern government for information about its citizens. The Congress has established by Public Law 93–579 the Privacy Protection Study Commission in order to examine the right of privacy including specifically the right to privacy of one's financial records. In addition, there have been many court cases and pieces of proposed Federal legislation concerning this issue.

One critically important facet of the right of financial privacy issue concerns the rights of bank customers in connection with IRS examination of bank records in the course of a taxpayer investigation. In these situations both the rights of bank customers who are under investigation and the rights of those who are not under investigation need to be protected against abuses of the IRS summons power.

The ABA is not trying to aid the criminal nor impede the efficient system of tax collection, but only trying to protect the rights of the innocent and to establish some clear-cut standards for the use of IRS summons.

One of the keystones of all bank activity is the relationship between the bank and its customers. This relationship is established when a bank accepts a customer's money for checking, time or savings deposits, or when a bank makes a loan to a customer, or when a bank provides any of the many other full banking services which are offered to the public.

In the course of making its full banking services available to the public, the bank participates in the private financial affairs of its customers and may receive personal information such as the amount and source of earnings and other income, the amount and type of property owned by a customer, the amounts and types of a customer's indebtedness, the amount of payments made to creditors, and other information

It is hardly necessary to point to the sensitivity of this information. Historically, banks have treated customers' financial affairs as confidential in nature, not to be revealed except to the minimum extent required by law.

When an IRS agent wishes to examine bank customer records in connection with a tax investigation, he must do so through the use of an administrative summons form 2039. This summons can be completed by an Internal Revenue agent without prior judicial approval and should be used only to obtain specific books and records relevant to the tax investigation. The law requires that the bank be given at least 10 days to produce the information requested in the summons.

When an IRS summons for customer records is personally served on a bank officer, he must then determine that the summons is properly executed and contains all of the necessary information. The bank will have to identify the customer, determining what kinds of records are requested under the summons and where they might be located, assess the burden of complying with the summons and determine whether the bank will respond by complying with the summons or by considering whether a challenge to the summons is appropriate.

Banks are required under Public Law 91–508, the Bank Secrecy Act, to maintain extensive records on customer transactions. For example,

the law requires banks to keep for a period of 5 years, all checks, clean drafts, or money orders drawn on the bank or issued and payable by it. Many banks maintain such records on microfilm.

In addition to the complexity of recordkeeping problems faced by banks, a further difficulty in responding to IRS summonses exists because records are filed by type of service rather than by customer names. For example, separate sets of files and microfilm are maintained for canceled checks, another separate file on savings account records, certificates of deposit, loans, and other types of services. And I have in my written testimony a list of the other kinds of bank records which may be covered by an IRS administrative bank summons, most of which are maintained in separate file systems.

To keep it short I will not read down through that list. It follows, though, for example, in the case of our bank, we must secure information from a number of banking sources. We are not that large a bank, but we still maintain 86 banking locations, and a host of different departments that cover the banking services; all of those areas must be inquired into in order to determine whether or not we either presently have an account relationship with that customer or whether we have had one in the past.

Senator HASKELL. Because the summons will say "give me any dealings you have had with Bill Smith?" Or something like that?

Mr. BRUBAKER. Yes; that is correct, and it generally covers a period of time, a timespan that I talk about a little bit later in my written comments here.

Most of the banks that, for example, are automated, keep on that automated file only accounting information and not historical information because if you or I may have had a loan with a specific bank or checking account with a specific bank, but it has been closed out for a year or two, that would not be maintained on that automated file. Those records would be in the back office somewhere in a manual system, either a file of closed signature cards and things like that, which still must be accessed, even though computerized files are available to check and determine whether a customer might have an open account at the present time.

Senator HASKELL. Thank you.

Mr. BRUBAKER. Inquiries must be made of all of these different areas and if an account relationship had existed during that span of time, as I just mentioned, then those records would have to be checked manually.

In addition to that, many banks do not maintain automated record systems. Even many large banks do not maintain their records on a centralized basis but instead maintain them on a branch-by-branch basis. In such cases, it may be necessary to contact each individual banking location or department in order to obtain the records requested in an IRS summons.

Many summonses received by commercial banks request "records of all transactions with a bank" or another comment might be—

all books, papers, records, and other documents relating to material required to be included in the income tax returns of the named individual, including but not limited to the following items.

So most of the records are rather open-ended and it puts the burden on the bank for trying to determine exactly what records might be needed to complete the response to that summons.

The very broad scope of the all records summons, especially when viewed in the light of the complexity of bank customer records, imposes quite a burden on banks.

The Internal Revenue Service in Rev. Proc. 55-6 stated that only one form, form 2039, would be used as an administrative summons under section 7602. Nonetheless, I have heard of Internal Revenue Service agents who use a wide variety of forms. And some of the forms the ABA has compiled, and they are contained in the ABA's "Bankers Guide to IRS Procedures for Examinations of Customer Records, and Levies on Customer Accounts."

There are many other factors which will affect the ways in which banks elect to respond to an IRS administrative summons for bank customer records.

The number and capabilities of personnel in the bank who can be devoted to the process of responding to IRS records requested. Presumably, this will be affected by the relative size of the bank.

Whether the bank is a single unit bank or whether it has multiple branches; the number and location of the bank's branches is very relevant in this case.

The method or methods under which the bank maintains its customer records, for example, a centralized records system, a noncentralized records system, fully or partially automated systems, or a completely manual records system.

The number of IRS administrative summonses received annually by that given bank.

Whether the bank has ready access to legal counsel familiar with these issues and whether the bank can afford to have legal counsel review all or even some of the records requested.

Depending upon any combination of these factors, banks may adopt different procedures on how the records are actually produced by the bank for the Internal Revenue Service. I have listed some examples here.

A small bank with few employees maintaining a manual records system with no knowledge of the legal aspects of the summons problem may allow IRS agents to enter the bank's premises and permit free access of all of the files located in the bank. Under this circumstance, an IRS agent may well encounter information which would suggest a tax liability on the part of another taxpayer not presently under investigation. This situation could compromise the duty of the bank to maintain the confidentiality of the records for the customers who are not under investigation.

Under facts similar to what we have just talked about, a bank may limit the Internal Revenue Service agent access to the records in the specific customer's files, but without screening material so as to produce only those records specifically requested in the summons.

A large bank with many employees, and perhaps an automated recordkeeping system, may use its own employees to search through its records and produce copies of the material for the Internal Revenue Service agent. This situation may be forced upon a bank with limited resources because of unique aspects of its recordkeeping system which require that experienced employees of the bank conduct the search. This procedure is more burdensome to the bank, but does protect the confidentiality of taxpayers not under investigation.

A bank which receives many summonses and has the opportunity to assign one or more bank officers to the job of reviewing IRS summonses may be able to analyze IRS record requests before it conducts a search through its own records. This provides the bank further opportunity to raise questions with an IRS agent as to whether all of the information requested is actually needed in the investigation.

In many cases where banks have raised questions concerning the broad scope of an IRS summons, the agent has substantially reduced the request, thereby reducing the burden on the bank. Then the procedure of the bank conducting the search through its own records is less burdensome.

Finally, a bank which has in-house counsel or retained outside legal counsel may be able to go one step beyond review by a bank officer and refer to legal counsel summonses which appear to raise substantive legal questions and which might justify a challenge of the summons to be reviewed by a Federal district court judge.

From the five different scenarios described above, it can be seen that the manner in which banks respond to IRS summons vary to a great degree. They indirectly are affected by the number of personnel in the bank and the nature of the recordkeeping process. In situations where the banks are able to analyze a summons and discuss the scope of the summons with an Internal Revenue Service agent, the burden on the bank and the degree of invasion of the confidentiality of other bank customers are reduced.

If there are any questions, I would be happy to answer them at this point in time.

Senator HASKELL. I think it might be better to hear from Mr. Merritt and then maybe there will be some joint questions.

Mr. MERRITT. Mr. Chairman, my name is James E. Merritt. I am an attorney with the firm of Morrison & Foerster and appear today as counsel for Crocker National Bank.

I would like to say at the outset that Mr. Brubaker, and myself and Mr. Rolph have submitted additional written comments and I would like to have them incorporated in the record.

Senator HASKELL. They will be incorporated in the record. You may go on and talk, however, if you wish.

Mr. MERRITT. In addition, there is an American Bankers Association publication entitled "A Banker's Guide to IRS Procedures for Examination of Customer Records and Levies on Customary Accounts" which I would like to make part of the record.[1] I do not have sufficient copies to turn it over to the staff at this time, but would ask the ABA to submit copies to the staff.

Senator HASKELL. That will be received.

Mr. MERRITT. I do not intend to read in any detail my prepared statement. I would like to say at the outset that this is a matter of extreme importance to Crocker National Bank and other members of the American Bankers Association. To illustrate that I would point out that yesterday I fit in somewhere in a regular busy day for an attorney, time to prepare a statement and catch the redeye special back to Washington, in order to be here.

I disgree with some of the implications of prior speakers and indeed some of the areas of questioning as to what is the major issue before

[1] See p. 203.

you. I think the key issue here is not any substantive basis for restricting the use of an IRS summons, but is really a procedural basis. It is a due process problem which we are facing, and it is illustrated by a flood of cases that have been in the courts. These cases involve a conflict between the right of privacy of bank customers or taxpayers generally in records relating to their financial activities and the established and current procedures of the Internal Revenue Service in the use of the section 7602 summons.

Now, let me say in the beginning the problem with the current procedures is this: a taxpayer is not granted any notice of a summons unless the summons is directed to that taxpayer. Thus, when his records are sought from a bank or any other custodian, the taxpayer has no idea a summons has been served.

The second problem is: can the taxpayer intervene? Now, 10 or 11 years ago we thought the answer was "Yes." There is the famous case of *Reisman* v. *Caplin* which the Supreme Court decided in 1964, and in doing so stated that, of course, if the taxpayer is not a party to the summons procedure, he may intervene. At that time everybody took great hope and felt that this gives a real remedy to the taxpayer under investigation to contest the summons on whatever grounds he might have to contest.

In the subsequent decade, that promise has been eliminated entirely by substantive decisions, the most recent of which is the *Donaldson* decision in 1971. Under the ruling in *Donaldson*, as interpreted and applied by the lower Federal courts, unless the taxpayer has either a property right, a proprietary interest, or a privileged interest in the records summoned, he has no standing to intervene, either before a hearing officer, a revenue agent at the administrative level, or in the courts.

Now, there are some possibilities of interpreting *Donaldson* to say that you may be able to establish a case sufficient to grant intervention. The problem with regard to bank records specifically is that it is well-established law that the bank has custody of the records, No. 1; and No. 2, they are the property of the bank under the traditional property law concepts. Thus, the taxpayer does not have a property interest in those records.

At this time we have at least two cases: one by the California Supreme Court and one by the Court of Appeals for the Fifth Circuit, which have held that the taxpayer may have a right in the nature of privilege in his financial records maintained by banks. Those cases are the *Burrows* case in California and the *United States* v. *Miller* case from the fifth circuit. The *Miller* case is currently pending before the U.S. Supreme Court.

You might ask, since you do have these judicial decisions and if the Supreme Court affirms in *Miller* and says that a bank customer has standing to suppress records obtained from the bank, why should Congress act? I would like to make it very clear we think it is crucial that Congress act. We do not believe that this is an area in which the courts can reasonably be expected to develop procedures that will be fair and easily administered by the IRS, the taxpayer under investigation, and the custodian of the records.

Even if *Miller* is affirmed, you will be left with many questions. You will have, No. 1, the continued efforts of law enforcement agencies generally to narrow the scope of the judicial opinion, which is a typical

litigation approach by everyone. We have the further question of what is sufficient legal process. And that is all that *Miller* or *Burrows* requires. These cases say that a bank customer has a right of privacy of his records, and those records may be obtained by the Internal Revenue Service or any other law enforcement agency, only if they use a valid summons or subpena.

The remaining question is: What is a valid summons or subpena? The last problem that will be left by these cases is that the remedy is a motion to suppress the use of the evidence in a subsequent criminal trial. They do not provide for standing to sue, to challenge the summons before the documents are produced, nor do they provide for notice that a summons had indeed been issued.

I think those latter two points are the key points which the House Ways and Means Committee in the October 22, 1975, committee print of the tax reform bill dealt with in this area by providing notice to a taxpayer; by providing a right to intervene in both the administrative proceedings and in judicial proceedings, to enforce that summons. And I would like to make it clear that it is our position that the taxpayer should not have to initiate those proceedings in court.

Instead, the current procedures whereby the IRS must initiate a summons enforcement procedure should be followed. If those two remedies are made available, then I think you will have solved most of the complaints and most of the problems presented to the banks and other custodians of financial records.

Senator HASKELL. Let us go back over that, if you do not mind, Mr. Merritt.

Mr. MERRITT. Not at all.

Senator HASKELL. Your feeling is to—say, my return is being audited. A summons is being made at the Crocker Bank, assuming I had an account there. Your first suggestion is that I should have a right to contest the summons. The bank should notify me, or the IRS should notify me concurrently with issuing the bank and therefore, I should have standing to contest the production of documents by your client. That is your first point.

Now, your second point eluded me.

Mr. MERRITT. I am sorry. There are two elements of the first point. One is to give you notice of the summons; and the second is to give you a right to intervene and make a contest, if you wish.

Senator HASKELL. OK. Then we are OK.

Mr. MERRITT. Notice from the Internal Revenue Service, and not from the custodian of the records.

Senator HASKELL. Right. I understand.

Mr. MERRITT. Let me go back on that a bit. I think the problem can be demonstrated by the types of objections that might be raised. There are a series of objections that have been listed by both Mr. Rolph and myself which can appear on the face of the summons, or the manner in which it is served. It is very common practice for a lot of district offices to serve an IRS summons by mail. The statute very clearly requires personal delivery; so do the regulations; so does a Revenue ruling but it is still the common practice to serve a lot of these by mail.

Now, throughout Crocker Bank, I know people are aware that service by mail of summons from the IRS is invalid and such summons are being returned. Some of them get up to me, and I have to return them.

That is something the custodian or the recipient of the summons, who ever it is, can handle themselves.

Other things, such as a lack of a signature, improper date, these types of things, can easily be dealt with by the custodian. And those are not major problems, those are real technical issues that can be cured easily, and a new summons issued.

The major problems, the ones that concern the people around the country are, as mentioned by Mr. Lynn, is this summons purely for a criminal prosecution purpose, and hence, invalid? Are these records subject to an attorney-client privilege? Can I exercise my fifth amendment privilege of these records? Is this summons issued for the purpose of harassing the taxpayer?

I have had letters from customers of the bank, in response to our notice to them, of IRS summons, claiming each of these grounds as a basis for objecting, and a request to the bank not to turn over the records sought in the summons. The bank has no way of determining whether any one of those grounds for objection is valid. Only the taxpayer and his or her attorney can say what stage in the criminal investigation proceedings this summons is being issued. Only the customer of the bank, or his attorney perhaps, has any indication as to whether this might be an attorney-client privilege matter. Certainly, only the customer can assert the fifth amendment privilege. Indeed, harassment is a ground for nonenforcement of an IRS summons that has been recognized by the U.S. Supreme Court in the *Powell* decision, which was also a 1964 decision. So if you have a customer or a taxpayer that says this is harassment, the bank really has no choice—any custodian has no choice but to try and resist enforcement of that summons so that the customer can come in and make his or her case to show why it is harassment.

Now, very infrequently will any of these substantive grounds prevail, but it seems eminently unfair that the taxpayer cannot argue these grounds. That is the position the IRS has taken, and it is frustrating a lot of courts. I have a rather current opinion from the district court in Maryland, in an unusual situation, which I would like to relate to you. It is the *Bowser* case. This opinion was filed by the district court in Maryland in July of this year.

The scenario which led to this decision was an injunction action brought by a taxpayer against two banks, to restrain them from complying with an IRS summons. It went to the fourth circuit, and the fourth circuit rendered the same decision as the U.S. Supreme Court had in *Reisman*. It said an injunction is not proper, because you have an adequate remedy at law, the classical equity basis for denying relief. All you have to do is intervene in the administrative proceedings or intervene in the judicial enforcement proceedings. So they said no injunction would be granted to the taxpayer. Lo and behold, the taxpayer's attempts to intervene administratively were resisted successfully by the IRS. The taxpayer initiated a second injunction proceeding, and this time the district court granted an injunction, on the grounds that the IRS would not allow him to intervene and, therefore, in fact, he did not have an adequate remedy at law.

The case which I am going to quote is the third step in the proceeding when, subsequent to the injunction, the Internal Revenue Service sought judicial enforcement proceedings for the summons which it had

served, and that is the appropriate legal process. I think a little bit of the court's frustration becomes apparent from this quotation: "When the IRS seeks to enforce a summons to a taxpayer to produce his records for examination by the IRS during a tax investigation, the Government does not use self-help. Rather the Government files a petition in a Federal district court and seeks a show cause order. The Government has obtained, in recent years"—and he is referring only to the instant court—"in every such case, the orders it has sought. The safeguards inherent in such a procedure are obvious. There is always the chance that the IRS or any Government agency or official is harassing, or proceeding discriminatorily or arbitrarily against the taxpayer. Providing the taxpayer with the opportunity to be heard with regard to any such possible governmental malfunctioning is entirely in line with the spirit of our fourth amendment restrictions on searches and seizures and our American concepts of due process and equal protection.

There would appear no more reason to take away that opportunity to be heard simply because the taxpayer's records are in the hands of someone such as a bank acting for him or in relationship with him, rather than in his own hands. The taxpayer's right to be heard is not bottomed on his Fifth Amendment privilege not to incriminate himself, a privilege he may well have lost, if he has relinquished personal custody. Instead, the taxpayer's right to be heard is simply his basic procedural, due process right.

That is not a very technically elaborate opinion of the court, but it does grasp the concept of due process; that is, the right of the taxpayer and the IRS, the two protagonists involved in the summons enforcement proceeding, to be able to make objections and responses thereto directly. It should not give the IRS the right to make its arguments in court and deny to the other a right to respond to those arguments, which is the current situation.

I will comment on one further aspect of this legislation on the "John Doe" summons. Although I have not had one of these myself—I would point out that I believe the instances in which they are most frequently used really have not required the use of a summons. They are getting cooperation from the parties to whom they make a request for these records. The typical party would be a granary, for example, in California, that buys grain from maybe 200, 300 farmers in substantial quantities during the course of a year. The Internal Revenue Service would go to that granary and ask for their records showing the amounts of payments to the farmers. They will take those records then, see how much income each of those farmers should be reporting from that granary, and examine the returns on the basis of that information.

I think that type of situation, I believe, was alluded to by Mr. Fink in one of the cases he referred to, not in California, but in another area. It is probably the most frequent use of John Doe type examination, whether or not it is in the form of a summons.

Our recommendation with regard to John Doe summons is that there should be a court review—a court review not just of the necessity of issuing a summons, but a court review of the very summons which is to be issued itself, so that a court can be satisfied that (1) the Government has a legitimate basis to get to this information; (2) that it looks like there has been a transaction that will not be reported; (3) for one reason or the other, the information is not readily available

from any other source; and (4) the summons itself is properly worded. The court should review all four of those aspects of the John Doe summons.

Once that is done, we would have no objection to use the use of a John Doe summons, as they have been used in the past.

Senator HASKELL. Well, on that point of the John Doe summons, I can see its misuse. On the other hand, I can see the need for it. The very case that the Supreme Court decided, if somebody comes in with a sackful of $100 bills, it kind of looks on the surface of it, suspect, or at least it seems to me, and I cannot see that it is inappropriate there to ask a bank to give whatever information they may have surrounding it. You do not object to John Doe summons per se, then, I gather, Mr. Merritt?

Mr. MERRITT. I do not object to it per se. I have a little problem with the particular case, the *Bisceglia* case, that was described. My experience, when I worked with the Internal Revenue Service, was that you did get information with regard to the identity of the person who would make such unusual currency transactions, and I believe that a part of the Bank Secrecy Act's requirements, is to report unusual currency transactions.

I think there is a danger in the way in which the Bisceglia summons apparently was enforced by allowing an agent to rummage through the bank's records. This is a problem that has been solved in the Western District of Pennsylvania, a case in which Mr. Brubaker had some association, by requiring the IRS to pay the expenses of having bank personnel make this search. Judge Teitelbaum, in that case, expressed good reasons that this will really put the Service to the test of whether it wants this information badly and whether it can obtain it more reasonably through some other source. But I do agree—I think there are situations where a John Doe summons is proper. I would not prohibit them across the board.

Senator HASKELL. In your experience, Mr. Merritt or Mr. Brubaker, do banks receive these John Doe summonses frequently, or infrequently, once in a lifetime, or what?

Mr. BRUBAKER. I have never seen, personally, a John Doe summons. Ours are more specifically to certain taxpayers, so I have no familiarity with the John Doe summons. The most information that I have heard on them, I have heard in here today. I would assume that they probably are growing, from the discussions I have heard with other bankers. However, I have no firsthand knowledge. We have never been served with a John Doe summons.

Senator HASKELL. Your suggestion, Mr. Merritt, is that in the John Doe summons, there be kind of a showing to the court of a necessity for it. That is basically it, is it not?

Mr. MERRITT. That is correct. I think that would restrict the potential misuse of it, and I think *Humble Oil*, and possibly the *Sun Bank of Orlando* case, which was decided just this year illustrate the misuse of the John Doe summons, where you really want to ask somebody that may have participated or been the custodian of records for a variety of transactions, please tell us of everybody else who might have participated in these transactions, just really as a matter of curiosity, without having any reason to believe there is income there that is not being reported.

Senator HASKELL. Thank you gentlemen very much indeed.

Thank you, Mr. Merritt, for getting on that Red Eye Special.

Now, I guess it would be time to go back to the hotel and take a nap.

Thank you.

The hearing will be recessed until 10 o'clock tomorrow morning.

[The prepared statements of Messrs. Brubaker, Merritt, and Rolph, with attachment, follow:]

[Whereupon at 12:57 p.m., the subcommittee recessed, to reconvene at 10 a.m. the following day.]

STATEMENT OF J. ROBERT BRUBAKER ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

Mr. Chairman, my name is J. Robert Brubaker, Vice President, Operations, for Euibank, N.A., Pittsburgh, Pennsylvania. I am accompanied by John F. Rolph, III, Tax Counsel, American Bankers Association. We are here to testify for the American Bankers Association on behalf of its nearly 14,000 commercial bank members. We wish to express our appreciation for this opportunity to testify on the procedures used by the Internal Revenue Service in conducting tax investigations through the use of administrative summonses to obtain bank customer records. The question of how and when the Internal Revenue Service may examine the financial records of bank customers involves the fundamental question of the individual rights of more than 125,000,000 bank customers.

Our testimony today will outline the factual circumstances surrounding IRS summons of bank customer records and discuss the legal implications of the current IRS summons practices, concluding with certain specified recommendations for legislative changes concerning the IRS administrative summons power. My testimony will be directed towards the kinds of bank records which are subject to summons, the scope of the summonses for bank records, and how banks respond to IRS summonses. Mr. Rolph will discuss the legal aspects of these issues including the questions of ownership of the records, procedural safeguards for the taxpayer under investigation such as notice, right to intervene, and right to challenge the summons; and the propriety of the use of John Doe summonses.

Recently, there has been an extensive public debate on the concerns of many Americans over the quest of modern Government for information about its citizens. The Congress has established by P.L. 93-579 the Privacy Protection Study Commission in order to examine the right of privacy including specifically the right to privacy of one's financial records. In addition, there have been many court cases and pieces of proposed Federal legislation, such as H.R. 2752, concerning this issue.

One critically important facet of the right of financial privacy issue concerns the rights of bank customers in connection with IRS examination of bank records in the course of a taxpayer investigation. In these situations both the rights of bank customers who are under investigation and the rights of those who are not under investigation need to be protected against abuses of the IRS summons power.

The ABA is not trying to aid the criminal nor impede the efficient system of tax collection but only trying to protect the rights of the innocent and to establish some clear-cut standards for the use of IRS summons.

One of the keystones of all bank activity is the relationship between the bank and its customers. This relationship is established when a bank accepts a customer's money for checking, time or savings deposits, or when a bank makes a loan to a customer, or when a bank provides any of the many other full banking services which are offered to the public. In the course of making its full banking services available to the public, the bank participates in the private financial affairs of its customers and may receive personal information such as the amount and source of earnings and other income, the amount and type of property owned by a customer, the amounts and types of a customer's indebtedness, the amount of payments made to creditors, etc. It is hardly necessary to point to the sensitivity of this information. Historically, banks have treated customers' financial affairs as confidential in nature, not to be revealed except to the minimum extent required by law.

FACTUAL CIRCUMSTANCES SURROUNDING IRS SUMMONSES

When an IRS agent wishes to examine bank customer records in connection with a tax investigation he must do so through the use of an administrative summons Form 2039. This summons can be completed by an Internal Revenue Agent without prior judicial approval and should be used only to obtain *specific* books and records *relevant* to the tax investigation. The law requires that the bank be given at least ten days to produce the information requested in the summons. When an IRS summons for customer records is personally served on a bank officer, he must determine that the summons is properly executed and contains all of the necessary information. The bank will have to identify the customer, determining what kinds of records are requested under the summons and where they might be located, assesses the burden of complying with the summons and determine whether the bank will respond by complying with the summons or by considering whether a challenge to the summons is appropriate.

BANK CUSTOMER RECORDS AND RECORD SYSTEMS

Banks are required under P.L. 91–508, the Bank Secrecy Act, to maintain extensive records on customer transactions. For example, the law requires banks to keep for a period of five years, all checks, clean drafts, or money orders drawn on the bank or issued and payable by it. Many banks maintain such records on microfilm. In addition to the complexity of recordkeeping problems faced by banks, a further difficulty in responding to IRS summonses exists because records are filed by type of service rather than by customer names. For example, separate sets of files and microfilm are maintained for cancelled checks, savings account records, certificates of deposit, loans, etc.

The following is a list of some of the kinds of bank records which may be covered by an IRS administrative summons, most of which are maintained in separate file systems:

(1) Checking accounts (signature cards, resolutions, statements, checks, and deposit tickets).
(2) Savings accounts (signature cards, deposit and withdrawal tickets, interest payments, ledger sheets or activity journals).
(3) Cashiers checks or personal money orders.
(4) Safe Deposit box signature cards, payment records and access records.
(5) Certificates of Deposit.
(6) Corporate Resolutions.
(7) Loan agreements.
(8) Loan payments and disbursements.
(9) Trust agreements.
(10) Loan ledgers.
(11) Credit and correspondence files including financial statements.
(12) Shareholder transactions.
(13) Bond purchases or sales.
(14) Credit Card transactions; purchases, payments, statements.
(15) Safekeeping or custodial transactions.
(16) Loan collateral files.
(17) Stock transfer activity.

In the case of our bank, we must secure information from the following banking areas in order to properly reply to a summons:

(1) Eighty-six Banking Locations.
(2) Mortgage Department.
(3) Installment Loan Department.
(4) Master Charge Department.
(5) Commercial Loan Department.
(6) Charge Account Checking Dept.
(7) Controllers Department (Bonds and Certificates).
(8) Trust Department.
(9) Safekeeping Department.
(10) Credit Department.
(11) International Department.
(12) Investment Department.

Inquiries must be made of these various areas because the centralized, automated files only contain current accounting information. If an account relationship had existed during the span of time requested in the IRS summons, but was inactive or closed out sometime during the time span, it most probably would not be carried in the automated system. Records must then be checked manually for closed accounts.

Many banks do not maintain automated records systems. Moreover, even many large banks do not maintain their records on a centralized basis but instead maintain them on a branch-by-branch basis. In such cases, it may be necessary to contact each individual banking location or department in order to obtain the records requested in an IRS summons.

SCOPE OF SUMMONS

Many summonses received by commercial banks request "records of all transactions with a bank" or "all books, papers, records, and other documents relating to material required to be included in the income tax returns of the named individual, including but not limited to the following items. . . .". The very broad scope of the "all records" summons—especially when viewed in the light of the complexity of bank customer records—imposes an onerous burden on banks.

DIFFERENT KINDS OF SUMMONS

The Internal Revenue Service in Rev. Proc. 55-6 stated that only one form, Form 2039, would be used as an administrative summons under Section 7602. Nonetheless, I have heard of Internal Revenue Service agents who use a wide variety of forms. See for example, forms contained in the ABA Banker's Guide. The fact that these unauthorized forms are used complicates the problem for banks on how to respond to IRS requests.

HOW BANKS RESPOND TO SUMMONSES

There are many factors which will affect the ways in which banks elect to respond to an IRS administrative summons for bank customer records.

(1) The number and capabilities of personnel in the bank who can be devoted to the process of responding to IRS records requested. (Presumably, this will be affected by the relative size of the bank).

(2) Whether the bank is a single unit bank or whether it has branches; the number and location of the bank's branches is also relevant.

(3) The method or methods under which the bank maintains its customer records, i.e., a centralized records system, a noncentralized records system, fully or partially automated systems, or a manual records system.

(4) The number of IRS administrative summonses received annually.

(5) Whether the bank has ready access to legal counsel familiar with these issues and whether the bank can afford to have legal counsel review all or even some of the records requested.

Depending upon any combination of these factors, banks may adopt different procedures on how the records are actually produced by the bank for the Internal Revenue Service. For example—

(1) A small bank with few employees maintaining a manual records system with no knowledge of the legal aspects of the summons problem may allow IRS agents to enter the bank's premises and permit free access to all of the files located in the bank. Under this circumstance, an IRS agent may well encounter information which would suggest a tax liability on the part of another taxpayer not presently under investigation. This situation could compromise the duty of the bank to maintain the confidentiality of the records of its customers who are *not* under investigation.

(2) Under facts similar to number 1 above, a bank may limit the Internal Revenue Service agent access to the records in the specific customer's files, but without screening material so as to produce only those records specifically requested in the summons.

(3) A large bank with many employees, and perhaps an automated recordkeeping system, may use its own employees to search through its records and produce copies of the material for the Internal Revenue Service agent. This situation may be forced upon a bank with limited resources because of unique aspects of its recordkeeping system which require that experienced employees conduct the search. This procedure is more burdensome to the bank, but does protect the confidentiality of taxpayers not under investigation.

(4) A bank which receives many summonses and has the opportunity to assign one or more bank officers to the job of reviewing IRS summonses may be able to analyze IRS record requests before it conducts a search through its own records. This provides the bank further opportunity to raise questions with an IRS agent as to whether all of the information requested is actually needed in the investigation. In many cases where banks have raised questions concerning the broad scope of an IRS summons, the agent has substantially reduced the request, thereby reducing the burden on the bank. Then, the procedure of the bank conducting the search through its own records is a less onerous one.

(5) Finally, a bank which has in-house counsel or retained outside legal counsel may be able to go one step beyond review by a bank officer and refer to legal counsel summonses which appear to raise substantive legal questions and which might justify a challenge of the summons to be reviewed by a Federal District Court Judge.

From the five scenarios described above, it can be seen that the manner in which banks respond to IRS summonses vary to a great degree. They indirectly are affected by the number of personnel in the bank and the nature of the record-keeping system. In situations where the banks are able to analyze a summons and discuss the scope of the summons with an Internal Revenue Service agent, the burden on the bank and the degree of invasion of the confidentiality of other bank customers is substantially reduced.

The legal implications of these procedures will be discussed by Mr. Rolph.

STATEMENT OF JAMES E. MERRITT ON BEHALF OF CROCKER NATIONAL BANK

Mr. Chairman, my name is James E. Merritt. I am a member of the law firm of Morrison & Foerster and appear today as counsel for Crocker National Bank. My statement regarding IRS administrative summons will supplement Mr. Brubaker's statement and the written statement of John E. Rolph, III.

Crocker National Bank is concerned with maintaining the confidentiality which exists with its customers regarding records of their financial transactions. Of course, Crocker does not wish ti refuse to comply with any proper request to produce documents or records to the Internal Revenue Service or any other governmental agency.

Fair procedures governing access to bank records is a particularly appropriate subject for Congress to consider at this time. At no prior time during my experience has the state of the law been as unclear as it is today. The records of bank customers are protected by a right of privacy based upon recent legislation such as the Fair Credit Reporting Act, 15 U.S.C. § 1681 *et seq.*, and court decisions as well as the established custom and practice of confidentiality. To protect those expectations of privacy Crocker National Bank is taking heretofore unprecedented steps to require law enforcement agencies including the Internal Revenue Service to obtain court orders before records are released. These efforts are placing unaccustomed burdens upon the Internal Revenue Service.

In these circumstances legislation which will clearly set forth fair procedures to protect taxpayers' rights of privacy in a manner that can be readily administered is needed.

In past years and at the present, with the probable exception of California, the normal situation has been for an Internal Revenue Agent to appear at a bank branch in person and request certain records relating to a specific customer. (Those situations in which the customer is unidentified, as in *United States* v. *Bisceglia*, —— U.S. —— (1975), present a much different problem.) Normally, the investigating agent will speak with the manager of the branch. If the manager is hesitant in producing the records the agent will prepare a so-called "pocket summons" and serve it upon the manager.

At this point there is pressure upon the bank personnel: (1) to comply with an apparently authorized law enforcement official, and (2) to permit review of the records immediately with the promise, express or implied, that if the bank officer turns over the records it will have time and money. This inducement for immediate production is premised upon the representation that the investigating agent by an immediate review can limit the number of records and, if copies are produced, can make it unnecessary for the officer to personally deliver such records to an agency or court at a future date.

These pressures are not inconsiderable. Moreover, it should be borne in mind that the bank official is not a lawyer nor is he or she generally familiar with the statutory and other requirements which apply to determine the validity of such a demand. As a result, in the past, these informal requests and subtle pres-

sures have frequently achieved the objective of the investigating agent and the records have been made available.

This is no longer the normal practice in California. In 1974 the California Supreme Court decided *Burrows* v. *Superior Court*, 13 Cal. 3d 328 (1974), modified 13 Cal. 3d 732 (1975). *Burrows* is a landmark case. The circumstances involved an informal demand by the police to obtain copies of an attorney's financial statements from various banks. The attorney was under investigation for grand theft arising from the misappropriation of a client's funds. At least one bank complied with the informal request.

The attorney moved to suppress the use of such bank information and the California Supreme Court held that it should be suppressed. The Court held that under the California Constitution's provisions equivalent to the Fourth Amendment prohibition against illegal searches and seizures that bank customers have a reasonable expectation of privacy in the records relating to their financial affairs maintained by the bank even though the records are owned by the bank and are in its custody. In *Burrows*, *supra*, the California Supreme Court granted a bank customers' motion to suppress documents obtained informally by police from a bank. It stated that:

> We have held, consonant with *Katz* v. *United States*, . . . that, in determining whether an illegal search has occurred under the provisions of our Constitution, the appropriate test is whether a person has exhibited a reasonable expectation of privacy and, if so, whether that expectation has been violated by unreasonable governmental intrusion.
>
> A bank customer's reasonable expectation is that, absent compulsion by legal process, the matters he reveals to the bank will be utilized by the bank only for internal banking purposes. Thus, we hold petitioner had a reasonable expectation that the bank would maintain the confidentiality of those papers which originated with him in check form and of the bank statements into which a record of those same checks had been transformed pursuant to internal bank practice. 13 Cal. 3d at 242–243.

The result of *Burrows* is that without sufficient "legal process," however that is defined, it is a violation of a bank customer's California constitutional rights if financial information is obtained from a bank by law enforcement officials. On rehearing the Court engrafted an exception relating to crimes committed against the bank.

A similar result was reached by the United States Fifth Circuit Court of Appeals in *United States* v. *Miller*, 500 F.2d 751 (1974), which the United States Supreme Court has agreed to hear upon the Solicitor General's petition for certiorari. 33 U.S. Law Week 3641 (Supreme Ct. No. 75–1179). The Fifth Circuit based its decision upon *Boyd* v. *United States*, 116 U.S. 616 (1886), *Roe* v. *Wade*, 410 U.S. 113 (1973) and the Fourth Amendment, and stated as follows:

> The Supreme Court determined almost 90 years ago that "a compulsory production of a man's private papers to establish a criminal charge against him . . . is within the scope of the Fourth Amendment. . . ." Boyd v. United States. . . . The venerable *Boyd* doctrine still retains its vitality; the government may not cavalierly circumvent Boyd's precious protection by first requiring a third party bank to copy all of its depositors' personal checks and then, with an improper invocation of legal process, calling upon the bank to allow inspection and reproduction of those copies. 500 F.2d at 757 (footnote omitted)

In light of this judicial activity the obvious question is *why should Congress act?* I submit it is clear Congress should act for several reasons. First, as with all judicial opinions the law enforcement agencies continue to contest the scope and applicability of the Court's opinion. Second, it is not at all clear that the individual bank customer will prevail in the *Miller* case. Third, federal law enforcement officials have informally stated their position to be that *Burrows* has no application to federal investigations after July 1, 1975. Their theory is that *Burrows* created a state privilege and that under the new Federal Rules of Evidence state privileges do not apply to federal questions including specifically Internal Revenue Service investigations. Fourth, even under *Burrows* and possibly *Miller*, if it is sustained, the individual's remedy is a motion to suppress after the information has been obtained. Neither case clearly provides standing to a taxpayer to receive notice of the demand for his records or the opportunity to contest the validity of that demand in advance of production of the records.

Lastly, what constitutes sufficient "legal process" is unclear. Under *Burrows* and *Miller* it would be left to be resolved on a case-by-case basis. Legislation such as the amendment to the Internal Revenue Code before you would specify clearly

the procedures which must be used and thereby eliminate substantial litigation regarding the legal sufficiency of Internal Revenue summons.

Let me discuss several of the recent cases and situations I have encountered which I believe demonstrate the desirability and need to provide notice to taxpayers and a right to intervene.

I would like to call your attention to the published opinion in *United States* v. *Burbank*, ——— F. Supp. ———, 74-2 USTC ¶ 9779 (S.D.N.Y. 1974) (on appeal), which illustrates the need for these procedures. In *Burbank*, the IRS served an administrative summons under section 7602 of the Internal Revenue Code of 1954 upon two financial institutions requesting records relating to a Canadian company for purposes of obtaining information to provide the Canadian tax authorities in order to determine the company's Canadian tax liability. The basis for this cooperation between the IRS and Canada was cited to be Article 19 of the Income Tax Treaty Between Canada and the United States.

The point of referring you to the *Burbank* case is that the Court held the summons invalid because section 7602 only grants the IRS authority to obtain information in order to determine a United States tax liability. Most importantly, however, the Court dismissed the taxpayer's suit on the grounds the taxpayer lacked standing. Therefore, if the financial institutions had not joined in resisting the summons an illegal summons would have been enforced over the taxpayer's objections. Indeed, the opinion implies that the taxpayer's attorney had to convince the financial institutions to resist the summons as they were otherwise inclined to comply.

As an attorney for a bank this is my pet peeve, so to speak. The taxpayer has the greatest interest in insuring that the demands for information are proper. Under current law, even in California after *Burrows*, law enforcement officials refuse to provide notice to the taxpayer and take the position, sustained by the courts, that the taxpayer lacks standing to object and participate in the summons enforcement process. Not only is this a denial of fairness, if not due process to the taxpayer, but it imposes an intolerable burden on the financial institutions who are unfamiliar with the particular matter and cannot judge whether the information sought is relevant, a harassment of the customer, an invasion of attorney-client privileged matter, or otherwise might be properly objectionable.

In this basic legal framework as it exists today (and I hope I have made it clear that this area of the law is in a statae of flux and is likely to remain unstable without appropriate legislation) I would like to recite several examples of the types of demands which are daily being made upon banks, other financial institutions and third parties.

Yesterday I appeared in the United States District Court in San Francisco to move to quash a grand jury subpoena for records of a bank customer's financial transactions. The customer, an attorney, had notified us that he believed the records were protected by the attorney-client privilege. Crocker participated in order to insure that the customer had standing to make known the grounds for his objections. In that situation only the taxpayer or customer can prove that the materials requested are privileged.

Similar situations have arisen with regard to alleged harassment of a taxpayer or the use of a section 7602 summons after the investigation has become purely for the purpose of criminal prosecution. In all of these situations the bank or other custodian of the records cannot determine from the summons and the records requested whether the objections are proper.

These situations should be contrasted with those in which the objection is apparent upon the face of the summons which are common. Illustrations are:

(1) Section 7602 summons served by mail instead of by personal delivery;

(2) Records requested are not specifically identified; and

(3) The request is overly broad, for example, not limited to records located at the particular office of the bank which is served.

Earlier this year in connection with an IRS criminal investigation we advised the IRS Special Agent that we would require that notice be given to the taxpayer and that the taxpayer be allowed to appear in connection with any summons enforcement proceedings. Shortly thereafter a grand jury subpoena duces tecum was served upon the branch manager for the records the Special Agent had sought.

In addition to certain specified accounts for which specific documents were requested the subpoena requested all cashier's checks purchased by or made payable to 14 individuals or companies throughout a 21-month period during 1972 and 1973.

I was unable to contact the taxpayer or the taxpayer's attorney and appeared in the United States District Court to move to quash the subpoena. I contended that the subpoena could be interpreted to require all branches of the bank and its subsidiaries to search their records. Crocker National Bank has over 360 branch offices in California and various lending offices outside California and the United States. Thus compliance would involve searches at more than 360 locations and involve costs estimated to be in excess of $28,000. The Judge limited the scope of the subpoena to the records located at the branch served.

I further contended that *Burrows* established a privileged interest of the taxpayer in the records and that the taxpayer was entitled to notice and the opportunity to appear. On these grounds the Judge overruled the motion to quash and ordered compliance. He did order payment of the costs of providing copies.

Other situations which I have not included as cases involve frequent demands by IRS Special Agents to review the bank's mecrofielm records of checks. Although the Agent may have a specific taxpayer in mind his review of the microfilm would provide access to information regarding thousands of other customers. These other customers' privacy would be invaded and I am certain if a particularly prominent or controversial name appeared it might catch the attention of the Agent.

Lastly during the Vietnam War there were many so-called telephone tax protests. It was not uncommon to receive requests to reveal the account for a list of 50 or more individuals from the IRS without specifying from which branch of the bank such information was sought and without the use of an administrative summons. The IRS was generally most cooperative in withdrawing these requests, but the fact they were made implies some compliance may have been obtained.

Other cases demonstrate that the Internal Revenue Service seeks bank records to determine if a crime has been committed and frequently solely to determine civil liabilities for taxes. These types of activities have been sanctioned by the United States Supreme Court since *United States* v. *Powell*, 379 U.S. 48 (1964) which held that to enforce an IRS summons under section 7602 the IRS need not make a showing of "probable cause."

