'TRUE AND CORRECT:' STANDARDS FOR TAX RETURN REPORTING

by Calvin Johnson

Calvin Johnson is a professor at the University of Texas Law School. This article arises from Professor Johnson's work on a penalties task force of the 1989 IRS Commissioner's Advisory Group and from a statement submitted to the Hearings on Civil Tax Penalties before the Subcommittee on Oversight of the House Ways and Means Committee on February 22, 1989. The work assumes the framework and reacts to the arguments advanced by an IRS Executive Task Force on Civil Penalties chaired by then-Special Assistant Richard Stark.

This article discusses legislative proposals to clarify standards for positions a taxpayer may rely on in reporting tax on a tax return. It examines three possible standards for undisclosed, unflagged positions: the "as-likely-as-not" standard, the "substantial authority" standard, and litigation or "reasonable basis" standards. It concludes that Congress should support the mission of the IRS to collect tax primarily through self-assessment, rather than by expensive, intrusive, and hostile tax audits. Only the "as-likely-as-not" standard is consistent with the self-assessment of correct tax.

Johnson also analyzes the soundness of arguments for reporting specially disclosed or flagged positions under a lower, litigation standard. He concludes that disclosure of positions sufficiently meritorious to be litigated, in order to achieve "a day in court," is attractive in theory, but in practice the "disclosure" remedy is not promising, within the bounds of acceptable administrative and litigation costs. What is needed is higher standards for self-assessment of tax, not more litigation. The article also analyzes the structure of penalties, including low-rate automatic penalties. Finally, Johnson discusses appropriate standards for taxpayers' representatives, including lawyers, accountants, and tax return preparers.

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Taxpayers should be reporting the *correct* tax on their tax returns. In a world that is inevitably uncertain, this article argues, correct tax does not mean that the taxpayer should resolve all possible doubts in his favor. Revenue must be collected through the most efficient means, even though tax law never will be simple and tax issues never will all be resolved beyond a reasonable doubt. Taxpayers should be required to self-assess their tax, in an uncertain world, relying only on positions which they believe to be correct, this article argues, that is, on positions that are at least as likely as not to prevail if challenged. Tax should be collected overwhelmingly through taxpayer self-assessment on tax returns, rather than by intrusive and hostile IRS audits. Audits should serve as a backup to correct taxpayer breaches of the reporting standard, not as the frontline for collecting revenue that was never required to be reported.

Tax should be collected overwhelmingly through taxpayer self-assessment on tax returns, rather than by intrusive and hostile IRS audits.

Enforcing high standards governing tax return reporting positions is the fairest way to raise revenue. It is unfair to ask the majority of honest Americans to pay more taxes, unless every effort has been made to ensure that taxpayers report and pay over the amount that Congress thought it was imposing when it enacted tax legislation in the past.

This article also analyzes the arguments for lower standards for positions a taxpayer flags. In an ideal world, taxpayers would be able to litigate positions, before paying tax, even though the position is considerably less likely than not to prevail. A taxpayer ideally should be entitled to rely on a position that is sufficiently meritorious to litigate by specially disclosing the position in a way that is sure to cause an IRS reaction. The IRS then would meet *all* such flagged positions with a 30-day and 90-day letter and the taxpayer would achieve his day in court. But while full litigation of dubious positions is a taxpayer's right in theory, we in fact do not want to encourage more litigation or even greater IRS and taxpayer costs in contesting litigation positions administratively. If we do not intend for the IRS to meet all flagged positions in court, a "disclosure" remedy is not sufficient and the case for a lower standard for flagged positions is weak. The right to a day in court does not mean that the taxpayer has a right to report and pay less tax in absence of litigation.

This article, finally, discusses the structure of penalties to enforce reporting standards. Penalties based on provable bad faith or lack of effort should be supplemented by an automatic penalty at a low rate of five to seven percent if it turns out that the taxpayer has in fact breached his obligation to pay correct tax. Practitioners and preparers also should be subject to monetary penalties short of suspension or disbarment.