I do not believe it is necessary or desirable to require a showing of "probable cause." However, it is essential that procedures be adopted which will insure that requests for bank records are made only in connection with proper governmental functions in administering the law. Procedures whereby the taxpayer who may be adversely affected may challenge the request and which place the financial burden upon the party seeking production of the records will provide such insurance.

The proposed legislation before you, particularly Section 7609, pages 41 and 42 of the October 22, 1975 Committee Print, should be carefully reviewed to insure that the taxpayer whose tax liability is under examination is entitled to notice and is granted standing to intervene. The potential problem may be demonstrated by the following example:

> An IRS summons is served on Bank A requesting the records of Mr. Y. The purpose of the summons is to determine what amounts Mr. Y paid to Mr. X and to establish that such payments are income to Mr. X.

In this example unless the summons requests only records relating to transactions between Mr. Y and Mr. X or states that is is related to Mr. X's tax liability, Section 7609 would appear not to require that notice be provided to Mr. X, the taxpayer whose tax liability is under examination.

That result appears to me to be contrary to the intent of this legislation. I believe the intent of this legislation is to enact the *dictum* of the United States Supreme Court in *Reisman* v. *Caplin*, 375 U.S. 440 (1964) that:

> . . . in the event the taxpayer is not a party to the summons before the hearing officer, he, too, may intervene.

As we know that statement has been eroded by subsequent decisions.

Similar legislation was considered by the Senate Committee on Banking in August 1972.

At that time the Treasury Department opposed such legislation on the grounds it would impede civil and criminal investigations and because there was no showing that law enforcement agencies were abusing taxpayer's rights of privacy.

Eugene Rossides, then Assistant Secretary of the Treasury, alleged that to provide notice to the taxpayer would endanger the safety of informers or under-

cover agents; that records might be destroyed; funds concealed or the suspect may flee.

Such hazards are unreal in the vast majority of cases. In the only criminal tax investigations I have been involved in on behalf of the bank or the taxpayer, the taxpayer under investigation was aware of the investigation well before the IRS made any attempts to obtain bank records. Thus, notice that bank records were sought was not and never has been in my experience the "tip off" so to speak that the IRS was conducting an investigation.

Thus, I would put the shoe on the other foot and suggest that law enforcement agencies, including the IRS, have not made a showing that providing notice to the taxpayer and granting the taxpayer standing will impede legitimate investigations.

An important reservation I have concerns the statute of limitations. For tax crimes the IRS must obtain an indictment within 6 years after the return is, or should have been, filed. In the past it has been suspected that taxpayers under criminal investigation resisted summons as a delaying tactic to prevent the IRS from obtaining sufficient proof to obtain an indictment within the 6-year period.

That result is avoided by proposed Section 7609(e) which provides for a suspension of the statute of limitations during the pendency of any contested summons enforcement proceedings in which the taxpayer participates.

Lastly, in those *rare* instances in which law enforcement agencies can establish a substantial likelihood that notice of a summons will endanger the lives of informers or agents or otherwise seriously jeopardize the prosecution of a crime, an exception could be provided to the notice and standing requirements. However, a strong showing of that likelihood should be required before a court and a court order prohibiting disclosure should be required.

In my opinion, provisions of this nature would provide adequate safeguards to protect legitimate law enforcement needs in sensitive areas without depriving the vast majority of bank depositors *not* involved in criminal activities of their right to privacy.

In conclusion, on behalf of Crocker National Bank, I recommend enactment of legislation of the nature you are presently considering. Privacy is of great concern to all of us. The courts are being flooded with cases involving taxpayers seeking to assert their rights. Without readily administered procedures whereby the protagonists—the taxpayer and the Internal Revenue Service—can fairly present their views litigation in this area will frustrate legitimate law enforcement investigations and deprive many citizens of privacy in their financial transactions.

This legislation is important for the Internal Revenue Service, for taxpayers and for parties such as Crocker National Bank who are the custodians of vast amounts of records.

Statement of John F. Rolph III, on Behalf of the American Bankers Association

Mr. Chairman, my name is John F. Rolph, III. I am Tax Counsel for the American Bankers Association. My statement regarding various legal problems connected with IRS administrative summonses will supplement Mr. Brubaker's statement.

First, it is elementary that no bank wishes to refuse to cooperate with the Internal Revenue Service or any other State or Federal agency in the conduct of its proper law enforcement activities. However, with respect to the individual rights of their customers, banks are under a burden to defend their customers' rights against questionable legal practices. The legal rules which govern the rights of taxpayers in connection with IRS administrative summons procedures are ambiguous and in a state of flux. Inconsistent judicial rules severely limit the rights of taxpayers with respect to IRS tax investigations.

I will now discuss several of the important legal principles which control or relate to taxpayer rights in connection with their banking records which are sought by the IRS for investigative purposes.

I. A TAXPAYER HAS NO PROPRIETARY INTEREST IN HIS BANK RECORDS

Under long-standing principles of personal property law and business custom, the records of the financial transactions of bank customers which are maintained by a bank *are the property of the bank.* Thus, under established judicial concepts, bank customers do not have a proprietary interest in their bank records.

When the Internal Revenue Service issues an administrative summons under § 7602 of the Internal Revenue Code for bank customer records in a tax investigation of the customer, it is the property of the bank, rather than the property of the taxpayer, which the IRS seeks to examine. This has led Federal courts to rule that because a taxpayer has no proprietary interest in his bank records he does not have the right to intervene in a court proceeding to enforce an IRS summons for such records. See *Donaldson* v. *U.S.*, 400 U.S. 517 (1971).

II. THE INVESTIGATION OF AN INDIVIDUAL'S TAXES GIVE HIM NO RIGHT TO CHALLENGE IRS SUMMONS FOR HIS BANK RECORDS

In 1971, the U.S. Supreme Court in *Donaldson v. U.S.*, *supra*, laid down a substantial restriction on the rights of bank customers and other taxpayers whose financial records are held by third parties. In this case, the Court ruled that the fact that a taxpayer's tax liability is the subject of an IRS investigation does not give him the right to intervene in an action to enforce an IRS summons for his financial records in the hands of a third party. It is interesting to note that the Supreme Court's decision in *Donaldson* had the effect of narrowing an earlier decision of the Supreme Court which was handed down in 1964 in *Reisman v. Caplin*, 375 U.S. 440 (1964). In the *Reisman* case, the Supreme Court held that, ". . . in the event the taxpayer is not a party to the summons before the hearing officer, he, too, may intervene."

In *Reisman*, the Court also held that a witness, for example a third party who has possession of the taxpayer's records, may challenge a summons on any appropriate ground.

Prior to the Supreme Court's decision in *Donaldson* in 1971, three United States Circuit Courts of Appeal had held that under the *Reisman* doctrine a taxpayer may intervene as of right simply because it is his tax liability that is the subject of the summons. However, three other Circuit Courts reached the opposite conclusion. Thus, the 1971 decision of the Supreme Court in *Donaldson* resolved this highly controversial issue *against* the taxpayer.

While denying intervention as of right, the *Donaldson* case did leave permissive intervention within the discretion of the trial court to determine whether or not a taxpayer will be given leave to intervene. However, many lower courts have misread *Donaldson* as forbidding altogether intervention by the taxpayer unless he owns the records summoned. As it stands, it would appear that a taxpayer's grounds for obtaining leave to intervene are limited only to a few situations. For example, intervention may be permitted where there is a claim that an attorney-client privilege would be breached if the attorney's records of the taxpayer's financial transactions are turned over to the IRS. Another situation is where criminal prosecution is the sole purpose of the IRS request for the taxpayer's financial records. In these situations, the taxpayer *may* be given leave to intervene by the district court, but he is not permitted to intervene as a matter of right.

III. CONFIDENTIALITY OF BANK CUSTOMER RECORDS

One important legal principle which governs the general status of bank customer records is that banks must treat such records as being confidential in nature. This means that a bank may not turn over the financial records of its customers except under proper legal process required by Federal or State law.

Courts have enunciated the general rule that banks have a legal duty to maintain the confidentiality of customer records. In a leading case, the Idaho Supreme Court stated, "It is inconceivable that a bank would at any time consider itself at liberty to disclose the intimate details of its depositors' accounts. Inviolate secrecy is one of the inherent and fundamental precepts of the relationship of the bank and its customers or depositors." *Peterson v. Idaho First National Bank*, 83 Ida. 578, 367 P. 2d 284 (1961)

In a recent decision of the California Supreme Court, *Burrows v. Superior Court, County of San Bernardino*, 118 Ca. Rptr. 166, 529 P. 2d 590 (1974), it was held that bank customers should be afforded the protection of due process when the Government seeks to examine their financial records. In commentary on the confidential nature of bank records, the Court stated:

"It cannot be gainsaid that the customer of a bank expects that documents, such as checks, which he transmits to the bank in the course of his business operations, will remain private, and that such an expectation is reasonable . . . Thus, we hold petitioner had a reasonable expectation that the bank would maintain the confidentiality of those papers which originated with him in check form

and of the bank's statements into which a record of those same checks had been transformed pursuant to internal bank operations." (At 593)

The Court further noted that:

"For all practical purposes, the disclosure by individuals or business firms of their financial affairs to a bank is not entirely volitional, since it is impossible to participate in the economic life of contemporary society without maintaining a bank account. In the course of such dealings, a depositor reveals many aspects of his personal affairs, opinions, habits and associations. Indeed the totality of bank records provides a virtual current biography . . . All papers which the customer has supplied to the bank to facilitate the conduct of his financial affairs [are] upon the reasonable assumption that the information would remain confidential." (At 596)

Similarly, the Federal courts have held that records of individuals' financial transactions with a bank are entitled to the fundamental right of privacy guaranteed by the Fourth Amendment and that such records may only be obtained by the Government through lawful process. See *U.S. v. Miller*, 500 F. 2d 751 (1974).

Although confidentiality is an important concept as it relates to bank customer records generally, it does not in fact afford an individual bank customer the right to challenge an IRS administrative summons to a bank for his financial records. This is because a valid administrative summons is a "lawful process" under which the IRS may obtain an individual's banking records. However, the concept of confidentiality should be deemed to protect the rights of bank customers who are not named in an IRS tax investigation and whose records may be subject to a "fishing expedition", as in the case of a John Doe summons. At this point, I will briefly describe certain aspects of the IRS administrative summons procedure, and the rights of bank customers, or the lack thereof, under these procedures.

Notice

Under current procedures, the Internal Revenue Service does not notify taxpayers when a summons has been issued to examine their bank records. The only way a taxpayer finds out about an IRS summons is if a bank notifies him for reasons of courtesy and good customer relations. Many banks have adopted the practice of notifying their customers of an IRS summons for their records—but many banks have not.

It is gratuitous to point out that a taxpayer cannot take any steps to question the validity of an IRS summons of his records if he does not know about the summons. Therefore, the law should be changed to require the Internal Revenue Service to send a copy of its summons to the taxpayer under investigation in every case. This would give the taxpayer the opportunity to consult legal counsel and to make a decision on whether to challenge the summons. The House Ways and Means Committee bill would require such IRS notice.

Procedure for challenging a summons

Under current practice, a third party record holder, such as a bank, which receives an IRS administrative summons has the right to challenge that summons on good faith grounds. That challenge must be reviewed by a Federal district court before the summons will be enforced. Some of the grounds upon which banks have challenged IRS summonses are:

(1) the records sought are not relevant to a legitimate tax investigation;

(2) the records are not adequately described in the summons;

(3) the summons is overly broad;

(4) the summons was not properly served, or is defective on its face;

(5) to produce the records requested would impose an unreasonable burden on the bank; and

(6) the records sought are subject to the Fair Credit Reporting Act and cannot be turned over without a court order.

As I indicated earlier, some banks have found it necessary to challenge a summons on grounds which should be available to the taxpayer if he had the right to challenge the summons or to intervene in an enforcement proceeding. One reason is that under State law, if a summons is not valid, a bank may be liable to the customer for turning over his records to the IRS.

One very troublesome area of the law involves situations in which an IRS summons for a customer's records is served on the bank by a special agent of the IRS. Some banks make it a practice in such cases to ask the special agent whether there has been a recommendation for criminal prosecution of the cus-

tomer. This is because the courts have held that where a criminal prosecution is the sole purpose of the IRS investigation, the records may not be obtained with an administrative summons. In such cases, they may be obtained only under court order or by grand jury subpena. On the other hand, where the investigation has both a civil and criminal purpose, or where it may begin as a civil investigation and develop into a criminal investigation, an administrative summons may be used to obtain bank records of the taxpayer—but only if a recommendation for criminal prosecution has not been made.

Thus, in an increasing number of situations banks believe that they may have a legal duty to challenge an IRS administrative summons, if only because the customer does not have such a right. It is obvious that in many cases challenges which should probably be made are not made.

Clearly, a more equitable solution would be to give the taxpayer the right to make his own challenges to IRS administrative summonses in order to prevent his financial records from being turned over to the IRS before a Federal court can rule on the challenges. This would resolve long-standing judicial conflicts and legal ambiguities. The Ways and Means Committee bill permits the taxpayer to make such a challenge.

Intervention in enforcement proceedures by the taxpayer

A bank or other third party record holder has the right to challenge an IRS administrative summons for *any* good faith reason, in which case the IRS must seek enforcement under § 7604. As indicated in my earlier discussion of the *Reisman* and *Donaldson* cases, the taxpayer is not, as a matter of right, entitled to intervene in this enforcement proceeding. As noted, this is because the courts have held that he does not have legal standing because he has no proprietary interest in the bank records and his standing as a taxpayer is not of sufficient magnitude to warrant intervention.

The American Bankers Association believes that the question of legal ownership of the bank records should not be posed as a bar to the taxpayer's intervention in the enforcement proceeding. Moreover, if the taxpayer is given the right to intervene by statute, as has been proposed under the House Ways and Means Committee bill, this would resolve a long history of judicial conflicts on this point. More importantly, it would serve as a great leap forward in the preservation of the fundamental rights of the individual. It would also relieve banks of the onerous and sometimes dubious responsibility of having to interpose challenges to administrative summonses which should be raised by the taxpayer rather than the bank.

John Doe summonses

In some tax investigations, the Internal Revenue Service will issue a § 7602 summons for bank records without having the name or any other means of identifying the person whose records they are seeking. These are called "John Doe" summonses because they are issued "in the matter of the tax liability of John Doe". This practice has been extensively criticized on the grounds that it permits fishing expeditions by the Internal Revenue Service and also because it imposes a great burden on the third party record holder to search among all or a large volume of its records to find the records of an unnamed individual.

The real problem in such cases—from the point of view of protecting the rights of the individual—is that the IRS in a John Doe summons examines or has broad access to the records of persons who are *not* under a tax investigation.

Earlier this year, the Supreme Court ruled in *U.S.* v. *Bisceglia* that the Internal Revenue Service may use a John Doe summons to examine a wide range of bank records where it has some evidence, however slight, of an upaid tax liability on the part of an unknown individual. The American Bankers Association filed an Amicus Curiae brief in this case opposing the use of the John Doe summons in searching bank records because such a procedure gives the IRS broad if not unlimited access to the financial records of *other bank customers* who are not under investigation by the IRS on the mere suspicion of a tax liability of an unknown person. In essence, the use of a John Doe summons breaches the whole concept that bank customers records must be treated as being confidential except where they may be obtained under lawful process. We do not consider the use of the John Doe summons in cases such as *Bisceglia* to be "lawful process".

The American Bankers Association also opposed the issuance of a John Doe summons for bank records on the ground that it imposes an unreasonable burden on the bank to search all or a large volume of its records for evidence of a potential tax liability on the part of an unknown individual.

The *Bisceglia* case, which has been characterized essentially as a 5 to 4 decision, attracted widespread criticism in the press and criticism from the Tax Bar. This criticism of the *Bisceglia* case has been reflected in the Federal courts as well. The fifth Circuit U.S. Court of Appeals, which was asked to review an earlier ruling in light of the *Bisceglia* decision, gave a narrow reading to the Supreme Court ruling by stating,

"[W]e decline to construe that holding as a blanket endorsement of the use of 'John Doe' summonses in every situation without reference to the purpose of the summons or to the factual circumstances which underlie its issuance." *U.S. v. Humble Oil*, No. 72-3029 (5th Cir September 8, 1975)

IV. CONCLUSION AND RECOMMENDATIONS

Last Friday, the House Ways and Means Committee, in a legislative drafting session, agreed to adopt amendments to the Internal Revenue Code which will explicitly provide for a substantially greater measure of protection to the privacy of individuals' financial records in the hands of a third party record holder, such as a bank. The American Bankers Association recommends that this Subcommittee adopt similar charges in §§ 7602 and 7604 of the Internal Revenue Code which would amend the administrative summons authority of the Service in the following important respects:

(1) The Internal Revenue Service will be required to give notice to a taxpayer whose records are sought in connection with his tax investigation prior to the issuance of an administrative summons for such records:

(2) The taxpayer is given a specified period in which to notify by certified mail the Internal Revenue Service and the third party record holder, such as a bank, that his records may not be turned over to the IRS under the administrative summons procedure;

(3) If the taxpayer provides such notice to the Internal Revenue Service and to the third party record holder, the IRS must seek enforcement of the administrative summons through a hearing in the Federal district court, as provided by § 7604 (b) of the Internal Revenue Code; and

(4) In the event of an enforcement proceeding by the Internal Revenue Service under § 7604, the taxpayer under investigation is given notice of this proceeding and is provided standing before the district court to intervene in order to challenge the production of his books and records.

The Ways and Means Committee also decided to restrict the use of the "John Doe" or non-name administrative summons for financial records of an individual by requiring that the IRS establish in a Federal district court that there is "reasonable cause" to believe that there has been a taxable transaction which would justify the investigation. The American Bankers Association agrees that there is a need for John Doe summonses to be judicially reviewed prior to issuance to prevent fishing expeditions by the Internal Revenue Service through bank records. However, the language of the House Ways and Means Committee provision provides only that the IRS proves to the satisfaction of the court reasonable cause for an investigation even though the IRS does not know the name of the taxpayer being investigated. We believe that this language is deficient because it does not provide for prior review by the courts of the actual John Doe summons which will be issued to the bank or other third party record holder. This deficiency could result in fishing expeditions by the IRS in the form of a very broadly worded summons, after they satisfy the district court of the need for the investigation. We believe a better procedure would be that the district court review the actual John Doe summons to be used by the Internal Revenue Service to determine not only the reasonableness of investigation through the use of a John Doe summons but also the relevancy of the records to be summoned by that John Doe request.

The amendments recommended by the American Bankers Association, and adopted by the House Ways and Means Committee, provide safeguards in maintaining the privacy of bank records, and will extend the protections of due process of law to persons under investigation by the Internal Revenue Service.

(Slip Opinion)

NOTE: Where it is feasible, a syllabus (headnote) will be released, as is being done in connection with this case, at the time the opinion is issued. The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States* v. *Detroit Lumber Co.*, 200 U.S. 321, 337.

SUPREME COURT OF THE UNITED STATES

Syllabus

UNITED STATES ET AL. *v.* BISCEGLIA

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

No. 73–1245. Argued November 11–12, 1974—
Decided February 19, 1975

The Internal Revenue Service (IRS) has authority under §§ 7601 and 7602 of the Internal Revenue Code of 1954 to issue a "John Doe" summons to a bank or other depository to discover the identity of a person who has had bank transactions suggesting the possibility of liability for unpaid taxes, in this instance a summons to respondent bank officer during an investigation to identify the person or persons who deposited 400 deteriorated $100 bills with the bank within the space of a few weeks. Pp. 7–10.

(a) That the summons was styled in a fictitious name is not a sufficient ground for denying enforcement. Pp. 7–8.

(b) The language of § 7601 permitting the IRS to investigate and inquire after "*all* persons . . . who *may* be liable to pay *any* internal revenue tax . . ." and of § 7602 authorizing the summoning of "*any* . . . person" for the taking of testimony and examination of books and witnesses that may be relevant for "ascertaining the correctness of *any* return, . . . determining the liability of *any* person . . . or collecting *any* such liability . . . ," is inconsistent with an interpretation that would limit the issuance of summonses to investigations which have already focused upon a particular return, a particular named person, or a particular potential tax liability, and moreover such a reading of the summons power of the IRS ignores the agency's legitimate interest in large or unusual financial transactions, especially those involving cash. Pp. 8–9.

486 F. 2d 706, reversed and remanded.

BURGER, C. J., delivered the opinion of the Court, in which BRENNAN, WHITE, MARSHALL, BLACKMUN, POWELL, and REHNQUIST, JJ., joined. BLACKMUN, J., filed a concurring opinion, in which POWELL, J., joined. STEWART, J., filed a dissenting opinion, in which DOUGLAS, J., joined.

SUPREME COURT OF THE UNITED STATES

No. 73–1245

United States et al., Petitioners, *v.* Richard V. Bisceglia. | On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.

[February 19, 1975]

MR. CHIEF JUSTICE BURGER delivered the opinion of the Court.

We granted certiorari to resolve the question whether the Internal Revenue Service has statutory authority to issue a "John Doe" summons to a bank or other depository to discover the identity of a person who has had bank transactions suggesting the possibility of liability for unpaid taxes.

I

On November 6 and 16, 1970, the Commercial Bank of Middlesboro, Kentucky, made two separate deposits with the Cincinnati Branch of the Federal Reserve Bank of Cleveland, each of which included $20,000 in $100 bills. The evidence is undisputed that the $100 bills were "paper thin" and showed signs of severe disintegration which could have been caused by a long period of storage under abnormal conditions. As a result the bills were no longer suitable for circulation and they were destroyed by the Federal Reserve in accord with established procedures. Also in accord with regular Federal Reserve procedures, the Cincinnati Branch reported these facts to the Internal Revenue Service.

It is not disputed that a deposit of such a large amount of high denomination currency was out of the ordinary for the Commercial Bank of Middlesboro; for example, in the 11 months preceding the two $20,000 deposits in $100 bills, the Federal Reserve had received only 218 $100 bills from that bank. This fact, together with the uniformily unusual state of deterioration of the $40,000 in $100 bills, caused the Internal Revenue Service to suspect that the transactions relating to those deposits may not have been reported for tax purposes. An agent was therefore assigned to investigate the matter.

After interviewing some of the bank's employees, none of whom could provide him with information regarding the two $20,000 deposits, the agent issued a "John Doe" summons directed to respondent, an executive vice president of the Commercial Bank of Middlesboro. The summons called for production of "[t]hose books and records which will provide information as to the person(s) or firm(s) which deposited, redeemed, or otherwise gave to the Commercial Bank $100 bills which the Commercial Bank sent in two shipments of (200) two hundred each $100 bills to the Cincinnati Branch of the Federal Reserve Bank on or about November 6, 1970 and November 16, 1970." This, of course, was simply the initial step in an investigation which might lead to nothing or might reveal that there had been a failure to report money on which federal estate, gift or income taxes were due.[1]

[1] The Internal Revenue Service agent testified:

"Q: What possible tax effect could this have on the taxpayer if his identity is determined?

"A: Well, it could be anything from nothing at all, a simple explanation, or it could be that this is money that has been secreted away for a period of time as a means of avoiding the tax.

"Q: Then you have really not reached first base yet, is that correct.

"A: That's correct."

Respondent, however, refused to comply with the summons even though he has not seriously argued that compliance would be unduly burdensome.

In due course, proceedings were commenced in United States District Court for the Eastern District of Kentucky to enforce the summons. That court narrowed its scope to require production only of deposit slips showing cash deposits in the amount of $20,000 and deposit slips showing cash deposits of $5,000 or more which involved $100 bills, and restricted it to the period between October 16, 1970, and November 16, 1970. Respondent was ordered to comply with the summons as modified.

The Court of Appeals reversed, holding that § 7602 of the Internal Revenue Code of 1954, 26 U. S. C. § 7602, pursuant to which the summons had been issued, "presupposes that the Internal Revenue Service has already identified the person in whom it is interested as a taxpayer before proceeding." 486 F. 2d 706, 710. We disagree and reverse the judgment of the Court of Appeals.

II

The statutory framework for this case consists of §§ 7601 and 7602 of the Internal Revenue Code of 1954 which provide:

> "Section 7601. Canvass of Districts for Taxable Persons and Objects.
>
> "(a) General Rule. The Secretary or his delegate shall, to the extent he deems it practicable, cause officers or employees of the Treasury Department to proceed, from time to time, through each internal revenue district and inquire after and concerning all persons therein who may be liable to pay any internal revenue tax, and all persons owning or having the care and management of any objects with respect to which any tax is imposed.

"Section 7602. Examination of Books and Witnesses.

"For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax . . . or collecting any such liability, the Secretary or his delegate is authorized—

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

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

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

We begin examination of these sections against the familiar background that our tax structure is based on a system of self-reporting. There is legal compulsion to be sure, but basically the Government depends upon the good faith and integrity of each potential taxpayer to disclose honestly all information relevant to tax liability. Nonetheless, it would be naive to ignore the reality that some persons attempt to outwit the system, and tax evaders are not readily identifiable. Thus, § 7601 gives the Internal Revenue Service a broad mandate to

investigate and audit "persons who *may be* liable" for taxes and § 7602 provides the power to "examine any books, papers, records or other data which may be relevant . . . and to summon . . . any person having possession . . . of books of account . . . relevant or material to such inquiry." Of necessity, the investigative authority so provided is not limited to situations in which there is probable cause, in the traditional sense, to believe that a violation of the tax laws exists. *United States* v. *Powell,* 379 U. S. 48 (1964). The purpose of the statutes is not to accuse, but to inquire. Although such investigations unquestionably involve some invasion of privacy, they are essential to our self-reporting system, and the alternatives could well involve far less agreeable invasions of house, business, and records.

We recognize that the authority vested in tax collectors may be abused, as all power is subject to abuse. However, the solution is not to restrict that authority so as to undermine the efficacy of the federal tax system, which seeks to assure that taxpayers pay what Congress has mandated and prevents dishonest persons from escaping taxation and thus shifting heavier burdens to honest taxpayers. Substantial protection is afforded by the provision that an Internal Revenue Service summons can be enforced only by the courts. 26 U. S. C. § 7604 (b); *Reisman* v. *Caplin,* 375 U. S. 440 (1964). Once a summons is challenged it must be scrutinized by a court to determine whether it seeks information relevant to a legitimate investigatory purpose and is not meant "to harass the taxpayer or to put pressure on him to settle a collateral dispute, or for any other reason reflecting on the good faith of the particular investigation." *United States* v. *Powell,* 379 U. S. 58. The cases show that the federal courts have taken seriously their obligation to apply this standard to fit particular situations, either by refusing enforcement or narrowing the scope of the sum-

mons. See, *e. g.*, *United States* v. *Matras*, 487 F. 2d 1271 (CA8 1973); *United States* v. *Theodore*, 479 F. 2d 749, 755 (CA4 1973); *United States* v. *Pritchard*, 438 F. 2d 969 (CA5 1971); *United States* v. *Dauphin Deposit Trust Co.*, 385 F. 2d 129 (CA3 1967). Indeed, the District Judge in this case viewed the demands of the summons as too broad and carefully narrowed them.

Finally, we note that the power to summon and inquire in cases such as the instant one is not unprecedented. For example, had respondent been brought before a grand jury under identical circumstances there can be little doubt that he would have been required to testify and produce records or be held in contempt. In *Blair* v. *United States*, 250 U. S. 273 (1919), petitioners were summoned to appear before a grand jury. They refused to testify on the ground that the investigation exceeded the authority of the court and grand jury, despite the fact that it was not directed at them. Their subsequent contempt convictions were affirmed by this Court:

> "[The witness] is not entitled to set limits to the investigation that the grand jury may conduct. . . . It is a grand inquest, a body with powers of investigation and inquisition, the scope of whose inquiries is not to be limited narrowly by questions of propriety or forecasts of the probable result of the investigation, or doubts whether any particular individual will be found properly subject to an accusation of crime. As said before, the identity of the offender, and the precise nature of the offense, if there be one, normally are developed at the conclusion of the grand jury's labors, not at the beginning." 250 U. S. 282.

The holding of *Blair* is not insignificant for our resolution of this case. In *United States* v. *Powell*, *supra*, Mr.

Justice Harlan reviewed this Court's cases dealing with the subpeona power of federal enforcement agencies, and observed:

> "[T]he Federal Trade Commission . . . 'has a power of inquisition, if one chooses to call it that, which is not derived from the judicial function. It is more analogous to the Grand Jury, which does not depend upon a case or controversy for power to get evidence but can investigate merely on suspicion that the law is being violated, or even just because it wants assurance that it is not.' While the power of the Commissioner of Internal Revenue derives from a different body of statutes, we do not think that analogies to other agency situations are without force when the scope of the Commissioner's power is called into question." 379 U. S. 57, quoting *United States* v. *Morton Salt Co.*, 383 U. S. 632, 642–644.

III

Against this background, we turn to the question whether the summons issued to respondent, as modified by the District Court, was authorized by the Internal Revenue Code of 1954.[2] Of course, the mere fact that the summons was styled "In the matter of the tax liability of John Doe" is not sufficient grounds for denying enforcement. The use of such fictitious names is common in indictments, see, *e. g.*, *Baker* v. *United States*, 115 F. 2d 533 (CA8 1940), cert. denied, 312 U. S. 692

[2] Respondent also argues that, even if the summons issued in this case was authorized by statute, it violates the Fourth Amendment. This contention was not passed upon by the Court of Appeals. In any event, as narrowed by the District Court the summons is at least as specific as the reporting requirements which was upheld against a Fourth Amendment challenge by banks in *California Bankers Assn.* v. *Schultz*, 416 U. S. 21, 63–70 (1974).

(1941), and other types of compulsory process. Indeed, the courts of appeals have regularly enforced Internal Revenue Service summonses which did not name a specific taxpayer who was under investigation. *E. g., United States* v. *Carter*, 489 F. 2d 413 (CA5 1973); *United States* v. *Turner*, 480 F. 2d 272, 279 (CA7 1973); *Tillotson* v. *Boughner*, 333 F. 2d 515 (CA7), cert. denied, 379 U. S. 913 (1964). Respondent undertakes to distinguish these cases on the ground that they involved situations in which either a taxpayer was identified or a tax liability was known to exist as to an unidentified taxpayer. However, while they serve to suggest the almost infinite variety of factual situations in which a "John Doe" summons may be necessary, it does not follow that these cases define the limits of the Internal Revenue Service's power to inquire concerning tax liability.

The first question is whether the words of the statute require the restrictive reading given them by the Court of Appeals. Section 7601 permits the Internal Revenue Service to investigate and inquire after "*all* persons . . . who *may be* liable to pay *any* internal revenue tax . . . ." To aid in this investigatory function, § 7602 authorizes the summoning of "*any* . . . person" for the taking of testimony and examination of books which may be relevant for "ascertaining the correctness of *any* return, . . . determining the liability of *any* person . . . or collecting *any* such liability . . . ." Plainly, this language is inconsistent with an interpretation that would limit the issuance of summonses to investigations which have already focused upon a particular return, a particular named person, or a particular potential tax liability.

Moreover, such a reading of the Internal Revenue Service's summons power ignores the fact that it has a legitimate interest in large or unusual financial transactions, especially those involving cash. The reasons for that interest are too numerous and too obvious to catalog.

Indeed, Congress has recently determined that information regarding transactions with foreign financial institutions and transactions which involve large amounts of money is so likely to be useful to persons responsible for enforcing the tax laws that it must be reported by banks. See generally *California Bankers Assn.* v. *Schultz,* 416 U. S. 21, 26–40 (1974).

It would seem elementary that no meaningful investigation of such events could be conducted if the identity of the persons involved must first be ascertained, and that is not always an easy task. Fiduciaries and other agents are understandably reluctant to disclose information regarding their principals, as respondent was in this case. Moreover, if criminal activity is afoot the persons involved may well have used aliases or taken other measures to cover their tracks. Thus, if the Internal Revenue Service is unable to issue a summons to determine the identity of such persons, the broad inquiry authorized by § 7601 will be frustrated in this class of cases. Settled principles of statutory interpretation require that we avoid such a result absent unambiguous directions from Congress. See *Labor Board* v. *Lion Oil Co.,* 352 U. S. 282, 288 (1957); *United States* v. *American Trucking Assn.,* 310 U. S. 534, 542–544 (1940). No such congressional purpose is discernible in this case.

We hold that the Internal Revenue Service was acting within its statutory authority in issuing a summons to respondent for the purpose of identifying the person or persons who deposited 400 decrepit $100 bills with the Commercial Bank of Middlesboro within the space of a few weeks. Further investigation may well reveal that such person or persons have a perfectly innocent explanation for the transactions. It is not unknown for taxpayers to hide large amounts of currency in odd places out of a fear of banks. But on this record the deposits were extraordinary and no meaningful inquiry can be made

until respondent complies with the summons as modified by the District Court.

We do not mean to suggest by this holding that respondent's fears that the § 7602 summons power could be used to conduct "fishing expeditions" into the private affairs of bank depositors are trivial. However, as we have observed in a similar context:

> "That the power may be abused is no ground for denying its existence. It is a limited power, and should be kept within its proper bounds; and, when these are exceeded, a jurisdictional question is presented which is cognizable in the courts." *McGrain* v. *Daugherty*, 273 U. S. 135, 166 (1927), quoting *People* v. *Keeler*, 99 N. Y. 463, 482–483.

So here, Congress has provided protection from arbitrary or capricious action by placing the federal courts between the government and the person summoned. The District Court in this case conscientiously discharged its duty to see that a legitimate investigation was being conducted and that the summons was no broader than necessary to achieve its purpose.

The judgment of the Court of Appeals is reversed and the cause is remanded to it with directions to affirm the order of the District Court.

SUPREME COURT OF THE UNITED STATES

No. 73–1245

United States et al., Petitioners, *v.* Richard V. Bisceglia. | On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.

[February 19, 1975]

MR. JUSTICE BLACKMUN, with whom MR. JUSTICE POWELL joins, concurring.

I join the Court's opinion and its judgment, and add this word only to emphasize the narrowness of the issue at stake here. We decide today that the Internal Revenue Service has statutory authority to issue a summons to a bank in order to ascertain the identity of a person whose transactions with that bank strongly suggest liability for unpaid taxes. Under the circumstances here, there was an overwhelming probability, if not a certitude, that one individual or entity was responsible for the deposits. The uniformly decrepit condition of the currency and the amount, combined with other unusual aspects, gave the Service good reason, and, indeed, the duty to investigate. The Service's suspicion as to possible liability was more than plausible.* The summons was closely scrutinized and appropriately narrowed in scope by the United States District Court.

The summons, in short, was issued pursuant to a genuine investigation. The Service was not engaged in researching some general problem; its mission was not exploratory. The distinction between an investigatory

*The Service may not have reached "first base," see *ante*, at 2 n. 1, but it had been at bat before, and it knew both the game and the ball park well.

and a more general exploratory purpose has been stressed appropriately by federal courts, see, *e. g., United States* v. *Humble Oil & Refining Co.*, 488 F. 2d 953, 958 (CA5 1974), petition for certiorari pending, No. 73–1827; *United States* v. *Armour*, 376 F. Supp. 318 (Conn. 1974), and that distinction is important to our decision here.

We need not decide in this case whether the Service has statutory authority to issue a "John Doe" summons where neither a particular taxpayer nor an ascertainable group of taxpayers is under investigation. At most, we hold that the Service is not always required to state a taxpayer's name in order to obtain enforcement of its summons, and that under the circumstances of this case it is definitely not required to do so. We do not decide that a "John Doe" summons is always enforceable where the name of an individual is lacking and the Service's purpose is other than investigatory.

Upon this understanding, I join the Court's opinion.

SUPREME COURT OF THE UNITED STATES

No. 73–1245

United States et al., Petitioners, *v.* Richard V. Bisceglia. | On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.

[February 19, 1975]

MR. JUSTICE STEWART, with whom MR. JUSTICE DOUGLAS joins, dissenting.

The Court today says that it "recogniz[es] that the authority vested in tax collectors may be abused," *ante*, p. 5, but it is nonetheless unable to find any statutory limitation upon that authority. The only "protection from abuse" that Congress has provided, it says, is "placing the federal courts between the government and the person summoned," *ante*, p. 10. But that, of course, is no protection at all, unless the federal courts are provided with a measurable standard when asked to enforce a summons. I agree with the Court of Appeals that Congress has provided such a standard, and that the standard was not met in this case. Accordingly, I respectfully dissent from the opinion and judgment of the Court.

Congress has carefully restricted the summons power to certain rather precisely delineated purposes:

> "ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability." 26 U. S. C. § 7602.

This provision speaks in the singular—referring to "the correctness of any return" and to "the liability of any person." The delineated purposes are jointly denominated an "inquiry" concerning "the person liable for tax or required to perform the act," and the summons is designed to facilitate the "[e]xamination of books and witnesses" which "may be relevant or material to such inquiry." 26 U. S. C. §§ 7602 (1), (2), and (3). This language indicates unmistakably that the summons power is a tool for the investigation of particular taxpayers.

By contrast, the general *duties* of the IRS are vastly broader than its summons authority. For instance, § 7601 mandates a "canvass of districts for taxable persons and objects." Unlike § 7602, the canvassing provision speaks broadly and in the plural, instructing Treasury Department officials

> "to proceed, from time to time, through each internal revenue district and inquire after and concerning *all persons* therein who *may be liable* to pay any internal revenue tax, and *all persons* owning or having care and management of *any objects* with respect to which any tax is imposed." [Emphasis added.]

Virtually all "persons" or "objects" in this country "may," of course, have federal tax problems. Every day the economy generates thousands of sales, loans, gifts, purchases, leases, deposits, mergers, wills, and the like which—because of their size or complexity—suggest the possibility of tax problems for somebody. Our economy is "tax relevant" in almost every detail. Accordingly, if a summons could issue for any material conceivably relevant to "taxation"—that is, relevant to the general *duties* of the IRS—the Service could use the summons power as a broad research device. The Service could use that power methodically to force disclosure of whole categories of transactions and closely monitor the operations of

myriad segments of the economy on the theory that the information thereby accumulated might facilitate the assessment and collection of some kind of a federal tax from somebody. Cf. *United States* v. *Humble Oil & Refining Co.*, 488 F. 2d 953. And the Court's opinion today seems to authorize exactly that.

But Congress has provided otherwise. The Congress *has* recognized that information concerning certain classes of transactions is of peculiar importance to the sound administration of the tax system, but the legislative solution has not been the conferral of a limitless summons power. Instead, various special-purpose statutes have been written to require the reporting or disclosure of particular kinds of transactions. *E. g.*, 26 U. S. C. §§ 6049, 6051–6053, and 31 U. S. C. §§ 1081–1083, 1101, and 1121–1143. Meanwhile, the scope of the summons power itself has been kept narrow. Congress has never made that power coextensive with the Service's broad and general convassing duties set out in § 7601. Instead, the summons power has always been restricted to the particular purposes of individual investigation, delineated in § 7602.[1]

[1] The canvassing duties and the summons power have always been found in separate and distinct statutory provisions. The spatial proximity of the two contemporary provisions is utterly without legal significance. 26 U. S. C. § 7806 (b). The general mandate to canvass and inquire, now found in § 7601, is derived from § 3172 of the Revised Statutes of 1874. See *Donaldson* v. *United States*, 400 U. S. 517, 523–524. The summons power, however, has different historical roots. Section 7602, enacted in 1954, was meant to consolidate and carry forward several prior statutes, with "no material change from existing law." H. R. Rep. No. 1337, 83d Cong., 2d Sess., p. A536; S. Rep. No. 1622, 83d Cong., 2d Sess., p. 617. The relevant prior statutes were §§ 3614 and 3615 (a)–(c) of the Internal Revenue Code of 1939. See Table II of the 1954 Code, 68A Stat. 969. Section 3614 granted the summons power to the Commissioner "for the purpose of ascertaining the correct-

Thus, a financial or economic transaction is not subject to disclosure through summons merely because it is large or unusual or generally "tax relevant"—but only when the summoned information is reasonably pertinent to an ongoing investigation of somebody's tax status. This restriction checks possible abuses of the summons power in two rather obvious ways. First, it guards against an overbroad summons by allowing the enforcing court to prune away those demands which are not relevant to the particular, ongoing investigation. See, *e. g., First Nat'l Bank of Mobile* v. *United States,* 160 F. 2d 532, 533–535. Second, the restriction altogether prohibits a summons which is wholly unconnected with such an investigation.

The Court today completely obliterates the historic distinction between the general duties of the IRS, summarized in § 7601, and the limited purposes for which a summons may issue, specified in § 7602. Relying heavily on § 7601, and noting that the IRS "has a legitimate interest in large or unusual financial transactions, especially those involving cash," *ante*, p. 8, the Court approves enforcement of a summons having no investigatory predicate. The sole premise for this summons was the Service's theory that the deposit of old wornout $100 bills was a sufficiently unusual and interesting transaction to justify compulsory disclosure of the identities of all the large-amount depositors at the respondent's bank over a one-month period.[2] That the summons was not

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ness of any return or for the purpose of making a return, where none has been made." Section 3615 (a)–(c) granted the summons power to "collectors" and provided that a "summons may be issued" whenever "any person" refuses to make a return or makes a false or fraudulent return. Thus, like the present § 7602, these earlier provisions clearly limited use of the summons power to the investigation of particular taxpayers.

[2] The summons here used a scattershot technique to learn the identity of the unknown depositor. Rather than merely asking bank officials who the depositor was, the IRS required production of all

incident to an ongoing, particularized investigation, but was merely a shot in the dark to see if one might be warranted, was freely conceded by the IRS agent who served the summons.[3]

The Court's opinion thus approves a breathtaking expansion of the summons power: There are obviously thousands of transactions occurring daily throughout the country which, on their face, suggest the *possibility* of tax complications for the unknown parties involved. These transactions will now be subject to forced disclosure at the whim of any IRS agent, so long only as he is acting in "good faith." *Ante*, p. 5.

This is a sharp and dangerous detour from the settled course of precedent. The decision of the Court of Appeals in this case has been explicitly accepted as sound by the courts of appeals of two other Circuits. See *United States* v. *Berkowitz*, 488 F. 2d 1235, 1236 (CA3), and *United States* v. *Humble Oil & Refining Co.*, 488 F. 2d 953, 960 (CA5). No federal court has disagreed with it.

The federal courts have always scrutinized with particular care any IRS summons directed to a "third party," *i. e.*, to a party other than the taxpayer under investigation. See, *e. g.*, *United States* v. *Humble Oil & Refining*

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deposit slips exceeding specified amounts that had been filled out during the period when the suspect deposits were, presumably, made. Thus, enforcement of the summons, even as redrafted by the District Court, will doubtlessly apprise the IRS of the identities of many bank depositors other than the one who submitted the old and worn-out $100 bills.

[3] He testified at the enforcement hearing:

"Q: What possible tax effect could this have on the taxpayer if his identity is determined?

"A: Well, it could be anything from nothing at all, a simple explanation, or it could be that this money that has been secreted away for a period of time as a means of avoiding the tax.

"Q: Then you have really not reached first base yet, is that correct?

"A: That's correct."

Co., 488 F. 2d, at 963; *Venn* v. *United States*, 400 F. 2d 207, 211–212; *United States* v. *Harrington*, 388 F. 2d 520, 523. When, as here, the third party summons does not identify the party under investigation, a presumption naturally arises that the summons is not genuinely investigatory but merely exploratory—a device for general research or for the hit-or-miss monitoring of "unusual" transactions. Unless this presumption is rebutted by the Service, the courts have denied enforcement.

Thus, the IRS was not permitted to summon from a bank the names and addresses of all beneficiaries of certain types of trust arrangements merely on the theory that these arrangements were unusual in form or size. *Mays* v. *Davis*, 7 F. Supp. 596. Nor could the Service force a company to disclose the identity of whole classes of its oil land lessees merely on the theory that oil lessees commonly have tax problems. *United States* v. *Humble Oil & Refining Co.*, *supra*. See also *McDonough* v. *Lambert*, 94 F. 2d 838; *First Nat'l Bank of Mobile* v. *United States*, 160 F. 2d, at 533–535; *Local 174, Int'l Bros. of Teamsters* v. *United States*, 240 F. 2d 387, 390.

On the other hand, enforcement has been granted where the Service has been able to demonstrate that the John Doe summons was issued incident to an ongoing and particularized investigation. Thus, enforcement was granted of summonses seeking to identify the clients of those tax return preparation firms which *prior investigation* had shown to be less than honest or accurate in the preparation of sample returns. *United States* v. *Theodore*, 479 F. 2d 749; *United States* v. *Turner*, 480 F. 2d 272; *United States* v. *Berkowitz*, *supra*; *United States* v. *Carter*, 489 F. 2d 413. Similarly, enforcement was granted of summonses directed to an attorney, and his bank, seeking to identify the client for whom the attorney had mailed to the IRS a large, anonymous check, purporting to satisfy an outstanding tax deficiency of the

client. *Tillotson* v. *Boughner*, 333 F. 2d 515; *Schultz* v. *Rayunec*, 350 F. 2d 666. Like the prior investigative work in the tax return preparer cases, the receipt of the mysterious check established the predicate of a particularized investigation which was necessary, under § 7602, to the enforcement of a summons. In each case, the Service had already proceeded to the point where the unknown individual's tax liability had become a reasonable possibility, rather than a matter of sheer speculation.

Today's decision shatters this long line of precedent. For this summons, there was absolutely no investigatory predicate. The sole indication of this John Doe's tax liability was the unusual character of the deposit transaction itself. Any private economic transaction is now fair game for forced disclosure, if any IRS agent happens in good faith to want it disclosed. This new rule simply disregards the language of § 7602, and the body of established case law construing it.

The Court's attempt to justify this extraordinary departure from established law is hardly persuasive. The Court first notes that a witness may not refuse testimony to a grand jury merely because the grand jury has not yet specified the "identity of the offender," *ante*, p. 6, *quoting Blair* v. *United States*, 250 U. S. 273, 282. This is true but irrelevant. The IRS is not a grand jury. It is a creature not of the Constitution but of legislation and is thus peculiarly subject to legislated constraints. See *In re Groban*, 352 U. S. 330, 346 (Black, J., dissenting). It is true that the Court drew an analogy between an IRS summons and a grand jury subpoena in *United States* v. *Powell*, 379 U. S. 48, 57, but this was merely to emphasize that an IRS summons does not require the support of "probable cause" to suspect tax fraud when the summons is *issued incident to an ongoing, individualized investigation of an identified party*. A major premise of *Powell* was that an extrastatutory "probable cause" requirement

was unnecessary in view of the "legitimate purpose" requirements already specified in § 7602, *id.*, at 56–57.

The Court next suggests that this expansion of the summons power is innocuous, at least on the facts of this case, because the Bank Secrecy Act of 1970[4] itself compels banks to disclose the identity of certain cash depositors. *Ante*, p. 9. Aside from the fact that the summons at issue here forces disclosure of some deposits not covered by the Act and its attendant regulations,[5] the argument has a more basic flaw. If the summons authority of § 7602 allows preinvestigative inquiry into any large or unusual bank deposit, the 1970 Act was largely redundant. The IRS could have saved Congress months of hearings and debates by simply directing § 7602 summonses on a regular basis to the Nation's banks, demanding the identities of their large cash depositors. In *California Bankers Assn.* v. *Schultz*, 416 U. S. 21, we gave extended consideration to the complex constitutional issues raised by the 1970 Act; some of those issues—*e. g.*, whether and to what extent bank depositors have Fourth Amendment and Fifth Amendment rights to the secrecy of their domestic deposits—were left unresolved by the Court's opinion, *id.*, at 67–75. If the disclosure requirements in the 1970 Act were already encompassed within the Service's summons power, one must wonder why the Court labored so long and carefully in *Schultz*.

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[4] Pub. L. 91–508, 84 Stat. 1114, 12 U. S. C. §§ 1829b, 1730d, 1951–1959, and 31 U. S. C. §§ 1051–1062, 1081–1083, 1101–1105, 1121–1122. See *California Bankers Assn.* v. *Schultz*, 416 U. S. 21.

[5] As limited by the District Court, the summons calls for production of deposit slips showing cash deposits in the amount of $20,000 and deposit slips showing cash deposits of $5,000 or more involving $100 bills, for deposits made between October 16 and November 16, 1970. Current regulations under the Bank Secrecy Act require reporting only with respect to cash transactions exceeding $10,000. 31 CFR § 103.22 (1974).

Finally, the Court suggests that respect for the plain language of § 7602 would "undermine the efficacy of the federal tax system, which seeks to assure that taxpayers pay what Congress has mandated and prevents dishonest persons from escaping taxation and thus shifting heavier burdens to honest taxpayers." *Ante*, p. 5. But the federal courts have applied the strictures of § 7602, and its predecessors, for many decades without occasioning these dire effects. If such a danger exists, Congress can deal with it. But until Congress changes the provision of § 7602, it is our duty to apply the statute as it is written.

I would affirm the judgment of the Court of Appeals.

IN THE

Supreme Court of the United States

No. 73-1245

UNITED STATES OF AMERICA, *Petitioner*

v.

RICHARD V. BISCEGLIA, as Vice President of the Commercial Bank of Middlesboro, Kentucky, *Respondent*

On Writ of Certiorari from the Judgment of the United States Court of Appeals for the Sixth Circuit

BRIEF FOR THE AMERICAN BANKERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF THE RESPONDENT

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TABLE OF CONTENTS

	Page
ISSUE PRESENTED FOR REVIEW	1
STATEMENT OF THE CASE	2
STATEMENT OF THE FACTS	3
INTEREST OF AMICUS CURIAE	4
SUMMARY OF THE ARGUMENT	6
ARGUMENT	8
I. The "No Name" Summons Issued By The Internal Revenue Service Requiring The Bank To Produce Records Is Invalid And Beyond The Authority Granted To The Internal Revenue Service Under Section 7602 Of The Internal Revenue Code of 1954	8
A. The summons is invalid because it fails to specify a particular taxpayer whose tax liability is under investigation	8
B. The summons is invalid because it does not satisfy any of the four conditions contained in the statute as proper grounds for the issuance of such summons	12
C. The summons issued to the bank cannot be justified under the authority of Section 7601 of the Code	17
D. Requiring the IRS to either identify the taxpayer or to specify that a tax liability does exist will not unduly hamper the IRS in the performance of its duties	19
II. The "No Name" Summons Issued By The Internal Revenue Service Requiring The Bank To	

Page

Produce Records Is Invalid And Constitutes An Unreasonable Search In Violation Of The Fourth Amendment 21

CONCLUSION 25

APPENDIX 26

TABLE OF CITATIONS

CASES:

Hubner v. *Tucker*, 245 F.2d 35 (9th Cir., 1957) 22, 23
McDonough v. *Lambert*, 94 F.2d 838 (1st Cir., 1938) 9, 15, 16
Mays v. *Davis*, 7 F. Supp. 596 (W.D. Pa., 1934) .9, 11, 15, 16
Oklahoma Press Publishing Company v. *Walling*, 327 U.S. 186, 208 (1946) 21, 23, 24
Peterson v. *Idaho First National Bank*, 84 Ida. 10, 367 P.2d 284 (1961) 5
Reisman v. *Caplin*, 375 U.S. 440 (1964) 20
Tillotson v. *Boughner*, 333 F.2d 515 (7th Cir., 1964) *cert. denied* 379 U.S. 913 (1964) 11, 15, 19
Tillotson v. *Boughner*, 225 F. Supp. 45, (N.D. Ill., 1963) 16
United States v. *Armour*, 74-1 U.S.T.C., Par. 9479 (D. Conn., 4/25/74) 19
United States v. *Dauphin Deposit Trust Company*, 385 F.2d 129 (3rd Cir., 1967) 22
United States v. *First National Bank of Mobile*, 295 F.142 (S.D. Ala., 1924) *aff'd without opinion* 267 U.S. 576 (1925) 22
United States v. *Harrington*, 388 F.2d 520 (2nd Cir., 1968) 23
United States v. *Humble Oil & Refining Company*, 488 F.2d 953, 960 (5th Cir., 1974) 10, 15, 18

CONSTITUTION:

United States Constitution, Amendment IV ...1, 2, 7, 20, 21, 24, 25

Table of Contents Continued iii

STATUTES: Page

Internal Revenue Code,

Section 6201(a) 19

Section 6301 19

Section 7402(b) 2

Section 7601 .....17, 18, 19

Section 7601(a) 17

Section 7602 .....1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 12, 15, 16, 17, 18, 19, 20

Section 7604(a) 2

Section 7801(a) 19

Section 7802 19

RULINGS:

Internal Revenue Service Rev. Proc. 55-6, 1955-2 Cum. Bull. 903 5

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On Writ of Certiorari from the Judgment of the United States Court of Appeals for the Sixth Circuit

BRIEF FOR THE AMERICAN BANKERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF THE RESPONDENT

ISSUES PRESENTED FOR REVIEW

1. Whether the "no name" summons issued to the bank was invalid and beyond the authority granted to the Internal Revenue Service in Section 7602 of the Internal Revenue Code of 1954.

2. Whether the "no name" summons issued to the bank constituted an unreasonable search in violation of the Fourth Amendment to the United States Constitution.

STATEMENT OF THE CASE

On April 22, 1971, B. L. Brutscher, Special Agent for the Internal Revenue Service, caused a summons to be served on Richard V. Bisceglia as Vice President of the Commercial Bank of Middlesboro, Kentucky, requesting him to testify and bring with him documents pertaining to the deposit of certain deteriorated $100 bills. The summons was entitled, "In connection with the tax liability of 'John Doe' ". When Mr. Bisceglia refused to comply with the summons, the Internal Revenue Service filed a petition for enforcement of the summons under Sections 7402(b) and 7604(a) of the Internal Revenue Code of 1954 in the United States District Court for the Eastern District of Kentucky.

The respondent bank opposed the enforcement of the summons by raising four affirmative defenses. These defenses were (1) that the summons was not authorized under Section 7602 of the Internal Revenue Code and it violated the Fourth Amendment prohibition against unreasonable searches and seizures because it did not specify a taxpayer whose tax liability was being investigated, (2) that the Section 7602 summons was improper because the Internal Revenue Service was conducting a criminal investigation, (3) that the blanket request in the summons was so broad that the bank could not reasonably comply because it could not notify every depositor who transacted business with the bank during the period specified in the summons, and (4) that the Internal Revenue Service did not issue the summons in good faith. The District Court rejected each of these arguments, and in a Memorandum Opinion issued June 1, 1972, the Court authorized enforcement of the summons. That opinion is unofficially reported at 72-1 U.S.T.C. Par. 9474. The Court's order

65-738 O—76——10

modified the summons and required the bank to produce copies of all deposit tickets showing the identity of every depositor who made a cash deposit of $20,000 or more from October 16, 1970 to November 16, 1970, and all deposit tickets of every depositor who made a deposit during that period of $5,000 or more which involved $100 bills. The bank sought and obtained a stay on the execution of the summons pending appeal of the District Court order.

The United States Court of Appeals for the Sixth Circuit reversed the lower court ruling on the ground that the summons was beyond the authority of Section 7602 because the IRS failed to specify a taxpayer whose tax liability was being investigated. The Court did not find it necessary to reach the constitutional issue raised by Bisceglia. The Court's opinion is officially reported at 486 F.2d 706 (6th Cir., 1973). From that ruling, the Government sought a writ of certiorari to this Court. This Court granted the writ of certiorari on April 15, 1974.

STATEMENT OF FACTS

On or about November 6, 1970 and November 15, 1970, the Federal Reserve Bank in Cincinnati, Ohio, received two shipments from the Commercial Bank of Middlesboro, Kentucky, each shipment containing two hundred $100 bills. The bills were in a deteriorated condition and no longer fit for circulation. The Cincinnati Branch of the Federal Reserve Bank reported the deposits to the Internal Revenue Service and stated that the deteriorated condition apparently resulted from a long period of storage. The Internal Revenue Service apparently suspected that such money may not have been properly reported for Federal income tax purposes. Accordingly, the IRS attempted

to determine the identity of the persons who transferred the funds to the bank. In the course of this investigation a summons was issued to the bank requesting Richard Bisceglia, Vice President, to testify and to bring all records concerning the person or persons who deposited, redeemed, or otherwise gave to the bank the deteriorated $100 bills. The summons was allegedly issued under the authority of Section 7602 of the Internal Revenue Code. The summons was entitled, "In the matter of the tax liability of 'John Doe' ". The Internal Revenue Service has indicated that John Doe is a fictitious name which was substituted in the form because the IRS did not know the name of the person who transferred the money to the bank. The IRS also admitted that they did not have any specific taxpayer or specific liability under investigation. Bisceglia refused to comply with the summons, and the Government commenced this action by filing a petition for enforcement in the District Court.

INTEREST OF AMICUS CURIAE

The American Bankers Association is a national trade association having approximately 14,000 commercial banks as members. These banks, operating under both state and national charters, comprise virtually the entire commercial banking system of the United States.

A keystone of all banking activity is the relationship between the bank and its customers. This relationship is established when the bank accepts a customer's money for deposit, or when the bank makes a loan to a customer, or when the bank provides any other financial service. In the course of this financial services relationship the bank participates in the private financial affairs of its customers. Traditionally, the bank has treated customers' financial affairs as

confidential matters which are not revealed to others except, of course, under compulsion of law. The issue in this case involves the fundamental question of whether a bank is required by law to provide the Internal Revenue Service with broad access to bank records to establish the identity of unknown bank customers in order to determine whether or not such customers have unsatisfied tax liabilities.

The American Bankers Association has received a large number of inquiries from its member banks in connection with the broad issue of when and how a bank must comply with a request of the Internal Revenue Service to obtain information from bank records in connection with tax investigations of bank customers. Banks have experienced considerable difficulty and misunderstanding of their legal duties in attempting to comply with these requests. The Internal Revenue Service itself sought to establish a standard form summons and standardized procedure under Rev. Proc. 55-6, 1955-2 Cum. Bull. 903, for the purpose of defining when and how the IRS may examine records of taxpayers and third parties. In spite of the issuance of Rev. Proc. 55-6, which establishes Form 2039 as the one standard form summons to be issued under Section 7602, the Internal Revenue Service is using a variety of procedures and forms not defined by the Revenue Procedure, the Code, or the Federal income tax regulations to obtain information concerning bank customers. In this connection, it is to be noted that a bank may be liable to its customer for disclosing information when such disclosure is not required by law. See *Peterson* v. *Idaho First National Bank* 84 Ida. 10, 367 P.2d 284 (1961). Thus, it is critical to banks that the IRS obtain bank records only in accordance with procedures authorized under law.

Finally, we believe that the resolution of this case will have a broad impact on the interpretation of the authority granted to the Internal Revenue Service under Section 7602 of the Internal Revenue Code of 1954. Under these circumstances, the American Bankers Association seeks the leave of this Court to present information concerning the examination of bank records by the Internal Revenue Service in connection with a tax investigation of a bank customer which we believe will be helpful to the Court in the consideration of this case.

SUMMARY OF ARGUMENT

The records of customer transactions maintained by banks have traditionally been recognized as confidential materials. In some cases, the courts have recognized a legal duty of banks to maintain the confidentiality of these records except in cases where the bank is required to release the records under compulsion of law. Banks disclose information concerning their customers' accounts only in very limited circumstances.

The circumstances under which the Internal Revenue Service may obtain records for the purpose of conducting a tax investigation have been spelled out by Congress in Section 7602 of the Internal Revenue Code. We contend that this clear and comprehensive statute establishes the complete parameters of the authority of the Internal Revenue Service with respect to these examinations. Under the clearly defined requirements established by Section 7602, the IRS cannot issue a summons unless (1) it knows the identity of the potential taxpayer it seeks to investigate or (2) it has evidence that a tax liability exists. However, in this case the IRS did not know the identity of the potential taxpayer it sought to investigate and it did not have any

evidence that there was a tax liability yet unsatisfied. Under the purposes set forth in Section 7602, where the identity of the taxpayer is unknown, the IRS should not be allowed to use such innocent facts as deposits or exchanges of $40,000 in old $100 bills as a basis for inferring that a tax liability exists in order to establish grounds for the issuance of a summons for a broad examination of bank records. We maintain that the IRS was engaging in a fishing expedition in the hope of finding a tax liability.

The Fourth Amendment to the Constitution protects individuals against unreasonable searches and seizures. It has long been established that the test of unreasonableness is predicated upon two basic requirements, i.e., the records or other materials sought to be obtained must be relevant to the investigation, and such records or materials must be described with sufficient particularity so as not to constitute an unreasonable burden. In the instant case, the Government sought to examine the records of a large number of bank customers during a thirty day period in order to determine the identity of one potential taxpayer and whether an unsatisfied tax liability existed. We maintain that the extreme breadth of the records sought to be examined to identify a single taxpayer violates the requirement of relevancy and fails to meet the requirement of sufficient particularity under the reasonableness test of the Fourth Amendment. Moreover, we urge that this investigation jeopardized the constitutional rights of a large number of bank customers and placed an unreasonable burden on the bank.

In summary, the statutory and constiutional limitations pertaining to IRS summons for records prohibit fishing expeditions where the identity of the taxpayer

is unknown to the IRS and where there is no evidence of a tax liability. Therefore, we urge that the bank properly rejected this summons and that the law requires the bank to maintain the confidentiality of these records until such time as a legally authorized summons is issued.

ARGUMENT

I.

THE "NO NAME" SUMMONS ISSUED BY THE INTERNAL REVENUE SERVICE REQUIRING THE BANK TO PRODUCE RECORDS IS INVALID AND BEYOND THE AUTHORITY GRANTED TO THE INTERNAL REVENUE SERVICE UNDER SECTION 7602 OF THE INTERNAL REVENUE CODE OF 1954

A. The Summons Is Invalid Because It Fails To Specify a Particular Taxpayer Whose Tax Liability Is Under Investigation.

The IRS summons received by the bank in this case did not indicate the name of the bank customer or customers whose tax liability was being investigated. Indeed, the Sixth Circuit emphasized that not only did the IRS not know the identity of the bank customers, but also the IRS admitted that it neither suspected nor was it investigating a particular person or taxpayer. *United States* v. *Bisceglia,* 486 F.2d 706 (6th Cir., 1973). Nonetheless, the IRS inserted the ficticious name "John Doe" on the form and sought from the bank records on some unknown bank customer or customers who deposited certain unusual $100 bills in the bank sometime during a particular four-week period. The IRS contends that a civil summons may be used to obtain certain records in spite of the fact that the IRS does not know the identity of the person or persons about whom they seek the information. We strongly contend that Section 7602 does not authorize the IRS to conduct inquiries into the private affairs of U.S. citi-

zens and other taxpayers at random, but only allows the IRS to investigate specific persons for certain specific purposes. (Subpart B of this argument will address the purposes for which a summons may be issued.)

Previous case law authority supports the proposition that the Internal Revenue Service cannot use a summons to conduct tax investigations when the identity of the taxpayer is not known and where there is no evidence to indicate that any tax liability exists.

In *Mays* v. *Davis,* 7 F. Supp. 596 (W.D. Pa., 1934) the Internal Revenue Service sought information from a bank concerning the names of beneficiaries of a trust created by a will. In that case, the Internal Revenue Service argued that the information that they would receive from this summons would contribute in determining the correctness of certain tax returns. The bank resisted the summons, arguing that the statutory authority of the predecessor to Section 7602 did not authorize the Internal Revenue Service to seek such private information without further indication that a tax investigation was under way. The Court agreed with the bank, saying that to grant approval of this summons "would be to grant a mere explanatory search for information on the part of the petitioner and that not being within the law, that the petition should be refused". At p. 596.

Similarly, in the case of *McDonough* v. *Lambert,* 94 F.2d 838 (1st Cir., 1938), the Internal Revenue Service served a summons on a corporate treasurer for the purpose of determining certain information about the corporation's tax return. The summons also sought information concerning certain payees of corporate funds.

The Court, in that case, refused to order enforcement of the summons as it applied to information about third parties because it was the corporation's tax liability which was being investigated, and information about the third parties would not affect that tax liability. The Court said,

> We do not think the provisions of this section can be given such a broad construction; that by its terms it is more limited in scope and confined to the procurement of evidence, oral or documentary, bearing upon matters required by law to be included in a given tax return to determine the correct tax liability of the person who made the return or who failed to make one, and was not intended to authorize the procurement of evidence that might be material in verification of the tax return of some other person, not known to the Bureau of Internal Revenue, and who may or may not have a return. At p. 841.

More recently, the United States Court of Appeals for the Fifth Circuit ruled that the Internal Revenue Service cannot use its investigatory authority under Section 7602 unless a specific investigation of specific individuals has been undertaken. The Court said,

> We agree with the District Court that "[t]here must be some nexus between information sought and a specific individual before the government can compel third parties, at their own expense, to give information to the Internal Revenue Service." *United States* v. *Humble Oil & Refining Company,* 346 F. Supp. 944, 947 (S.D. Tex. 1972). Before a Section 7602 summons may issue, the IRS must have traversed the data gathering stage and initiated an investigation. See *United States* v. *Humble Oil Refining Company,* 488 F.2d 953, 960 (5th Cir., 1974).

In reviewing *Bisceglia,* the Sixth Circuit pointed out that the Internal Revenue Service may not examine and summon records in the hope of finding a person who owes a tax liability. The Court said,

> In the past, whenever the IRS has sought to use its summons power as an exploratory or identifying device to compel the production of records pertaining to a group of otherwise unidentified persons in the hope of discovering whether persons in this group may be taxpayers or, if so, may be liable for income taxes, courts have moved swiftly to arrest or curtail the attempt. *Bisceglia, supra,* p. 710-11.

The Government relies strongly on the case of *Tillotson* v. *Boughner,* 333 F.2d 515 (7th Cir., 1964) *cert. denied,* 379 U.S. 913 (1964), for the proposition that an Internal Revenue summons can be used, even though the Internal Revenue Service does not know the name of the taxpayer under investigation. In that case, an attorney had sent a check to the Internal Revenue Service with a letter explaining that the check was anonymous payment for previously underpaid taxes. The Internal Revenue Service issued a summons to the attorney for the purpose of determining the identity of this taxpayer. The lower court in this case distinguished *Tillotson* on the ground that a specific investigation of a tax liability had already begun and that, in fact, there was an admission by the taxpayer's lawyer that a tax liability existed. That situation is quite unlike this case where the Internal Revenue Service is operating on the unsupported assumption that the deteriorated $100 bills deposited in the bank had not been reported for tax purposes. It is also important to note that the Court in the *Tillotson* case was careful to distinguish the *Mays* case, so that the rule established in that earlier decision is still valid.

B. The Summons Is Invalid Because It Does Not Satisfy Any of the Four Conditions Contained in the Statute as Proper Grounds for the Issuance of Such Summons.

Section 7602 (see Appendix) provides that the Secretary or his delegate may (1) examine books and records, (2) summons persons having books and records to produce such materials and give testimony, and (3) take testimony of the taxpayer concerned, for any one of the four specific purposes. These four purposes are:

(1) Ascertaining the correctness of any return,

(2) Making a return where none has been made,

(3) Determining the liability of any person for any Internal Revenue tax, or

(4) Collecting any such liability.

We strongly contend that the summons in this case was not issued for any of the purposes listed. Indeed, after reviewing the four permissible purposes for which a summons may be used, the Sixth Circuit concluded that, "The IRS has not made the demonstration requisite for the enforcement of a summons". *Bisceglia, supra,* p. 712.

Taking the purposes set forth in the statute in order, first, for a summons to be issued for the purpose of ascertaining the correctness of any return, the IRS must have a return in their possession which they have selected for verification. In this case the IRS is not reviewing any specific tax return.

Second, and similarly, a summons cannot be issued for the purpose of compiling information to make a return where none has been made unless the IRS has established that a taxpayer has failed to file a return. There is no evidence that a taxpayer has failed to file a return in this case.

Third, it is possible that this summons has been issued for the purpose of determining the liability of any person for any IRS tax. *We contend that no summons may be issued for this purpose unless the IRS either*

(1) *knows the identity of the taxpayer being investigated, or*

(2) *has some evidence that there is a tax liability yet unsatisfied.*

In this case, neither of these alternative prerequisites are met. The IRS does not know the identity of the taxpayer being investigated, and it does not have the slightest evidence that there is any tax due to the Government for failure to report as income the $100 bills deposited or exchanged in the bank. The only information that the IRS does have is that a sum of money, in somewhat deteriorated condition, has recently been deposited in a bank. The Government in its brief (pages 16 and 17) arrives at several extraordinary conclusions, which are not supported by the facts of this case, in regard to deposits of cash, particularly when they are made in old bills. While acknowledging that there is nothing illegal in using cash as an exchange medium, the Government contends that "a large sum of cash" (in this case, only $40,000) always suggests the possibility that the owner has evaded taxes. Moreover, the Government draws unsupported inferences from the fact that the bills were of a deteriorated quality, going so far as to speculate that the bills had been hidden which further contributes to the Government's inferences of possible tax evasion. Further, the Government makes the extraordinary contention that there is "a strong suggestion that *additional taxes* might be owed

by the owner of [this] cash hoard"—a suggestion that is totally unsupported by the facts of the case.

The mere fact of a deposit or exchange of $40,000 in old bills per se does not in any way support an inference of tax evasion or any other unsatisfied tax liability. The Government through these thinly contrived inferences seeks to establish a basis for conducting a tax investigation and for determining the identity of "an unknown potential taxpayer" through the use of a summons issued in the name of "John Doe".

Thus, we urge that the assumption that there was a tax liability owing to the Government in this case is completely unfounded. There is an unlimited number of reasonable circumstances in which a person would deposit or exchange a large number of old $100 bills in a bank which have nothing to do whatever with evasion of Federal income taxes. There is no evidence in this case to refute a presumption that the circumstances surrounding these deposits were proper and legal, nor is there any evidence to establish a tax liability which should be investigated by the Internal Revenue Service.

Under the two alternative prerequisites stated above (i.e., identity of the taxpayer or some evidence of tax liability), the IRS does not have sufficient grounds for issuing a summons for the purpose of "determining the liability of any person". If this Court were to give a broader reading to this provision of the Code, the IRS would be able to investigate anyone, for any purpose, without any requirement of establishing a nexus between established facts and an existing, unsatisfied tax liability. The IRS would be able to investigate any

person engaged in any transaction which *might* not have been properly reported for income tax purposes. This kind of general authority is inconsistent with the scheme established under Section 7602 which contains four specific conditions under which the IRS is authorized to conduct investigations.

If the Court employs the two alternative prerequisites discussed above, it will find a line of consistency in the previous case law.[1] Under the above interpretation, the summonses issued in *May* v. *Davis, McDonough* v. *Lambert,* and *U.S.* v. *Humble Oil & Refining Company* would be invalid because in those cases neither the identity of the person to be investigated, nor the fact that any tax liability existed was established by the IRS. And the courts in those cases *did rule* that the summonses were invalid. Conversely, the "no name" summonses in the case of *Tillotson* v. *Boughner,* which the Court upheld, would be valid under the above cri-

[1] This two-part test would also shed some light on court decisions handed down since the Sixth Circuit decision in *Bisceglia.* In *United States* v. *Armour,* 74-1 U.S. Tax Court Par. 9479 (D. Conn. 4/25/74), it was undisputed that additional tax would be owed by many of the stockholders of the Hartford Fire Insurance Company because the IRS had reversed itself on an earlier ruling which had approved as tax-free an exchange of stock transaction involving those stockholders. In that case the Government sought to obtain the names of the stockholders from bank records. The Court in *Armour* upheld the use of the summons even though the IRS did not have the names of the stockholders because it was clear that there was a tax liability to be investigated. While we do not approve the use of "no name" summonses in any circumstance because, *inter alia,* such a device provides access to the financial records of a very large number of bank customers, we recognize, as have the Federal Courts, that in some situations such as *Armour* the IRS may actually be investigating a tax liability of a specific person and yet not have his name. In that circumstance a summons would be valid under the two alternative tests offered above. Thus there is no real conflict between the decisions in *Bisceglia* and *Armour.*

teria because even though the IRS did not know the name of the taxpayer it sought to investigate, the IRS had established that a tax liability did exist, that its payment was at least delinquent and perhaps partially unsatisfied, and that a criminal prosecution might be appropriate. These facts were established because the check sent by the taxpayer's attorney was for taxes due and payable. It is important to note that the District Court in the *Tillotson* case distinguished *McDonough* and *Mays* on this ground. The Court said,

> Moreover, these cases [*McDonough* and *Mays* and others] are factually distinguishable because in none did the Commissioner have reason to believe that unpaid taxes were owed by a taxpayer whose name he did not know, and in none did a taxpayer admit his tax liability while concealing his identity. See 225 F. Supp. 45, (N.D. Ill. 1963).

We believe that the case before this Court is similarly distinguishable from the *Tillotson* case and that, under the two-part test mentioned above, the summons was not properly issued for the purpose of "determining the tax liability of any person".

Fourth, and finally, the IRS has not contended in this case that they are collecting a tax liability. Therefore, the fourth purpose for the issuance of a summons under Section 7602 does not apply to this case.

In light of the foregoing analysis of the application of the statute to the facts of the case, it is to be concluded that the IRS summons was not issued for any one of the four specific purposes set forth in Section 7602. Therefore, we argue that the summons is invalid since it does not satisfy the conditions contained in the statute establishing proper grounds for the issuance of the summons.

C. The Summons Issued to the Bank Cannot Be Justified Under the Authority of Section 7601 of the Code.

The summons issued to the bank in this case (Form 2039) cites Section 7602 of the Internal Revenue Code, which is entitled, "Examination of Books and Witnesses". From this reference one can only assume that this particular summons is issued under the authority of Section 7602. Nowhere on Form 2039 is there any reference to Section 7601. It is our contention that Section 7601 (see Appendix) cannot provide the IRS with any statutory authority for the issuance of the summons in this case.

However, when this case was appealed to the Sixth Circuit, the Government attempted to cite both Section 7601 and Section 7602 as authority to conduct the investigation proposed in this case. The Government has made the same argument in its brief to this Court (pages 6 & 9). The Government argues that Section 7602 merely elaborates and specifies some of the investigative powers granted to the Secretary in furtherance of the duties placed upon him under Section 7601(a).

In support of the argument that Section 7601 cannot be used as a basis for issuing summonses such as the one that was issued in this case, we cite the decisions of the Fifth and Sixth Circuits, both of which have recently ruled that Sections 7601 and 7602 are not coterminous.

In ruling on the *Bisceglia* case, the Sixth Circuit stated that Section 7601 did not give the Internal Revenue Service broad authority to issue IRS summons. The Court said,

> Section 7601, however merely "flatly imposes upon the Secretary the duty to convey and in-

> quire." *Donaldson* v. *U.S.*, 400 U.S. 517, 523 (1971). Accordingly, we do not believe that Congress intended to provide in this section grounds additional to those specified in Section 7602 for the issuance of a summons. At p. 708-9 n. 3.

In *United States* v. *Humble Oil & Refining Company, supra,* the Fifth Circuit considered a situation where the IRS attempted to use a Section 7602 summons for the purpose of conducting a research project under Section 7601. The Court refused to permit the Internal Revenue Service to treat these two sections of the Code as supplements to each other. The Court said,

> Thus, we hold that the Internal Revenue Service is not empowered by Section 7602 to issue a summons in aid of its Section 7601 research projects or inquiries, absent an investigation of taxpayers or individuals and corporations from whom information is sought. Section 7602 simply cannot be read to give the IRS an unrestricted license to enlist the aid of citizens in its data gathering projects. At pp. 962-963.

Thus, we conclude that Section 7601 cannot be used as a basis to justify the issuance of a summons to determine the identity of a potential taxpayer. The only section of the Internal Revenue Code which can be used for this purpose is Section 7602. In other parts of this brief we have argued that the Internal Revenue Service has not satisfied the requirements of Section 7602 for the purpose of issuing the summons which the bank received.

The Government, in its brief filed with this Court (pages 20-22), has further attempted to find statutory

65-738 O—76——11

authority for the issuance of a "no name" summons in this case in the general administration and enforcement statutes of the Code, such as Sections 7801(a), 7802, 6201(a), and 6301. The Government had not sought to use these sections of the Internal Revenue Code as authority for the issuance of the summons in this case or in previous cases. We suggest that these very general statutes are even less relevant than Section 7601 to the scope of the authority of the Internal Revenue Service to issue a summons as part of a tax investigation. We maintain that these general statutes cannot be read to overcome the specific language contained in Section 7602 concerning the purposes for which the IRS may issue a summons.

D. Requiring the IRS Either To Identify the Taxpayer or To Specify that a Tax Liability Does Exist, Will Not Unduly Hamper the IRS in the Performance of Its Duties.

The Government has contended in its brief (page 8) that the ruling of the Sixth Circuit in this case "would seriously undermine the ability of the Internal Revenue Service to insure that all Federal taxes due are reported and paid". In the first instance, we find no information which would support the accuracy of that statement. In cases where the IRS has determined that, in fact, a tax liability does exist, it will be able to issue a summons even though it may not know the name of the taxpayer being investigated. See for example, *Tillotson* v. *Boughner, supra* and *United States* v. *Armour, supra.* Thus, the only situation in which the IRS might be restricted from conducting investigations is where the IRS obtains information concerning a particular transaction in which it does not know the name of the parties to the transaction, *and in which it can only sur-*

mise that a tax liability theoretically might be owing without any evidence of such liability.

Second, in spite of the statutory duties of the Internal Revenue Service concerning the collection of taxes due to the United States, it is clear that there are limitations placed on the authority of the IRS to use Section 7602 summonses to conduct tax investigations.

For example, the Fourth Amendment prohibition against unreasonable searches and seizures applies to every investigation by the Government, including administrative summonses issued by the Internal Revenue Service (See Part II, p. 21.) In addition, the Supreme Court has acknowledged that the recipient of a summons can resist its enforcement on the ground that the material is sought for the improper purpose of obtaining evidence in a criminal prosecution or for obtaining evidence that is protected by the attorney-client privilege. *Reisman* v. *Caplin,* 375 U.S. 440-449 (1964). Further, Congress did not give the IRS absolute authority to investigate the payment of income taxes without any restriction. Section 7602 specifies four particular purposes for which an examination may be conducted. That section *cannot* be read so as to infer that the IRS may make a tax investigation at any time, for any purpose, even though it is pertinent to the collection of taxes which *might* be due to the United States. Thus, the Government's statement that the IRS will be hampered in its ability to perform unless it can use the so-called "no name" summons virtually without limit to identify potential taxpayers is without merit.

II.

THE "NO NAME" SUMMONS ISSUED BY THE INTERNAL REVENUE SERVICE REQUIRING THE BANK TO PRODUCE RECORDS IS INVALID AND CONSTITUTES AN UNREASONABLE SEARCH IN VIOLATION OF THE FOURTH AMENDMENT

The first issue in this case involves the interpretation of the statute which authorizes the Internal Revenue Service to examine and/or summons records. We also urge that there are compelling constitutional limitations on the Secretary's authority to examine records. These limitations have been transgressed in the case of the "no name" summons served on the Commercial Bank, Middlesboro, Kentucky.

The courts have previously indicated that the principles of the Fourth Amendment apply to the investigations conducted by administrative agencies and, specifically, to the IRS summonses such as the one issued in this case. In *Oklahoma Press Publishing Company* v. *Walling,* 327 U.S. 186, 208 (1946), the Supreme Court indicated that the Fourth Amendment required that the Government particularly describe the material requested and that the material requested must be relevant to the inquiry being conducted. In discussing the applicability of constitutional safeguards to subpoenas for corporate records, this Court stated,

> . . . and the Fourth, if applicable, at the most guards against abuse only by way of too much indefiniteness or breadth in the things required to be "particularly described," if also the inquiry is one the demanding agency is authorized by law to make and the materials specified are relevant. The gist of the protection is in the requirement, expressed in terms, that the disclosure sought shall not be unreasonable. At p. 208.

The principles of this Court's decision in that case were applied to an IRS summons in the case of *United States* v. *Dauphin Deposit Trust Co.*, 385 F.2d 129 (3rd Cir., 1967).

The relevancy requirement has been a long standing test of the validity of an IRS summons. The general rule is that bank records are relevant to tax investigations. See *United States* v. *First National Bank of Mobile*, 295 F.142 (S.D. Ala., 1924), *aff'd. without opinion*, 267 U.S. 576 (1925). However, the relevancy requirement has been clarified so that a more specific determination of relevancy must be made. Thus, the IRS may not investigate all of the records of a third party on the ground that such records are relevant to the tax liability of a given taxpayer. See for example, *Hubner* v. *Tucker*, 245 F.2d 35 (9th Cir., 1957), where the Court said,

> It has heretofore been held that, so far as a member of the general public is concerned, not a taxpayer, the privilege against an unreasonable search and seizure should be given great effect. Echoes of the American Revolution are found in this protest against a general warrant which permits the search and seizure of all the papers of an individual. We do not believe that, simply because some taxpayer may have had a grocery account entered upon the books of the grocer, the intention of Congress was to allow the Internal Revenue Service to investigate all the records of the grocer on the theory that some of them might be relevant to the inquiry of the tax status of another person. At p. 41.

We urge upon the Court the consideration that the relevancy test applied in *Hubner* v. *Tucker, supra,* which was recognized by this Court as one of the prin-

cipal ingredients of the requirement that "the disclosure shall not be unreasonable" in *Oklahoma Press Publishing Company, supra,* is particularly applicable to the facts of the *Bisceglia* case. In *Hubner,* although the Government knew the identity of the taxpayer, it sought to examine all of the records of a third party on the theory that some of them might be relevant to the taxpayer's unsatisfied tax liability. The Ninth Circuit rejected the validity of this investigation on the ground that these records were not shown to be relevant and that therefore the investigation was unreasonable. In the instant case, *without* knowing the identity of the taxpayer, the Government sought to examine all deposit and cash tickets of every depositor who made a deposit in excess of a certain amount during a thirty-day period. We urge upon the Court that the extreme breadth of this inquiry should be held to be invalid on the ground that the deposit records of a large number of depositors other than the potential taxpayer have not been shown to be relevant to an investigation to establish the identity of a single taxpayer.

In *United States* v. *Harrington,* 388 F.2d 520 (2nd Cir., 1968), the Court of Appeals indicated that the appropriate test for relevancy was "whether the inspection sought might have thrown light upon the correctness of the taxpayer's return". It is also to be emphasized that the question of relevancy is not satisfied by a simple declaration by the Internal Revenue agent. See *Hubner* v. *Tucker, supra.*

As we discussed previously, we do not believe that the IRS has established any evidentiary connection between the deposits or exchanges of $40,000 in deteriorated $100 bills and the tax liability of any person. There is no foundation for the assumption that because the

bills are in a deteriorated condition they are unreported for tax purposes. The IRS is simply engaging in a fishing expedition in the hope of finding some tax liability which may or may not exist. Such a fishing expedition, without any demonstration of how these transactions relate to the non-payment of taxes or the correctness of a tax return, violates the relevancy requirement which is embodied in the Fourth Amendment prohibition against unreasonable searches by the Government.

We also urge that the summons was insufficient in its description of the information sought for the purpose of determining the identity of one potential taxpayer and that, accordingly, it has failed to meet the particularity requirement established in *Oklahoma Press Publishing Company, supra.* In *Bisceglia* the IRS sought to examine the deposit records of the bank for the period October 22 through November 13, 1970 (later modified by the District Court to cover the period October 16 to November 16, 1970). The bank received deposit tickets and/or cash tickets at the rate of approximately 1,800 to 2,200 tickets a day during that period. Even if it were possible to examine all of the bank's records during that period, there still may be no indication as to where the money came from. Further, the IRS has not supplied any name or account number with which the bank might be more readily able to provide the information sought. As stated above, the breadth of this investigation covering the deposit records of a large number of bank customers clearly jeopardizes their right against unreasonable searches under the Fourth Amendment. Moreover, to request the bank to produce such a large volume of records to identify a single potential taxpayer would be to put an unreasonable burden on the bank. Such unreasonable burdens are prohibited by the Fourth Amendment.

Thus, we urge that the summons issued in this case is invalid and violates the Fourth Amendment prohibition against unreasonable searches, both on the ground that the Government has not established the relevancy of the records sought, and on the ground that the large number of records sought would jeopardize the constitutional rights of other bank customers and would impose an unreasonable burden on the bank.

CONCLUSION

The American Bankers Association respectfully urges the Court to affirm the decision of the United States Court of Appeals for the Sixth Circuit, and hold that the "no name" summons issued to the Commercial Bank of Middlesboro, Kentucky was invalid for the reasons stated in this brief.

Respectfully submitted,

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APPENDIX

Section 7601(a) and Section 7602 of the Internal Revenue Code of 1954

SEC. 7601. CANVASS OF DISTRICTS FOR TAXABLE PERSONS AND OBJECTS.

(a) GENERAL RULE.—The Secretary or his delegate shall, to the extent he deems it practicable, cause officers or employees of the Treasury Department to proceed, from time to time, through each internal revenue district and inquire after and concerning all persons therein who may be liable to pay any internal revenue tax, and all persons owning or having the care and management of any objects with respect to which any tax is imposed.