I. STANDARDS OF REPORTING

On February 21, 1989, an IRS executive task force chaired by then-Assistant to the Commissioner Richard Stark (the "Stark Task Force") released a report, prepared for the Commissioner, on civil tax penalties.[1] After a serious study of the philosophy, history, and administration of penalties, it made a series of recommendations, including recommendations for standards for tax returns.[2] The Stark Task Force concluded that many current controversies seemingly about penalties were in fact controversies over what standards the penalties should be trying to enforce.[3] The overriding purpose of penalties, the Task Force concluded, is to encourage compliance with the appropriate standards.[4] Penalties best raise revenue, not directly in the dollars of penalties collected, but collaterally by encouraging full compliance with the standard.[5] Penalties validate an appropriate standard and remind taxpayers of their duty to adhere to the standard, as well as deterring or punishing taxpayer departures from the standard.[6] Controversies purportedly about disciplining accountants or lawyers, moreover, in fact require us first to settle the standards governing the taxpayer. A discussion of penalties or tax adviser rules is impossible without a discussion of the taxpayer standards to be enforced by those penalties. The Stark Task Force also concluded that standards should be set, not by unilateral action of the IRS or professional groups, but by Congress through the political process.[7] The Stark report thus shifted the focus of the debate from proposed regulations governing practitioners before the IRS[8] to legislation clarifying the taxpayer's own reporting obligations.

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The debate on civil penalties, whether for breach of a tax return duty or some other issue, have no effect on egregious cases or on noncompliers in jeopardy even currently for criminal sanctions. Raising standards for reporting tax will not affect taxpayers who breach even current civil standards. Thus the debate must necessarily focus on standards applicable to quite ordinary taxpayers who expect ordinarily to follow the law.

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[1]Executive Task Force, Commissioner's Penalty Study, IRS, *Report on Civil Tax Penalties* (Richard Stark, Chair) (Feb. 21, 1989) (hereinafter "Stark Task Force"), *reprinted as* Special Supplement, *Tax Analysis Daily Tax Highlights & Documents* (Feb. 27, 1989).

[2]*Id.*, ch. VIII.

[3]*Id.* at III-1.

[4]*Id.* at II-2.

[5]*Id.* at II-2-3.

[6]*Id.* at ch. III; p. VIII-1.

[7]Executive Task Force, IRS Commissioner's Penalty Study, *Working Draft of Chapters of Civil Penalties Study, reprinted in Daily Tax Exec.* No. 237, at ch. 8, pt. III(A)(1) (Dec. 9, 1988) (hereinafter "Stark Draft").

[8]Prop. Amendments to Circular 230, Prop. Treas. reg. section 10.34 (Aug. 14, 1986) (practitioners may not advise clients to take position that would subject client to absence of substantial authority penalty of IRC section 6661).

A. Current Law

Under current law, taxpayers must affirm their tax return is "true and correct" and it is a felony to willfully file a return known not to be "true and correct."[9] The first tier negligence penalty is five percent, with "negligence" usually defined in practice as what we think of as intentional behavior or reckless disregard.[10] There is also a "substantial authority" penalty, currently at 25 percent, for substantial underpayments taken under positions without substantial authority.[11] The "authority" a taxpayer may rely on is defined, through a "legal-list" approach, to exclude legal commentaries and many quasi-law sources that sound practitioners commonly rely on.[12] Current ABA and AICPA ethical standards allow a practitioner to advise clients to take a position on their return, without disclosure, if they have a realistic possibility of prevailing,[13] although the professionals' ethical standards have no congressional sanction nor basis in enacted tax law.

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B. The Uncertain World

Standards of reporting operate in a world that is inevitably complex and uncertain. Tax law is commonly vague and ambiguous. Facts, even if known, do not fit automatically into the categories recognized by current law. Laymen commonly consider "the law" to be a set of rules providing fixed and definite answers that can be looked up, much as one looks up the fines for parking violations in a municipal ordinance. While some rules may be definite, the dominant view of "law" within the legal profession is that law is a process that can produce a range of possible outcomes. Before final decision, the law is just a prediction. According to Oliver Wendell Holmes, for instance, "the law" itself is nothing but a prophecy of what a court will in fact do.[14]

Litigation thus will settle what a court will do, but judged before final decision, the range of possible tax outcomes inevitably is very wide. All experienced lawyers know that "the facts" can be planned or shaded or characterized to fit favorable categories and know that they can generate "reasonable" arguments in favor of their clients, even in the face of apparently adverse certainty. All experienced lawyers know of cases they should have lost—judged solely as a matter of prediction—but in fact won. All experienced lawyers know of case outcomes that could not have been reasonably predicted in advance. Even on a philosophical level, there always exists a difference between specific events and intellectual categories into which the events must be placed—categorizing events requires judgments that are not fixed by logical necessity.