SEC. 7602. EXAMINATION OF BOOKS AND WITNESSES.

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

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

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

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

IN THE

United States Court of Appeals

FOR THE THIRD CIRCUIT

75-1480

UNITED STATES OF AMERICA and WILLIAM L. BEERMAN, Special Agent, Internal Revenue Service,
Petitioners-Appellees-Cross Appellants

v.

PITTSBURGH NATIONAL BANK, MELLON BANK, N.A. and EQUIBANK, N.A., *Respondents-Cross Appellees*

v.

MORRIS KIRSHENBAUM and JOY KIRSHENBAUM,
Intervenors-Appellants-Cross Appellees

On Appeal from the Order of the United States District Court for the Western District of Pennsylvania

BRIEF FOR THE AMERICAN BANKERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF THE RESPONDENTS-CROSS APPELLEES

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TABLE OF CONTENTS

Page

ISSUE PRESENTED FOR REVIEW 1

STATEMENT OF THE CASE 2

STATEMENT OF THE FACTS 3

INTEREST OF AMICUS CURIAE 5

SUMMARY OF THE ARGUMENT 7

ARGUMENT 8

REIMBURSEMENT ISSUE 8

I. The Federal courts will not enforce an Internal Revenue Service summons which imposes an unreasonable financial burden on a third party record holder 8

II. Federal courts should consider factors which take into account the unique situation of banks in processing Internal Revenue Service summons of customer records in order to determine whether a summons constitutes an unreasonable financial burden on a bank, and whether an order for reimbursement can be supported 13

A. The nature and complexity of bank customer records 14

B. The costs to banks to respond to summonses 19

C. The cumulative burden of IRS summonses. 25

D. The banks' duty of maintaining the confidentiality of bank customer records 27

CONCLUSION 31

TABLE OF CITATIONS

CASES:

California Bankers Association v. *Schultz*, 416 U.S. 21 (1974) 14

Page

First National Bank of Mobile v. *United States*, 160 F.2d 532 (5th Cir. 1947) 10
Fox v. *House*, 29 F. Supp. 673 (E.D. Okla. 1939) 12
Hurtado v. *United States*, 410 U.S. 578 (1973) 26
Peterson v. *Idaho First National Bank*, 83 Ida. 578, 367 P.2d 284 (1961) 29
Reisman v. *Caplin*, 375 U.S. 440 (1964) 9
United States v. *Bisceglia*, 420 U.S. 141 (1975) 9
United States v. *Continental Bank & Trust Company*, 503 F.2d 45 (10th Cir. 1974) 6, 12, 27
United States v. *Dauphin Deposit Trust Company*, 385 F.2d 129 (3d Cir. 1967), *cert. den.* 390 U.S. 921 (1968) 10, 24
United States v. *Davey*, 426 F.2d 842 (2d Cir. 1970).. 12
United States v. *Easter*, C.A. #3286 (D. N.H. 1971).. 12
United States v. *Farmers & Merchants Bank*, C.A. #74-1490-F (C.D. Cal. August 5, 1975) .. 10, 11, 12, 24
United States v. *First National Bank of Fort Smith*, 173 F. Supp. 176 (W.D. Ark. 1959) 10, 11
United States v. *Jones*, 351 F. Supp. 132 (M.D. Ala. 1972) 12, 27
United States v. *Northwest Pennsylvania Bank & Trust*, 355 F. Supp. 607 (W.D. Pa. 1973).... 11, 29, 30
United States v. *Powell*, 379 U.S. 48 (1964) 10
United States v. *Puntorieri*, 379 F. Supp. 332 (E.D. N.Y. 1974)..... 10
United States v. *Third Northwestern National Bank*, 102 F. Supp. 879 (D. Minn. 1952) 17
United States v. *Zions First National Bank*, 75-2 U.S.T.C. ¶9581 (D. Utah 1975) 26

STATUTES:

Bank Secrecy Act, Public Law 91-508, 84 Stat. 1114.. 14

Dockery Act of July 31, 1894, C. 174, 28 Stat. 207, 31 U.S.C. 74 11

Fair Credit Reporting Act, 15 U.S.C. 1681 *et seq.* ... 10

Table of Citations continued iii

Page

Internal Revenue Code of 1954 (26 U.S.C.)
Section 7402 ..... 2, 9
Section 7602 ..... 2, 3, 9, 11
Section 7603 16

MISCELLANEOUS:

43 Comp. Gen. 110 (1963) 12

*Fed. R. Civ. P. 45(b) 7, 11, 12

Wigmore, *Evidence* 26

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* Principle Reliance

IN THE

United States Court of Appeals

FOR THE THIRD CIRCUIT

75-1480

UNITED STATES OF AMERICA and WILLIAM L. BEERMAN, Special Agent, Internal Revenue Service,
Petitioners-Appellees-Cross Appellants

v.

PITTSBURGH NATIONAL BANK, MELLON BANK, N.A. and EQUIBANK, N.A., *Respondents-Cross Appellees*

v.

MORRIS KIRSHENBAUM and JOY KIRSHENBAUM,
Intervenors-Appellants-Cross Appellees

On Appeal from the Order of the United States District Court for the Western District of Pennsylvania

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BRIEF FOR THE AMERICAN BANKERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF THE RESPONDENTS-CROSS APPELLEES

ISSUE PRESENTED FOR REVIEW

Whether the District Court erred in requiring the Internal Revenue Service to reimburse third-party banks for the cost of burdensome administrative summonses issued in the course of a tax investigation of bank customers.[1]

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[1] There are other issues before this Court in this case. However, this Amicus Curiae brief submitted by the American Bankers Association is limited to the reimbursement issue. Our decision to limit the brief should not be construed as implying anything about the other issues involved.

STATEMENT OF THE CASE

Internal Revenue Service Special Agent William L. Beerman served three IRS summonses, one each to Pittsburgh National Bank, Mellon Bank, and Equibank, requesting records relating to Morris and Joy Kirshenbaum and the Ivy School of Professional Arts, Inc., for the tax years 1969-1972. Upon notification by each of the banks that the summons had been issued, the taxpayers filed a complaint in the United States District Court for the Western District of Pennsylvania seeking to quash the summonses. The District Court ruled that the plaintiffs had no standing to maintain the action since they were not named as parties to the summonses. See *Kirshenbaum* v. *Beerman*, 376 F. Supp. 398 (W.D. Pa. 1974).

The three banks which had received the summonses subsequently refused to comply with them. The IRS then brought an action in the District Court under the authority of sections 7402(b) and 7602(a) of the Internal Revenue Code to enforce the summonses.

At this point the taxpayers were permitted to intervene in the case to represent their own interest. During the course of the hearings in the District Court on this action, the IRS substituted six new summonses replacing the original three. The substituted summonses requested the same information as the original summonses, but offered government personnel to search and copy the bank records, and indicated that all of the information did not have to be produced at once.

The three banks challenged the summonses on three principal grounds. First, they raised the question of whether the investigation was being conducted pursuant to legitimate purposes. Second, they questioned whether the information sought was relevant to the investigation. Third, the banks objected to the scope and breadth of the summonses, arguing that they constituted an unreasonable financial burden on the banks. The District Court enforced the substituted summonses except that the IRS was denied access to the safety deposit box records on the

grounds that an administrative summons cannot be used to obtain information which can only be used in a criminal proceeding. The District Court also rejected the proposal of the Internal Revenue Service that IRS personnel and equipment could be used to conduct the searches in the three banks for the records requested. In order to protect the banks from the unreasonable financial burdens which would be incurred in responding to these summonses, the District Court ordered the Internal Revenue Service to reimburse the banks for their cost of record search, retrieval, and production. The District Court opinion in this case is officially reported *sub nominee United States* v. *Friedman*, 388 F. Supp. 963 (W.D. Pa. 1975).

The taxpayers appealed this case to this Court of Appeals on the grounds that the District Court erred in finding there was a legitimate purpose for the tax investigation. The Government has cross-appealed on the reimbursement issue and on the question of production of records which pertain to entry to the safety deposit boxes.

STATEMENT OF FACTS

On December 11, 1973, three Internal Revenue Service summonses (Treasury Form 2039) were issued by IRS Special Agent William L. Beerman to Pittsburgh National Bank, Mellon Bank, and Equibank under the authority of section 7602 of the Internal Revenue Code. The summonses requested all books, records, correspondence or memoranda relating to transactions with Morris and Joy Kirshenbaum and the Ivy School of Professional Art, Inc. for the years 1969-1972. Each of the three banks duly notified their taxpayer customers of the IRS summonses. The customers sought to enjoin the IRS from obtaining these records with the administrative summonses. However, their suit was dismissed for lack of standing. The banks refused to comply with the summonses and the IRS brought this action to enforce the summonses in the United States District Court.

65-738 O—76——12

During the course of the trial the IRS substituted six new summonses to replace the original three. The substituted summonses again requested all books, records, correspondence or memoranda relating to transactions with Morris and Joy Kirshenbaum and the Ivy School of Professional Art, Inc. for the years 1969-1972. The summonses specified in particular but were not limited to the following records:

(1) Ledger sheets of savings and checking accounts, open or closed, and signature cards of each account.

(2) Original deposit tickets and cancelled checks.

(3) Account ledger sheets of loans and mortgages together with loan and mortgage applications and financial statements submitted in support thereof.

(4) Safe deposit box applications, signature cards, and entry records.

(5) Cashier's checks.

(6) Trust agreements, purchase and sale of stock and/or bonds, and related documents.

(7) Records of certificates of deposits.

(8) Records of savings certificates.

In addition, the substituted summonses contained an offer by the Internal Revenue Service to supply its own personnel to carry out the search of each bank's records and to provide its own copying facilities. The IRS further offered that in the event the banks elected to use their own personnel to search their records, the IRS would not require that all of the records be produced at one time. The IRS was willing to examine only the items listed above as 1, 3, and 4. The IRS indicated that it might be able to limit the scope of the examination of the other items after reviewing the initial material requested.

The banks again refused to comply with the substituted summonses on several grounds which were presented to

the District Court in the enforcement hearing brought by the Internal Revenue Service.

At trial the District Court received into evidence a substantial amount of information concerning the reimbursement issue. The Court heard evidence on the complex record maintenance procedures of the banks and the cost to the banks of retrieving information from their record systems. For example, see the testimony of Richard L. Lechnar, Assistant Operations Officer and Manager of the Records Management Section of Mellon Bank, R. 293-A *et. seq.* The Court also heard evidence on the confidential nature of bank records and the duty owed by the banks not to disclose the customer's financial records, except under compulsion of law. See Lechnar testimony, R. 313-A. Further, there was evidence at trial as to the number of summonses received by the banks in the last year. See for example, the testimony of Robert Brubaker, Vice President of Operations, Equibank, R. 349-A. All of this information was admitted into evidence in spite of objections by Counsel for the Government that the information was not relevant to the question of whether the six summonses in this case constitute an unreasonable financial burden.

INTEREST OF AMICUS CURIAE

The American Bankers Association is a national trade association representing approximately 14,000 commercial bank members. These banks, operating under both Federal and state charters, comprise virtually the entire commercial banking system of the United States.

The key issue before the Court in this case is whether costs incurred by the banks, which are third party record holders, in responding to an administrative summons of the Internal Revenue Service for bank records in Federal tax investigations of bank customers constitute an unreasonable financial burden on the bank and whether the IRS should be required to reimburse the banks for such costs. The outcome of this case will depend upon the application of general principles of law to the unique and

highly complex nature of bank customer records. The purpose of the Amicus Curiae brief in this case is to present this Court with information on the manner in which banks maintain customer records, information pertaining to the nature and extent of costs which banks incur in responding to an IRS summons for bank customer records, and the legal aspects of the relationship between a bank and its customers in connection with such records.

Over a period of years, the American Bankers Association has received many inquiries from its member banks concerning the manner in which banks should respond to an administrative summons of the Internal Revenue Service and the extent of the costs which must be borne by a bank in searching for and retrieving the records requested in these administrative summonses. It appears that a few banks have received some reimbursement under informal arrangements with IRS district offices; however the great majority of banks have been unable to obtain any kind of payment for the costs of record search and retrieval.

This is the second case involving this issue to reach a United States Court of Appeals. In the first case, *United States* v. *Continental Bank & Trust Co.*, 503 F.2d 45 (10th Cir. 1974), the Court simply reviewed the denial of a request for reimbursement. There was no finding of fact by the District Court in that case of undue financial burden which would sustain a full consideration of reimbursement as an appropriate remedy.

In contrast, the District Court in the present case did find justification for reimbursement. Therefore, the facts of the present case provide a more appropriate background for a discussion of reimbursement as a correct remedy. The decision in this case will affect the expenses that third party banks will be expected to bear in handling IRS summonses. Because of the impact of this decision on commercial banks, the American Bankers Association on behalf of its membership is vitally interested in the outcome of this case.

SUMMARY OF THE ARGUMENT

The District Court ruled that the three respondent banks should not have to bear the financial burden of the six summonses received from the Internal Revenue Service as part of a tax investigation of bank customers. The remedy applied by the Court of requiring reimbursement for the banks' expenses served a twofold purpose; i.e., (1) to induce the Internal Revenue Service—with the carrot of its own budget constraints—to review and limit the summonses only to information necessary in the investigation, and (2) to protect the banks from having to absorb record search and retrieval costs beyond what should be reasonably required.

The Government contends that this finding and ruling by the District Court was in error. We disagree with the Government on this issue and believe that there are compelling factual and legal grounds for the District Court's ruling.

As a general principle, the authority of the IRS to issue an administrative summons is not without limit. There are many constraints on that authority which are not spelled out in the statute. The constraint with which we are concerned in this case is that an IRS summons cannot impose an unreasonable financial burden on a third party witness. A District Court is free to construct a remedy which will protect the witnesses. The three remedies available to the Court are, (1) refusing to enforce the summons, (2) modifying the summons, and (3) requiring the moving party (the IRS) to pay the costs of production of the records sought. These remedies are identical to the procedures available in Rule 45 of the Federal Rules of Civil Procedure to protect persons summoned by a subpoena duces tecum.

In determining whether an unreasonable financial burden existed, the District Court heard evidence at trial on several key factors, i.e., the complexity of the records maintenance system used, typical expenses incurred by each bank in responding to a summons, the number of sum-

monses received by the banks each year, and the confidential nature of the customer records kept by the banks. It is implicit in the Court's decision that these factors were found persuasive on whether the summonses in this case were unreasonable. Indeed, the American Bankers Association strongly contends that these factors should always be considered in determining whether a summons issued to a bank constitutes an unreasonable financial burden. They are:

(1) The nature and complexity of bank customer records;

(2) The cost to the banks of record search and retrieval;

(3) The cumulative burden of IRS summonses; and

(4) The banks' duty to maintain the confidentiality of bank customer records.

When the broad summonses issued in this case were analyzed together with the evidence on these four factors, the burden on the banks was found to be excessive. The banks would have incurred unreasonable costs if they were required to supply all of the information requested in the six summonses. The IRS procedures in this case failed to take into account the complex nature of the banks' customer records in processing the IRS summonses. It would seem inappropriate that the banks should be expected "to pick up the tab" for this IRS investigation as a cost of doing business. Finally, the offer of IRS to supply its own personnel to conduct an investigation should not be permitted to mitigate the unreasonable financial burden, due to the confidential relationship existing between a bank and its customers.

ARGUMENT

I.

The Federal Courts Will Not Enforce an Internal Revenue Service Summons Which Imposes an Unreasonable Financial Burden on a Third Party Record Holder.

The authority of the Internal Revenue Service to issue an administrative summons for records to a third party is subject to reasonable limitations for the protection of

the third party. This protection is afforded to witnesses summoned under section 7602 through the operation of the enforcement procedure.

The Internal Revenue Service has neither the power to enforce the summons nor the power to impose sanctions for non-compliance. See *Reisman* v. *Caplin*, 375 U.S. 440, 445 (1964). If the IRS wishes to enforce a summons, it must invoke the jurisdiction of the United States District Court as provided in section 7402(b) of the Code. A hearing is then held during which the witness may show cause why the summons should be narrowed or should not be enforced at all. The Supreme Court has stated several times that the purpose of this enforcement proceeding is to protect third party witnesses against abuse of the IRS administrative summons power.

> Any enforcement action under this section would be an adversary proceeding affording a judicial determination of the challenges to the summons and *giving complete protection to the witness. Reisman* v. *Caplin, supra,* at 446 (emphasis supplied)

and,

> Substantial protection is afforded by the provision that an Internal Revenue Service summons can be enforced only by the courts . . . . Congress has provided protection from arbitrary or capricious action by placing the Federal courts between the Government and the person summoned. *United States* v. *Bisceglia,* 420 U.S. 141, 146, 151 (1975).

The Federal Courts have recognized several grounds which serve as a basis for challenging an IRS summons. In cases where the challenge has been established, the courts have fashioned a remedy designed to protect the witness from the unauthorized reaches of the IRS summons. Some examples of these abuses which require court protection include, (a) summons for material subject to a legal privilege,[2] (b) summons issued solely for the pur-

[2] *Reisman* v. *Caplin, supra,* at 449.

pose of conducting a criminal investigation,[3] (c) summons for records not relevant to the tax investigation,[4] (d) summons which does not sufficiently describe the records requested,[5] (e) summons which imposes an undue financial burden on the witness,[6] and (f) summons which request records subject to the Fair Credit Reporting Act.[7] The basis for the challenge to the summonses raised by the three banks in this case is that they are seeking protection from unreasonable summonses—in this case by requesting reimbursement for their expenses incurred in responding to summonses that would otherwise constitute an unreasonable financial burden.

The principal cases which are cited for the proposition that the Internal Revenue Service cannot impose an unreasonable financial burden of compliance upon banks (or other witnesses) are *United States* v. *Dauphin Deposit Trust Company,* 385 F.2d 129 (3d Cir. 1967) *cert. den.* 390 U.S. 921 (1968), and *United States* v. *First National Bank of Fort Smith,* 173 F. Supp. 716 (W.D. Ark. 1959). In these cases, it is clear that a bank can challenge a summons on the ground of undue financial burden and that if such burden is proved, the Court will not enforce the summons without protecting the bank from the costs.

The recent decision in *United States* v. *Farmers & Merchants Bank,* Civil Action #74-1490-F (C.D. Cal. August 5, 1975) contains one measure of what constitutes an unreasonable financial burden on the witness. In that case, the Court ruled that expenses of $2545.28 in the aid of a Government tax investigation are too great for a citizen to bear as a duty to his government. The second section of the brief discusses additional factors which should be considered in determining whether an IRS summons imposes unreasonable costs on a bank.

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[3] *Ibid.*

[4] *United States* v. *Powell,* 379 U.S. 48, 58 (1964).

[5] *First National Bank of Mobile* v. *United States,* 160 F.2d 532, 534 (5th Cir. 1947).

[6] *United States* v. *First National Bank of Fort Smith, infra.*

[7] *United States* v. *Puntorieri,* 379 F. Supp. 332 (E.D. N.Y. 1974).

Once the financial burden is found to be unreasonable, there are three possible judicial remedies—all of which are analogous to procedures available to protect a witness in a Federal Court from an unreasonable subpoena duces tecum under Rule 45(b) of the Federal Rules of Civil Procedure. First, a court could elect to refuse to enforce the summons. *See, for example, United States* v. *First National Bank of Fort Smith, supra.* Second, the Court can require the Internal Revenue Service to narrow the scope of the summons. For example, the case of *United States* v. *Northwest Pennsylvania Bank & Trust,* 355 F. Supp. 607 (W.D. Pa. 1973), involved a summons for all ledger sheets, deposit tickets, cancelled checks, and withdrawal and debit memos for the 41 individuals and also "family members" for a period of six years. In order to comply with the summons, the bank would have had to examine approximately 60,000,000 items. The Court chose to limit the summons by requiring the bank to turn over to the IRS ledger sheets and deposit tickets for *some* of the named individuals. Using these records, the IRS might be able to determine more specifically what additional information was needed.

The third remedy, which can be used in cases where the IRS insists that it needs a large volume of records, is to require the IRS to reimburse the third party record holder for the record production expenses incurred in responding to the section 7602 summons. *United States* v. *Farmers & Merchants Bank, supra.* This was the remedy ordered by the District Court in the present case to protect the banks from the unreasonable financial burden of the summonses.

The Government contends on page 28 of its brief that the IRS cannot be required to reimburse the banks without specific statutory authorization. However, the responsibility for determinations as to the legality of disbursements of public funds by Government agencies rests with the Comptroller General of the United States. 31 U.S.C. Section 74. There is a decision of the Comptroller General which is a precedent for reimbursement by the Internal Revenue Service for bank expenses such as the expenses

in this case. 43 Comp. Gen. 110 (1963). The decision states in part,

> This Office, in 1 Comp. Gen. 442, recognized that the expenses incident to compliance with a subpoena duces tecum when burdensome to the party to whom directed and such party is not a party to the suit or proceeding, should be borne by the Government where the documents needed will serve a Government purpose. At 112.

The question of whether a District Court has the authority to order reimbursement has not been seriously challenged. In fact, in several IRS summons enforcement hearings where the undue financial burden issue has been raised, the Federal courts have consistently indicated that they do have the authority to require reimbursement if they find it appropriate.[8]

Similarly, Rule 45(b) empowers a United States District Court to condition the enforcement of a subpoena duces tecum by requiring that the summoning party pay to the witness "the reasonable cost of producing the books, papers, documents, or tangible things." In some cases banks have been protected under Rule 45(b) from the financial burden of producing records in Federal court proceedings. For example, in *Fox* v. *House,* 29 F. Supp. 673 (E.D. Okla. 1939), a subpoena duces tecum, issued to a non-party bank for customer records, was enforced by the court only on the condition that the party seeking the records advance to the bank payment for reasonable costs. The bank customer records sought for production in the *Fox* case were the same kinds of records sought by the IRS in the present case, i.e., ledger accounts, deposit tickets, cash letters, and "any and all records and correspondence relating to said accounts," a catch-all phrase similar to the one used in the summonses in this case. Further, the *Fox* case is similar to the case before this Court in that some of the bank

[8] *See United States* v. *Continental Bank & Trust Co., supra; United States* v. *Davey,* 426 F.2d. 842 (2d Cir. 1970); *United States* v. *Farmers & Merchants Bank, supra; United States* v. *Jones,* 351 F. Supp. 132 (M.D. Ala. 1972); and *United States* v. *Easter,* C.A. #3286 (D. N.H. 1971).

records requested are in storage and will have to be retrieved by experienced employees familiar with the records. In view of the nearly identical facts in these cases, we believe that the application of the same protective remedy—reimbursement—is appropriate.

II.

Federal Courts Should Consider Factors Which Take Into Account the Unique Situation of Banks in Processing Internal Revenue Service Summons of Customer Records in Order to Determine Whether a Summons Constitutes an Unreasonable Financial Burden on a Bank, and Whether an Order for Reimbursement Is Proper Remedy.

The legal principles described above articulate only general rules relating to the authority of the Internal Revenue Service to issue summonses including the reasonable limitations on that authority, and the protective remedies which can be afforded to witnesses who receive administrative summonses. When a Federal court is asked to consider whether it should enforce an IRS summons, it must apply these general principles to the particular facts and circumstances surrounding the issuance of the summons. For example, there may be no need to issue an order protecting a witness from undue burden in the case of a onetime summons issued to a small business for employee records for a short period of time, where the records are stored in a simple vertical file. On the other hand, a protective order modifying a summons or requiring reimbursement may be necessary in a more complex situation such as a summons issued to a bank for financial records covering a long period of time, where the records are contained in a large volume of files or are maintained on microfilm as part of a sophisticated system of records maintenance.

In view of the nature of the factual and legal circumstances which surround bank records and IRS summons of those records, Federal courts should consider special factors in determining whether a bank is faced with an unreasonable burden. These special factors give recognition to the unique aspects of banking, bank records, and bank

customer relations vis-a-vis the summons authority of the Internal Revenue Service. They are

(a) the nature and complexity of bank customer records,

(b) the costs to banks of record search and retrieval in responding to an IRS summons,

(c) the cumulative burden of IRS summonses, and

(d) the banks' duty of maintaining the confidentiality of bank customer records.

In cases where the courts have given proper recognition to the nature and complexity of bank records, the costs to banks of record retrieval, the cumulative burden of summonses received by banks, and the confidentiality of bank records, the courts have afforded banks protection from unreasonable summonses. On the other hand, in cases where such criteria were not used by the courts, banks have been required to absorb the cost of unreasonable summons requests.

The following material analyzes the recent cases in this area in terms of the unique problems of banks in dealing with administrative summonses. The District Court in the instant case admitted evidence on all four of these factors in reviewing the question of unreasonable burden on the three banks. In the light of the evidence on all these points, the Court determined that the remedy of reimbursement was appropriate.

A. THE NATURE AND COMPLEXITY OF BANK CUSTOMER RECORDS

The large volume of different kinds of financial records maintained by banks increases the difficulty and expense for banks in responding to a summons. Banks are required by the Bank Secrecy Act, P.L. 91-508, to keep extensive records on customer transactions. *See California Bankers Association* v. *Shultz,* 416 U.S. 21 (1974). The maintenance of so many records complicates the record retrieval process. For example, banks must keep, for a period of five years, all checks, clean drafts, or money orders drawn on the bank or issued and payable by it. Reproductions must show face and reverse of all checks except those on which

the reverse is blank. If there is no check or draft corresponding to a pre-authorized paper entry, it is necessary to maintain the customer's authorization to charge his account and a memorandum list of entries. This requirement is waived for all checks drawn for $100 or less or drawn on accounts that normally average 100 or more checks per month over the calendar year or over 100 checks on each occasion when issued, provided these checks fall in one or more of the following categories: payroll, dividend, employee benefit, insurance claims, medical benefit, government agency, brokers or dealers in securities, fiduciary account, pension or annuity, and checks drawn on other financial institutions.

Sophisticated records maintenance systems also affect record retrieval as, for example, in the case of cancelled checks. In banks with automated systems, such as the banks in this case, checks received on a particular date are fed into the computer, which then sorts them by account number and makes the appropriate entries to the account. As the checks clear the computer, they are microfilmed, verified for signature, and filed by account. Once a month these cancelled checks are returned to the customer together with his monthly statement and deposit ticket. The bank's records consists of the microfilm copy of the cancelled checks. This microfilm copy is filed by date of transaction rather than account. To locate the microfilm copies of checks drawn on a particular account would require an individual to ascertain from the monthly statement the date on which checks were posted to an account and then review the microfilm for that date to locate the specific cancelled check or checks.

In addition to the complexity of the record keeping problems of banks, there is a further difficulty in responding to a summons because records are filed by categories rather than by customer name. For example, separate sets of files and microfilm are maintained for cancelled checks, savings account records, certificates of deposit, loans, etc. The following is a list of the kinds of bank records which

may be covered by an IRS administrative summons, most of which are maintained in separate file systems.

(1) Savings and checking account statements, signature cards, deposit and withdrawal tickets;

(2) Checks drawn and deposited;

(3) Cashier's checks and personal money orders purchased;

(4) Safe deposit box signature cards, payment records and access records;

(5) Bond transaction records;

(6) Certificates of deposit;

(7) Stock transfer records;

(8) Credit files and correspondence;

(9) Corporate resolutions;

(10) Loan agreements;

(11) Loan ledgers; and

(12) Trust account information.

Similarly, banks which operate branch offices generally maintain customer records in each branch separately, with no central record system for the entire bank. The majority of banks do not maintain customer records on a central records system. As a result of both categorization and decentralization of records, an IRS summons for "all records" of a given customer may force the bank to examine the files for each separate kind of banking transaction at each separate branch location of the bank.

In view of these complex record keeping systems, banks have a special need for the Internal Revenue Service to follow the dictate of section 7603 of the Code which states in part that

> [S]uch books, papers, records, and other data are described with reasonable certainty.

It is critical that a bank be advised precisely which bank records are sought by the IRS and at what branch these

records are located. A District Court in Minnesota gave special recognition to the "reasonable certainty" concept in the case of *United States* v. *Third Northwestern National Bank*, 102 F. Supp. 879 (D. Minn. 1952).

> The performance of the substantial job by the bank at the expense of the bank can be made reasonable and within the scope of the statute only if there is some factual indication that there is some likelihood that among some of the thousands of documents which the bank would be required to check will be papers which have a bearing on the tax liability of the taxpayer under investigation.

and

> To disregard this lack of proof, ignore the burden on the bank, and look only to the fact that tax fraud investigations must be given liberal scope would give the Government a blank summons whose limits need be drawn only by the imagination. Such a limitless right and power obviously was not intended by the statute. At 883.

The IRS Audit Manual, introduced into evidence at the trial below, gives recognition to the specificity problem in instructions to agents about drafting summonses for bank records. It states in part,

> When the summons requires the production of books and records, papers or other data, it is important that they be properly designated and described with reasonable certainty; that is, that they be specified with sufficient precision for their identification. The following are examples which are not considered legally adequate:
>
> (A) Bank books, bank statements, cancelled checks, and check stubs.
>
> (B) All books and records pertaining to the operation of the business of the witness. R. 251-A.

In spite of these IRS Audit Manual instructions, long-term experience in the banking industry clearly indicates that the majority of banks receive summonses which re-

quest "records of all transactions with the bank" or "*all books, papers, records, and other documents* relating to materials required to be included in the income tax returns of the above named individual, including, *but not limited to the following items . . . .*" (emphasis added).

The "all records" summons is typical of the great majority of administrative summonses served on commercial banks. The very broad scope of the "all records" summons—especially when viewed in the light of the complexity of bank customer records—imposes an onerous burden on banks. Most banks, particularly small and medium-sized institutions or those without tax-oriented legal counsel, do not question or challenge such summonses, but instead attempt to comply with each summons as received. In a great many cases, it is reasonable to assume that the "all records" summons involves record search and retrieval beyond that which is really necessary for the IRS tax investigation.

The dimensions of this problem are illustrated by the fact that some large banks have recently established the practice of referring all or a large number of the administrative summonses that they receive to law firms specializing in Federal income tax matters for review. This practice reflects the increasing volume and complexity of IRS administrative summonses for bank customer records and the fact that banks increasingly find it necessary to seek expert legal advice to assess the validity of the summons and whether, *ab initio,* the summons should be honored or challenged. It is gratuitous to comment that legal fees incurred by banks to review IRS administrative summonses substantially increase the cost of processing these record requests.

As noted elsewhere in this brief, the Federal courts in enforcing an IRS summons challenged by a bank frequently have narrowed the scope of the summons. Those banks that do not question IRS summonses or challenge them in the Federal courts are less apt to have the scope of each summons narrowed by the IRS. In reviewing this problem from

an industry point of view, it is the conclusion of the American Bankers Association that only the larger banks, i.e., the banks with large financial resources and with sophisticated management personnel and legal counsel, are in a position to question or challenge IRS summonses. Some do this on an informal basis with the IRS local office, with the result that the IRS narrows the summons without resorting to a court proceeding. Others, which have not been able to work out such a procedure with their IRS agents or District Offices, resort to the good faith challenge, in which case the IRS must seek enforcement under the section 7402 court proceeding.

With respect to this aspect of the problem, it may be reasonably concluded that large banks are in a better position to try to reduce excessive IRS record search costs and to afford their customers greater protection against breaches of bank record confidentiality than smaller banks which have fewer resources to deal with this complex problem. In the final analysis, IRS administrative summonses impose onerous and unreasonable cost burdens on banks.

B. THE COSTS TO BANKS TO RESPOND TO SUMMONSES

The American Bankers Association has obtained information from some of its members on the costs incurred by banks in responding to IRS summonses. First National Bank of Chicago completed a detailed study of the costs of handling summonses received in the last year. On the basis of this study it was determined that a typical summons used in the examination of a commercial account involved the following types of records, the typical periods of time for each record requested, and the cost to the bank for each item.

65-738 O—76——13

Record Requested	*Typical Period of Time*	*Cost to Bank*
Commercial Checking Account Transcripts	7 yrs.	$ 42.00
Commercial Checking Accounting Checks, Debits and Credits	3 yrs.	540.00
2 Savings Account Transcripts	6 yrs. (each)	162.00
Savings Account Deposit & Withdrawal Tickets	3 yrs. (each)	66.00
Loan Ledgers	5 yrs.	3.20
National Safe Access Tickets	2 yrs.	5.50
Records Management Employee per summons		23.60

Where all of these items are requested, as in the case of a typical business customer, the total cost to the bank is $842.30. In reviewing all summonses received in a recent 12 month period, the average cost of a summons for information from individual and commercial accounts was $225.00 per summons. Of course, the actual cost of a single summons will vary in accordance with its scope, and the breadth of the records sought by the IRS. Based on 212 summonses received annually, the total annual cost to First National Bank of Chicago is approximately $48,000.

It should be noted that the First National Bank of Chicago is a unit bank with only a main office, as it is not permitted to establish branches under Illinois law. However, the large majority of states permit branches. Only 12 states prohibit branching under state law. Twenty-one states and the District of Columbia permit banks to establish branches on a statewide basis. Seventeen states per-

mit bank branches within a specified geographical area, i.e., branches may be established within a specified distance from the main banking office, or may be established only within the county in which the main office is located. In Pennsylvania, banks may establish branches only in the home office county or in a contiguous county. The Nation's 14,000 banks have a total of over 40,000 banking locations. In cases of banks with branch offices, the records in those branches usually must be searched, which substantially increases the cost of complying with an IRS summons.

The American Bankers Association conducted a preliminary survey of a limited number of banks in connection with this case. The limits imposed by the filing deadline for this brief would not permit a banking industry survey based on well established statistical techniques of a scientifically selected sample of several thousand banks. Such a survey requires a minimum period of five to six months to complete. Nonetheless, the results of this preliminary survey are surprisingly consistent and informative.

Each bank in the survey was asked to indicate the number of IRS summons received in the last year and the average cost to the bank for responding to a typical IRS summons. In determining an "average cost" per summons, each bank took into account the full range of summonses received in a 12-month period, i.e., the estimated cost of summonses ranging from those for which little search was required to those for which extensive record search was required. This average cost figure includes direct expenses such as machine time, duplication, typing, and the cost of a bank officer's review time and employee time for the actual record search and retrieval of the information requested. This average cost figure does take into account the fact that summonses request varying amounts of records for varying numbers of taxable years of each bank customer who is being investigated by the IRS. For example, a summons for all records covering a three or four year period of a business customer with many types

of bank accounts and bank relationships would involve a substantially greater number of records (and therefore be more costly) than a summons for the records of an individual customer who has only one personal account and no other banking relationship.

Of the 22 banks shown in the table, 21 have deposits in excess of $1 billion, as indicated by the deposit range figures in the second column. Bank "D" has deposits of approximately $700 million. The survey was based on banks in the $1 billion and above deposit range because this is the deposit range of the three Pittsburgh banks involved in this case. The purpose was to obtain compliance cost data from banks of relatively similar size. As of December 31, 1974, approximately 87 banks had deposits in excess of $1 billion. Most of the banks with deposits in excess of $1 billion have either limited-area or statewide branching systems.

As shown in the table, eighteen of the banks which responded reported average costs in excess of $150 per summons. *Of these, 13 banks reported costs in excess of $200 per summons, including five which reported average costs of $250 or more per summons.* In the case of Bank C which reported an unusually low average cost per summons, the bank (which has no branches) does not comply with IRS summonses as originally drafted. Instead, each time a summons is received, a bank officer contacts the agent who served the summons to determine what lesser amount of information the IRS would accept. The bank then provides the IRS only with this lesser amount of information. The bank concluded that if it had to comply with each summons as originally drafted, its costs would be ten times greater.

The information on the total number of summonses received in the last year by each bank has been included to show that in some cases this figure is extremely large, particularly in the case of banks with branches. In cases where the banks have received large numbers of summonses, the total annual costs to the banks shown on the table can only be viewed as extraordinary.

Survey Responses

	Deposit Range (In Billions)	Annual Number Of Summonses	Average Cost Per Summons	Estimated Annual Cost
Bank A**	1-5	350	$230.00	$ 80,500.00
B**	10-20	1,240	$118.00	$ 146,320.00
C*	1-5	15	$ 20.00	$ 300.00
D***	under 1	25	$160.00	$ 4,000.00
E**	1-5	40	$229.00	$ 9,160.00
F***	5-10	300	$140.00	$ 42,000.00
G**	over 20	—	$220.00	—
H**	over 20	1,619	$151.56	$ 245,375.64
I**	1-5	96	$100.00	$ 9,600.00
J***	10-20	1,800	$274.85	$ 494,730.00
K**	1-5	200	$354.99	$ 70,998.00
L***	10-20	1,000	$300.00	$ 300,000.00
M**	1-5	120	$175.00	$ 21,000.00
N***	1-5	300	$200.00	$ 60,000.00
O***	over 20	2,040	$250.00	$ 510,000.00
P*	10-20	212	$225.00	$ 47,700.00
Q**	1-5	90	$175.00	$ 15,750.00
R**	1-5	75	$200.00	$ 15,000.00
S**	1-5	100	$220.00	$ 22,000.00
T***	10-20	1,000	$175.00	$ 175,000.00
U**	over 20	400	$200.00	$ 80,000.00
V**	5-10	212	$275.00	$ 58,300.00

KEY—
* branches prohibited
** limited area branching
*** statewide branching

The following factors will affect the total costs, as well as the cost per summons, which a bank will incur in responding to IRS administrative summonses for bank customer records:

(1) The size of the bank, i.e., its level of deposits;

(2) The nature of the bank's business, e.g., whether it emphasizes retail, consumer, or wholesale banking;

(3) The number and type of individual and business accounts and banking services that the bank offers to the public;

(4) The economic character and size of the geographic area in which the bank offers customer services or maintains banking facilities;

(5) The number and location of the bank's branches;
(6) The method or methods under which the bank maintains its bank customer records, i.e., a centralized records system, a non-centralized records system, a fully or partially automated records system, or a manual records system;
(7) The number and capability of personnel who process IRS records requests, including access to legal counsel for summons review; and
(8) The number of IRS administrative summonses received each year, which will be variously affected by factors 1 through 5.

One of the principal questions in the cost issue is whether the expenses incurred should be considered a cost of doing business. It is well established in this circuit that banks have a duty of cooperation, including shouldering some financial burden, in responding to IRS summonses. *See United States* v. *Dauphin Deposit Trust Company, supra.* However, a more detailed analysis is necessary.

The cost of doing business issue was considered in depth in *United States* v. *Farmers & Merchants Bank, supra.* The Court considered the totality of the Governmental regulation of banks in analyzing what items might be properly considered a cost of the business of banking, to wit,

> The regulation of banks is an exercise of fundamental powers by a legislature which has presumably considered an issue of public concern and has determined that banks, in order to operate within the pale of government protection and approval, must do certain things . . . [T]hese regulations fall equally on all of the regulated class—all banks must comply, and bear the related costs. It is, for all a cost of doing business.
>
> That situation is quite different from our case, even though the government would label the costs of complying with a summons as a "cost of doing business." This "cost" is not predictably part of the banking business, does not fall upon all equally, and was not specifically evaluated by the legislature and imposed by it upon all those who do a banking business. At 5 Slip Opinion.

The Court concluded that because expenses incurred in responding to an IRS summons do not fall equally on the banks, that such costs are not a cost of doing business. In any event, the Court concluded that a bank should not be required to bear anything other than nominal costs in responding to summonses.

In summary, we strongly disagree with the argument that banks which are in the business of providing financial services to their customers should be forced to absorb the burdensome costs of continuous government investigations of their customers' financial transactions as part of their costs of doing business.

C. THE CUMULATIVE BURDEN OF SUMMONSES

There is no question that financial records such as those maintained by banks concerning the customer transactions are important to the IRS in taxpayer investigations. In testimony before a House Judiciary Subcommittee on September 8, 1975, IRS Commissioner Donald Alexander stated that, "Access to the records of an individual or organization's financial transactions is necessary to permit the Service's Agents to determine whether a taxpayer has filed a correct return." However, the practical result of the importance of bank records to IRS tax investigations is that each year banks are receiving an increasingly greater number of IRS administrative summonses requesting an increasingly greater amount of information from customer records. This is due in part to improved IRS audit techniques and a greatly increased emphasis on the significance of bank records in tax investigations.

The Government, in its brief, cites the general proposition that, "The public . . . has a right to everyman's evidence. . ." as a basis for saying that the banks should produce the documents requested by the Internal Revenue Service without reimbursement. However, the analogy between the production of documents in response to an IRS summons and presenting evidence in court as a public duty fails. "Everyman's evidence" has to be made avail-

able to the public without reimbursement once.[9] On the other hand, bank customer records are constantly sought by the IRS. The information in bank files cannot be treated as "everyman's evidence."

On the basis of the select survey conducted by the American Bankers Association in preparation for this brief, it is estimated that a number of large banks receive in excess of 1,000 summonses per year. Three of the 22 responding banks reported receiving in excess of 1,500 summonses per year. Twenty-one of the banks listed in the table received an estimated total in excess of 10,000 summonses in a period of one year. In view of the magnitude of these numbers, it is appropriate for Federal courts to consider the cumulative impact of IRS summonses on the commercial banking system in determining whether they constitute an unreasonable burden.

The trial brief filed by the three banks in this case indicates that it is the cumulative impact of the summonses received which creates the need for reimbursement. The brief states in part,

> Indeed, if these were the last summonses the IRS would serve on the banks, they would gladly withdraw the defense . . .

It is obvious that Judge Teitlebaum found the cumulative number of summonses received by these banks as pertinent, admitting into the record evidence of the number of summonses received in the last year by each bank. *See* R. 347-349-A.

The issue of the cumulative burden of summonses has been explored recently by the United States District Court in Utah in the case of *United States* v. *Zions First National Bank,* unofficially reported at 75-2 U.S.T.C. ¶ 9581. Relying

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[9] The Supreme Court in *Hurtado* v. *United States,* 410 U.S. 578 (1973) stated, "It is beyond dispute that there is in fact a public obligation to provide evidence * * * and that this obligation persists no matter how financially burdensome it may be." (Citations and footnote omitted.) However one commentator has indicated that this duty is not unlimited. "The individual may fairly demand that society make the duty as little onerous as possible . . . that some sort of compensation for loss of time be provided." Wigmore, *Evidence* Section 2192(4) (McNaughton Rev. 1969).

on *United States* v. *Continental Bank & Trust Co., supra,* the Court in the *Zions* case rejected the discussion of cumulative burden. It concluded that if a bank has some duty of cooperation in handling summonses, it cannot subsequently aggregate its expenses and argue that the total would be considered burdensome. This general statement might be appropriate for third party record holders who do not receive many IRS summonses annually, but it should not be applied to banks. The extraordinary number of summonses received annually by the banking industry is a compelling reason why courts should consider the cumulative burden on each bank in determining whether an unreasonable financial burden exists in any given case.

D. THE DUTY TO MAINTAIN THE CONFIDENTIALITY OF BANK CUSTOMER RECORDS

The final factor which should be considered in assessing the burden imposed on banks in responding to IRS summonses is the duty of banks to preserve the confidential nature of their bank customer records. The confidential nature of bank customer records is directly affected by the reimbursement issue because the IRS frequently offers to conduct the search through the bank's files with its own personnel,[10] as it did in this case, ostensibly to reduce the record search and retrieval costs to the bank.

Most banks refuse to permit IRS personnel to conduct the record search for the essential reason that such a procedure would jeopardize or breach the confidentiality of the records of other bank customers who are not involved in the tax investigation at hand. To permit IRS personnel to conduct the record search presents the tempting opportunity to "fish" for evidence of tax liabilities of *other* bank customers who are not under investigation.

A bank participates in the private affairs of its customers as part of the financial service relationship that is provided for them. This relationship is created when a

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[10] *United States* v. *Continental Bank & Trust Co., supra,* and *United States* v. *Jones, supra.*

bank accepts a customer's money for deposit, or when it makes a loan to the customer or when it provides other financial or fiduciary services. A bank often receives personal information such as the amount and source of a customer's earnings and other income, the amount and types of a customer's indebtedness, and the amount of payments made to creditors. Historically, banks have treated customers' financial affairs as confidential in nature, not to be revealed except as required by law. The right of privacy of an individual's financial records—in the absence of a known violation of law by the individual involving his finances—is an integral element of the American concept of the personal freedom of the individual.

The Government offered in this case to supply its own personnel to carry out the search of the records in each of the banks and also offered to provide its own copying facilities. See R. 194, 196, and 198-A. The Government has contended in its brief that this offer would reduce the financial burden on the banks, implying that reimbursement would then not be necessary. We urge that any offer by the Internal Revenue Service to conduct a search through the banks' files with its own personnel is not a valid consideration which affects or otherwise reduces the right of a bank to reimbursement for expenses incurred in responding to a summons.

The Answer to the Petition to Enforce filed by each of the banks in this case states that the information and data contained in the records sought by the summonses in this case are treated as confidential by each bank. Further, testimony at the trial of Richard Lechnar, Manager of the Records Management Section of Mellon Bank, states,

> We maintain these records for our customers and we do have a privacy agreement and that is in quotes, it is not a written agreement, with them that we will protect the confidentiality of their records. They are not a matter of public record. (R. 313-A).

The District Court Judge recognized the problem of maintaining the confidentiality of the banks' records and the necessity that bank personnel conduct the search itself.

> The alternative proposed by the Government in their substituted summons, that is, a search of banking records by IRS personnel other than bank personnel is unacceptable. The unavoidable fact is that in conducting such a search, no well-trained IRS Agent would be able to ignore or forget the information he found of other criminal violations, real or potential, pertaining to other people. (R. 461-2-A).

In supporting the District Court evaluation of this sensitive situation regarding the records of bank customers who are not being investigated, we are not seeking to prevent the Internal Revenue Service from enforcing the provisions of the tax code. Rather, the IRS should be required to conduct its investigations in accordance with established procedures which safeguard the legal rights of taxpayers who are not under investigation.

Other courts have ruled that a legal duty exists upon banks to maintain the confidentiality of their customers' records. Any bank which fails to do so may be liable to its customers for disclosing information when such disclosure is not required by law. In *Peterson* v. *Idaho First National Bank,* 83 Ida. 578, 367 P.2d 284 (1961), the Idaho Supreme Court stated

> It is inconceivable that a bank would at any time consider itself at liberty to disclose the intimate details of its depositors' accounts. Inviolate secrecy is one of the inherent and fundamental precepts of the relationship of the bank and its customers or depositors. At 290.

In the case of *United States* v. *Northwest Pennsylvania Bank & Trust Co., supra,* the Court refused to enforce the summons as written because it would give the Internal Revenue Service unlimited access to the bank's records.

> This should not, however, allow the Government to wander at will through all of the records of the bank. The IRS must specify what records it wants and what specific persons, whose records are quoted and not merely designate the records of a given family.

and,

> The summons which is sought to be enforced is unnecessarily broad and its enforcement in toto would be unduly burdensome on the bank as heretofore set forth and would give the Internal Revenue Service a license to roam at will through the bank's records.

Further, the Court rejected the IRS offer of assistance,

> While the IRS has offered to assist the bank, we do not believe that the Internal Revenue Service is authorized to look at all of the transactions of all of the depositors on any given day and that the bank should search against the specific cancelled checks requested by the Internal Revenue Service itself. At 614.

Thus, the offer by the Internal Revenue Service to conduct a search through the bank files with its own personnel should not be considered as a mitigating factor which would affect the right of the bank to be reimbursed for expenses in responding to the summonses. In view of the well-established duty to maintain the confidentiality of bank customer records, bank personnel should be the only persons permitted to conduct a search for the material requested by the IRS.

CONCLUSION

The American Bankers Association respectfully urges this Court to affirm the decision of the United States District Court for the Western District of Pennsylvania with respect to the reimbursement issue and to hold that the Internal Revenue Service must reimburse the Pittsburgh National Bank, Mellon Bank and Equibank for the costs that will be incurred in responding to the six IRS summonses in this case, for the reasons stated in this brief.

Respectfully submitted,

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A Banker's Guide to IRS Procedures for Examinations of Customer Records and Levies on Customer Accounts

PREFACE

The American Bankers Association has received many inquiries from its member banks concerning Internal Revenue Service summonses and examinations of bank records, and levies on bank customers' accounts and other property in connection with IRS tax investigations of bank customers. Banks have experienced many difficulties and misunderstandings in attempting to comply with IRS procedures in these areas. This has led to considerable expense, customer complaints, and possible penalties which may be imposed for failure to comply properly with IRS requirements.

This manual is intended to assist bank officers who are charged with handling IRS summonses and examinations of bank records, and levies on customers' accounts and other property. This manual explains Internal Revenue Code requirements, suggests practical procedures to be used in complying with the Code requirements, explains options which are available to bankers in certain situations, and recommends certain procedures for dealing with customers in connection with these issues.

The manual does *not* pertain to IRS examinations made in connection with a bank's own tax return. Moreover, it does not contain information concerning investigations of bank customers by other U.S. government agencies such as the FBI.

Warning: This manual is not a substitute for legal counsel. Each IRS summons, examination, or levy situation may involve matters which are not treated in this manual and should be referred to the bank's legal counsel.

Inquiries concerning this publication should be directed to John F. Rolph III, Tax Counsel (202-467-4202) or Henry C. Ruempler, Assistant Tax Counsel (202-467-4932), or c/o The American Bankers Association, 1120 Connecticut Ave., N.W., Washington, D.C. 20036.

One. Examination and Summons of Bank Books and Records—Sections 7601-7605 of the Internal Revenue Code

A. PRIOR TO AN OFFICIAL IRS SUMMONS

The Internal Revenue Service is authorized to investigate all persons who may be liable to pay any internal revenue tax.[1] As part of an investigation, it is common for the IRS to seek to examine the bank records of the taxpayer under investigation. In addition to this authority, the IRS may also summon bank officers to produce such records and/or give testimony.[2]

The IRS has developed certain time-saving procedures which are designed to produce information about taxpayers while enabling the IRS to examine a taxpayer's bank records without resorting to the issuance of an official IRS administrative summons for the production of records. If a bank does not respond to these informal procedures, or if the information supplied is deemed insufficient, the IRS will generally issue an official summons.

At the outset, it is important for a banker to identify an informal—and unofficial—request for financial information about a customer when he receives it. Since an official IRS summons is made only on Form 2039 (Exhibit 1), any other form used to make an examination request should be considered unofficial. Some examples of such informal requests are attached as Exhibits 2 and 3. Exhibit 2 is Form 3N81. Exhibit 3 is Form PL-426. The IRS also uses other forms to examine and produce records, but none is the official summons. In addition, the IRS agent may simply present himself at the bank and ask to examine records on the premises.

When an unofficial request for information is made, or when an agent presents himself at the bank to examine records, *the bank has the right to refuse to furnish the information or to refuse to permit the examination of its records without statutory penalty.*

It is to be emphasized that a bank may choose either to respond affirmatively to a request to examine or produce records, or it may refuse to respond to such a request. At least two factors to be weighed in making this decision are:

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[1] 26 U.S.C. § 7601(a) Internal Revenue Code. (All subsequent section references will be to Internal Revenue Code unless otherwise designated.)

[2] § 7602 (1), (2) and (3).

1. *Maintenance of Good Customer Relations*—This involves maintaining, to the maximum possible degree, the confidential nature of its customers' banking transactions. In many cases this means a bank will elect to refuse an unofficial request and instead require an official IRS summons. However, some IRS requests are fairly routine and inconsequential—such as whether a given taxpayer has an account with that particular bank. In those situations it my be to the advantage of the bank and the customer (and the IRS) to respond to the request when it does not involve a breach of the confidentiality of customers' affairs. A bank could be liable to its customer for disclosing information when such disclosure is not required by law.[3]

2. *Costs to Bank*—The costs to a bank in connection with an IRS investigation of a bank customer may vary, depending upon the approach that the bank takes. These costs may involve the diversion of bank employees' work effort, and the use of reproduction and other bank equipment. The cost may vary depending upon whether (a) the bank responds to an unofficial request for records or information, and uses its own employees and equipment to produce the information requested or (b) the bank permits an on-premises examination by the IRS in which case the IRS may use its own reproduction equipment or the bank's reproduction equipment, and bank personnel monitors the examination, or (c) the bank refuses to respond to an unofficial request, in which case an IRS summons may be issued, which may involve an appearance by a bank officer before the IRS and the production of books and records, etc. which pertain to the tax investigation.

The costs which a bank incurs in connection with an IRS tax investigation of a bank customer may or may not be reimbursable by the IRS, depending upon circumstances. (See Part Three.)

If the bank voluntarily chooses to comply with unofficial requests, it should consider the following procedure:

1. Ask the IRS agent for his identification.

2. Verify the name, address, and possibly the social security number of the bank customer against that of the person being investigated.

3. Ask the agent if this *specific* taxpayer is under investigation for his own tax liability. If the answer is no, the bank should request an official summons. There is a substantial legal question as to the validity of an IRS investigation of other than a specific taxpayer.[4]

4. Determine whether the investigation is civil or criminal in nature. Criminal investigations cannot be conducted with an administrative summons.[5]

5. Some initial determination of relevance must be made. Generally speaking, bank records are relevant material in any income tax investigation.[6] However, if there is concern that the material requested does not seem to be appropriate for a tax investigation, the bank should consider refusing the request.

6. The bank should consider whether the records are sufficiently described to avoid requiring a burdensome search for vaguely specified records.

7. The bank should also consider whether the request would impose an unsatisfactory financial burden on the bank.

8. Keep a record of the cost incurred, date of compliance with the request, and what documents were turned over to the IRS.

If a bank begins to comply with an unofficial request for the production or examination of a taxpayer's bank records, and encounters difficulties or does not obtain answers from the IRS agent in connection with the foregoing procedures, it is recommended that the bank should consult counsel on whether to refuse to honor the request and request an official summons (Form 2039). The recourse to the Form 2039 summons will ensure that the confidentiality of the records of a customer's banking transactions is protected to the maximum possible degree.

In any situation in which a bank chooses to cooperate with an on-the-premises examination of bank records, *the bank should make every possible effort to preserve the confidentiality of the records of any other bank customer.* For example, if records of more than one depositor are in a particular file or on a particular

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[3] See *Peterson* v. *Idaho First National Bank*, 83 Ida. 10, 367 P. 2d 284, (1961). *Paton's Digest of Legal Opinions*, Banks and Banking § 19: 11, Supplement Vol. 1. Compare also with note 20.

[4] See for example the following recent cases: *U.S.* v. *Humble Oil & Refining Co.*, 74-1 U.S.T.C. ¶ 9186 (5th Cir., 1974), aff'g 346 F. Supp. 944 (S.D. Tex., 1972); *U.S.* v. *Theodore*, 73-1 U.S.T.C. ¶ 9477 (4th Cir. 1973); *U.S.* v. *Clayton & Co.*, 73-1 U.S.T.C. ¶ 9452 (S.D. Miss., 1973); *U.S.* v. *Berkowitz*, 355 F. Supp. 897 (E.D. Pa. 1973).

[5] *Reisman* v. *Caplin*, 375 U.S. 440, 449 (1964).

[6] *U.S.* v. *First National Bank of Mobile*, 295 F. 142 (S.D. Ala., 1924), aff'd without opinion 267 U.S. 576 (1925).

role of microfilm, the bank should permit the IRS to examine only such files or film as pertain to the particular taxpayer.

B. IRS ADMINISTRATIVE SUMMONS

The official administrative summons described in Section 7602(2) of the Code is Form 2039 (Exhibit 1). This summons is used to obtain the production of specific books and records which may be relevant to a tax investigation. The Code provides that the person named in the summons will be required to appear before the IRS not less than 10 days from the date of the summons.[7] The request for information may include information concerning a customer's checking account records or loan applications.[8]

A summons is required to be served in person by an IRS agent. If the summons is mailed, the bank should refuse it automatically. A summons should be properly executed. On its face, it should contain the name of the taxpayer, the periods under investigation, the name and address of the bank to which the summons is directed, and the name of the IRS officer before whom an appearance will be made. The summons must identify specific books and records which are to be brought to the hearing by a bank officer in connection with the tax investigation. The summons will designate the place and time for appearance as well as the date of issue and the signature and title of the IRS officer by whom service is made.

A summons will always be accompanied by a Certificate of Service of Summons which certifies that the summons was served by a designated IRS representative on the bank on a specified date and time.

If the summons is properly executed and contains all of the information described above, the bank should then decide how to respond. The bank may choose to comply with the summons or may refuse to comply. Refusal may be based on one or more good faith challenges to the summons.[9]

If the bank chooses not to comply with the summons, it is recommended that it communicate its intentions to the IRS. A willful failure to respond or appear may result in a penalty under Section 7210 of the Code.[10]

In determining whether or not there is a basis for making a good faith challenge to a summons (and thereby requiring the IRS to obtain a court order), the following factors may be taken into consideration:

1. Is the investigation of a civil or criminal nature? If it is criminal in nature, the bank should challenge the summons because criminal investigations cannot be conducted with an administrative summons.[11]

2. Is the date for appearance designated in the summons at least 10 days after the date the summons was served? If the date of appearance is less than 10 days, the bank should challenge the summons.[12]

3. In the best judgment of a bank officer, are the books and records designated in the summons relevant to a bona fide tax investigation? If they are not relevant, this is one basis on which the bank can challenge the summons.[13]

4. Are the books and records described sufficiently in the summons to enable the bank to find the records without undue burden? A bank may challenge a summons on the ground that the books and records sought are so vaguely described as to impose an undue burden on the bank.[14]

5. Does the request for information in this summons, standing alone, or in combination with other IRS summonses in tax investigations, impose an undue financial burden on the bank? If this is the case, it is a basis for making a good faith challenge.[15]

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[7] § 7605(a).

[8] *U.S.* v. *Cleveland Trust Co.*, 474 F. 2d 1234 (6th Cir., 1973), cert. den. 42 U.S.L.W. 3190, Oct. 9, 1974.

[9] *Reisman* v. *Caplin, supra,* note 5, at 445–46. It is understood that some banks, in refusing to comply with the summons, have successfully requested the IRS to obtain a court order without spelling out their reasons for challenging the summons.

[10] See discussion of penalty under § 7210 in *Reisman* v. *Caplin, supra,* note 5, at 446–47 and nn. 6 and 8.

[11] See note 5.

[12] See note 7.

[13] *U.S.* v. *Powell,* 379 U.S. 48 (1964).

[14] *Oklahoma Press Pub. Co.* v. *Walling,* 327 U.S. 186, 208–9 (1946); *U.S.* v. *First National Bank of Mobile,* 160 F. 2d 532 (5th Cir., 1947). See also *U.S.* v. *Union National Bank,* 363 F. Supp. 629 (W.D. Pa., 1973) where a catch-all request was ruled unduly vague.

[15] *U.S.* v. *Dauphin Deposit Trust Co.*, 385 F. 2d 129 (3rd Cir., 1967), cert. denied 390 U.S. 921 (1968); *U.S.* v. *First National Bank of Fort Smith, Arkansas,* 173 F. Supp. 716 (W.D. Ark., 1959).

If the answers to any of the above questions indicate a basis for challenging the summons, the bank should consult counsel and consider making such a challenge.

Although it is under no statutory obligation to do so, the bank may notify its customer of an IRS summons for records. The bank may have some reference in its contract with each depositor concerning notification. The bank should not attempt to advise the customer of his legal rights. If the customer objects to the IRS examination of the bank's records, the bank should advise him that, unless there is a basis for challenging the summons, the bank is compelled by law to comply.

The bank may not avoid the problem of a summons by turning the records over to the taxpayer and then responding to the IRS by saying the bank no longer has the records. In that situation, the bank could be found guilty of civil contempt and liable to the government for damages.[16]

C. COURT ORDERS

When a bank does not comply with or challenges an IRS summons, the IRS may seek a court order to require bank compliance.[17] A hearing is held in a United States District Court for the purpose of discovering if there is any cause why the administrative summons should not be enforced. It is at this time that the bank should seek a judicial determination as to the validity of any and all of its challenges to the summons.[18] The court will review the challenges and then determine whether or not to issue a court order to enforce the summons.[19] If the court issues such an order, the bank must comply with that order and it may do so without fear of any liability to its customer.[20]

TWO. NOTICE OF LEVY ON BANK CUSTOMERS' PROPERTY—(SECTIONS 6331–6334 OF THE INTERNAL REVENUE CODE)

A. LEVY

If a taxpayer fails to pay his tax for any reason, the government is authorized to collect the tax by means of a levy on all the property owned by the recalcitrant taxpayer.[21]

In the case of a bank customer who fails to pay his tax, the IRS may serve a Notice of Levy on the bank to seize all of the customer's property which is held by the bank.[22] Thus, any funds held in the customer's accounts or any other property held, such as money in a safe deposit box, are seized by the government at the time the bank receives a Notice of Levy. After receiving the Notice of Levy, the banks may disperse the funds only to the IRS.[23]

1. Service of a notice of levy

A Notice of Levy (Form 668–A, attached as Exhibit 4) should be served on the bank in person by an IRS agent. However, it has been common practice in some areas of the country to serve a Notice of Levy by mail. *Service of a Notice of Levy by mail is invalid and should be refused by the bank, unless a prior agreement has been reached between the IRS and the bank to accept such service.* According to the IRS this agreement (Form 4427, attached as Exhibit 5) validates subsequent service of Notice of Levy by mail and designates the particular bank official to whom the Notice of Levy should be directed. However, there is no independent authority which supports the conclusion that service by mail is valid. According to the IRS many banks have found this procedure useful and have executed such agreements. If a bank chooses to accept a Notice of Levy served by mail, without having previously executed Form 4427, the bank may

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[16] *U.S.* v. *Edmond*, 355 F. Supp. 435 (W.D. Okla., 1972).
[17] § 7604(b); *Reisman* v. *Caplin*, *supra*, note 5, at 445–6.
[18] *Donaldson* v. *U.S.*, 400 U.S. 517 (1971); *Reisman* v. *Caplin*, note 5, at 446.
[19] The court may enforce only part of the summons or require the IRS to narrow its request. See *U.S.* v. *Union National Bank*, *supra*, note 14.
[20] *U.S.* v. *Jones*, 351 F. Supp. 132 (M.D. Ala., 1972); *Brunwasser* v. *Pittsburgh National Bank*, 64–2 U.S.T.C. ¶ 9871 (W.D. Pa., 1964), aff'd per curiam 351 F. 2d 951 (3rd Cir., 1966).
[21] § 6331(a).
[22] § 6331(a); 26 C.F.R. § 301.6331–1(a)(1) Income Tax Regulations. (All subsequent references to regulation sections will be from the Income Tax Regulations, unless otherwise designated.)
[23] § 6332(a).

be liable to its customer in damages if the levy turns out to be wrongful or invalid.

There is no statutory duty requiring the bank to notify the customer of the Notice of Levy. According to the IRS, in all cases, a copy of the Notice of Levy is mailed by the IRS to the taxpayer.[24] Thus, the taxpayer will have already received notice of the tax assessment and deficiency.

Final Demand (Form 668-C, Exhibit 6) is often received by banks in connection with a levy. This form is a follow-up to the original Notice of Levy to remind the bank to turn over the property to the IRS. If a bank fails to turn over property to the IRS, it is subject to liability and penalties.[25]

2. Effect of a notice of levy

A Notice of Levy takes effect when it is received by the bank officer.[26] In the case of personal service, this means that the notice takes effect when the form is handed to the officer by the IRS agent. In the case of a Notice of Levy served by mail, the levy is effective when the designated bank officer receives the notice. In either case, the bank should record on the form the time and date when the notice is received.

The IRS maintains that once a Notice of Levy is received by any office of a bank (main office or branch), the levy is effective for *all* bank offices, as of the time and date of service.[27] The levy covers any property owned by the taxpayer and held by the bank, regardless of which office actually has the property.

In certain situations, banks have worked out informal agreements with their local IRS representatives that the IRS will serve the Notice of Levy only on the branch where the customer's property is held. These agreements only establish an informal procedure and do not change the IRS position that a Notice of Levy served on any office of the bank is effective with respect to property held in all offices of the bank.

3. Property subject to the levy

The general rule is that all property owned by the taxpayer which is in the hands of the bank is subjected to the levy.[28] It should be noted, however, that *state law* governs the question of whether and to what extent the taxpayer actually has an interest in property held by the bank in the taxpayer's name.[29] For example state law is in control concerning the extent of a taxpayer's interest in joint account in a bank,[30] or in a partnership.[31]

With respect to checks in the process of clearance, the general rule is that the levy extends only to those funds actually on hand at the bank at the time the Notice of Levy is served and not to any other additional amounts which might have been acknowledged at that time.[32]

The IRS policy with respect to safe deposit boxes is that a levy merely freezes access to any box owned by the taxpayer. *The bank should not allow the IRS to examine or remove the contents of any safe deposit box without the taxpayer's consent or a court order.*

In certain situations the bank may claim or assert a superior interest in amounts owed to it by the taxpayer against the amount subject to the levy. This can be accomplished in one of two ways. First, the bank may simply set off the amount and turn over the remaining funds subject to the levy and communicate in a reasonable way to the IRS that it is asserting the right of set-off.

The bank right of set-off has been the subject of controversy. The courts have said that a right of set-off exists if it is exercised by the bank to the extent required by state law before the service of the Notice of Levy.[33]

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[24] Form 668A is actually a three-part form; an original and two carbons. The last carbon is labelled, "Part 3—To Be Furnished To Taxpayer."

[25] § 6332(c) (1) and (2).

[26] See generally, *U.S.* v. *Pittman*, 449 F. 2d 623 (7th Cir., 1971); *U.S.* v. *Elland*, 223 F. 2d 118 (5th Cir., 1955).

[27] There is a different rule governing a levy on property held in a foreign branch of a U.S. bank. See Regulations § 301.6332-1(a)(2).

[28] Regulations § 301.6331-1(a)(1).

[29] *Aquilino* v. *U.S.*, 363 U.S. 509 (1963); *U.S.* v. *Bess*, 357 U.S. 51 (1958); *Morgan* v. *Commissioner*, 309 U.S. 78 (1940).

[30] Rev. Rul. 55-187, 1955-1 C. B. 197.

[31] Rev. Rul. 54-213, 1954-1 C. B., 285.

[32] Rev. Rul. 73-310, IRB 1973-29, 11; *U.S.* v. *Guaranty Bank & Trust Co.*, 56 F. Supp. 470 (E.D. N. C., 1944).

[33] See *U.S.* v. *Sterling National Bank & Trust Co.*, 73-2 U.S.T.C. ¶ 9494 (S. D. N.Y., 1973) appeal docketed No. 73-2300 01 2d Cir., 1973; *U.S.* v. *Bank of America National Trust & Savings Assn.*, 229 F. Supp. 906 (S. D. Cal., 1964), aff'd 345 F. 2d 624 (9th Cir., 1965), cert. denied 382 U.S. 927; *Bank of Nevada* v. *U.S.*, 251 F. 2d 820 (9th Cir., 1957), cert. den. 356 U.S. 939 (1959).

In exercising a right of set-off, a bank should consult an attorney on its priorities vis-a-vis the government.[34] Banks which have withheld funds because of a mistaken belief that they had a superior interest—and therefore exercised a right of set-off—have been subject to the penalty for failure to turn over the funds to the IRS.[35] Also, the bank may turn over all the property subject to the levy and then bring a civil action under Section 7426 to recover which is subject to a superior interest in the bank's favor.[36]

Once the bank has turned over the property to the IRS it is discharged from any obligation to the owner of such property.[37] However, if the property surrendered *is not properly subject to levy*, the bank is not relieved from liability to the owner of such property.[38]

The federal income tax regulations provide that the owner of property which has been mistakenly surrendered in response to an IRS levy may obtain administrative relief under Section 6343 of the Code or may sue to recover the property under Section 7426.[39] If a bank has mistakenly surrendered property in response to an IRS levy, the bank may seek to recover such property under the same Code provisions.

4. Penalty provisions

Failure to turn over property subject to a levy can result in liability in the amount of property levied plus costs and interests, and 50 percent of such amount as a penalty under Section 6332(c) of the Code.[40] The penalty for failure to surrender property will not be applied if a bona fide dispute exists regarding the amount of property subject to the levy or concerning the legal effectiveness of the levy itself.[41] However, there is no formalized procedure on how this bona fide dispute is handled. Banks should consider consulting counsel if there is some reason to believe that the amount of property levied is incorrect or if there is some reason to feel that the Notice of Levy is defective in any way.

B. EXHIBITION OF BOOKS AND RECORDS IN CONNECTION WITH AN IRS LEVY

If an IRS levy "has been made or is about to be made" on a bank customer's property held by the bank, the IRS is authorized to request the bank to exhibit books and records concerning the customer's property.[42]

If the bank has not received a Notice of Levy prior to or in conjunction with any form of request to exhibit books and records, the bank should determine whether a levy has been made or is about to be made. Unless the answer is in the affirmative, the bank should refuse to exhibit its books and records. It is possible that the IRS may wish to examine records prior to a levy; *however, the agent must inform the bank that a levy is about to be made, and an assessment has already been made.*

The IRS may make the request for bank records in any one of three ways. First, an IRS agent may request, in person, to see the records. Second, the IRS may serve Form 2270—Notice of Requirement to Exhibit Books and Records—(Exhibit 7) either in person or by mail. This form requires no written response on the part of the bank. It advises the bank that the IRS wishes to examine the bank records of a named taxpayer. Third, the IRS may use some form such as Form RC SE FORM ACTS 11 (Exhibit 8) which requests the bank to answer certain questions concerning the taxpayer's accounts and mail such answers to the IRS. According to the IRS, the bank may refuse to respond to any of these requests without statutory penalty. However, in the event of such refusal, the IRS may issue a summons under Section 7602 to examine the records.

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[34] See §§ 6321–6325 which determine the priority of competing interests in property subject to a federal tax lien. For example, see *U.S.* v. *Wyoming National Bank of Casper*, 74–1 U.S.T.C. ¶ 9203, (D. Wyo., 1973).

[35] *U.S.* v. *First National Bank of Commerce in New Orleans*, 73–2 U.S.T.C. ¶ 9751, (E. D. La., 1973) and *U.S.* v. *Sterling National Bank & Trust Co.*, *supra*, note 33.

[36] *Citizens Bank & Trust Co., of Md.* v. *U.S.*, 344 F. Supp. 866 (D. Md., 1972).

[37] § 6332(d).

[38] Regulations § 301.6332–1(c).

[39] *Ibid.*

[40] § 6332(c) (1) and (2).

[41] Regulations § 301.6332–1(b)(2).

[42] § 6333.

THREE. REIMBURSEMENT FOR PRODUCTION OF BANK RECORDS

As previously discussed, a bank usually incurs certain costs when it responds to an IRS request for information about a particular bank customer. The amount of these costs varies depending on (1) the amount of information requested, (2) how the bank records are stored, and (3) the method by which the information is retrieved from the bank files. It is established that a bank must bear some of the cost of cooperating with the IRS in a tax investigation.[43] However, in cases where the costs of record retrieval are substantial, the IRS may be asked to share in those costs. In fact, some banks routinely charge the IRS in cases which a large amount of information is requested.

The major difficulty in this area is that there is no uniform practice for reimbursement of bank costs. There is no statutory provision authorizing IRS reimbursement of any cost in connection with the examination and production of bank records. However, a standardized witness fee and mileage fee is paid for any bank representative who appears before the IRS and gives testimony.[44] Some banks have obtained reimbursement through informal agreements with revenue agents and district directors, whereas other banks have been unsuccessful in obtaining such agreements.

The National Office of the IRS takes the position that banks should not be reimbursed for record production costs (including extra bank man-hours) because the IRS will bring its own reproduction equipment and personnel onto the bank premises to reproduce the records without cost to the bank. This IRS position ignores the fact that the bank is under a duty to preserve the confidentiality of the records of its other bank customers who are not under investigation at that time. Thus, it would always be necessary for the bank to have at least one employee monitoring the IRS investigation. The IRS states that, in the examination authorized under Section 7602, it usually does not seek to obtain copies of bank records but, instead, seeks to examine the actual records of the bank customer. It is understood that if the IRS requests a bank to make copies of a taxpayer's financial records, it will reimburse the bank for the copies requested.[45]

According to the IRS, the only situation in which the bank will be reimbursed for costs other than costs of reproduction is the situation in which a prior agreement has been executed between the bank and the IRS Assistant Commissioner (Compliance) concerning such reimbursement. Presently, there is only one such agreement in operation and that situation involves a central storage facility situated in a separate location and used by a large number of banks.

At the present time, several cases are pending in the federal courts concerning the extent of the bank's right to reimbursement from the IRS for these costs. The adjudication of these cases may result in a more definitive rule which will be uniformly applied.

FOUR. IRS FORMS

Exhibit 1—Form 2039
Summons
Exhibit 2—Form 3N81
Unofficial Summons
Exhibit 3—Form PL-426
Unofficial Summons
Exhiibt 4—Form 668A
Notice of Levy
Exhibit 5—Form 4427
Agreement to Accept Notice of Levy by Mail
Exhibit 6—Form 668C
Final Demand for Levy
Exhibit 7—Form 2270
Notice of Requirement to Exhibit Books and Records
Exhibit 8—Form RC SE ACTS 11
Unofficial Request for Information in Connection with Levy

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[43] *U.S.* v. *Dauphin Deposit Trust Co., supra,* note 15.
[44] 5 U.S.C. § 503(b)(2); *Roberts* v. *U.S.,* 397 F. 2d 968 (5th Cir., 1968); Rev. Rul. 68-645, 1968-2 C.B. 599.
[45] *U.S.* v. *Jones, supra,* note 20; 43 Comp. Gen. 110 (1963).

Exhibit 1—Form 2039

Form 2039
(Rev. Oct. 1969)

Summons

Department of the Treasury
Internal Revenue Service

In the matter of the tax liability of

_____

Internal Revenue District of _____

Period(s) _____

The Commissioner of Internal Revenue

To _____

At _____

Greetings: You are hereby summoned and required to appear before

_____
an officer of the Internal Revenue Service, to give testimony relating to the tax liability or the collection of the tax liability of the above named person for the period(s) designated and to bring with you and produce for examination the following books, records, and papers at the place and time hereinafter set forth:

Place and time for appearance:

at _____

on the _____ day of _____, 19 ____ at _____ o'clock __.M.

Failure to comply with this summons will render you liable to proceedings in the district court of the United States or before a United States commissioner or magistrate to enforce obedience to the requirements of this summons, and to punish default or disobedience.

Issued under authority of the Internal Revenue Code

this _____ day of _____, 19____

Original

_____ _____
Signature Title

Form 2039 (Rev. 10-69)

Certificate of Service of Summons

(Pursuant to Section 7603, Internal Revenue Code)

I certify that I served the summons shown on the front of this form on:

Date	Time

How Summons Was Served

☐ I handed an attested copy of the summons to the person to whom it was directed,

_____

_____

☐ I left an attested copy of the summons with the following person at the last and usual place of abode of the person to whom it was directed

_____

_____

Signature	Title

Sec. 7603

Service of Summons

A summons issued under section 6420(e)(2), 6421(f)(2), 6424(d)(2), or 7602 shall be served by the Secretary or his delegate, by an attested copy delivered in hand to the person to whom it is directed, or left at his last and usual place of abode; and the certificate of service signed by the person serving the summons shall be evidence of the facts it states on the hearing of an application for the enforcement of the summons. When the summons requires the production of books, papers, records, or other data, it shall be sufficient if such books, papers, records, or other data are described with reasonable certainty.

Form 2039 (Rev. 10-68)

Form 2039-A
(Rev. Oct. 1969)

Summons

Department of the Treasury
Internal Revenue Service

In the matter of the tax liability of

_____

Internal Revenue District of _____

Period(s) _____

The Commissioner of Internal Revenue

To _____

At _____

Greetings: You are hereby summoned and required to appear before

_____

an officer of the Internal Revenue Service, to give testimony relating to the tax liability or the collection of the tax liability of the above named person for the period(s) designated and to bring with you and produce for examination the following books, records, and papers at the place and time hereinafter set forth:

Place and time for appearance:

at _____

on the _____ day of _____, 19 ____ at _____ o'clock ___.M.

Failure to comply with this summons will render you liable to proceedings in the district court of the United States or before a United States commissioner or magistrate to enforce obedience to the requirements of this summons, and to punish default or disobedience.

Issued under authority of the Internal Revenue Code

this _____ day of _____, 19_____

Attested Copy _____ _____

Signature Title

Form 2039-A (Rev. 10-69)

Excerpts From the Internal Revenue Code

Sec. 7602

Examination of Books and Witnesses

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

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

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

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

Sec. 6420

Gasoline Used on Farms

• • •

(e) Applicable Laws—

• • •

(2) Examination of books and witnesses.—For the purpose of ascertaining the correctness of any claim made under this section, or the correctness of any payment made in respect of any such claim, the Secretary or his delegate shall have the authority granted by paragraphs (1), (2), and (3) of section 7602 (relating to examination of books and witnesses) as if the claimant were the person liable for tax.

• • •

Sec. 6421

Gasoline Used for Certain Nonhighway Purposes or by Local Transit Systems

• • •

(f) Applicable Laws—

• • •

(2) Examination of books and witnesses.—For the purpose of ascertaining the correctness of any claim made under this section, or the correctness of any payment made in respect of any such claim, the Secretary or his delegate shall have the authority granted by paragraphs (1), (2), and (3) of section 7602 (relating to examination of books and witnesses) as if the claimant were the person liable for tax.

• • •

Sec. 6424

Lubricating Oil Not Used in Highway Motor Vehicles

• • •

(d) Applicable Laws—

• • •

(2) Examination of Books and Witnesses.—For the purpose of ascertaining the correctness of any claim made under this section, or the correctness of any payment made in respect of any such claim, the Secretary or his delegate shall have the authority granted by paragraphs (1), (2), and (3) of section 7602 (relating to examination of books and witnesses) as if the claimant were the person liable for tax.

• • •

Sec. 7605

Time and Place of Examination

(a) Time and place.—The time and place of examination pursuant to the provisions of section 6420(e)(2), 6421(f)(2), 6424(d)(2), or 7602 shall be such time and place as may be fixed by the Secretary or his delegate and as are reasonable under the circumstances. In the case of a summons under authority of paragraph (2) of section 7602, or under the corresponding authority of section 6420(e)(2), 6421(f)(2), or 6424(d)(2), the date fixed for appearance before the Secretary or his delegate shall not be less than 10 days from the date of the summons.

• • •

Sec. 7603

Service of Summons

A summons issued under section 6420(e)(2), 6421(f)(2), 6424(d)(2), or 7602 shall be served by the Secretary or his delegate, by an attested copy delivered in hand to the person to whom it is directed, or left at his last and usual place of abode; and the certificate of service signed by the person serving the summons shall be evidence of the facts it states on the hearing of an application for the enforcement of the summons. When the summons requires the production of books, papers, records, or other data, it shall be sufficient if such books, papers, records, or other data are described with reasonable certainty.

Sec. 7604

Enforcement of Summons

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

(b) Enforcement.—Whenever any person summoned under section 6420(e)(2), 6421(f)(2), 6424(d)(2), or 7602 neglects or refuses to obey such summons, or to produce books, papers, records, or other data, or to give testimony, as required, the Secretary or his delegate may apply to the judge of the district court or to a United States commissioner[1] for the district within which the person so summoned resides or is found for an attachment against him as for a contempt. It shall be the duty of the judge or commissioner[1] to hear the application, and, if satisfactory proof is made, to issue an attachment, directed to some proper officer, for the arrest of such person, and upon his being brought before him to proceed to a hearing of the case; and upon such hearing the judge or the United States commissioner[1] shall have power to make such order as he shall deem proper, not inconsistent with the law for the punishment of contempts, to enforce obedience to the requirements of the summons and to punish such person for his default or disobedience.

[1] Or United States magistrate, pursuant to P.L. 90-578.

• • •

Sec. 7210

Failure To Obey Summons

Any person who, being duly summoned to appear to testify, or to appear and produce books, accounts, records, memoranda, or other papers, as required under sections 6420(e)(2), 6421(f)(2), 6424(d)(2), 7602, 7603, and 7604(b), neglects to appear or to produce such books, accounts, records, memoranda, or other papers, shall, upon conviction thereof, be fined not more than $1,000, or imprisoned not more than 1 year, or both, together with costs of prosecution.

U. S. GOVERNMENT PRINTING OFFICE : 1969 O - 347-440

E I. 88-1118873 Form 2039-A (Rev. 10-69)

Exhibit 2—Form 3N81

Address any reply to:

Department of the Treasury

District Director
Internal Revenue Service

Date: | In reply refer to:

Names of Taxpayers:

Years:

We would appreciate your help in connection with a Federal tax matter concerning the taxpayers named above. Please send us the information requested below.

We are making this request under the authority of section 7602 of the Internal Revenue Code, and any information you furnish will be held in strict confidence. We have enclosed a self-addressed, postpaid envelope for your convenience in replying. The copy of this letter is for your records.

Thank you for your cooperation.

Sincerely yours,
District Director

Enclosures:
Copy of this letter
Envelope

REPLY

Records of our institution show the above taxpayers have or had accounts as checked below. Details of the accounts checked YES are shown on the back of this letter.

	YES	NONE		YES	NONE
Checking Accounts	☐	☐	Safe Deposit Boxes	☐	☐
Savings Accounts	☐	☐	Other Accounts or Transactions	☐	☐
Savings Certificates	☐	☐			

SIGNATURE OF BANK OFFICIAL _____ TITLE _____ DATE _____

FINANCIAL INFORMATION

CHECKING ACCOUNTS

IN NAME OF, AND ADDRESS - ACCOUNT NUMBER	TYPE	BALANCE JAN. 1, 19	BALANCE JAN. 1, 19	BALANCE JAN. 1, 19

SAVINGS ACCOUNTS

IN NAME OF, AND ADDRESS - ACCOUNT NUMBER	INTEREST 19	19	19

TRUST ACCOUNTS

IN NAME OF, AND ADDRESS - ACCOUNT NUMBER	BALANCE JAN. 1, 19	JAN. 1, 19	JAN. 1, 19

SAFE DEPOSIT BOXES

IN NAME OF, AND ADDRESS - ACCOUNT NUMBER	LOCATION MAIN OFFICE OR BRANCH ADDRESS

LOANS OR MORTGAGES OF LAST 3 YEARS

IN NAME OF, AND ADDRESS	DATE MADE	ORIGINAL PRINCIPAL	CLOSED YES/NO	IF OPEN - MONTHLY PAY'T.

SAVINGS CERTIFICATES

IN NAME OF, AND ADDRESS	DATE MADE	AMOUNT PURCHASED	LENGTH OF PERIOD	REMARKS

OTHER TRANSACTIONS

Exhibit 3—Form PL-426

U. S. TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE
DISTRICT DIRECTOR

IN REPLY REFER TO

Code 421

In connection with routine activities of the Internal Revenue Service information is desired regarding the financial transactions reflected on your records with regard to _____
_____.

The information desired is requested in accordance with authority granted in Section 7602 of the Internal Revenue Code, and it would be appreciated if you would make your records available to the extent required by the Internal Revenue Service.

Very truly yours,

Internal Revenue Agent

Exhibit 4—Form 668A

FORM 668-A
(REV. OCT. 1971)
DATE

DEPARTMENT OF THE TREASURY—INTERNAL REVENUE SERVICE

NOTICE OF LEVY

TO

ORIGINATING DISTRICT

You are hereby notified that there is now due, owing and unpaid to the United States of America from the taxpayer whose name appears below the sum of → $

KIND OF TAX	TAX PERIOD ENDED	DATE OF ASSESSMENT	IDENTIFYING NO.	UNPAID BALANCE OF ASSESSMENT	STATUTORY ADDITIONS	TOTAL
				$	$	$
					TOTAL AMOUNT DUE	

You are further notified that demand has been made for the amount set forth herein upon the taxpayer who has neglected or refused to pay, and that such amount is still due, owing, and unpaid from this taxpayer. Accordingly, you are further notified that all property, rights to property, moneys, credits, and bank deposits now in your possession and belonging to this taxpayer (or with respect to which you are obligated) and all sums of money or other obligations owing from you to this taxpayer, or on which there is a lien provided under Chapter 64, Internal Revenue Code of 1954, are hereby levied upon and seized for satisfaction of the aforesaid tax, together with all additions provided by law, and demand is hereby made upon you for the amount necessary to satisfy the liability set forth herein, or for such lesser sum as you may be indebted to him, to be applied as a payment on his tax liability. Checks or money orders should be made payable to "Internal Revenue Service".

SIGNATURE	TITLE	ADDRESS (CITY AND STATE)

(Name and Address of Taxpayer)

CERTIFICATE OF SERVICE

I hereby certify that this levy was served by delivering a copy of this notice of levy to the person named below.

NAME

TITLE

DATE AND TIME

SIGNATURE OF REVENUE OFFICER

PART 1 — TO BE RETURNED TO INTERNAL REVENUE SERVICE

FORM 668-A (REV. 10-71)

Exhibit 6—Form 4427

Agreement to Accept Notice of Levy by Mail

Department of the Treasury
Internal Revenue Service

Instructions for Responding to a Notice of Levy

A Notice of Levy, Form 668-A, attaches funds due an employee, a depositor, or other person named on it. When you receive a Notice of Levy, we would appreciate your following these instructions:

1. Please have your representative sign, date, and note the time received above your name and address on all three parts of the form.