For our generation, moreover, tax legislation will be complex and changing. Enacted legislation commonly is a set of convoluted compromises. Tax law is not an engineered system in which the pieces fit together with precision. The forces that change legislation—that is, the desire for revenue and the desire for tax cuts—will not abate within our lifetimes. Some uncertainty might be taxpayer-generated to avoid adverse categories, some might be congressionally generated, and some is just inevitable in a complex world. When Heaven walks on Earth, tax will be simple and clear. But any standard now, whether strict or lax, will operate in a less-than-ideal, uncertain world in which no one can truly "know" the law.

This article examines three competing standards for reporting positions on a tax return.

II. POSSIBLE REPORTING STANDARDS

A. As Likely As Not

A taxpayer should be able to report tax, this article argues, under an interpretation of law or facts favorable to the taxpayer, without specifically disclosing his position, only if the position is at least as likely as not to prevail if challenged.[15] Stated in lay terms, the tax return should be true and correct to the best of the taxpayer's knowledge.

1. Correct Tax. The Internal Revenue Service has the fiduciary duty to its government to collect correct tax. Taxpayers have a legal obligation to pay correct tax. The IRS should collect the correct tax by enforcing a taxpayer's obligation to self-assess tax, rather than by intrusive, hostile audits.

Standards of reporting operate in a world that is inevitably complex and uncertain.

The tax return requires that a taxpayer sign a statement that, "to the best of knowledge, the return is true, correct, and complete." It is a felony for a taxpayer to willfully file a return "which he does not believe to be true and correct as to every material matter."[16]

"Correct and true" tax, within a system that inevitably generates a wide range of possible outcomes, is best translated into a phrase indicating a 50-percent chance of prevailing, i.e., "as likely as not to prevail." (If there is a plurality of positions with no one position more likely than not to prevail, a 50-percent chance of prevailing

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[9] IRC section 7206(l).

[10] Asimow, *Civil Penalties for Inaccurate and Delinquent Tax Returns*, 23 U.C.L.A. L. Rev. 637, 658 (1976) (report prepared for the Administrative Conference).

[11] IRS section 6661(a) as clarified by Technical and Miscellaneous Revenue Act of 1988 section 1015(a). An underpayment is substantial if it exceeds 10 percent of tax or $5,000. IRC section 6661(b).

[12] Treas. reg. section 1.6661-3(b)(2).

[13] Formal Ethics Opinion 85-352 (1985), 39 *Tax Lawyer* 631, 634 (1986). The AICPA standard has a "realistic possibility of being sustained administratively or judicially on its merits if challenged." AICPA, *Statements on Responsibilities in Tax Practice* section .02 a. at p. 4 (1988 Revision).

[14] Oliver Wendell Holmes, *Path of the Law*, 10 *Harv. L. Rev.* 457, 460 (1897).

[15] The December 1988 Draft of the Stark Task Force report had recommended that taxpayers be required to exercise reasonable care that each tax return position was more likely than not to prevail. Stark Draft ch. 8, pt. VI.1. The final report, however, recommended a variation of "substantial authority" instead. See *infra* notes 24-29 and accompanying text.

[16] IRC section 7206(1).

would mean that all the positions generating the same or less tax than reported have chances that sum to a 50-percent chance.) A 50-percent or "as-likely-as-not" standard would mean that ties go to the taxpayer.

A taxpayer should be able to report...only if the position is at least as likely as not to prevail.... Stated in lay terms, the tax return should be true and correct to the best of the taxpayer's knowledge.