2. If you have funds due the person named, please send us your check, payable to the Internal Revenue Service, attached to Part 1. You may keep Part 2 for your records. Please give Part 3 to the person named.

3. If you do not have funds due the person named, please note this on the face of Part 1. Then return all three parts of the form to us.

Thank you for your cooperation.

Form 4427 (Rev. 3-72)

Name:

The firm or individual named above agrees:

1. That the District Director may serve Notices of Levy, Forms 668-A, by mail to;

   _____

   _____

   and further agrees

2. To send the amounts due under the Notices of Levy to the District Director by check or money order, payable to the Internal Revenue Service.

If employer, please furnish the following information:

Our paydays for employees are _____.

We will require Forms 668-A _____ days before paydays.

_____
Signature of firm representative or individual named above

_____ _____
Area code and phone number Date

_____
Signature of Internal Revenue Service representative

_____ _____
Area code and phone number Date

GPO 928-554

Exhibit 6—Form 668C

FORM 668-C (REV. MAY 1967)	U. S. TREASURY DEPARTMENT - INTERNAL REVENUE SERVICE **FINAL DEMAND**

DISTRICT	DATE

TO:

On _____, 19___, there was served upon you a levy, by leaving with _____ at _____ a notice of levy, on all property, rights to property, moneys, credits and bank deposits then in your possession, to the credit of, belonging to, or owned by _____ of _____, who was at the time, and still is, indebted to the United States of America for unpaid internal revenue taxes, together with additions provided by law which had accrued thereon at the time of levy, and which amounted at that time to the sum of $_____. Demand was made upon you for the amount set forth in the notice of levy, or for such lesser sum as you may have been indebted to the taxpayer, which demand has not been met.

Your attention is invited to the provisions of section 6332, Internal Revenue Code, as follows:

SEC. 6332. SURRENDER OF PROPERTY SUBJECT TO LEVY.

(a) Requirement.—Except as otherwise provided in subsection (b), any person in possession of (or obligated with respect to) property or rights to property subject to levy upon which a levy has been made shall, upon demand of the Secretary or his delegate, surrender such property or rights (or discharge such obligation) to the Secretary or his delegate, except such part of the property or rights as is, at the time of such demand, subject to an attachment or execution under any judicial process.

(c) Enforcement of Levy.—

(1) Extent of Personal Liability.—Any person who fails or refuses to surrender any property or rights to property, subject to levy, upon demand by the Secretary or his delegate, shall be liable in his own person and estate to the United States in a sum equal to the value of the property or rights not so surrendered, but not exceeding the amount of taxes for the collection of which such levy has been made, together with costs and interest on such sum at the rate of 6 percent per annum from the date of such levy. Any amount (other than costs) recovered under this paragraph shall be credited against the tax liability for the collection of which such levy was made.

(2) Penalty for Violation.—In addition to the personal liability imposed by paragraph (1), if any person required to surrender property or rights to property fails or refuses to surrender such property or rights to property without reasonable cause, such person shall be liable for a penalty equal to 50 percent of the amount recoverable under paragraph (1). No part of such penalty shall be credited against the tax liability for the collection of which such levy was made.

(d) Effect of Honoring Levy.—Any person in possession of (or obligated with respect to) property or rights to property subject to levy upon which a levy has been made who, upon demand by the Secretary or his delegate, surrenders such property or rights to property (or discharges such obligation) to the Secretary or his delegate (or who pays a liability under subsection (c)(1)) shall be discharged from any obligation or liability to the delinquent taxpayer with respect to such property or rights to property arising from such surrender or payment. In the case of a levy which is satisfied pursuant to subsection (b), such organization shall also be discharged from any obligation or liability to any beneficiary arising from such surrender or payment.

(e) Person Defined.—The term "person," as used in subsection (a), includes an officer or employee of a corporation or a member or employee of a partnership, who as such officer, employee, or member is under a duty to surrender the property or rights to property, or to discharge the obligation.

Demand is again made for the amount set forth in the notice of levy, $_____, or for such lesser sum as you may have been indebted to the taxpayer at the time the notice of levy was served. If you comply with this final demand within five days from its service, no action will be taken to enforce the provisions of section 6332 of the Internal Revenue Code. If, however, this demand is not complied with within five days from the date of its service, it will be deemed to be finally refused by you and proceedings may be instituted by the United States as authorized by the statute quoted above.

SIGNATURE	TITLE	ADDRESS *(City and State)*

CERTIFICATE OF SERVICE

I hereby certify that this Final Demand was served by handing a copy thereof to:

NAME	TITLE	
PLACE	DATE	TIME
REVENUE OFFICER *(Signature)*		DATE

FORM 668-C (REV. 5-67)

U. S. GOVERNMENT PRINTING OFFICE : 1971 O - 401 - 873

Exhibit 7—Form 2270

FORM 2270
(REV. MAR. 1968)

DEPARTMENT OF THE TREASURY · INTERNAL REVENUE SERVICE

NOTICE OF REQUIREMENT TO EXHIBIT BOOKS AND RECORDS

To *(Name and address of person holding books or records)*

Taxpayer *(Name and address)*

Please make available for my examination any books or records in your possession or control containing evidence relative to property or rights to property belonging to the above named taxpayer (or in which the taxpayer has an interest) as of the date of service of this Notice, or if a notice of levy has been served, as of the time of service of such notice of levy. The inspection of these records is necessary because a levy has been made or is about to be made on property or rights to property belonging to the above named taxpayer. Authority for this request is provided by section 6333 of the Internal Revenue Code and corresponding regulations, which are quoted below.

REVENUE OFFICER *(Signature)*	OFFICE ADDRESS	DATE

EXCERPT FROM INTERNAL REVENUE CODE OF 1954

SECTION 6333. PRODUCTION OF BOOKS

If a levy has been made or is about to be made on any property, or right to property, any person having custody or control of any books or records, containing evidence or statements relating to the property or right to property subject to levy, shall, upon demand of the Secretary or his delegate, exhibit such books or records to the Secretary or his delegate.

REGULATIONS ISSUED UNDER SECTION 6333

SECTION 301.6333-1. **Production of Books.** If a levy has been made or is about to be made on any property or rights to property, any person, having custody or control of any books or records containing evidence or statements relating to the property or rights to property subject to levy, shall, upon demand of the internal revenue officer who has made or is about to make the levy, exhibit such books or records to such officer.

GPO 875-101

FORM 2270 (REV. 3-69)

Exhibit 8—Form RC SE ACTS 11

Department of the Treasury

District Director
Internal Revenue Service

Date: | In reply refer to:

Notice is given that _____

_____

is indebted to the United States for unpaid Internal Revenue tax. Therefore, under authority of section 6333 of the Internal Revenue Code (quoted below), please furnish the information indicated by the box checked.

DISTRICT DIRECTOR

By: _____
(Revenue Officer)

☐ BANK ACCOUNTS AND SAFE DEPOSIT BOX

Present credit balance on deposit in →	CHECKING ACCT.	SAVINGS ACCT.	SERIAL NO. OF SAFE DEPOSIT BOX (If any)
	$	$	

☐ LOAN INFORMATION, ETC.

ORIGINAL AMOUNT OF OUTSTANDING LOAN	PRESENT UNPAID BALANCE	DATE LOAN MADE
$	$	
REPAYMENT TERMS	DESCRIPTION OF COLLATERAL	

OTHER INFORMATION *(As requested)*

EXCERPT FROM INTERNAL REVENUE CODE

Section 6333. PRODUCTION OF BOOKS — If a levy has been made or is about to be made on any property, or right to property, any person having custody or control of any books or records, containing evidence or statements relating to the property or right to property subject to levy, shall, upon demand of the Secretary or his delegate, exhibit such books or records to the Secretary or his delegate.

RC SE FORM ACTS-11 (12-71)

APPENDIX

Communications Received by the Committee Expressing an Interest in These Hearings

AMERICAN CIVIL LIBERTIES UNION,
Washington, D.C., November 17, 1975.

HON. FLOYD K. HASKELL,
Chairman, Subcommittee on Administration of the Internal Revenue Code, Senate Finance Committee, Washington, D.C.

DEAR SENATOR HASKELL: We appreciate the invitation by Subcommittee staff to testify at your hearings held November 5 on the use of I.R.S. summons for taxpayer financial records. As we were unable to appear that day, we would like to submit this prepared statement for the hearing record.

I would like to take this opportunity on behalf of the ACLU to urge you to consider as a model for dealing with I.R.S. inspection of bank records S. 1343, a bill which would insure that bank customers have notice of and an opportunity to challenge any federal government access to thir bank records *before* such access takes place. As it now stands, the bank customer is totally helpless unless the bank insists on a subpoena and chooses to notify the customer, steps which involve the bank in expense, inconvenience and, perhaps most significant, controversy with the government. S. 1343, which has had bipartisan sponsorship in both Houses of Congress for several years, would solve the problem.

Of course, we would be happy to work with you or members of your staff at any time on this problem.

Sincerely yours,

HOPE EASTMAN,
Associate Director.

AMERICAN CIVIL LIBERTIES UNION

STATEMENT OF HOPE EASTMAN, ASSOCIATE DIRECTOR, WASHINGTON NATIONAL OFFICE, AMERICAN CIVIL LIBERTIES UNION ON INTERNAL REVENUE SERVICE SUMMONS FOR TAXPAYER'S FINANCIAL RECORDS

My name is Hope Eastman. I am a lawyer and the Associate Director of the Washington National Office of the American Civil Liberties Union, a non-profit organization wholly devoted to the protection of our rights and liberties under the Constitution.

It is the position of the ACLU that individuals who choose to conduct their financial and political lives with the aid of a bank should in no way lose the constitutional and statutory protections they would otherwise have if they alone kept a record of their financial dealings.

As will be developed more fully in this statement, there is an urgent need for legislative action to safeguard the expectation of privacy held by each citizen who uses the facilities of banking institutions to conduct his or her routine affairs. We urge you to enact legislation to stop informal government access to bank records without the knowledge of the customer and to provide that the customer will have notice of and an opportunity to challenge attempts to search his or her bank records.

The need for legislative safeguards

An individual's banking transactions are a mirror to his or her life, especially political life. Information about the groups one joins, the publications to which one subscribes, the books one buys, and the causes one supports may all be determined from an examination of bank records. The revelations over the last few years suggest that fears that bank records will become a tool of political surveillance are quite real and deserve Congressional attention.

A person writing a check or making a deposit in a bank assumes that these transactions are no one's business but his or her own. People assume they can use checking accounts without there being dossiers on their lives and political associations. Traditionally, the guarantee of confidentiality and privacy had been thought to be at the heart of the relationship between the bank and its customers. Courts have traditionally recognized that this is so.

> "Inviolate secrecy is one of the inherent and fundamental precepts of the relationship of the bank and its customers and depositors." *Peterson v. Idaho First National Bank*, 83 Ida. 578, 367 F.2d 284, 290 (1961); see also *Zimmerman v. Wilson*, 81 F.2d 847 (3d Cir. 1936); *United States v. First National Bank of Mobile*, 67 F. Supp. 616 (S.D. Ala. 1946); *Brex v. Smith*, 146 Atl. 34, 36–7 (Ch. N.J. 1929).

In fact, however, bank customers do not enjoy the privacy that they thought they had, since the federal government asserts an essentially unrestricted right to examine bank accounts, limited only by the bank's willingness to cooperate. An examination of the government's brief filed in a case pending in the Supreme Court demonstrates the position being taken by the Department of Justice:

> "[Bank] records do not constitute the bank depositor's private papers, since the bank owns and possesses them . . . A bank depositor has no justifiable expectation that information he conveys to the bank in the course of his transactions with it will remain private.

Brief for the United States, *United States v. Miller*, *cert. granted* (No. 74–1179), p. 11–2. Indeed, in that case the government argues that the Court should refrain from any action to safeguard the privacy of bank records as "this is a matter of legislative policy for determination by Congress, not a constitutional imperative." Id. at 31.

It is clear that when it enacted the Bank Secrecy Act in 1970, Congress believed it could impose record-keeping requirements on financial institutions without sacrificing the privacy and confidentiality expected by bank customers. The Senate Banking Committee report on the bill states at page 5 that:

> "Access by law enforcement officials to bank records required to be kept under this title *would, of course, be only pursuant to a subpena or other lawful process as is presently the case.* The legislation in no way authorizes unlimited fishing expeditions on the part of law enforcement officials." Senate Report No. 91–1139, 91st Cong. 2nd Sess., (emphasis added).

Similar language appears in the House Report:

> "It should be kept in mind that records to be maintained pursuant to regulations of the Secretary of the Treasury will not be automatically available for law enforcement purposes. They can only be obtained through *existing legal processes.*" House Report No. 91–631, 91st Cong. 2nd Sess. (1970), (emphasis added).

Moreover, floor debate prior to enactment of the Bank Secrecy Act reveals House members were under the clear impression that government access to bank records would be limited to subpenas. See e.g. 116 Cong. Rec. 16963–4 (1970). Furthermore, Congress recognized that bank customers have a reasonable expectation of privacy concerning their accounts. See e.g. 116 Cong. Rec. 16962; Senate Hearings pp. 154–5, 177–9; House Hearings, p. 131.

Even the Supreme Court, which rejected the arguments raised by those seeking to protect their privacy to uphold the constitutionality of the Bank Secrecy Act, believed that bank customers still had a way to protect themselves against fishing expeditions and other abuses. Said the court:

> Claims of depositors against the compulsion by lawful process of bank records involving the depositors' own transactions must wait until such process issues.
>
> * * * * * * *
>
> Neither the provisions of Title I nor the implementing regulations require that any information contained in the records be disclosed to the government; both the legislative history and the regulations make specific reference to the fact that access to the records is to be controlled by existing legal process. *California Bankers Association* v. *Shultz*, 416 U.S. 21, 51–2 (1974).

However, this talisman—"existing legal process"—now turns out to be a total sham. In fact, informal access to bank records without subpenas is a favorite tool of government investigators, subject only to the willingness, or lack thereof, of the banks. Consider, for example, the following portion of the Internal Revenue Manual, the basic training guide for agents of the I.R.S.

> "The importance of bank records to Intelligence investigators and the rapid changes in banking procedures brought about by automation, makes it highly desirable for management officials in the field to meet with and get to know banking officials personally. The objective of such actions is to improve relationships with these officials and to open channels of communi-

cation beneficial to both parties." Int. Rev. Manual, § 937 (12), MT 9300-49 (2-19-75).

The following portion of testimony by James E. Merritt, an attorney for Crocker National Bank of California, before the House Subcommittee on Courts Civil Liberties and the Administration of Justice (July 25, 1975), graphically demonstrates the means by which the government normally procures access to confidential bank records. It reveals the not inconsiderable pressures placed on the bank to comply without invoking legally process and without giving the customer the notice which would allow him or her an opportunity to assert his or her rights before access is allowed.

". . . The normal situation has been for a police officer, an Internal Revenue Agent, or another law enforcement official to appear at a bank branch in person and request certain records relating to a specific customer. . . . Normally the investigating agent will speak with the manager of the branch. If the manager is hesitant in producing the records the agent will prepare a so-called "pocket summons" and serve it upon the manager. [A pocket summons is merely a blank subpena signed in advance by a person authorized to do so, with the details to be filled in on the spot when a reluctant bank official is encountered.]

At this point there is pressure upon the bank personnel: (1) to comply with an apparently authorized law enforcement official, and (2) to permit review of the records immediately with the promise, express or implied, that if the bank officer does it will save time and money. This inducement for immediately production is premised upon the representation that the investigating agent by an immediate review can limit the number of records and, if copies are produced, can make it unnecessary for the officer to personally deliver such records to an agency or court at a future date.

These pressures are not inconsiderable. Moreover, it should be borne in mind that the bank official is not a lawyer nor is he or she generally familiar with the statutory and other requirements which apply to determine the validity of such a demand. As a result, in the past, these informal requests and subtle pressures have frequently achieved the objective of the investigating agent and the records have been made available."

Crocker National Bank has adopted a policy of requiring government officials to obtain court orders before inspection of a customer's records is permitted and the bank makes an effort to notify the customer involved. However, not all banking institutions are equally careful to ensure the privacy of their customers. In April of 1972, the ACLU wrote to the presidents of the nation's largest banks seeking information on their policies and urging them to formulate procedures to protect the confidentiality of customer records and insure that customers will be notified when investigative agencies seek personal account information. Similar letters were sent by ACLU affiliates in the 50 states to banks in their areas.

We received replies from approximately one-quarter of these banks. There was no uniform practice among banks on these questions and no clear law compelling banks to keep their customer's records confidential.

Some institutions reported that they resist informal inquiries by government agencies for customer account information and release such data only if they are served with a subpena or court order. Yet exceptions to this rule were pointed out frequently. Others indicated that they release information only after a subpena is served on them, but do not notify customers that the government has demanded such information. A few alert customers to the fact that the government wants to monitor their accounts, thereby giving the customers the opportunity to take legal action if they so desire. Still others agree with the principle of notifying customers of subpoenas, but assert that there are unspecified times when they must make ad hoc exceptions to this rule.

The Congress must establish clear standards. The current situation puts the bank in the uncomfortable position of having to decide whether or not to accede to a government request without any way to evaluate the request and without any way of knowing what is at stake for the customer. Especially when critical First Amendment rights may be at stake, as bank records can reveal important features of the customer's political life, reliance on the bank to protect the customer's privacy is wholly inadequate. The customer does not have the opportunity to defend against unwarranted government access because in many instances he or she will simply be unaware that the government is seeking access to his or her records. The burden of notifying the customer should not rest with the bank. Rather the government agency itself should take the

responsibility for notification. Enforcement of the summons should be delayed until the customer has been given a reasonable period of time in which to resist enforcement if he or she chooses to do so.

Improper government access to bank records for political purposes has clearly occurred. Perhaps the most well-known is that of Daniel Ellsberg whose bank records helped lead The Plumbers to Dr. Lewis Fielding. The Internal Revenue Service too is now known to have badly abused its authority in the tax collection area. Attached to this statement is a compilation of information detailing the abuses which we have witnessed over the past few years of the authority of the Internal Revenue Service. This information has been derived from facts on the public record, and prepared by the Center for National Security Studies.

Important as it is, however, our concern is not only with possible political abuses of the I.R.S. subpoena power. Whatever the extent of abuse for political purposes, informal I.R.S. access to bank records without benefit of legal process is the rule. Legislation is needed to govern agency practices in this area in order to protect all citizens from routine access to their bank records by federal agencies without any supervision by the courts.

Safeguards in I.R.S. Summons Procedure Meaningless Without Notice

The Internal Revenue Service is vested by law with authority to require the production of "books, papers, records, or other data which may be relevant or material" to an inquiry into the correctness of any tax return or other determination of potential tax liability. 26 U.S.C. § 7602. This broad power of investigation has been likened to that possessed by a Grand Jury.

The Supreme Court has held that probable cause is not required to support the issuance of an I.R.S. summons. *United States* v. *Powell*, 379 U.S. 48 (1964). In the same case, however, the Court developed some of the limitations which exist on the exercise of the summons power:

> It is the court's process which is invoked to enforce the administrative summons, and a court may not permit its process to be abused. Since an abuse would take place if the summons had been issued for an improper purpose, such as to harass the taxpayer or to put pressure on him to settle a collateral dispute, or for any other purpose reflecting on the good faith of the particular investigation. *Powell* id. at 58 (citations omitted).

In a more recent case, the Court also indicated that an administrative summons could not be issued solely for the purpose of a criminal investigation. *See Donaldson* v. *United States*, 400 U.S. 517 (1971).

Thus, although the I.R.S. has broad powers to compel the production of documents and other relevant materials, there are limits on that authority. However, as outlined above, these limits are illusory if the person in the best position to evaluate whether the I.R.S. has exceeded or abused its authority—the bank customer—is denied notice and the opportunity to defend his or her privacy.

Congress can remedy this situation requiring that when a subpoena is issued by the I.R.S. to a bank, the Service must also notify the customer of the proposed inspection and delay enforcement for a reasonable period to allow the customer the opportunity to challenge the subpoena if he or she so desires. To insure that this notification is effective, we also urge you to place a flat prohibition, together with appropriate sanctions, on "informal" access to customer's bank records in the absence of a court order requiring production by the bank, unless the customer consents to the examination.

The Congress should also make it clear in such legislation that the customer will have standing to raise the kind of objections foreseen by the Supreme Court in the *Powell* case, *supra*, to insure that the summons power was not abused.

Until recently, it was clear that bank customers and others who gave records in confidence to persons such as their accountants could look to the courts to give them standing to protect their rights. In *Reisman* v. *Caplin*, 375 U.S. 440 (1964), the Supreme Court took the position that a taxpayer had the right to intervene when an I.R.S. summons was improperly directed to a third-party to gather information about taxpayer.

However, the scope of that holding has been placed in doubt by recent cases. In *Donaldson* v. *United States*, 400 U.S. 517 (1971), the Court indicated that, in order to intervene, the taxpayer must have a "significantly protectable interest" in the records being sought from the third-party witness. The contours of that interest have not yet been clearly defined especially with respect to bank records. Cf. *Couch* v. *United States*, 409 U.S. 322 (1973); *California Bankers Association* v. *Schultz*, 416 U.S. 21 (1974).

As we indicated early in this testimony, the government argues that the bank customer has *no* interest in the records for they belong to and are possessed by the bank. Relying on this simple property law notion, the government claims that the customer has no "reasonable expectation of privacy." However, in the very case from which that phrase was taken, *Katz* v. *United States*, 389 U.S. 347, 352 (1967), the Supreme Court abandoned the property approach to the Fourth and Fifth Amendments. The Congress has already implicitly recognized that customers have certain expectations of privacy with respect to information in their bank accounts by invoking the "existing legal process" phrase to ally the fears of fishing expeditions which preceded the Bank Secrecy Act. In enacting new legislation here, the Congress should make this explicit.

CONCLUSION

In conclusion, we would like to commend to you as a model for protecting the privacy of bank customers S. 1343, a bill presently pending before the Senate Banking Committee. Its combination of a prohibition on informal access in the absence of customer consent, along with a requirement for with timely notice and standing to intervene will provide citizens the right to insure that the Service does not abuse its admittedly vast authority to compel disclosure of information.

In opposing legislation of this kind in the past, representatives of the Justice Department and the I.R.S. have urged the Congress not to legislate, but to rely instead on the good faith and reasonableness of those empowered to seek these records on behalf of the government. In evaluating the need for this legislation, we urge you to keep firmly in mind the words of Mr. Justice Powell:

> "The historical judgment, which the Fourth Amendment accepts, is that unreviewed executive discretion may yield too readily to pressures to obtain incriminating evidence and to overlook potential invasions of privacy and protected speech." *U.S.* v. *U.S.D.C., E.D. Mich.*, 407 U.S. 297 (1972)

Internal Revenue Service

SUMMARY

The Internal Revenue Service is a unit of the Treasury Department charged with enforcing the tax laws. It is authorized by Congress to investigate possible violations of these laws and has broad power to examine records and other relevant data. The IRS has from time to time used its power to conduct audits of groups and individuals whose political views and activities were of concern to others. Special groups were established to conduct such audits under the Kennedy, Johnson and Nixon Administrations. On at least one occasion an audit was conducted at the request of a congressional committee. The IRS has also established files on politically active groups and individuals, and has disclosed tax information, in violation of its rules, to officials outside the IRS on groups and on individuals such as George Wallace's brother and Ronald Reagan.

The IRS, in general, relies on information from tax audits and from other agencies, but from time to time it conducts its own surveillance, including infiltration of tax protest groups. The Special Services Staff set up during the Nixon Administration was the most concentrated effort by the IRS to use all available means to investigate and harass groups and individuals because of their political beliefs and activities. The IRS has halted most of these activities.

AUTHORITY

Under Section 7601 of the Internal Revenue Code, the Secretary of the Treasury is authorized to "cause officers or employees of the Treasury Department to . . . inquire after and concerning all persons . . . who may be liable to pay any internal revenue tax. . . ."[1] To establish liability, Section 7602 gives the IRS, a unit of the Treasury Department, the authority to examine "any books, papers, records or other data which may be relevant or material" in ascertaining the correctness of any return or making a return where none has been made.[2] The IRS "seeks to encourage and achieve the highest possible degree of voluntary compliance" with federal tax regulations and employs random and selective audit procedures to stimulate such compliance.[3]

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[1] 26 U.S. Code 7601.
[2] 26 U.S. Code 7602.
[3] 39 Federal Register 11572, March 29, 1974.

The authority for the IRS to inquire into political activities of persons and groups is defined solely in terms of its authority to insure that all tax-exempt organizations comply with the provisions of Section 501(c)(3) of the Internal Revenue Code, which provides that tax-exempt charitable, educational organizations cannot participate or intervene in political campaigns for public office or devote a substantial part of their activities to "carrying on propaganda, or otherwise attempting, to influence legislation." [4]

Section 6103(a) of the Internal Revenue Code provides that income tax returns are to be "open to inspection only upon order of the President and under rules and regulations prescribed by the Secretary of the Treasury or his delegate and approved by the President." [5]

ACTIVITIES AND PROGRAMS

Politically motivated audits

Either on its own initiative or at the request of the White House, other Executive Branch officials, or congressional committees, the IRS conducted audits and otherwise harrassed organizations and individuals because of their political beliefs or lawful political activities.

Lenske Audit.—The IRS spent two and one half years (1955–1958) conducting a total audit of Reuben G. Lenske, including the interviewing of between 500 and 1500 witnesses, and made assessments many times the real value of Lenske's worth. IRS files included law enforcement information alleging that Lenske was a Communist and was affiliated with the National Lawyers Guild. A federal court in reversing an IRS decision claiming Lenske owed money to the Government, charged the IRS with conducting "a crusade . . . to rid our society of unorthodox thinkers and actors by using federal income tax laws and federal courts to put them in the penitentiary." [6]

Communist Party Harassment.—From 1954 until 1964, the IRS employed a number of delaying tactics to prevent the Communist Party from appealing an IRS ruling that it owed back taxes for the year 1951. In 1964, a United States Court of Appeals, after examining the record, ordered the appeal, finding that the Communist Party "cannot be thrown out of court, for the reasons and under the circumstances obtaining without verging too closely towards the wholly unacceptable proposition that the rules of the game vary with the players." [7]

Kennedy/Johnson "Extremist Groups".—In 1961, the IRS launched an investigation aimed at 22 organizations, 12 "right-wing" and 10 "left-wing." This action was stimulated by a press conference statement made by President Kennedy raising the possibility that tax-exempt funds of "right-wing" organizations were being diverted for non tax-exempt purposes, and a followup suggestion by Attorney General Robert Kennedy to investigate the tax status of extremist groups. As a consequence, the tax-exempt status of two "right-wing" organizations was revoked.[8]

In 1963, the IRS again focused on "extremist" organizations because, according to former IRS Commissioner Mortimer Caplin, President Kennedy told him in a phone call "to go ahead with an aggressive program—on both sides of center." [9] Four of 25 organizaitons examined lost their exempt status, including one "left-wing" group. This program, started under President Kennedy, was terminated in 1966 under President Johnson.[10]

Nixon Enemies List.—At various times from 1969 through 1973, President Nixon, acting through his White House staff, applied pressure on the IRS to use its powers against political opponents. Proposals to the IRS ranged from a 1969 White House request to go after "left-wing groups" [11] to the 1972 effort to have the IRS audit key persons on the White House "Enemies List," which included a score of persons and organizations across the political spectrum.[12] Individuals

[4] 26 U.S. Code 501(c)(3).
[5] 26 U.S. Code 6103(a).
[6] *Reuben G. Lenske* v. *United States*, 383 F. 2d 20 (CA 9, 1967), page 27.
[7] *Communist Party U.S.A.* v. *Commissioner of Internal Revenue*, 332 F. 2d 325 (App. D.C. 1967), page 329. The case was concluded in 1967 when the Court of Appeals again reversed a Tax Court ruling and held that CPUSA had shown its central contention that, like other political parties, it was not subject to federal income taxes. (*Communist Party U.S.A.* v. *Commissioner of Internal Revenue*, 373 F. 2d 682, 1967).
[8] Special Service Report, 1975, Source 11, pages 13, 105.
[9] Special Service Report, 1975, Source 11, page 106.
[10] Special Service Report, 1975, Source 11, page 14.
[11] Special Service Report, 1974, Source 12, page 9.
[12] Impeachment Book VIII, Source 13, pages 9–11, 25–26. The list was compiled from June 24, 1971 through June, 1972, and included over 200 names of individuals. On September 11, 1972, John Dean gave the list to Commissioner of Internal Revenue Johnnie

such as Larry O'Brien, [12] Harold Gibbons of the Teamsters Union,[14] and Senator McGovern's campaign staff [15] were subjects of particular White House requests. Although IRS officials have stated that they resisted these efforts (a claim substantiated in part by White House staff memorandums accusing the IRS of "lack of guts and effort" [16]), certain enforcement actions were taken. For example, the Center for Corporate Responsibility, a Washington, D.C. public interest group started by Ralph Nader was denied tax-exempt status. On May 2, 1978, the group filed suit claiming that it had been unlawfully denied tax-exempt status as a result of selective treatment for political, ideological and other improper reasons having no basis in the statute and regulations. In 1978, a United States District Court held that the tax exemption had been unlawfully denied, and drew an inference of political interference and bias when the White House refused to comply fully with discovery orders.[17]

Black Panthers Audit.—On October 14, 1970, the IRS responded to a request of the House of Representatives Committee on Internal Security [18] with the assurance that it was "strictly enforce" the provisions of the U.S. tax regulations against the Black Panther Party. The Committee was then examining the Party as possibly "subversive". In a letter from IRS Commissioner Randolph W. Thrower to Committee Chairman Richard H. Ichord, Thrower stated: "The organization and its principals are currently under a full scale investigation. . . . I appreciate your giving me the opportunity to inform you of the Service's action in the matter, and want to assure you that any tax obligation for which the organization may be found liable will be strictly enforced." [19]

Intelligence Files

The IRS has established files on politically active groups and individuals ostensibly for tax enforcement purposes. Various methods were used to gather information with the aim of affecting political activity.

Intelligence Gathering and Retrieval System.—Between 1973 and 1975 the IRS developed the "Intelligence Gathering and Retrieval System" or IGRS, a nationwide index system for intelligence gathering and retrieval. The initial stated purpose of IGRS was "to provide an effective, uniform means of gathering, evaluating, cross-indexing, retrieving, and coordinating data relating to the individuals and entities involved in *illegal activities* and have potental tax violations on a district and individual basis." (emphasis added) [20] Under ths program, suspended in January, 1975,[21] the IRS had indexed information on 465,442 individuals, organizations and other entities. Indexed items included news articles, tax return information, memorandums or reports from special agents, police reports, financial information from public records, and information from informants.[22] According to one account of the IGRS files, they include information on public political figures, primarily "liberals, anti-war activists, ghetto

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Walters and requested that the IRS begin investigations or examinations on individuals on the list. Upon the advice of Secretary of the Treasury Shultz, no action was taken. On September 25, 1972, Dean telephoned Walters to inquire about the progress made on the list, and when informed that no action had been taken requested that perhaps the list could be reduced to fifty to seventy individuals, and action taken against this smaller list. Again, no IRS action resulted.

[13] Johnnie Walters Affidavit, June 10, 1974, Impeachment Book VIII, Source 13, page 218. John Ehrlichman of the White House staff contacted Commissioner Walters several times to inquire as to the status of the audit on Lawrence O'Brien; when no action resulted, the matter eventually reached the attention of President Nixon.

[14] Charles Colson Memorandum, June 12, 1972, Impeachment Book VIII, Source 13, page 216.

[15] Johnnie Walters Affidavit, May 6, 1974, Impeachment Book VIII, Source 13, page 238.

[16] Impeachment Book VIII, Source 13, page 196. A November 1971 "talking paper" discussed specifically the problem of making IRS politically responsive to the White House. It read, in part:

> . . . The Republican appointees appear afraid and unwilling to do anything with IRS that could be politically helpful. For example:
> —We have been unable to obtain information in the possession of IRS regarding our political enemies
> —We have been unable to stimulate audits of persons who should be audited.
> —We have been unsuccessful in placing RN supporters in the IRS bureaucracy.

[17] Impeachment Book VIII, Source 13, page 32, and *Center for Corporate Responsibility v. Schultz*, 368 F. Supp. 863, pages 871–872.

[18] October 14, 1970 letter from Randolph Thrower to Richard Ichord, Black Panther Hearings, Source 5, page 5096.

[19] October 14, 1970 letter, Black Panther Hearings, Source 5, page 5096.

[20] FY 76 Appropriations Hearings, Source 14, page 461.

[21] FY 76 Appropriations Hearings, Source 14, page 461.

[22] FY 76 Appropriation Hearings, Source 14, page 462.

leaders and the like,"[22] including Los Angeles Mayor Thomas Bradley, Ex-Attorney General Ramsey Clark, and Congressman Augustus Hawkins, and groups such as the American Civil Liberties Union, the Communist Party, the Baptist Foundation of America and the Medical Committee for Human Rights.[24]

Disclosing Tax Information

Without using its formal procedures IRS disclosed tax information which was used for political purposes to the White House and other agencies. For example, in April, 1968, the IRS formalized a "National Security Case" procedure with the Internal Security Division of the Justice Department whereby it made tax data available upon request on various political organizations and individuals.[25] Then, during the Nixon Administration, IRS files were turned over to the White House staff. The returns made available to the White House included those of the brother of George Wallace (Gerald Wallace),[26] the Brookings Institution,[27] Lawrence Goldberg,[28] Reverend Billy Graham,[29] Ronald Reagan,[30] John Wayne and other entertainers.[31] In the Wallace case, the material was used by a reporter to write an article charging corruption in the Wallace Administration.[32] The IRS also disclosed tax information about *Ramparts* magazine to the CIA, which was seeking a means to suppress a forthcoming story on CIA ties to the National Student Association.[33]

Surveillance Activities

Although in most cases the IRS appears to have relied on tax audits or other agencies to gather information, from time to time it engaged in its own surveillance activities.

Operation Leprechaun.—In Miami, Florida, IRS agents developed "Operation Leprechaun" in April, 1972. The program was designed to gather information on the sex and drinking habits and on the political activities of prominent individuals in the area; 34 informers were employed for this purpose.[34]

Tax Protesters.—From June, 1972 through January, 1975, the IRS maintained surveillance on 5 tax protest groups. Agents of the IRS went to tax protest meetings and took down names, license plate and telephone numbers of persons attending. Agents' memorandums include the political and other opinions expressed at these meetings.[35]

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[23] Donner, Source 3, page 56. Donner's source for this information was a selective printout of 172 names leaked to the public in late Spring of 1975, presumably by an IRS employee.

[24] Donner, Source 3, pages 56, 57. Donner's source is described above.

[25] Special Service Report 1974, Source 12, page 22.

[26] Impeachment Book VIII, Source 13, page 3. On or about March 21, 1970, Special Counsel to the President Clark Mollenhoff sent a memorandum to H. R. Haldeman transmitting material on the federal income tax returns of Gerald Wallace. Mollenhoff has testified that he obtained the material from the IRS on instructions from Haldeman who assured him that the report was to be obtained at the request of the President. On April 13, 1970 an article by Jack Anderson appeared containing information from confidential IRS field reports, and detailing IRS investigation charges of corruption in the Wallace administration and the activities of Gerald Wallace. The origins of the leak are unclear, although Former Commissioner Thrower has stated that an IRS investigation concluded the material had not been leaked by the IRS or the Treasury Department. Clark Mollenhoff Memorandum, March 21, 1970 and "IRS Probes Wallace, Lurleen Reigns", *Washington Post,* April 13, 1970, Source 11, pages 36, 37.

[27] Memorandum from John Dean to Bud Krogh, July 20, 1971, Impeachment Book VIII, Source 13, page 80.

[28] Memorandum from John Caulfield to John Dean, October 6, 1971. Impeachment Book VIII, Source 13, page 133. A memorandum dated October 6, 1971 from John Caulfield to John Dean contained a list of charitable contributions obtained from Goldberg's tax returns, and was sent to the White House outside of "regular channels" by IRS Assistant Commissioner (Inspection) Vernon Acree. Acree was subsequently promoted to Commissioner of the U.S. Customs Service.

[29] Memorandum from John Caulfield to John Dean, September 30, 1971, Impeachment Book VIII, Source 13, page 147. Tax information on Graham was also sent to the White House by Vernon Acree.

[30] Memorandum from John Caulfield to John Dean, October 6, 1971, Impeachment Book VIII, Source 13, page 156.

[31] Memorandum from John Caulfield to John Dean, October 6, 1971, Impeachment Book VIII, Source 13, page 156.

[32] "IRS Probes Wallace, Lurleen Reigns," *Washington Post,* April 13, 1970, Impeachment Book VIII, Source 13, page 37.

[33] CIA Document Released to Church Committee, Source 6.

[34] Jacksonville Report, Source 9, pages 13–17. One IRS agent involved in "Operation Leprechaun" made use of 62 confidential informants, 34 paid and 28 unpaid, at a cost of $15,140.01. One of his paid informants was directed in 1972 to spy on 30 Miami residents, including federal judges and a state attorney. (source 9, pages 18, 24)

[35] Apr. 13, 1975, *New York Times,* Source 4.

Special Services Staff

Because its activities cut across many of the areas described above and because it is the most questionable activity of the IRS this report describes the activities of the Special Services Staff together here.

On July 18, 1969, the IRS established a Special Service Staff "to coordinate activities in all Compliance Divisions involving ideological, militant, subversive, radical and similar type organizations; to collect basic intelligence data, and to insure that the requirements of the Internal Revenue Code concerning such organizations have been complied with." [36]

The origin of the SSS appears to be a request by President Nixon to White House aide Tom Charles Huston "for the IRS to move against leftist organizations taking advantage of tax shelters." [37] Huston and Dr. Arthur Burns, a top domestic advisor to President Nixon, conveyed this request to IRS Commissioner Randolph Thrower at a meeting on June 16, 1969 and in followup letters and memorandums.[38]

At a meeting on July 2, 1969, officials of the Compliance Division of IRS discussed the creation of a group inside the IRS to examine "ideological organizations" and to collect intelligence on these groups through a "strike force" operational approach.[39] Following this meeting the SSS was established. The IRS admitted in a July 24th memorandum that, "from a strictly revenue standpoint, we may have little reason for establishing this committee or for expending the time and effort which may be necessary." However, the memo continued, "we must do it." [40]

On September 21, 1970, White House aide Huston said this about the SSS in an internal memo: "What we cannot do in a court room via criminal prosecutions to curtail the activities of some of these groups, IRS could do by administrative action. Moreover, valuable intelligence-type information could be turned up by the IRS as a result of their field audits." [41]

The Special Services Staff, from its inception until its termination in August, 1973, engaged in the following activities:

Used an informant to collect political intelligence information; from mid-1970 until August, 1973, the SSS received bi-weekly "intelligence digests" from an informant active in organizations engaged in anti-war activities in Washington, D.C.[42]

—Established post office "drop boxes" registered under assumed names to collect publications with information that might relate to activist political organizations and persons.[43]

—Received intelligence from other units of the IRS, particularly field offices, Service Centers, and the files of its divisional Intelligence files.[44]

—Collected intelligence-type information from other agencies of government on individuals and groups of certain political persuasions. The SSS received 11,818 separate reports from the FBI, over 6,000 of them classified, including FBI COINTELPRO reports, and an FBI list of over 2,300 organizations categorized as "Old Left," "New Left," and "Right-Wing." [45] Although 43% of its information came from the FBI, SSS also collected information from other agencies, including the Inter-Divisional Information Unit of the Department of Justice (16,000 persons and organizations who might potentially engage in civil disturbances),[46] the Social Security Administration (several hundred requests to identify and

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[36] Memorandum from D. W. Bacon to Assistant Commissioners, Special Service Report, 1974, July 18, 1969, Source 12, p. 123.

[37] Memorandum from Tom Huston to H. R. Haldeman, Sept. 21, 1970, Watergate Book 3, Source 7, p. 1338.

[38] Special Service Report 1975, Source 11, pp. 5 and 29–31. Mr. Thrower's memorandum to the file of June 16, 1969, concerning the meetings, states that Dr. Burns was "initially interested in expressing to me the concern of the President about enforcement in the area of exempt organizations. The President had expressed to him great concern over the fact that tax-exempt funds may be supporting activist groups engaged in stimulating riots both on the campus and within our inner cities." (Source 5, p. 18).

[39] Memorandum from D. O. Virdin for file, July 2, 1969, Special Service Report 1974, Source 12, pp. 120–121.

[40] Special Service Report 1974, Source 12, p. 329.

[41] Memorandum from Tom Huston to H. R. Haldeman, Sept. 21, 1970, Impeachment Book VIII, Source 13, p. 44.

[42] Special Service Report 1975, Sorce 11, p. 51.

[43] Special Service Report 1975, Source 11, p. 52.

[44] Special Service Report 1974, Source 12, pp. 32–34.

[45] Special Service Report 1975, Source 11, pp. 50, 57.

[46] Special Service Report 1975, Source 11, pp. 48, 50.

supply names of employers, wage records, etc.),[47] the Department of the Army, and the Internal Security Committees of Congress.[48]

—Developed files on political individuals and groups: By 1973, the IRS had political and tax intelligence files on 8,585 individuals and 2,873 organizations, of which 41% were on black and ethnic organizations and individuals, 18% on anti-war organizations and individuals, 11% on "New Left" radical groups and individuals, and 15% right-wing extremist or racist organizations.[49] According to the Senate Intelligence Committee, files were maintained on such persons as former Senator Charles Goodell (R-N.Y.), the late Senator Ernest Gruening (D-Alaska), former New York Mayor John Lindsay, columnist Joseph Alsop, and Nobel Prize winner Linus Pauling.[50] The organizations listed and filed by the IRS included the Student Non-Violent Coordinating Committee, the Minutemen, the Ku Klux Klan, Americans for Democratic Action, the Communist Party, the National Student Association, the Urban League, the California Migrant Ministry, and the Church League of America.[51] When the program was terminated in August, 1973, 78% of the files was "selected out" as not containing tax-related information.[52]

Used the compiled list as a basis for initiating tax audits: an IRS file on an individual typically includes a report on political affiliations and activities (e.g. "listed as anti-war speaker," "signed anti-war advertisement," and "officer under Communist Party discipline"), an FBI report, and his tax returns.[53] An organization file typically includes similar materials and such recommendations as "revocation of exempt status" or "no action necessary 'Returns filed and taxes paid. . . .' "[54] SSS requested 225 field audits of persons and organizations, including 63 black militant individuals, 24 anti-war group members, 3 religious organizations, 23 left-wing organizations, 3 welfare and anti-poverty organizations.[55] Generally, field referrals for audits were not made without some consideration of tax-related information, but in some cases the tax deficiency potential appeared marginal, and in other "national security cases" field referrals were made without evidence of potential tax violations.[56]

Distributed returns to other agencies. For example, some files indicated "requests from Internal Security Division, Department of Justice for tax returns."[57]

REACTION

As noted, the IRS has terminated the Special Services Staff. It has suspended "Operation Leprechaun." IRS files have been culled to remove non tax-related information. On September 24, 1974, President Ford issued Executive Order 11805 to provide that a taxpayer's return "shall be delivered to or open to inspection by the President only upon written request signed by the President personally." It further provides that no representative of the President may be authorized to see such tax returns "without the written direction of the President."[58]

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[47] Special Service Report 1975, Source 11, p. 61.
[48] Special Service Report 1975, Source 11, pp. 62, 64.
[49] Special Service Report 1975, Source 11, p. 45.
[50] IRS Data Article, Source 1.
[51] IRS Documents, Source 2.
[52] Special Service Report 1975, p. 44.
[53] Special Service Report 1974, Source 12, pages 44–47.
[54] Special Service Report 1974, Source 12, page 40.
[55] Special Service Report 1975, Source 11, page 11.
[56] Special Service Report 1975, Source 11, page 73.
[57] Special Service Report 1974, Source 12, pages 44–47.
[58] 39 Federal Register 11572, March 29, 1974.

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STATEMENT OF JEFF A. SCHNEPPER, RUTGERS COLLEGE

LEASHING THE INTERNAL REVENUE SERVICE

In the wake of the Watergate revelations, it becomes imperative for the American Congress to carefully review the broad powers of the Internal Revenue Service to subpoena books and records of a taxpayer without notifying the taxpayer, or, where the IRS believes a transaction has occurred which may affect the tax liability of an unidentified taxpayer, without even knowing who the taxpayer is.

The powers of the IRS are enormous. They include the jeopardy and termination assessments, which may be made whenever the IRS determines the collection of income tax is in jeopardy. Not only may these assessments be made without any notice to the taxpayer, but the property seized under a jeopardy assessment often may be sold even before the taxpayer has a chance to contest the underlying tax liability. Clearly, the inequities and potential danger here for financial disaster caused by overactive, underexperienced, eager beaver special agents, requires a Congressional mandate to discontinue the jeopardy assessment practice. The benefits of conserving assets which may be dissipated, is far outweighed by the potential permanent injuries to innocent taxpayers.

The problem of the "John Doe" summons is more difficult. The "John Doe" summons requires the presentation of books and records relating to certain transactions without specifying the taxpayer involved. They are normally issued

against banks to enable the IRS to discover the identities of persons whose transactions suggest the possibility of unpaid tax liabilities.

In *United States* v. *Bisceglia* 75–1 USTC 9247, 35 AFTR 2d 75–102 (Sup. Ct., 1975), decided on February 19, the Supreme Court upheld the use of the "John Doe" summons. In this case, the Federal Reserve Bank of Cleveland reported that two deposits of $20,000 in decrepit $100 bills had been made in the Commercial Bank of Middlesboro, Kentucky. Inferring from the condition of the bills that they had been stored for a long period of time, and further inferring that the bills were significant indicia of potential tax evasion, the IRS issued a "John Doe" summons against the Middlesboro bank requiring the records that would show who had made the deposits.

In upholding the summons, the Court pointed out that Section 7601 of the Internal Revenue Code permits the IRS to investigate "*all* persons . . . who *may be* liable to pay *any* internal revenue tax," while Section 7602 authorizes a summons of "*any* . . . person" and the examination of records for "ascertaining the correctness of *any* return . . . determining the liability of *any* person . . . or collecting *any* such liability." They rejected the contention of the Sixth Circuit Court below (486 F.2d 706 (1973) that the Code "presupposes that the Internal Revenue Service has already identified the person in whom it is interested as a taxpayer before proceeding."

I believe that the case was incorrectly decided, and, as was noted by Justices Stewart and Douglas, represents a "breathtaking expansion of the summons power." But the *Bisceglia* case is law. It represents the fact that the Internal Revenue Service now has the power, at the whim of any IRS agent, to force the disclosure of transaction records of unidentified taxpayers.

The broad implications of the Court's decision legitimize "fishing expeditions" that may be merely invasions of the taxpayer's privacy. They depart from established law by authorizing shot in the dark investigations of thousands of transactions, some of them involving possible criminal penalties, without the minimal due process requirements of notice to the unidentified taxpayer under investigation.

The "John Doe" summons must be legislatively eliminated. We must distinguish this shot in the dark fishing expedition from the legitimate uses of a subpoena in an ongoing tax investigation. The American citizen has already been stripped of too much of his right to privacy. 1984 is not here yet, but it is less than ten years away.

HOGAN & HARTSON,
Washington, D.C., January 30, 1976.

Re jeopardy assessments.
Hon. FLOYD K. HASKELL,
Chairman, Senate Finance Committee Subcommittee on Administration of the Internal Revenue Code, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HASKELL: I have some suggestions concerning the proposed procedure for jeopardy and termination assessments, as proposed in section 1209 of the Tax Reform Bill of 1975, as it passed the House. In part, these points were made in my testimony for Senator Haskell, but before the bill was reported to the House, and before a draft was available to me.

1. It is proposed that the taxpayer may petition the Tax Court for preliminary review of whether jeopardy exists and whether the assessment is excessive. The Tax Court then is to have not over 20 days to reach a decision, unless the taxpayer himself requests and shows reasonable grounds for an extension of the time. Neither the Government nor the Tax Court may initiate an extension. It is contemplated that the Tax Court will assign commissioners to hear such proceedings, subject to such review as the Tax Court may provide. At last count, there were seven Tax Court Commissioners, presumably busy riding circuit in various parts of the country (including their new and proposed declaratory judgment functions under ERISA and the Tax Reform Act). Even if their numbers are increased, there would seem to be a serious practical problem in detaching one of them from what he is hearing or working on at the time and sending him off to the situs of a jeopardy or termination assessment in time to hear the matter, reach a conclusion, and have it reviewed as the Tax Court may provide, all within 20 days after the petition is filed. If he arrives at a time when one of the parties, with good cause, is unready to present his facts, he may have to grant a continuance (within the brief confines of the time permitted), and

may have to stand by for several days since it may be impracticable or economic for him to return meanwhile to what he was doing. Figures given by the Service to Rep. Vanik's subcommittee on the House side, and presumably duplicated at your hearings, show that there were 548 jeopardy and termination assessments in 1975; and that was an exceptionally low year. Since it is safe to assume that a fair proportion of the affected taxpayers will feel put upon, and that some of those who do not will nevertheless welcome the respite afforded by the procedure, I can imagine the Commissioners being kept jumping around the country.

What I am driving at is that this kind of summary procedure with short deadlines does not seem suitable for handling by a nationwide court. The District Judge is on the scene (or at least within the area), and the court is always available. While the federal courts are not noted for their speed, neither is the Tax Court. The District Judge can act as speedily as he is directed to, once the priorities are established. Their courts handle habeas corpus and show cause orders with reasonable dispatch. The Tax Court has no peculiar expertise in finding the existence or absence of jeopardy, on which it has never before had the power to pass (H.R. Rep. 356, 69th Cong., 1st Sess. 42 (1926); Durovic v. Commissioner, 487 F. 2d 36, 40 (7th Cir. 1973); California Associated Raisin Co., 1 B.T.A. 1251 (1925)).

I urge, therefore, as I did before Senator Haskell, that the preliminary determinations be made by the District Courts, not the Tax Court.

2. The Supreme Court in the *Laing* case, after the bill passed the House, determined that the taxpayer whose taxable year is terminated under I.R.C. § 6851 is entitled (a) to a deficiency notice and review by the Tax Court, and (b) to a stay of the sale of his property until the Tax Court has finally decided the case or the taxpayer has failed to file a petition. The bill needs to be coordinated with these conclusions (assuming Congress does not wish to alter them, which would require amendments of another kind).

(a) The Ways and Means Committee viewed the preliminary expedited determination of jeopardy as a procedure that was preferable to allowing termination assessments to be appealed to the Tax Court on the merits, because under this latter requirement the courts would have to make a determination of tax liability based upon less than a full taxable year," which would be "inconsistent with the provisions of section 6581 requiring that the taxable year be reopened after termination until its normal end if the taxpayer has taxable income after its termination." H.R. Rep. No. 94–658, p. 304. The Supreme Court's *Laing* decision means that we will now have *both* procedures, unless the Congress reverses *Laing*. Although I was one who pointed out the anomaly in the procedure that *Laing* approved, there is much to be said for retaining it, perhaps with some modification to remove the anomaly. It is not alternative but in addition to the procedure established by the bill, since the bill provides quick relief for one who can negate the need for jeopardy treatment or who can show that the assessment is excessive even in light of facts in the Commissioner's possession, while *Laing* assures the person who is subjected to a termination assessment (and who cannot qualify to have it set aside at the preliminary stage) of the same opportunity for full tax Court review of the merits that has long been available in ordinary jeopardy cases.

Since it is inconceivable that the Tax Court will decide the case within the year during which the termination assessment is made—allowing for deficiency notice, petition, answer, trial, briefs and decision—as a practical matter it will be the tax determination for the full year on which the Tax Court will pass, unless the taxpayer has no income after the termination date. But, in order to bring the tax for the balance of the year before the Tax Court, the Commissioner will have to send another deficiency notice (*Laing* note 21) and, if the taxpayer has already petitioned the Tax Court, to assert the additional tax in his answer (*W. Cleve Stokes*, 22 T.C. 415, 423). Tax Court Rule 142(a) places the burden of proof on the Commissioner for increases in a deficiency asserted in the answer, including increases in jeopardy assessments (*Nathaniel Brooks, Sr.*, 34 CCH Tax Ct. Mem. 1287; see *Stokes, supra*). It does not make much sense to apply that rule to increases resulting from events subsequent to that for which the termination assessment was made.

Whether by legislation or amendment of the Tax Court (which never anticipated the *Laing decision*), procedure should be established for bringing the tax for the full year promptly before the Tax Court, without shifting the burden of proof to the Commissioner. If that is done, there is much to be said for the *Laing* procedure, which will give the taxpayer an early place in line in the Tax

Court and will force the Commissioner to act promptly on the full year's tax, instead of waiting as long as three after the return date while the taxpayer's property remains tied up (assuming he is unable to make the preliminary showing prescribed by the bill).

(b) Section 1209 of the bill (I.R.C. § 6863 (c)) provides for a stay of sale of seized property until the Tax Court has made its preliminary determination under proposed I.R.C. § 6866(b), or until the taxpayer has let the time expire for seeking such review. The proposal expressly made under section 6861(a) or 6862(a), or a taxable period has been terminated under section 6851(a)." That is fine, but it leaves in stark contrast the language of existing § 6863(b)(3), which stays the sale pending a petition to the Tax Court *on the merits* of the deficiency, and which refers only to jeopardy assessments "made under section 6861." The Supreme Court in *Laing* held that the § 6851 termination assessment is a form of § 6861 jeopardy assessment and thus entitled to the protection against sale during the Tax Court proceeding, even though § 6851 was the Tax Court proceeding, even though § 6851 was not mentioned in § 6863(b)(3). But if Congress now comes along and in a parallel provision finds it necessary to refer to § 6851 as something distinct from a § 6861 assessment, does that imply Congressional disapproval of a restraint on sale in the situation covered by the provision in which § 6851 is not mentioned. Unless it is the decision of the Committee to overturn the *Laing* decision, I urge that existing § 6863(b)(3) also be amended to refer expressly to § 6851, in terms parallel to proposed § 6863(c). (There is no occasion to refer to § 6862 in § 6863(b)(3), because there is no Tax Court review of the merits of the taxes covered by § 6862.) Possibly a clarifying statement in the Committee Report, to the effect that is is not intended to change the meaning of § 6863(b)(3) as construed in *Laign*, would suffice in lieu of amending that provision. But statements in reports of only the nonoriginating committee have had rough sledding recently as authoritative legislative history. *Cf. Hawkes* v. *Int. Rev. Serv.*, 567 F.2d 787, 794 (9th Cir. 1972).

3. I note that existing § 6861(g) of the Code permits administrative action to abate a jeopardy assessment, but not after "a decision of the Tax Court in respect of the deficiency has been reduced or, if no petition is filed with the Tax Court, after the expiration of the period for filing such petition." The new legislation introduces the possibility of two distinct petitions to the Tax Court and two decisions, with respect to the same deficiency. Unless it is made clear that the petition and decision in the preliminary proceeding is not what is referred to, the time within which voluntary administrative abatement can be made will be greatly shortened. Even though, for practical reasons, judicial abtement may have to be requested within 30 days after the assessment, the power to abate administratively if the taxpayer's circumstances change later on (before the Tax Court decides the merits) should not be altered. The same question arises the second sentence of § 6861(c), which authorizes administrative abatement of any part of a jeopardy assessment that the Service concludes is excessive, if the action is taken "before the decision of the Tax Court is rendered." (If it were *res nova*, I would be prepared to argue that those abatement powers exist without need for the statutory provisions; but Congress and the Treasury thought them necessary when they were added in 1953 and 1938, respectively, and they should not be inadvertently restricted now.) I am sure there are other provisions in the Code that date matters from the filing of a petition with or from a decision of the Tax Court. I suggest that a general provision be inserted in proposed § 6866 to the effect that the petition and decision there prescribed shall not be deemed the petition or decision referred to in any other provision unless expressly so stated. Of course, if the Committee goes along with my suggestion to put this preliminary matter in the hands of the district courts, this problem will not exist.

4. Another question arises in connection with § 6861(g), the last sentence o which suspends the statute of limitations in case the jeopardy assessment is abated by "the Secretary or his delegate" upon finding that jeopardy does not exist. Since the normal period of limitations may meanwhile have expired, this provision suspends the period of limitations for making a normal deficiency determination (in lieu of the abated jeopardy) from the date of the jeopardy assessment, to the tenth day after abatement. But what if the abatement for lack of jeopardy is ordered by the Tax Court under the new procedure, and the statute has meanwhile expired? A good argument could be made that it is still "the Secretary or his delegate" who abates the assessment, even when he is ordered to do so by the Tax Court. But should it be left to argument or spelled expressly?

5. A parallel problem arises if the court, in the preliminary proceeding, orders a reduction of the assessment. The House Report (page 304) says that this is to have "no effect upon the determination of the correct tax liability in a subsequent proceeding," so presumably all or part of the abated amount could be reinstated after the Service has more time to develop its evidence. But what if the time for assessing a further deficiency has meanwhile expired? If the taxpaper takes the merits of the deficiency to the Tax Court there is no problem, because the statute is suspended and an increased deficiency can be asserted at any time before the hearing. I.R.C. §§ 6214(a), 6503(a); *Teitelbaum* v. *Commissioner*, 346 F.2d 266, 267 (7th Cir. 1965); *Liebes* v. *Commissioner*, 63 F.2d 870 (9th Cir. 1933). But if the taxpayer refrains from taking the merits to the Tax Court, either being satisfied with the reduced figure or preferring to contest the balance by refund suit in a forum which cannot increase the liability after the period of limitations the interim running of the statute may bar the amount abated. Treas. Reg. § 301.6503(a)-1(a); *Commissioner* v. *Wilson*, 60 F.2d 501 (10th Cir. 1932). In that event, the necessarily hasty preliminary determination of the "appropriateness" of the amount will not have had "no effect" on the ultimate obligation. This problem is also inherent in § 6861(c), with regard to administrative abatement of an excessive assessment; but there the assessment is voluntarily made by the Service, presumably after full study has satisfied it that the excess cannot be sustained, which is quite different from a preliminary and supposedly non-final determination based on what evidence can be assembled in a hurry, I suggest, therefore, that some suspension provision, comparable to that in § 6861(g), be incorporated in § 6866 and made applicable to both forms of judicial abatement under § 6866(b).

Sincerely yours,

WILLIAM T. PLUMB, Jr.

MICHAEL I. SALTZMAN,
New York, N.Y., February 11, 1976.

Re termination-jeopardy hearings.

Hon. FLOYD K. HASKELL,
Chairman, Subcommittee on Administration of the Internal Revenue Code, U.S. Senate Committee on Finance, Washington, D.C.

DEAR SENATOR HASKELL: As you probably know, the *Hall* and *Laing* cases have been decided by the Supreme Court recently. In a split decision, the Court held that a termination assessment created a "deficiency" and that the authority for assessment of that deficiency was Section 6861 so that it was necessary where a termination assessment was made for the Service to send the taxpayer a notice of deficiency within 60 days of the assessment. This decision was a response to a rather unfavorable set of facts insofar as the government's position was concerned. However, the factual context in which the cases were decided hardly justifies, in my opinion, the Court's failure to deal with the many difficult questions which arise from treatment of a short period as a full taxable year subject to review in the U.S. Tax Court. I have pointed out these problems in the article and have also suggested that the solution in this area is for judicial review of the termination made by the Service both as to the existence of jeopardy and the reasonableness of the estimated tax asserted to be due. I use the term estimated tax purposely because again in my view the proper way to view the tax assessed on a termination of a taxable year is as an estimated tax imposed by the Service rather than confessed by the taxpayer.

The forum for judicial review that I believe is appropriate is the U.S. district courts simply because they are accustomed to dealing with the question of allegedly excessive agency action. The House bill's provision for Tax Court review is deficient in that the Tax Court is less accessible than the local district courts and the trial judges may not have the perspective of district court judges, but the House remedy is better than none at all.

I suggest that the Senate provide for no Tax Court review of a short taxable year created by a termination assessment (in effect overruling the Supreme Court) because of the difficulties which the Tax Court will have in determining the correct tax for a short period. In addition, there is serious question in my mind whether Tax Court review of tax liability (as opposed to the existence of jeopardy and the reasonableness of the estimated tax assessed) for a short period would be meaningful. The Service has 60 days to send a notice of defi-

ciencey, the taxpayer has 90 days to file a petition in the Tax Court, and the government has 60 days to answer the petition. Because of this built-in delay, Tax Court review would not be meaningful, despite the result in *Hall* and *Laing*, unless a termination assesment were made in the first or second month of the year.

If you have any questions that you think I might be of some assistance on, please do not hesitate to call me.

Best wishes,

Sincerely,

MICHAEL I. SALTZMAN.

Enclosure.

THE TERMINATION OF A TAXABLE YEAR

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Section of Taxation, American Bar Association, 1705 De Sales Street, NW., Washington, D.C. 20036.

THE TERMINATION OF A TAXABLE YEAR

(By Michael I. Saltzman*)

The federal income tax is an annual tax imposed (with certain exceptions) on income derived during a period of twelve calendar months. For the individual taxpayer who reports his tax on a calendar year basis, the tax owed for the previous 12 calendar months is not due and payable until April 15. However, the Internal Revenue Service may, by using section 6851, a Code provision as remarkable for its age as its effectiveness, demand and collect an estimated tax before the end of the calendar year or before the tax is due and payable on April 15.[1] Recently, the termination provision has occasioned considerable litigation and some publicity,[2] primarily because of its increased use in the Service's Narcotics Traffickers Program.[3]

The termination provision authorizes the Service to terminate a taxable year and demand immediate payment of the tax determined to be due for the terminated period and for the preceding taxable year. However, the termination provision does not specifically require that the Service send a notice of deficiency to the taxpayer affected by the termination. It has been the Service's administrative practice not to send such a notice. Since this notice is the prerequisite to Tax Court jurisdiction, the doors are firmly closed to the only forum which may review the Service's determination of the tax demanded on the termination of a taxable year before the taxpayer makes full payment. The Service's practice of not sending a deficiency notice when it terminates a taxable year is made more difficult to comprehend since the Service's power to make jeopardy assessments under section 6861, a comparable collection device, is checked by the statutory requirement that a notice of deficiency be sent to the taxpayer within sixty days after assessment is made.[4]

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[1] The Internal Revenue Service was first given the power to terminate a taxable year in the Revenue Act of 1918 § 250(g).

[2] The Wall Street Journal, April 10, 1974, at 1, reported that the Narcotics Traffickers Program operates in about ninety metropolitan areas, and that "in the two and a half years ended last Dec. 31, about $27 million was seized and an additional $101 million was assessed against 3,475 drug suspects." *See also* N.Y. Times, April 15, 1974, at 48, column 2.

[3] Prior to its use in the Narcotics Traffickers Program, section 6851 was used when large sums of money suddenly came to light. For example, the Service used this provision to collect taxes from prize fighters. *See e.g.*, United States v. Championship Sports, Inc., 284 F. Supp. 501 (S.D.N.Y. 1968). Commissioner Alexander stated on August 14, 1974, to the ABA's Tax Section that the Service was re-examining the Narcotics Traffickers Proram to insure that the Service's activities remained the enforcement of internal revenue rather than other laws.

[4] I.R.C. § 6861 (a) and (b). Assessments made under section 6861(a) will be referred to as "jeopardy assessments"; and assessments made in connection with section 6851, as "termination assessments".

The courts have divided over the issue whether a taxpayer has a right to have the validity of an assessment made upon the termination of a taxable year adjudicated in the Tax Court, and whether the Service has a concomitant duty to send the affected taxpayer a deficiency notice.[6] Moreover, the harshness of the Service's practice as well as the apparent inconsistency of treating termination taxpayers and jeopardy taxpayers differently has raised, in the opinion of some courts, "serious constitutional questions" of equal protection and due process.[8] Certiorari has been granted by the Supreme Court in *Hall* and *Laing* recently, and a petition for certiorari is pending in *Rambo*,[7] however, so that these issues may be resolved in the near future. The sharp division of the courts makes it appropriate to examine this provision of the federal tax laws, where the conflict between the requirements of the state and the rights of its citizens is more dramatically revealed than in most other tax disputes.

PURPOSE OF THE STATUTE

The purpose of the termination provision is to give the Service authority to take summary proceedings for the collection of income taxes in cases where there is evidence that the taxpayer plans to evade the tax by a sudden departure from the United States, or to remove or conceal his property to prevent collection of a tax ultimately determined to be due,[8] and in certain cases involving corporate liquidations. The effect is to secure the United States when it is found that a taxpayer is planning to take some action to defeat collection of the tax. In a real sense, what the Service is saying to the taxpayer whose year is terminated is that he cannot be trusted, as are other taxpayers, to make a return of his income for the taxable year, and to make payment of the tax at the time it is otherwise due.

The provision operates in the form of a demand for tax, but the tax demanded is, at best, an estimated tax, since it is computed under emergency conditions without the benefit of a full audit investigation. The tax demanded is, then, an interim, provisional or temporary determination made solely for collection purposes.[9] Thus, the termination provision serves much the same purpose in the context of the "untrustworthy taxpayer" as the withholding and estimated tax provisions do in the context of the average taxpayer. Both types of taxpayer make current payments of tax, and at the time their final returns are due, additional tax may be payable or refunds of tax may be receivable. In this context, the termination provision is not necessarily penal in nature, but is an administrative measure intended to insure the collection of the tax which otherwise might not be collectible.

If both section 6851 and section 6861 apply in jeopardy situations, how do they differ? The jeopardy assessment provision presupposes that a return has been

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[6] *For taxpayer:* Hall v. United States, 493 F.2d 1211 (6th Cir. 1974), *petition for cert. filed*, 43 U.S.L.W. 3087 (U.S. Aug. 5, 1974) (No. 74–75), *cert. granted*, 43 U.S.L.W.; Shaw v. McKeever, 74–1 USTC ¶ 9348 (D. Ariz. 1974); Lisner v. McCanless, 356 F. Supp. 398 (D. Ariz. 1973); Williams v. United States, 74–1 USTC ¶ 9139 (D. Nev. 1973); Rambo v. United States, 353 F. Supp. 1021 (W.D. Ky. 1972), *aff'd*. 492 F.2d 1060 (6th Cir. 1974), *petition for cert. filed*, 43 U.S.L.W. 3017 (U.S. Jul. 10, 1974) (No. 73–2005); Clark v. Campbell, 341 F. Supp. 171 (N.D. Tex., 1972), *aff'd*, — F.2d — (5th Cir. 1974); Schreck v. United States, 301 F. Supp. 1263 (D. Md. 1969), *aff'd on rehearing*, 33 AFTR 2d 402 (Dec. 19, 1973).

For the Service: Laing v. United States, 364 F. Supp. 469 (D. Vt. 1973), *aff'd* 74–1 USTC ¶ 9423 (2d Cir. 1974), *petition for cert. filed*, 42 U.S.L.W. 3679 (U.S. May 31, 1974) (No. 73–1808), *cert. granted*, 43 U.S.L.W. 3187 (Oct. 15, 1974). Willits v. Richardson, 362 F. Supp. 456 (S.D. Fla. 1973), *rev'd*. 74–2 USTC ¶ 9583 (5th Cir. 1974); Parrish v. Daly, 350 F. Supp. 735 (D. Ind. 1972); Parenti v. Whinston, 347 F. Supp. 471 (E.D. Pa. 1972); Irving v. Gray, 344 F. Supp. 567 (S.D.N.Y. 1972), *aff'd*, 479 F.2d 20 (2d Cir. 1973); Williamson v. United States, 24 AFTR 2d 5564 (N.D. Ill. 1969), *rev'd on other grounds*, 31 AFTR 2d 73–800 (7th Cir. 1973); Johnson v. Coppinger, 320 F. Supp. 171 (N.D. Ala. 1971).

[8] *See, e.g.*, Williams v. United States, 74–1 USTC ¶ 9139 (D. Nev. 1973); Rambo v. United States, 353 F. Supp. 1021 (W.D. Ky. 1972); Schreck v. United States, 301 F. Supp. (D. Md. 1969).

[7] Hall v. United States, 493 F.2d 1211 (6th Cir. 1974), *petition for cert. filed*, 43 U.S.L.W. 3087 (U.S. Aug. 5, 1974) (No. 74–75), *cert. granted*, 43 U.S.L.W. 3187 (Oct. 15, 1974), Laing v. United States, 364 F. Supp. 469 (D. Vt. 1973), *aff'd*, 74–1 USTC ¶ 9583 (2d Cir. 1974), *petition for cert.* filed, 42 U.S.L.W. 3679 (U.S. May 31, 1974) (No. 73–1808), *cert. granted*, 43 U.S.L.W. 3187 (Oct. 15, 1974). Rambo v. United States, 353 F. Supp. 1021 (W.D. Ky. 1972), *aff'd*. 492 F.2d 1060 (6th Cir. 1974), *petition for cert.* filed, 43 U.S.L.W. 3017 (U.S. July 10, 1974) (No. 73–2005). Oral arguments for *Hall* and *Laing* are scheduled to be heard by the Supreme Court in tandem.

[8] G.C.M. 17195, XV–2 C.B. 107, 109 (1936), *declared obsolete*, Rev. Rul. 69–420, 1969–2 C.B. 264.

[9] Ludwig Littauer & Co., 37 B.T.A. 840 (1938); G.C.M. 17195, XV–2 C.B. 107 (1936).

made, or that a deficiency has been or can be determined.[10] In other words, the jeopardy assessment provision applies to jeopardy situations arising after the time prescribed for filing the taxpayer's return. The termination provision presupposes a more exigent situation of jeopardy than the jeopardy assessment provision covers, a situation so extreme as to require immediate collection after income is earned or comes to light rather than to await the close of the normal taxable year and the determination of a statutory deficiency.[11]

THE OPERATION OF SECTIONS 6851 AND 6861 COMPARED

The termination provision authorizes the Service to "declare the taxable period for [a] taxpayer immediately terminated, and [to] cause notice of [its] finding and declaration to be given the taxpayer, together with a demand for immediate payment. . . ." [12] Unlike the normal situation involving an individual taxpayer, where the calendar year tax becomes due and payable only on April 15, the demanded tax becomes "immediately due and payable." [13]

The tax, payment of which may be demanded under section 6851, is not only for "the taxable period so declared terminated" but also for "the preceding taxable year or so much of such tax as is unpaid, whether or not the time otherwise allowed by law for filing [*sic*] return and paying the tax has expired . . . ." [14] The reason for this provision is to cover a jeopardy situation which arises before the date for filing the prior year's return. Since the jeopardy assessment provisions apply only after the return is due, without the termination provision the Service would not be able to collect the prior year's tax before the last date for filing the return.[15]

When a taxpayer's taxable year has been terminated, the Service takes the position that the tax demanded is assessed under section 6201 and not as a jeopardy assessment under section 6861.[16] Thereafter, the Service can levy on any property or rights to property of the affected taxpayer under section 6331(a) after notice and demand to him "without regard to the ten-day grace period." [17] Furthermore, although it has terminated a taxable year, the Service may reopen the terminated "period" each time the taxpayer is found to have received income within the "current taxable year." [18]

The Code provides a limited opportunity for a taxpayer to avoid the severity of a termination assessment. A taxpayer may reopen the terminated "taxable period" by filing a return for the "taxable period" along with such other information the Service may require. A taxpayer may also avoid having payment of the tax demanded enforced prior to the expiration of the time otherwise allowed for paying such taxes by furnishing a bond to insure the timely making of a return and payment of taxes determined to be due for the terminated year or for prior years.[19]

The termination power extends to three broad classes of taxpayers: the absconding taxpayer, the corporation in liquidation, and the departing alien or citizen.[20] The procedure for all three classes involves, however, a requisite "finding" by the Service. Where the absconding taxpayer is concerned, a taxable year may be terminated only where the Service "finds" that a taxpayer designs quickly to depart from the United States or to remove his property therefrom, or to conceal himself or his property therein, or to do any other act tending to prejudice or render wholly or partly ineffectual proceedings to

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[10] *See* Veeder v. Commissioner, 36 F.2d 342, 344 (7th Cir. 1929); Ludwig Littauer & Co., 37 B.T.A. 840, 842 (1938).
[11] Ludwig Littauer & Co., 37 B.T.A. 840, 842 (1938).
[12] I.R.C. § 6851(a)(1). *See also* I.R.C. § 6851(a)(2).
[13] I.R.C. § 6851(a)(1).
[14] *Id.*
[15] In the *Clifford Irving* case, the taxpayers' 1971 taxable year was terminated on February 4, 1972, and notices were sent to the taxpayers demanding immediate payment of taxes for such year. The taxpayers contended that the termination was procedurally defective on the grounds that the Service did not demand for the current year (1972), since the statute required the Service to demand payment not only for the preceding year, but also for the current year. The argument was rejected by both the district court and court of appeals. Irving v. Gray, 344 F. Supp. 567 (S.D.N.Y. 1972), *aff'd*, 479 F.2d 20 (2d Cir. 1973).
[16] Internal Revenue Manuel, CCH ¶ 5214.3(2).
[17] Internal Revenue Manuel, CCH ¶ 5214.3(3).
[18] I.R.C. § 6851(b).
[19] I.R.C. § 6851(e).
[20] I.R.C. §§ 6851(a)(1)-(2), and 6851(c)-(d).
as a case in court. *See* Bowers v. New York & Albany Lighterage Co., 273 U.S. 346 (1927).

collect the income tax for the current or preceding taxable year unless such proceedings be brought without delay.[21]

The jeopardy assessment provision does not specify what circumstances constitute "jeopardy" nor does it require the Service to "find" the circumstances constituting jeopardy. The Service need only "believe" that "the assessment or collection of a deficiency . . . will be jeopardized by delay." [22] The courts have generally held that this "belief" is a subjective judgment made in the uncontrolled discretion of the Service, free of any power of the courts to review it.[23]

While the jeopardy assessment provisions are less specific than the termination provision, they have four procedural safeguards. First, the Service is required to send a deficiency notice within sixty days after the assessment, with the result that the taxpayer is afforded an opportunity for Tax Court review.[24] Second, a taxpayer can stay all collection proceedings pending Tax Court review if he is able to post an adequate bond.[25] Third, property seized to satisfy the amount of the jeopardy assessment may not, except in certain limited circumstances, be sold during the pendancy of litigation in the Tax Court.[26] Fourth, the Service may abate a jeopardy assessment if it "finds" that jeopardy does not exist.[27]

The termination provision has two of the four procedural safeguards found in the jeopardy assessment provisions. The taxpayer whose year has been terminated may file a bond to stay collection, and he may file a short-period return, the effect of which may be to establish the collection of a tax for the current and preceding taxable year is not in jeopardy.[28] However, both of these procedural safeguards may be as inadequate for the jeopardy taxpayer as for a termination taxpayer.[29] If a taxpayer's resources have been seized by the Service, he can hardly furnish an adequate bond. Similarly, if the Service has made a jeopardy or termination assessment, it is unlikely to confess error merely because a jeopardy taxpayer has filed a claim for abatement or the termination taxpayer files a short-period return.

Consequently, the only meaningful safeguards available to the jeopardy taxpayer are the right to litigate in the Tax Court and the restrictions on sale by the Service pending Tax Court review. It is against these jeopardy assessment safeguards that the courts have measured the procedure of the Service in terminating a taxable year, while at the same time they have ignored the greater specificity and the finding requirement of the termination provision.

ANALYSIS OF THE CASES

All of the recent termination assessment cases in the district courts have been actions to enjoin the collection of termination assessments. At the outset, therefore, the taxpayers in these actions were faced with the Anti-Injunction Act which specifically withdraws jurisdiction from state and federal courts to entertain suits seeking to enjoin the assessment and collection of internal revenue taxes, except in specified circumstances.[30]

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[21] I.R.C. § 6851(a)(1). Historically "proceedings" includes levy and distraint as well as a case in court. *See* Bowers v. New York & Albany Lighterage Co., 273 U.S. 346 (1927).

[22] I.R.C. § 6861(a).

[23] *See, e.g.*, Lloyd v. Patterson, 242 F.2d 742, 744 (5th Cir. 1957); Publishers New Press, Inc. v. Moysey, 141 F. Supp. 340, 343 (S.D.N.Y. 1956); *criticized in* Plumb, *Federal Liens and Priorities*, 77 Yale L.J. 1104, 1135 (1968). Note, however, that the administrative practice of the Service only authorizes a jeopardy assessment under the same general conditions as those specified in section 6851(a)(1). Internal Revenue Manual, CCH ¶5214.21(2).

[24] I.R.C. § 6861(b). If the Service fails to send a deficiency notice within the time required by law, the Anti-Injunction Act, I.R.C. § 7421(a), does not apply, and assessment or collection may be enjoined. I.R.C. § 6213(a).

[25] I.R.C. § 6863(b)(3).

[26] There are three exceptions to the prohibition on sale: (1) if the taxpayer consents to the sale; (2) if the property is perishable; and (3) if the Service determines that costs of conserving and maintaining the property will greatly reduce the net proceeds of a sale. I.R.C. § 6863(b)(3)(B).

[27] I.R.C. § 6861(g).

[28] I.R.C. § 443(a)(3) and 6851 (b) and (e).

[29] *See* Kimmel v. Tomlinson, 151 F. Supp. 901 (S.D. Fla. 1957); Shelton v. Gill, 202 F.2d 503 (4th Cir. 1953).

[30] Section 7421(a) provides:

> . . . Except as provided in sections 6212 (a) and (c), 6213(a), and 7426 (a) and (b)(1), no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed.

One of the situations excepted from the application of the Anti-Injunction Act, however, is where the Service collects a tax without having sent a deficiency notice to the taxpayer.[31] While the Service may not generally collect a tax without sending a deficiency notice, it may make immediate collection of a tax where a jeopardy assessment is made. Since no similar exemption from the restriction on immediate collection of an assessment is provided in the section on termination assessments, the Service has argued that the restrictions which normally apply to it when it assesses a tax do not apply to the collection of a termination assessment because the "tax" demanded is not a "deficiency" for purposes of the restrictions on assessment. Consequently, taxpayers and the Service have joined issue over the statutory requirement of a deficiency notice because the resolution of this procedural issue affects the jurisdiction of the court to enjoin collection.

In attempting to resolve whether the Service must send a deficiency notice after making a termination assessment in the same manner as it is required to do by statute when it makes a jeopardy assessment, the courts have divided over three basic issues:

1. Whether legisaltive history supports the conclusion that the assessment authorization and procedural limitations of section 6861 are to be applied to section 6851;

2. Since section 6861 applies only to the jeopardy assessment of "a deficiency," as defined in section 6211, whether the tax demanded under section 6851 is a "deficiency;" and

3. Whether the procedural safeguards and remedies of section 6861 ought to be applied to a termination assessment to avoid harsh and possibly unconstitutional results.

A. Legislative history

In construing a statute, ordinarily one begins with the text.[32] Unfortunately, in the present instance the Code provisions do not, at least on first reading, help in resolving the issue. As has already been indicated, the termination provision, although requiring the Service to demand payment of tax, does not contain its own assessment authority in unmistakable words, nor does it refer to section 6861 for its assessment authority. Furthermore, although section 6851, which has no explicit assessment authority, and section 6861, which has this explicit authority, are grouped in the same chapter of the Code, this arrangement may not be considered in any construction of the statute.[32a] Moreover, had Congress intended section 6851 and 6861 to be read together, separate bonding provisions for termination and jeopardy assessments would have been unnecessary. Consequently, in the absence of any direction in the text of the statute, the courts have looked to legislative history, the most exhaustive examination of which is found in the *Schreck* case.[33]

The taxpayer in *Schreck* argued that the development of the structure of tax litigation shows a definite Congressional intent to mitigate the harshness of the "pay-first-litigate-later" rule by making available to all taxpayers judicial review by the Tax Court as a non-prepayment forum. The Service's refusal to give the termination taxpayer his "ticket to the Tax Court" violates this Congressional

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[31] Section 6213(a) provides, *inter alia:*

> . . . Except as otherwise provided in section 6861 no assessment of a deficiency in respect of any tax imposed by subtitle A or B or chapter 42 and no levy or proceeding in court for its collection shall be made, begun, or prosecuted until such notice has been mailed to the taxpayer, nor until the expiration of such 90-day or 150-day period, as the case may be, nor, if a petition has been filed with the Tax Court, until the decision of the Tax Court has become final. Notwithstanding the provisions of section 7421(a), the making of such assessment or the beginning of such proceeding or levy during the time such prohibition is in force may be enjoined by a proceeding in the proper court.

[32] *See* Frankfurter, *Some Reflections on the Reading of Statutes,* 2 RECORD OF N.Y.C.B.A. 213 (1947).

[32a] Section 7806(b) provides, *inter alia:*

> No inference, implication, or presumption of legislative construction shall be drawn or made by reason of the location or groupings of any particular section of provision or portion of this title, nor shall any table of contents, table of cross references, or similar outline, analysis, or descriptive matter relating to the contents of this title be given any legal effect.

But see Clark v. Campbell, — F.2d — (5th Cir. 1974); Lisner v. McCanless, 356 F. Supp. 398 (D. Ariz. 1973)).

[33] Schreck v. United States, 301 F. Supp. 1265 (D. Md. 1969).

intent. Accordingly, the taxpayer contended, the deficiency notice requirement of the jeopardy assessment provisions must also apply to a termination assessment. The Service countered that the statutory authority for the assessment of taxes declared due and payable under the termination provision is to be found in the general assessment authority of section 6861, because both the termination provision and the general assessment statute were in existence long before the jeopardy assessment provisions were enacted.

The district court in *Schreck* basically accepted the taxpayer's contention, although it stated candidly that it had not uncovered any legislative history which compelled this conclusion.[34] The Second Circuit, however, rejected essentially the same argument by the taxpayers in the *Clifford Irving* case,[35] based on a different reading of the legislative history. These conflicting conclusions call for an independent review of the legislative history.

The predecessor of section 6851 first appeared in the revenue laws in 1918. Under the Revenue Act of 1918, there was only one assessment statute, and consequently, only one provision under which the Service could assess a tax for a full or short tax year.[36] Limited administrative review was provided by an Advisory Tax Board in the Treasury which could pass on questions of interpretation and administration if requested by the Service and the taxpayer.[37] The only way a taxpayer could obtain judicial review of the Service's determination of the tax due, however, was to pay the tax and sue for a refund.[38]

In 1921, the procedure was modified to provide for administrative review of an assessment and the immediate assessment of tax in jeopardy situations. The Service was required to send a taxpayer notice of a deficiency and give him not less than thirty days to file an appeal with the Service and show cause why the tax or deficiency should not be paid.[39] If after this administrative review the Service determined a tax was due, the taxpayer was given ten days after a notice and demand to pay the tax. An exception to this procedure was provided in cases where "the Commissioner believes that the collection of the amount due will be jeopardized by such delay. . . ."[40]

In 1924, however, Congress recognized that review by another branch of the Treasury Department was inadequate and that the "right of appeal after payment of the tax is an incomplete remedy, and does little to remove the hardship occasioned by an incorrect assessment."[41] Accordingly, it permitted taxpayers an alternative to the 'pay-first-litigate-later" procedure and established a neutral Board of Tax Appeals to review claimed deficiencies in certain taxes prior to payment.[42] To accomplish its purpose Congress defined the term "deficiency" for the first time and also limited the power of the Service to assess and collect a deficiency.

Not only was the Service required to send the taxpayer notice of its finding that a deficiency was due and of its intention to assess and collect the deficiency, but it also could not take any collection action for a sixty-day period following that notification. During the sixty-day period, the taxpayer could petition the Board of Tax Appeals for redetermination of the income tax deficiency.[43]

In those cases in which the Service believed that the assessment or collection of a deficiency would be jeopardized by delay, no deficiency notice was required.[44] A taxpayer could have petitioned the Board of Tax Appeals only by filing a claim in abatement and posting a bond.[45] If the taxpayer could not post a bond, his only available remedy was to pay the tax and sue for a refund.