The IRS claim for the full proper amount of tax in accordance with the rule of law seems no weaker than the taxpayer's claim for as little tax as allowed by law. The weight of the two claims balance each other in civil cases. In civil cases, the trier of fact is asked to weigh all of the evidence and find according to the preponderance of the evidence. Equal balancing of the weight of law and evidence on both sides of a question implies an as likely as not standard. Criminal standards created to protect by an individual from jail—are taxes really due "beyond a reasonable doubt?"—are inappropriate for civil standard arguing only over the reporting of an amount of money due.

Equally valid claims by both IRS and taxpayer imply that uncertainties should be resolved in favor of the IRS as often as they are resolved in favor of the taxpayer. The IRS did not cause the inevitable uncertainty of the tax law, and it has to collect correct tax in the most efficient manner, even though the world will remain uncertain.

Standards lower than "as likely as not" are not consistent with the meaning of "correct and true" tax required by the current felony provisions and tax return affirmation. "Aggressive positions" taken on a tax return are not consistent with reporting of true and correct tax.

2. Audits and Self-Assessment. A more-likely-than-not standard would support accurate self-assessment by a taxpayer and minimize the role of IRS audits in the collection of the proper amount of revenue. Any lower standard necessarily will encourage taxpayers to underreport their liabilities and leave the IRS in the position of policing a perfectly legal "catch me if you can" standard.[17]

The mission of the IRS, according to its formal mission statement, is to collect the proper amount of tax efficiently and fairly. The IRS thus is to encourage the highest possible degree of voluntary compliance by taxpayers by self-assessment. Audits and penalties primarily are to serve a subsidiary function of supporting and encouraging such self-assessment.[18]

Audits of tax returns are expensive, intrusive, and unpopular. The IRS should not be required to audit to collect the correct amount of tax if taxpayers can be required instead to assess the correct amount of tax. The common understanding of taxpayers is that the IRS will propose deficiencies only when the taxpayer has done something wrong. That understanding implies that the taxpayer has assessed the correct amount of tax in the first place. If honest taxpayers have resolved all doubtful issues in their favor, moreover, the auditing agent cannot presume that even honest taxpayers are correct. Consistent with his duty to collect correct tax, an agent must assess deficiencies against even honest and good faith taxpayers. This promotes added friction in the system and the hatred of IRS agents who are just doing their job.

3. Public versus Private Tax Advice. The Guidelines for Tax Practice, promulgated by the Committee on Standards of Tax Practice of the ABA Section of Taxation, take the view that tax attorneys should not assist in the offering of tax shelters "unless there is a substantial likelihood that the tax consequences can be resolved in favor of the taxpayer."[19] This view is reflected in Treasury's Circular 230, which requires practitioners to "provide an opinion whether it is more likely than not that an investor will prevail on the merits of each material tax issue...."[20] The standard in Circular 230 was criticized, during its consideration, because it differentiated "between ethical standards of disclosure for clients and standards of disclosure for the public at large."[21] Taxpayers getting tax advice through tax opinions circulated in publicly traded investments likely are less wealthy than taxpayers getting tax advice in private. A 50-percent standard applied to both cases would end the discrimination.

4. No Tax Increase. There is considerable public sentiment supporting better compliance measures. In the 1982 Tax Act, for instance, Congress increased penalties, because

> Congress believed that it would be unfair to ask the majority of honest Americans to pay more taxes unless every reasonable effort was being made to make sure that tax evaders comply with the law.[22]

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President Reagan signed the 1982 Act relying in part on the argument that the revenue gain represented tougher enforcement for tax laws already on the books.[23] Polls support provisions perceived as improving equity: a 1982 Harris poll, for instance, showed a "shocking" 86-to-7 majority of responders in favor of the proposition that low- and middle-income taxpayers pay Federal tax, but "most higher-income people get out of paying most of

[17]Stark *Draft* ch. 8, pt. III(C).

[18][CCH] *IRS Manual* section 111.1 *Mission.*

[19]Guidelines to Tax Practice, Report of the Committee on Standards of Tax Practice, Section of Taxation, American Bar Association, 31 *Tax Lawyer* 551, 554 (1978) (Frederic Corneel, Chair).

[20]Circular 230, 31 C.F.R. Part 10, section 10.33(a)(4), 49 Fed. Reg. 6719, 7116 (1984).

[21]Gordon Henderson of the New York State Bar Association Tax Section, reported in 11 *Tax Notes* 1143 (Dec. 8, 1980).

[22]Staff of the Joint Committee on Taxation, *General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibility Act of 1982* at 14 (1982).

[23]President Reagan, Speech of August 16, 1982, cited *Wall Street Journal*, Aug. 17, 1982 at p. 3, col. 3.

their taxes by hiring clever tax accountants and high-priced lawyers."[24]

Raising the effective standard for reporting positions on a tax return might raise very substantial amounts of revenue. The difference between, say, a reasonable basis, five- to 10-percent chance of success and a 50-percent standard on every issue in which there is any doubt could mean a lot of revenue. The amount of revenue could well be hard to measure: taxpayers will react to higher standards, in part, just reporting the same amount of tax but becoming more optimistic about their chances of success. Many taxpayers, moreover, undoubtedly are already reporting tax under some standard equivalent to "correct" tax.

B. Substantial Authority

The Stark Task Force recommended a modified version of the "substantial authority" standard of current law for tax return positions. Section 6661 of the Internal Revenue Code now imposes a 25-percent civil penalty on positions taken without "substantial authority" if the position results in substantial underpayment of tax. The Stark Task Force would reduce the rate to 20 percent and extend the "legal list" of legitimate authorities a taxpayer could rely on to include "nonprecedential authorities of a sufficiently legal and institutional nature."[25] Private letter rulings, TAMs, GCMs, Tax Court Memoranda, and Bluebooks (General Explanations of a major tax act prepared by the staff of the Joint Committee on Taxation) could be relied on by the taxpayer to determine the substantiality of a reporting position, even if they were not generally considered to be legal precedents. But articles or commentaries (for instance, by Bittker & Eustice, Stanley Surrey, or McKee, Whitmire & Nelson), public speeches by elected or Treasury officials, and good tax theory still would not be permitted to be used.

The Stark Task Force Report also interpreted the judgment of "substantial authority" as a weighing process in which the strength of adverse authority was weighed against the strength of the authority supporting the taxpayer's position. Literally "substantial" authority might imply a threshold test: even authority heavily outweighed by adverse authority would be enough if it were sufficient legal authority standing alone. Under the Stark report, however, the taxpayer would meet the proposed standard only when the taxpayer had such authority that his chances of prevailing on the merits if challenged approached 50 percent. Substantial authority under current law has been characterized as requiring a 30- to 35-percent chance of success.[26] The Stark report characterized its substantial authority as involving a 45-percent chance of success.[27]

The Stark Task Force considered a "45-percent weight of the authority" standard to be an objective test that would be met or failed without requiring the IRS to inquire into the good faith of the taxpayer or exercise of reasonable care. Commonly, only the taxpayer has evidence of his reasonable care as to undisclosed evidence, or evidence of the taxpayer's actual knowledge or reasonable care will be found in "communications with professionals that are privileged and therefore not obtainable by the IRS."[28] The Stark report considered that the strength of an argument can "reasonably be weighed objectively in most circumstances by considering the existence and reasoning of certain authorities with respect to the issue."[29]

The Stark Task Force concluded that in the absence of IRS ability to judge good faith or reasonable care, a "more-likely-than-not" standard would result in too many "false positives," meaning that taxpayers would be subjected to penalty for underpaying tax, when their behavior ought to be excused because they in fact tried hard enough. The Stark Task Force considered a less strict objective standard (45-percent weight of authority) to be a compromise "surrogate" for the aspirational "more-likely-than-not" standard. It claimed that most taxpayers would maintain the "more-likely-than-not" standard anyway to stay clear of penalties.[30] It considered a lower objective standard to be a good "surrogate" for higher standards that required the IRS to ascertain subjective intent or level of care.

C. Criticism of the Substantial Authority Standard

1. Aspirational Standards. The Stark Task Force claimed that it wanted to maintain "more likely than not" as an aspiration. But it is a moralistic cant to suggest that taxpayers have any "aspirational" duty to follow a higher standard than required by enforced legal standards. Taxes are an exaction. There is no patriotic or moral duty to pay more than legally required. If Congress wants to collect correct tax or enforce some standard of reporting correct tax on a return, it will have to do so by enforcement of stated legal obligations and not by "moral suasion" or "aspirational" goals.