In 1926, some eight years after the termination provision was enacted, the jeopardy assessment provision appeared in substantially the same form as it

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[34] 301 F. Supp. at 1275; *cf.* Irving v. Grey, 479 F.2d 20 (2d Cir. 1973).
[35] Irving v. Grey, 479 F.2d 20 (2d Cir. 1973).
[36] Revenue Act of 1918 § 3176.
[37] Revenue Act of 1918 § 1301(d).
[38] The "pay-first-litigate-later" procedure had been the recognized method of obtaining judicial review of internal revenue taxes long before 1918. *See* Cheatham v. United States, 92 U.S. 85 (1875).
[39] Revenue Act of 1921 § 250(d).
[40] *Id.*
[41] H.R. REP. No. 179, 68th Cong., 1st Sess. 7 (1924), 1939-1 C.B. (Pt. 2) at 246.
[42] The Board of Tax Appeals was more of an advisory body than a court because a dissatisfied party could sue in a district court which tried the issues *de novo*. Revenue Act of 1924 §§ 274(b) and 279(d).
[43] Revenue Act of 1924 § 274(b).
[44] *Id.*
[45] Revenue Act of 1924 § 274(d).

takes today.[46] The deficiency notice requirement was retained where "normal" taxpayers were involved, but the Board of Tax Appeals was given expanded jurisdiction by having appeal from an adverse determination go directly to the courts of appeals rather than the district courts. This gave the normal taxpayer his choice of two routes to judicial review of the tax assessment: he could go directly to the Board of Tax Appeals without first paying the tax, or he could pay the tax first and then sue for a refund in the appropriate district court.

The 1926 Act also changed the rights and remedies of the jeopardy assessment taxpayer. While prior to 1926, the jeopardy assessment taxpayer was barred from review by the Board of Tax Appeals unless he could post an adequate bond, he was now given the absolute right to a redetermination of the jeopardy assessment by the Board of Tax Appeals albeit after the assessment was made.[47] The Service was authorized by the predecessor of section 6861 to assess an income tax deficiency immediately if it believed assessment or collection would be jeopardized by delay. At the same time, however, the Service was required to give notice of and to make demand for payment, and if no notice of deficiency had been sent, to send a deficiency notice within sixty days after the assessment. Thus, the jeopardy taxpayer could petition the Board of Tax Appeals for a review of the assessment within sixty days after the mailing of the deficiency notice.

The *Schreck* opinion did not discuss all the relevant legislative history. For example, in 1924, at the same time that Congress created the Board of Tax Appeals to review deficiencies and jeopardy assessments, technical amendments were made to the termination provision.[48] It would have been simple enough for Congress to provide for Board of Tax Appeals review of termination assessments when it made these amendments, and its failure to do so is hardly consistent with an intention to provide for such review.

Moreover, the *Schreck* opinion did not consider the fact that in 1954 Congress amended section 6851 by adding subsection (b) which permits the taxable year, once closed, to be reopened.[49] The purpose of this amendment was to insure that a taxpayer would not have more than one taxable year in the same 12 month period.[50] Since Congress did not intend that terminated taxpayers should have more than one taxable year in any 12 month period, it is unlikely that a terminated taxable year was intended to be a "taxable year" reviewable by the Tax Court since, in the usual termination situation, this would result in more than one taxable year in a 12 month period.

The legislative history not discussed by the district court in the *Schreck* case points to a contrary conclusion than the one that was reached. Congress may have intended the Tax Court to review deficiencies, but apparently it did not consider a tax collected upon the premature closing of a tax year to be a deficiency.[51] As a matter of legislative history, in fact, the tax collected upon the closing of a taxable year is more analogous to the quarterly installment payments of tax Congress provided for when the termination provision was originally enacted in 1918.[52]

B. The "Deficiency" Issue

The term deficiency is defined in the Code, but the definition does not assist comprehension because the statutory language uses that term, "deficiency" to

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[46] Revenue Act of 1926 § 279. The first jeopardy assessment provision appeared, however, in the Revenue Act of 1921.

[47] Revenue Act of 1926 § 279.

[48] Revenue Act of 1924 § 282.

[49] Section 6851(b) provides, *inter alia:*

> . . . Notwithstanding the termination of the taxable period of the taxpayer by the Secretary or his delegate, as provided in subsetion (a), the Secretary or his delegate may reopen such taxable period each time the taxpayer is found by the Secretary or his delegate to have received income, within the current taxable year, since a termination of the period under subsection (a). A taxable period so terminated by the Secretary or his delegate may be reopened by the taxpayer (other than a nonresident alien) if he files with the Secretary or his delegate a true and accurate return of the items of gross income and of the deductions and credits allowed under his title for such taxable period, together with such other information as the Seretary or his delegate may by regulations prescribe. If taxpayer is a nonresident alien the taxable period so terminated may be reopened by him if he files, or causes to be filed with the Secretary or his delegate a true and accurate return of his total income derived from all sources within the United States, in the manner prescribed in this title.

[50] H.R. Rep. No. 1337, 83d Cong., 2d Sess. A421 (1954); Matthew Klaas 36 T.C. 239 (1961).

[51] The term was not defined until 1924. *See* Revenue Act of 1924 § 273.

[52] Revenue Act of 1918 § 250(a).

define a "deficiency." [53] The regulations do not clarify the meaning of the term.[54] One commentator has cut through the statutory thicket by stating simply that a "deficiency" is the amount by which the correct amount of tax as determined by the Service exceeds the amount of tax reported by the taxpayer on his return.[55]

If a taxpayer has not filed a return, the deficiency is the amount by which the correct amount of the tax as determined by the Service exceeds the sum of any deficiency or deficiencies previously determined, decreased by the sum of all credits, refunds, and amounts otherwise repaid in respect of such tax.[56] Reduced to its elements, then, a deficiency generally requires (1) the determination of the correct tax imposed, and (2) the filing of a return.

1. The correct tax imposed

The critical factor in the deficiency equation is the determination of "the correct tax imposed by subtitle A or B or Chapter 42." Generally speaking, the income tax imposed by subtitle A is an annual tax computed on the basis of a calendar or fiscal year depending on the taxpayer's annual accounting period. Most individual taxpayers use a calendar tax year. In the usual section 6851 termination, however, the year is closed before December 31, and the balance of the full calendar year still remains.

The Service's position is that until the end of the calendar year, it is impossible to determine the correct amount of the tax imposed. The practical problems which would be created if a termination taxpayer could obtain Tax Court review weigh in favor of this position. For example, a taxpayer who owed a tax on September 30 might, because of losses incurred after that date before the end of the calendar year, owe less or no tax for the full 12 month period. If, after his year is terminated, a taxpayer were to file a petition with the Tax Court, would he in the computation of tax be entitled to one or more than one exemption for the same 12 month period? What rate of tax should apply, since presumably the termination taxpayer's short period income tax rate would be lower than the full-period rate? Since the books and records of the taxpayer and other parties are not likely to have been kept on the basis of the short-period tax year, how will relevant records be obtained? What happens if the Service thereafter assesses a deficiency for the whole year? Does the taxpayer file a full-period return and a separate short-period return? If petitions are filed subsequently in the Tax Court with respect to the terminated portion and the balance of the calendar year, do they remain separate or merge?

While the district courts and the courts of appeals have divided over the statutory requirement of a deficiency notice when a tax year is terminated; since 1938 the Tax Court has consistently ruled that it has no jurisdiction to review a short-period tax year. In *Ludwig Littauer*, the Board of Tax Appeals said that the amount of tax set forth in the termination notice to the taxpayer was not "an amount finally determined [by the Service] as a deficiency," but a provisional statement of the amount which must be presently paid as a protection against the impossibility of collection.[57] Thus, only after a full-period return is filed, "can it be determined whether there is a statutory deficiency or perhaps a refund of all or part of the amounts already collected . . . ." [58] The Tax Court has adhered to these views even to the present,[59] and although a recent decision indicates some dissatisfaction with the *Littauer* rule,[60] it has been upheld by the Second, Seventh and Ninth Circuits.[61]

There is other support for the *Littauer* rule. The Service has no authority to determine a deficiency for a fractional part of a taxpayer's correct tax year, and

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[53] I.R.C. § 6211(a).
[54] *See* Reg. § 301.6211-1(a).
[55] 9 MERTENS, LAW OF FEDERAL INCOME TAXATION, § 49.128 (1971 ed.).
[56] *See* Reg. § 301.6211-1(a); Cantrell & Cochrane Ltd. v. Shea, 39-1 USTC ¶ 9388 (S.D.N.Y. 1939).
[57] 37 B.T.A. at 842–43.
[58] *Id.*
[59] *See* Puritan Church—The Church of America, 10 T.C. 485, 494 (1948), *aff'd per curiam*, 209 F.2d 306 (D.C. Cir. 1953), *cert. denied*, 347 U.S. 975 (1954), *cert. denied*, 350 U.S. 810 (1955); Thomas A. DaBoul, unreported Tax Court decision, June 19, 1969, *aff'd*, 429 F.2d 38 (9th Cir. 1970); Aikens, unreported Tax Court decision, October 22, 1970 (Docket No. 4173–69); Armstrong, unreported Tax Court decisions, June 2, 1971 (Docket No. 7725–70); Charles P. Riley, 32 T.C. 847 (1973); Louis V. Musso, 32 TCM 849 (1973), *appeal docketed*, No. 73–3916, 5th Cir. 1974. O'Delle B. Morris, 32 TCM 852 (1973); William Jones, 62 T.C. No. 1 (1974).
[60] *See* William Jones, 62 T.C. No. 1 (1974).
[61] *See* Irving v. Gray, 479 F.2d 20 (2d Cir. 1973); Williamson v. United States, 31 AFTR 2d 73–800 (7th Cir. 1971); DaBoul v. Commission, 429 F.2d 38 (9th Cir. 1970).

where it determines a deficiency for an unauthorized period, there is no deficiency.[62] The *Littauer* line of cases merely constitutes the application of this rule in the context of a termination.

2. *Return Requirement*

The other factor in the deficiency equation is "the amount shown as the tax due by the taxpayer upon his return." Thus, the definition of "deficiency," and indeed the entire income tax system, ordinarily assumes the filing of a return. The question is whether a full-period return is required, or whether a short-period return will suffice.

Section 443(a)(3) requires a taxpayer to make a short-period return when the Service "terminates the taxpayer's taxable year under section 6851 (relating to tax in jeopardy)." Although a short-period return is required by section 443 and appears to be contemplated by section 6851 itself, neither the regulations nor any Service rule gives a taxpayer any assistance in preparing such a return. The regulations under section 443 merely repeat the statutory requirement, and refer to "section 6851 and the regulations thereunder."[63] The regulations under section 6851, however, do not provide instructions for the filing of a short-period return by citizens although certain instructions are provided for the filing of such a return when a resident or non-resident alien's "taxable period" is terminated.[64] Where citizens are involved, the regulations only state that a taxpayer whose "taxable year" has been terminated must file a full-period return.[65]

There is some support for the position of the Service that irrespective of the short-period return requirements, such a return does not constitute a "return" for purposes of computing a deficiency.[66] The absence of legislative directions for filing short-period returns on the termination of a taxable year is some evidence that Congress did not intend such a return to qualify for the computation of the correct tax and a deficiency, if any. For example, although it requires the filing of a short-period return when a taxable year is terminated, section 443 does not provide for the computation of tax as it does where a change of annual accounting period is involved.[67] Furthermore, no provision is made for the proration of the personal exemption.[68]

There are other indications in the Code and the regulations, however, that the terminated short period is a "taxable year." Section 441 says that the term "taxable year" means "the period for which the return is made, if a return is made for a period of less than 12 months."[69] Furthermore, the regulations state that the period of less than 12 months referred to is the short period provided for under section 443 which occurs when a termination of a taxable year for jeopardy is made under section 6851.[70] It seems to follow, therefore, that a short period created by a termination is a "taxable year."

In *Matthew Klaas*,[71] a case not cited in the *Schreck* opinion, the Tax Court answered these arguments and confirmed its view that it did not have jurisdiction to review a terminated taxable year. The petitioners were resident aliens on a calendar-year basis for filing their returns. On October 24, 1956, they left the United States to return to Switzerland, and on the same day the Service terminated their taxable year. Subsequently, the petitioners filed a joint return for the short-year January 1 to October 24, 1956. The Service refused to accept the return as a joint return because a joint return may only be filed if the alien

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[62] *See* Estate of Levi T. Scofield, 25 T.C. 774 (1956), *rev'd on other grounds*, 266 F.2d 154 (6th Cir. 1959); Columbia River Orchards, Inc., 15 T.C. 253 (1950).

[63] Reg. § 1.443-1(a)(3).

[64] Reg. § 1.6851-2(b)(3); *but see* Nino Sanzogno, 60 T.C. 321 (1973).

[65] Reg. § 1.6851-1(c) and § 1.6851-2(b)(5).

[66] The Service makes a dummy return for purposes of making a termination assessment. Internal Revenue Manual, CCH ¶5214.3. The Service's position is that this return is not a return within the meaning of the deficiency definition, nor is it a return prepared for the taxpayer pursuant to section 6020, because this provision is applicable only for full-period returns. Section 6020 does not apply to declarations of estimated tax, which are analogous to termination assessments. *See* I.R.C. § 6020(b).

[67] Note that no computation is provided for taxpayers who are not in existence for the entire taxable year.

[68] I.R.C. § 443(c). Curiously, such a proration is allowed for computing the minimum tax for tax preferences.

[69] Section 7701(a)(23) defines a "taxable year" to mean not only a calendar or fiscal year but "in the case of a return made for a fractional part of a year under the provisions of subtitle A or under regulations prescribed by the Secretary or his delegate, the period for which such return is made."

[70] Reg. § 441-1(b)(iii).

[71] 36 T.C. 239 (1961); *cf.* Nino Sanzogno, 60 T.C. 321 (1973).

spouses are residents for the entire taxable year. The petitioners claimed, however, that the terminated year was a "taxable year" citing sections 441(a) and (b)(3), 443(a)(3), and 7701(a)(23).

On or about April 11, 1957, petitioners filed a claim for refund and another joint return for the period January 1 to October 24, 1956. In response to this, a deficiency notice was sent stating that the petitioners were not entitled to file a joint return.

The Tax Court upheld the Service's view[72] that a full year return was required.[73] The court stated that the "termination of a taxable period under section 6851 temporarily closes a taxable period, but the taxpayer's taxable year is still his normal calendar or fiscal year.[74] The reasoning of the court was based on section 6851(b) and its legislative history discussed above, which discloses a purpose to avoid a taxpayer's having more than one taxable year in a 12-month period.

Thus, statutory analysis does not compel an answer to the issue; however, the Service appears to have the stronger position primarily because of the procedural difficulties of Tax Court review which have long been recognized by the Tax Court itself.

If section 6861 is not the assessment authority for section 6851 terminations, however, what section authorizes a termination assessment? The Service now says that assessment is not made under section 6861 but under section 6201.[75] That section provides general assessment authority for the Commissioner with respect to "all taxes imposed by this Title" or prior revenue laws, and "which have not been duly paid by stamp at the time and in the manner provided by law." Section 6201(a) states that this assessment authority "shall extend to and include" four situations, none of which involve terminations. Thus, the government's position has been that the phrase "extend to and include" authorizes an assessment made pursuant to a termination under section 6851 despite the fact that none of the four categories mentioned in section 6201(a) specifically refers to section 6851.

The Service claims that its own administrative practice supports its interpretation because it has made assessments under the general assessment authority of section 6201 since the predecessor of section 6851 first appeared in the revenue laws. The Service's administrative practice has apparently not been uniform, however.[76] Furthermore, there is some inconsistency in the Service's position that for purposes of the "deficiency" definition a tax is not "imposed" by a termination assessment, but is "imposed" for purposes of the assessment authority of section 6201.[76] There is, then, some ambiguity in the Service's position on its assessment authority; nonetheless, the courts have focused on the effect of the Service's position rather than on this statutory inconsistency.

C. Constitutional issues

A number of courts have said that the Service's position on the requirement of deficiency notice raises constitutional "problems" of equal protection and due process, and have resolved the statutory issue in favor of the taxpayers. When the constitutional "problems" are analyzed, however, it is not at all clear that the Service's position is tainted.

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[72] For the Service's position, *see* regulation § 1.6851–1(c).

[73] 36 T.C. at 243.

[74] *See* Internal Revenue Manual, CCH ¶5214.3(2).

[75] In Bonaguro v. United States, 294 F. Supp. 750 (E.D. N.Y. 1968), *aff'd sub nom.* United States v. Dono, 428 F.2d 294 (2d Cir.), *cert. denied*, 400 U.S. 829 (1970), the Service apparently used section 6861 as its assessment authority, and in Schreck v. United States, 301 F. Supp. 1265 (D. Md. 1969), it appears that it contended section 6851 was itself the assessment authority.

[76] There are two provisions other than section 6201 or section 6861 which might authorize assessment after the termination of a taxable year: section 6851 or section 6213. *See* Myers, *Termination of Taxable Year: Procedures in Jeopardy*, 26 TAX L. REV. 829 (1971). Section 6213(b)(3) provides for the assessment of amounts paid as a tax or in respect of a tax. This section applies to payments of amounts determined as deficiencies. However, the section is quite broadly worded and would appear to permit assessment of "any amount paid as a tax or in respect of a tax." Certainly, the statute does not prohibit the assessment of an amount which is not a deficiency. Section 1.6213–1(d)(3) of the regulations states that amounts paid prior to the mailing of a notice of deficiency shall be taken into account in determining the existence of a deficiency. The regulation not only provides authority for assessment of non-deficiency amounts, but is consistent with section 1.6851–1(c) of the regulations which provides that payments made under that section will be applied against the tax due for the taxpayer's current taxable year. The problem with such an analysis is simply that the administrative agency which has charge of the function does not now nor apparently has it ever utilized the section .

1. Equal protection

The "old" concept of equal protection requires that those who are similarly situated be similarly treated, although a statute providing for differences in treatment does not deny equal protection if it is rationally related to a legitimate government objective. The "new" concept of equal protection involves the rule that statutory classifications which are based upon certain suspect criteria (such as race and wealth) or which affect fundamental rights will be held to deny equal protection unless justified by a compelling governmental interest.[77]

In *Schreck*, the district court applied the "old" concept of equal protection, and reasoned that Congress may not rationally discriminate against one group of jeopardy taxpayers (termination assessment taxpayers) by not permitting Tax Court review while other jeopardy taxpayers (jeopardy assessment taxpayers) were permitted such review. An argument can be made, however, that the comparison should not be with jeopardy assessment taxpayers but with "normal" taxpayers. The effect of the termination assessment, after all, is to put a termination assessment taxpayer on the same footing as the employee whose tax is withheld and as other taxpayers who make estimated tax payments. The difference is that the Service, not the termination taxpayer, is making the determination of how much tax is to be paid.[78]

Even assuming that jeopardy assessment and termination assessment taxpayers are similarly situated (because both involve jeopardy situations), there is still a rational basis for treating termination and jeopardy assessment taxpayers differently. Termination assessments involve more extreme circumstances, requiring more immediate action, than jeopardy assessments. While the delay of a full-scale judicial review of the amount of tax demanded may be harsh, it nevertheless seems rational to delay such review as the amount demanded is only provisional in nature.

Furthermore, in the terminology of the "new" equal protection analysis, judicial review by the Tax Court is not a fundamental right. In fact, as the legislative history shows, a taxpayer had no right to any prepayment review before Congress established the Board of Tax Appeals. Even now the jurisdiction of the Tax Court does not apply to all taxes, *e.g.*, excise taxes, or to all taxpayers, *e.g.*, bankrupt taxpayers.[79]

The conclusion that the Service's position presents equal protection problems is based on certain assumptions as to the timing of judicial review as well. In *Schreck*, the court felt that judicial review might be unavailable for three years under the Service procedure, while Tax Court review of a jeopardy assessment would be substantially earlier. This assumption was erroneous.

On the one hand, the promptness of Tax Court review of a jeopardy assessment should not be over-estimated. After a jeopardy assessment, the Service may seize property immediately if it sends a deficiency notice to the taxpayer sixty days later. Thereafter, the taxpayer has ninety days to file a petition in the Tax Court, and then must wait sixty days for the government's answer.

On the other hand, a termination assessment taxpayer may institute a refund suit within six months after he files a full-period return upon the close of his taxable year. When the full-period return is filed, the terminated period would be reopened automatically.[80] The termination assessment would be suspended, and the Service would assess the amount of tax shown on the return.[81] At this point, then, the outstanding assessment would be the tax shown on the return. If the taxpayer's return shows an amount of tax due which is less than the tax declared due by the Service upon the termination of his taxable year, and satisfied by levy, the return itself would serve as an informal claim for refund,[82]

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[77] *See* GUNTHER & DOWLING, CONSTITUTIONAL LAW 983–1040 (6th ed. 1970).

[78] The court in Shreck cited a number of cases dealing with termination assessments made against bankrupt taxpayers under section 6871(a). It is clear from these cases, however, that the courts were comparing the normal taxpayer entitled to prepayment review by the Tax Court and bankrupt taxpayers who, the government was contending, were not entitled to such review. Prepayment review by the Tax Court is not a factor where both jeopardy assessment and termination assessment taxpayers are concerned because both taxpayers have tax collected from them before the Tax Court review.

[79] I.R.C. §§ 6862 and 6871(b).

[80] Section 6851(b) provides for the terminated taxable year to be reopened if the taxpayer files a return of his income, deductions, and credits together with such other information as the Service may require.

[81] I.R.C. § 6201(a)(1).

[82] *See* American Radiator and Sanitary Corp. v. United States, 318 F.2d 915 (Ct. Cl. 1963).

and a suit for refund could be instituted six months after the return is filed.[83] This suit for refund would be proper because the taxpayer would have paid the amount of the assessment, and the suit would be for the refund of the additional amount collected from him. Any deficiency assessment the Service may impose in this context would be a separate claim which the government must raise by counterclaim.

The procedure prerequisites for a refund suit would be met since the suit would be for the refund of income taxes alleged to have been erroneously collected.[84] The *Flora* "full payment" rule would also be satisfied because the assessment upon which the suit is based (the tax shown due on the return) would have been fully paid.[85] Alternatively, on the filing of a full-period return and the finding of a deficiency, the Service will send a deficiency notice to the taxpayer, and he could thereafter file a petition in the Tax Court.

The Service is on record in support of this procedure. In the *Clifford Irving* case, it represented to the court of appeals that the taxpayers whose 1971 year was terminated on February 4, 1972, could have filed their 1971 returns at any time after February 4 and "six months thereafter (or as early as August 4, 1972) could have commended a refund suit." [86] In *Schreck*, the taxpayers' year was terminated October 25, 1967; therefore, he would have been required to wait approximately two months until the end of the taxable year before filing a full-period return and starting the six-month pre-refund-suit period.

Accordingly, contrary to the belief of the court in *Schreck*,[87] a termination assessment taxpayer is not denied a right to institute any court proceedings for three years, but only for six months following the close of the taxable year and the filing of a full-period return. There is a difference between the termination and jeopardy assessments insofar as the prompt availability of judicial review is concerned, but the difference is not so substantial as the court in *Schreck* believed. Therefore, the inequality on this account between termination and jeopardy assessment taxpayers may not be constitutionally significant.

2. *Due Process*

The Sixth Circuit observed in *Rambo:* A system that permits the government to seize and sell property without affording the taxpayer any opportunity for a judicial determination of the validity of the tax prior to payment could very well raise a serious question of a denial to the taxpayer of his property without due process of law.[88]

The harshness of the pay-first-litigate-later title does seem to raise a due process question, since the general rule is that "due process requires a hearing before a deprivation of property takes effect." [89] The Supreme Court has long recognized, however, that there are "extraordinary situations" that justify postponing both the notice requirement and the opportunity for a hearing.[90] One of these "extraordinary situations," long recognized by the Supreme Court and apparently by the Sixth Circuit itself, is the summary collection of a tax.[91]

The teaching of the Supreme Court is that the requirements of procedural due process have been met where there is an opportunity for a hearing, even if the hearing is available only after the seizure of property from a taxpayer. In *Phillips v. Commissioner*, a case involving the liability of a transferee stockholder for his corporation's taxes, the Supreme Court said:

The right of the United States to collect its revenue by summary administrative proceedings has long been settled. Where, as here, adequate opportunity is

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[83] I.R.C. § 7422(a).

[84] 28 U.S.C. § 1346(a)(1).

[85] Flora v. United States, 357 U.S. 63 (1958), *rehearing*, 362 U.S. 145 (1960). The Service should not be able to avoid this result by claiming the amount collected as a forfeit, and not collected as a tax; and thus, that full payment of the tax has not been made. *But see*, Schreck v. United States, 301 F. Supp. 1265 (D. Md. 1969), where the Service apparently took this position.

[86] Government Brief at 15a, Irving v. Gray, 479 F.2d 20 (2d Cir. 1973). The taxpayers had argued that the *Flora* rule prevented them from suing for a refund of taxes. The Second Circuit held, 479 F.2d at 25 n.6, that the *Flora* rule was inapplicable "since there *a deficiency had been determined* and taxpayer had only paid a portion of it before seeking his refund claim in a federal district court. Here . . . no deficiency has been determined." (Emphasis added).

[87] *See* 301 F. Supp. at 1281.

[88] 492 F.2d at 1065.

[89] Fuentes v. Shevin, 407 U.S. 67, 88 (1972).

[90] *Id.* at 90.

[91] Phillips v. Commissioner, 283 U.S. 589 (1931); Rambo v. United States, 492 F.2d 1060, 1065 (6th Cir. 1974).

afforded for a later judicial determination of the legal rights, summary proceedings to secure proper performance of pecuniary obligations of the government have been consistently sustained.[92]

The same line of reasoning has permitted the government to seize summarily the property of citizens during wartime and to acquire property by exercise of its power of eminent domain prior to payment therefor, and has allowed public health officials to order summary destruction of property without notice or hearing.[93]

In the termination assessment procedure, judicial review is available after some delay (*i.e.*, six months after the taxpayer files a full-period return claiming a refund of taxes), but where property rights rather than personal rights are concerned, delay does not render the procedure constitutionally defective. As the Supreme Court said in *Phillips:*

Where only property rights are involved, mere postponement of the judicial enquiry is not a denial of due process, if the opportunity given for the ultimate judicial determination of the liability is adequate. . . . Delay in the judicial determination of property rights is not uncommon where it is essential that governmental needs be immediately satisfied.[94]

The view of some courts has been that the Service's position effectively denies a termination taxpayer access to the Tax Court. Even assuming that this were so, the unavailability of one forum is not a denial of due process provided that some alternative forum is available for the taxpayer to contest the validity of an assessment made against him.[95] As the legislative history indicates, Tax Court review was a privilege granted to certain taxpayers, but Congress has and still can require a taxpayer to pay first and litigate later.

Delayed judicial review of a termination assessment thus does not appear to present due process problems. However, it is less clear that the Service may sell property seized pursuant to a termination assessment prior to the time that the full-period return is due. The Service's procedure is not uniform, but in a number of cases it has attempted to sell seized property before the taxpayer filed a full-period return.[96] The termination assessment is provisional in nature, and concededly, an estimated tax. Therefore, consistency would require that the Service wait until a full-period return or a short-period return is filed before selling property it has seized. The provisional nature of the Service's determination when it terminates a tax year seems also to be a basis for limiting the *Phillips* case to approval of summary collection but not the sale of seized property prior to the close of the entire taxable year when the tax may be finally determined.

3. Procedural remedies

Before concluding that the problems with the Service's position reach constitutional proportions, the procedures available to termination taxpayers should be better understood.

a. *Short-Period Return.* The termination taxpayer is required to file a short-period return by section 443. This return presumably would report the income, deductions, and credits attributable to the taxpayer for the short period. While it is not likely that some taxpayers such as those engaged in "numbers", narcotics, and other profitable, although illegal, enterprises, will choose to file these returns or that the Service will confess error without a time-consuming audit,

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[92] Phillips v. Commissioner, 283 U.S. 589, 595 (1931).

[93] *Id.* at 597.

[94] *Id.* at 596–7. In St. Joseph Stock Yards Co. v. United States, 298 U.S. 39, 77 (1936), Justice Brandeis said: "A citizen who claims that his liberty is being infringed is entitled, upon habeas corpus, to the opportunity of a judicial determination of the facts. . . . But a multitude of decisions tells us that when dealing with property a much more liberal rule applies." Te distinction Justice Brandeis made between property rights and personal rights in applying constitutional principles of due process has not been further developed in the administrative law area. DAVIS, ADMINISTRATIVE LAW, § 28.19 n.6.

[95] Cohen v. United States, 297 F.2d 760, 772 (9th Cir. 1962), *cert. denied,* 369 U.S. 865; United States v. O'Connor, 291 F.2d 520, 525 (2d Cir. 1961).

[96] In Rambo v. United States, 353 F. Supp. 1021 (W.D. Ky. 1972), *aff'd,* 492 F.2d 1060 (6th Cir. 1974), and Millington v. Conley, 74–1 USTC ¶ 9136 (D. Conn. 1974), the Service attempted to sell seized property immediately. However, this practice may be "rare." *See* letter from Marvin Hagen, Regional Counsel, North Atlantic Region, to Louis Bender, Chairman of the Tax Section's Committee on Civil and Criminal Tax Penalties, dated March 6, 1974.

the remedy may well serve to assure the Service that continued collection activity is not appropriate.[97]

b. *Personal Surety Bond.* Another remedy which is available to a taxpayer is the furnishing of a bond pursuant to the provisions of section 6851(e) to stay the collection of the tax determined to be due. The taxpayer in *Millington v. Conley* was able to avoid the threatened sale of a car by posting a $2,000 bond.[98] While a taxpayer whose assets have been levied upon by the Service may not be able to secure a bond, he may, on meeting with Service officials, be able to provide security other than the distraint of assets. For example, he may be able to give a security interest in such assets as exist where he might not be able to provide a surety bond for the full amount claimed.

c. *Injunctive Relief.* Despite the seemingly absolute prohibition of the Anti-Injunction Act, the Supreme Court has ruled that an injunction restraining assessment and collection may be granted (i) "if it is clear that under no circumstances could the Government ultimately prevail . . . on the basis of information available to it at the time of suit . . . [taking] the most liberal view of the law and the facts," and (ii) "if equity jurisdiction otherwise exists."[99]

An injunction may issue to restrain actions taken by the Service which fail to comply with the standards prescribed by statute or with its own procedural rules. For example, in *United States v. Bonaguro*, the court granted the defendant-taxpayer's motion for an order directing the return of allegedly counterfeit currency and suppressing evidence that he possessed the currency at the time of his arrest.[100] The court found, *inter alia*, that the Service failed to show "that it took the formal steps under the statute at all, that it made even internally the findings and declaration required under section 6851(a), or entertained the belief required by section 6861(a). . . ."[101]

The *Bonaguro* case is extremely important because the district court did not fail, as district courts have where jeopardy assessments were involved, to review the jurisdictional basis for the Service's action. The termination provision specifically requires a "finding" that jeopardy exists. Without this finding, the Service has no jurisdiction—no power—to terminate a taxable year. Furthermore, there must be evidence to support the finding, because a "finding without evidence is arbitrary and baseless."[102] Moreover, the termination provision states that the Service's finding is only presumptive evidence of jeopardy in any court proceeding which the Service (not the taxpayer) institutes to enforce payment of the taxes made due pursuant to the termination provisions.[103] Under these circumstances, there is no reason for courts to have the same reluctance as in jeopardy assessment cases to review the Service's determination that jeopardy exists. However, in at least two cases, courts have refused to review the Service's finding.[104]

The Service must follow not only the statutory requirements but its own procedural rules as well. Under the doctrine that a governmental agency must scrupulously observe its own self-promulgated rules—the *Accardi* doctrine—an injunction would be proper if the Service failed to follow its own rules in the course of terminating a taxable year.[105]

The courts also have granted injunctions where the Service had no reasonable

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[97] Note that Charles Rambo did not file a short-period return. 492 F.2d at 1064. The Service's procedure is to request the filing of a short-period return.

[98] 74-1 USTC ¶ 9136 (D. Conn. 1974).

[99] Enochs v. Williams Packing Co., 370 U.S. 1, 7 (1962).

[100] 294 F. Supp. 750 (E.D.N.Y. 1968), *aff'd sub nom.* United States v. Dono, 428 F.2d 294 (2d. Cir), *cert. denied*, 400 U.S. 829 (1970).

[101] *Id.* at 753. The Service's finding of jeopardy was also reviewed in Rogan v. Mertens, 153 F.2d 937 (9th Cir. 1946).

[102] ICC v. Louisville & N.R.R., 227 U.S. 88, 91, (1913); *see also* JAFFE, JUDICIAL CONTROL of Administrative Action, 15 (Student's ed. 1965).

[103] I.R.C. § 6851(a).

[104] *See* Clark v. Campbell, 341 F. Supp. 171 (N.D. Tex. 1972); Parenti v. Whinston, 347 F. Supp. 471 (E.D. Pa. 1972).

[105] *See* Accardi v. Shaughnessy, 347 U.S. 260 (1964). In United States v. Heffner, 420 F.2d 809 (4th Cir. 1969), and United States v. Leahey, 434 F.2d 7 (1st Cir 1970), evidence was excluded in criminal fraud prosecutions because it was not obtained in compliance with the Service's press release that Special Agents will give *Miranda* warnings. This rule was recently extended to civil fraud cases as well. Romanelli v. Commissioner, 466 F.2d 827 (7th Cir. 1972).

basis for the amount of tax demanded.[106] In *Bonaguro*, for example, the court found that the Service failed to offer "any data that could induce a reasonable belief that a tax of $1,617.50 was in jeopardy, or filed an involuntary return which was both consistent with the data it had and free of intrinsic repugnancy."[107] The evidence revealed that the Service had artificially determined the tax due so as to seize the currency found on Bonaguro's person at the time of his arrest and had made "a merely colorable use of the statutory forms at the suggestion of another agency of government."[108]

Similarly, in *Rinieri* v. *Scanlon*,[109] $247,500 was seized from a French citizen pursuant to a termination asset when the plane on which he was a passenger landed in New York en route to Switzerland. The court found that the dummy return upon which the assessment was based was not itself "based on any factual information." The revenue agent had testified that he did not know whether Rinieri had earned any income in the United States. His only information was that Rinieri was found with the money at the airport and had refused to answer certain questions. The agent testified that he was instructed to prepare a return showing a tax of approximately $247,500 due and that he did so. He admitted that the cost-of-living income figure was a pure fiction constructed in order to make the tax due approximate the $247,500 found in Rinieri's possession.

In *Pizzarello* v. *United States*,[110] the Service averaged wagers allegedly accepted by Pizzarello on April 12, 13 and 14, 1962, and projected these wagers over a period beginning on April 1, 1960 and ending April 15, 1965. Thus, a three-day average was said to represent the taxpayer's business for the other 1,575 days. The government failed to show, however, that Pizzarello was accepting wagers since April 1, 1960. The Second Circuit observed that no court could properly make such inferences without some foundation of fact, and refused to accept the three-day average as a basis for computing income over a five-year period.[111]

More recently, in *Willis* v. *Richardson*,[112] the Fifth Circuit found a termination assessment made under the Narcotics Traffickers Program to be harassment in the guise of a tax. The taxpayer, an admitted gambler, associated with a suspected trafficker in cocaine, was arrested for speeding, and, after a search, was found to have two vials containing tablets determined to be barbiturates. On the basis of this evidence and a scrap of paper with notations, the Service terminated her tax year and demanded a tax on $60,000 gross commission income from sales of $240,000 worth of cocaine.

Courts have also granted injunctions where the Service has made a demand for and collection of tax on the basis of illegally seized evidence. In *Pizzarello* v. *United tSates*,[113] the Second Circuit granted an injunction against the Service on the ground that the jeopardy assessment in issue was made in substantial part on evidence seized incident to an illegal search. Pizzarello was the owner of a luncheonette and was suspected of being engaged in the business of "bookmaking', as well. When he was arrested, a search revealed ten horse bet slips, one pay and collect slip and $425 in currency. Internal Revenue Service agents later discovered a safe containing $123,017 and, wedged in a table next to the safe, $2,440 and policy slips. At a suppression hearing prior to his trial, the warrant under which Pizzarello had been arrested was declared invalid for lack of probable cause. With it fell the search and seizure by which the agents had

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[106] *See* United States v. Bonaguro, 294 F. Supp. 750 (E.D.N.Y. 1968), *aff'd sub nom.* United States v. Dono, 428 F.2d 204 (2d. Cir.), *cert. denied*, 400 U.S. 829(1970); Pizzarello v. United States, 408 F.2d 579 (2d Cir. 1969); Lassoff v. Gray, 266 F.2d 745 (6th Cir. 1969); *see also* Lucia v. United States, 474 F.2d 565, 573 (5th Cir. 1973); Rinieri v. Scanlon, 254 F. Supp. 469 (S.D.N.Y. 1966); Shapiro v. Sec. of State, 74-1 USTC ¶ 9445 (D.C. Cir. 1974); Woods v. McKeever, 73-2 USTC ¶ 9727 (D. Ariz. 1973); Aguilar v. United States.—F.2d—. *appeal docketed* No. 73-2454, 5th Cir. 1974.

[107] 294 F. Supp. at 753 (E.D.N.Y. 1968). When Bonaguro was arrested he was found to have $1,978. If the entire amount was taxable income, the tax could have been only $494.50. Only a single exemption was allowed, although Bonaguro was married and had two children, and the agent testified that the estimated Bonaguro's income and expenses on the basis of Bureau of Labor Statistics for a family of four. Since the estimated tax fell short of $1,978, the agent added a 25 percent penalty for violating section 6851, although Bonaguro had not yet been notified of the termination assessment.

[108] *Id.* at 753-54.

[109] 254 F. Supp. 469 (S.D.N.Y. 1966).

[110] 408 F.2d 579 (2d Cir. 1969).

[111] *But cf. Garcia* v. *United States*, 429 F.2d 427 (2d Cir. 1970); *Hamilton* v. *United States*, 30 AFTR 2d 72-5240 (S.D.N.Y. 1972).

[112] 497 F.2d 240 (5th Cir. 1974).

[113] 408 F.2d 579 (2d Cir. 1969).

obtained the $123,017 and $2,440 and bet slips wedged under the table top. Certain other evidence was not suppressed.

The Second Circuit noted that while some states admitted evidence obtained by illegal private searches and seizures, they had done so because those procuring such evidence were subject to civil and criminal liability and the existence of this liability as a deterrent was significant. Where the case is between the government and a citizen, there were no analogous remedies against government violations of the Fourth Amendment. The only deterrent to government action involving an illegal search was the exclusionary rule. Accordingly, the illegal seized evidence was suppressed, and the tax assessment against Pizzarello, based as it was on illegally procured evidence, was inavild.[114]

Finally, courts have granted injunctions where the financial burden imposed by levying against the personal and business property of the taxpayer could have resulted in irreparable injury. It is not suggested that financial hardship alone is a sufficient basis for issuing an injunction against the Service. However, there is authority to the effect that an allegation of irreparable injury, such as the forced sale of a taxpayer's business, is grounds for equitable jurisdiction.[115] In *Willits*,[116] for example, the district court ruled that the taxpayer was not irreparably injured by the Service's assessment and levy despite her claim that the seizure denied her all means of supporting herself and her children. In reversing the decision below, the Fifth Circuit held that the "financial ruin" inflicted on the taxpayer by the seizure was not mitigated by the fact that the suspected narcotics dealer with whom the taxpayer associated previously had supported her.

The Service has contended that the Anti-Injunction Act applies to proceedings to enjoin the collection of a termination assessment, so that the stringent tests applied to injunction proceedings make the remedy a narrow one at best. However, the applicability of the Anti-Injunction Act is undercut by the Service's own position on the statutory issue involving the requirement that it send a deficiency notice to the taxpayer. The Service is in the awkward posture of contending that the amount demanded when a taxable year is terminated is not a "tax" for purposes of the deficiency definition, but is a "tax" for the purposes of the assessment authority of section 6201. While the different positions may be rationalized, they make it more difficult for the applicability of the Anti-Injunction Act to be assumed. If the amount demanded is not a tax for deficiency purposes, is it certain that it is a "tax" whose collection Congress intended to be unimpeded under the Anti-Injunction Act?

It seems that the courts which have reviewed the administrative action of the Service in terminating a taxable year and collecting currency and property as tax have properly handled the issue, while the courts which have become ensnarled in the statutory question of the requirement of a deficiency notice have opened the way to unnecessary complications in litigation procedure. The Service's action should not go unquestioned—a court must review the Service's basis for its "finding" of jeopardy and for the amount it demands as tax. Courts can make this review in an injunction proceeding without ignoring the Anti-Injunction Act or allowing a premature suit for refund; and in doing so, the courts can prevent unchecked administrative action from injuring the rights, albeit property rights, of individual taxpayers. The distinction, then, is between judicial inquiry into a taxpayer's liability for a deficiency tax in a specific amount and judicial review of whether the Service has a reasonable basis for finding that collection of a tax is in jeopardy and the amount of the tax in jeopardy.

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[114] *See also Suarez* v. *Commissioner*, USTC No. 87 (1974). In *Iannelli* v. *Long*, 333 F. Supp. 407 (W.D. Pa. 1971), the seized assets were held in trust pending the outcome of the criminal prosecution. Note, however, that courts have taken jurisdiction on the basis that invasion of Fifth Amendment rights in pending or future criminal actions would result, *see United States* v. *United States Coin and Currency*, 401 U.S. 715 (1971), and under the authhority of the Pizzarello case would appear to have the jurisdiction to grant an injunction as well.

[115] *Shapiro* v. *Sec. of State*, 74-1 USTC ¶ 9445 (D.C. Cir. 1974); *Willits* v. *Richardson*, 362 F. Supp. 456 (S.D. Fla. 1973), rev'd, 497 F.2d 240 (5th Cir. 1974); *Pizzarello* v. *United States*, 408 F.2d 579 (2d Cir. 1969); *Midwest Haulers* v. *Brady*, 128 F.2d 496 (6th Cir. 1942).

[116] 362 F. Supp. 456 (S.D. Fla. 1973), received, 497 F.2d 240 (5th Cir. 1974).

CONCLUSION

The cases reveal a judicial determination that the power of the Service to make a termination assessment is not to be limited solely by the Service's internal policy that these procedures be used "sparingly" and only after several levels of internal review. In other words, the discretionary action of the Service is not to be uncontrolled and unreviewable until the full-period return is filed.

If this analysis is correct, then the *Schreck-Rambo* rule should not be followed. The Service should not be required to send a deficiency notice when it terminates a taxable year, since this procedure will create the substantial problems of premature review foreseen by the Tax Court. However, the administrative action by the Service should be reviewable by a district court in an injunction proceeding. Furthermore, since the Anti-Injunction Act may not apply to termination assessments, there is a basis for not imposing the heavy burden ordinarily required of taxpayers in obtaining an injunction against collection. On the contrary, it is appropriate to require the Service to have substantial evidence in support of its finding of jeopardy, and at least some basis in fact for the amount of tax claimed to be due.

[Whereupon, at 12:57 p.m., the subcommittee recessed, to reconvene at 10 a.m. the following day.

The November 6, 1975, hearings were printed as a separate hearing entitled "Public Inspection of IRS Private Letter Rulings."]

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