If Congress wants to collect the correct tax . . . , it will have to do so by enforcement of stated legal obligations and not by 'moral suasion' or 'aspirational' goals.

There is no reason, in any event, why a "45 percent weight of authority" test or any similar lower "objective" standard should foreclose enforcing a rule requiring that the taxpayer report correct tax, in those cases where the IRS can ascertain that the higher "subjective" standard has been breached. A weight of authority test, or some similar proxy standard, could be used as the most common trigger for penalties without preventing the IRS from also assessing penalties when the taxpayer was not trying to report correct tax. If the "more likely than not" test is too subjective to be proved or enforced, then it will not always be relied on. But why drop it as an enforced standard altogether, if, as the Stark report claims, it is indeed the appropriate aspirational standard that the law should reflect?

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[24] *Flat Tax: Hearings Before the Senate Finance Comm.*, 97th Cong., 2d Sess. at 244 (Sept. 29, 1982) (Statement of Lou Harris).

[25] Stark Task Force at VIII-40.

[26] Banoff, *Dealing with the "Authorities": Determining Valid Legal Authority in Advising Clients, Rendering Opinions, Preparing Tax Returns and Avoiding Penalties,* ____ *Taxes* 1072, 1128 (1988).

[27] Stark Task Force at VIII-39.

[28] *Id.* at VIII-38.

[29] *Id.* at VIII-38.

[30] *Id.* at VIII-39.

2. Absence of Authorities. A 50-percent chance of success standard is better for taxpayers when there is nothing that can technically qualify as "authority." In determining whether a legal position is likely to prevail, a model taxpayer sometimes has to rely on good tax theory, wise commentators, and public speeches by Treasury or congressional officials, even if such "quasi-law" sources do not technically qualify as "authority." A taxpayer should have the "right to the law," that is, the right to report his tax on his return according to a prediction as to what the outcome of a litigated case is likely to be, even if there was no technical "authority." Especially soon after a major tax bill is enacted, there is commonly no authority sufficient to clarify the ambiguities (or glitches) in the language of the enacted statute. Taxpayers predicting what outcomes will be then have to rely on the purposes of the Act and tax theory and prior understandings of normality.

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Both the current and proposed substantial authority rules rely on a legal list of authorities in order to control the generation of commentaries—or speeches—just to lower reporting standards. Practitioners can write articles espousing pro taxpayer resolutions of issues, or inventing new arguments and new issues. If such articles constitute sufficient authority, substantial authority will cease to be an objective standard raising the standards for reporting tax. But in seeking to exclude manufactured authority, the legal list also excludes respected sound authorities and even pro-government commentators because of an unwillingness to try to distinguish sound from manufactured authority. If law is just a prediction of how an enlightened court would rule, however, the taxpayer should be entitled to sound predictions, even if the reasons for the sound prediction are not found on the legal list. "Authority" that is available, however, would of course be relevant evidence of whether the taxpayer was likely to prevail.

3. Avoiding Subjectivity. The 45-percent-weight-of-authority test will produce "false positives" almost as commonly as a more-likely-than-not standard will. If a taxpayer after reasonable effort falsely believes that he has reported correct tax, he still will be penalized under the 45-percent weight standard if he fails it. The five-percent relaxation in chance of prevailing only rarely will make a difference. Why, then, not try to enforce correctness?

Taxpayers who would fail a subjective test—no good faith effort to ascertain correct tax—nonetheless can be given exemptions from penalty under better surrogates of the 50-percent test. For example, a taxpayer who had the preponderance or equal weight of authority on his side would be free from penalty even if he subjectively believed that more tax was due. Taxpayers who prevail even against the odds and in spite of all the predictions would not be penalized, even though subjectively the taxpayer breached his obligations. Taxpayers who relied on written opinions of their accountant or lawyer, after having fully advised the accountant and lawyer of the facts, can be relieved of penalty if the professional, by undertaking the writing, will absorb some risk of penalty. Objective defenses do not have to be laxer standards.

One of the best objective triggers indicating breach of standards is the substantiality of the underpayment of tax as ultimately determined.[31] Accuracy is more important when substantial amounts are at issue than for smaller amounts. Concerns about administrability will swap concerns about meticulous accuracy, when the tax in dispute is not material. The percentage of the departure from correct tax, as ultimately determined, is a fair proxy measure of how hard the taxpayer tried to predict the outcome. Substantiality is a requirement under current law. Thus, for instance, section 6661 of current law imposes a 25-percent penalty on an undisclosed position taken without substantial authority, but only if the underpayment is more than 10 percent of the tax determined to be due, and only if the underpayment also is more than $5,000 (or $10,000 for regular C Corporations). Similarly estimated taxes are required to be paid on a quarterly basis as income is earned during the year, but the estimated tax paid need only come within 10 percent of annual tax ultimately reported.[32] The analogy between estimated tax and reporting standards is especially apt: all law is in some sense just an estimate of what the ultimate outcome will be. Since we are willing to enforce estimates in the quarterly payment and to penalize misestimates at least to a certain extent, so we should be willing in the final reporting system to penalize misestimates of what the law will ultimately determine to be the tax amount. Carving out nonmaterial underpayments also clarifies the debate. We are debating big money issues in which greater accuracy is clearly worth the candle.

Taxpayers who fail to pay correct tax in a complicated and uncertain world are not moral lepers. But absence of moral condemnation is best reflected by making first tier penalties quite low—a reminder and incentive, rather than a stigmatization—instead of by reducing legal standards below their proper aspirational level.

Objective defenses do not have to be laxer standards. . . . Absence of moral condemnation is best reflected by making first-tier penalties quite low. . . .

D. Right to a Day in Court

Taxpayers may bring lawsuits and authorize briefs in support of positions that are considerably less than likely to prevail. A citizen has a fundamental right to seek redress in court for what he considers to be a wrong, and there is a strong public interest in affording every citizen freedom of access to the courts. A complaint or brief in

[31]My thanks to Frederick Corneel for making this argument especially cogently.

[32]IRC section 6654(d)(1)(B)(i) (individuals); IRC section 6655(d)(1)(B)(i) (corporations).

litigation is not supposed to represent a true and correct position. It is the opening round. The complainer makes his position; the responder responds, and the truth is to be shaped between the hammer and anvil of the adversary system. A lawsuit even may be used just to investigate the facts or to find records held by an adversary and may be based on extraordinarily novel legal theories.[33] Lawsuits are in fact commonly brought with less than a 50-percent chance of victory. Taxpayers won complete victories only in 22 percent of the tax refund cases in 1986, and partial victories only in another five percent of those cases.[34] Since a complaint starting a lawsuit will be met promptly by an adversary, quick dismissal of the complaint usually is a sufficient remedy for a nonmeritorious claim.[35] The cost of litigation also is a very effective control on the number of nonmeritorious claims.

Reporting standards need not be a 'compromise' with litigation standards, if litigation rights remain.

The American Bar Association and AICPA draw their professional standards regarding when a practitioner may advise a client to take a position on his tax return from adversary litigation. ABA Ethics Opinion 314 argued that the duty on a tax return is analogous to a lawyer's duty to his opposing lawyer: A lawyer is under no duty to disclose his weaknesses to the [IRS on a tax return] any more than he would be to make such disclosures to a fellow lawyer.[36] The duty of an attorney to his adversary in litigation, in sum, is to tell the truth and nothing but the truth, but not necessarily the whole truth. In Ethics Opinion 85-352, the ABA restated its standards to require "some realistic possibility of success if the matter is litigated" including by an "extension, modification, or reversal of existing law."[37] The new test was in response to attacks on the old "reasonable basis" standard as contributing to the audit lottery, but the change from "reasonable basis" to "realistic possibility" was intended to effect no substantive change, except to clarify the standard. The tax return still is thought of as the start of "what may be an adversary process."[38] The professional standards of the ABA and AICPA, it should be emphasized, are not law. The standards just represent the degree to which trade groups, whose members benefit from lax standards, are willing to police themselves.

E. Criticism of Right to a Day in Court

The Stark Task Force concluded that a litigation standard applied to *undisclosed* positions was a "fundamental bar to better tax administration.[39] Abusive tax shelters have been said to be "the progeny of the [reasonable basis'] standards set for reporting transactions on returns."[40] Much of the complex technical legislation reacting to tax shelters was caused by dissatisfaction with the reasonable basis standard.

The taxpayer's right to litigate should not undercut or be in conflict with his duty to pay correct tax. In an ideal world, taxpayers even can be given the right to litigate before paying tax, without affecting their reporting standard. For instance, if a disclosed position gives the taxpayer quick access to the IRS appeals process and to the Tax Court for judicial review before the payment of tax, the taxpayer could achieve his day in court simply by disclosing his position. Reporting standards need not be a "compromise" with litigation standards, if litigation rights remain.

An undisclosed position on a tax return is not a reasonable manner by which the law can support the taxpayer's right to his day in court. A tax return does not effect access to court in part because only about one percent of returns are audited[41] (and even then only on a spot basis). Realistically, a taxpayer filing a tax return does not want to get into court. As one respected commentator has said, "The premise of the adversary system that two adversaries will be in an equal position to uncover and present the facts, is unrealistic as applied [to tax returns]."[42]

It is impossible to protect a taxpayer's chances to pay the least that he possibly can without litigating, without also depriving the government of taxes that it has a legal right to and would get....

In an uncertain world in which not all uncertain questions can in fact be litigated, any standard of reporting some tax will mean that the taxpayer sometimes will have to sue to pay the least amount of tax that they can. Even allowing taxpayers to report a position without disclosure if they have a one-percent chance of success will mean that there will exist some taxpayer who will be able to

[33]Reisinger, *Honesty in Pleading and its Enforcement: Some "Striking" Problems with Federal Rule of Civil Procedure 11*, 61 *Minn. L. Rev.* 1, 56-57 (1976).

[34]Podolin, *Treasury Raises the Stakes in Circular 230 Proposal*, *J. of Accountancy* 60, 66 (April 1988). In Tax Court in 1986, taxpayers won a complete victory in only four percent of the cases, but won partial victories in another 50 percent of the cases. *Id.*

[35]*See generally* Wright and Miller, *Federal Prac. & Procedure* section 1334, 501-504 (1969) for a description of sanctions against frivolous civil lawsuits, concluding at 503 that sanctions are rare.

[36]Formal Ethics Opinion 314, 51 A.B.A.J. 671, 31 *Tax Lawyer* 555 (1965).

[37]Formal Ethics Opinion 85-352 (1985), 39 *Tax Lawyer* 631, 634 (1986). The AICPA standard has a "realistic possibility of being sustained administratively or judicially on its merits if challenged." AICPA, *Statements on Responsibilities in Tax Practice* section .02 a. at p. 4 (1988 Revision).

[38]Formal Ethics Opinion 85-352 (1985), 39 *Tax Lawyer* 631, 634 (1986).

[39]Stark Task Force at VIII-9.

[40]IRS Commissioner Kurtz, *Notes to a New Commissioner of Internal Revenue*, 12 *Tax Notes* 1195, 1196 (1981).

[41]Schmedel, *Tax Report, Wall St. J.* March 22, 1989 (quoting IRS Annual Report).

[42]Rowen, *When May a Lawyer Advise a Client That He May Take a Position on a Tax Return?* 29 *Tax Lawyer* 237, 249 (1976).

exploit a chance of success (under one percent) only by litigation. But it is impossible to protect a taxpayer's chances to pay the least that he possibly can without litigating, without also depriving the government of taxes to which has a legal right to and would get in some high percentage of the litigated cases. If the taxpayer may avoid reporting tax based on any reasonable basis, the IRS can collect tax by self-assessment only when the tax is due beyond a reasonable doubt, and that gives the taxpayer's claims absolute priority.

A 'reasonable basis' or 'realistic-possibility-of-prevailing' standard is not an enforceable standard.

A "reasonable basis" or "realistic-possibility-of-prevailing" standard is not an enforceable standard. A realistic possibility of prevailing can be based on reversal or modification of current law; even dispositive evidence of what current law is does not settle whether the taxpayer has breached his duties under a realistic-possibility standard. A realistic-possibility-of-prevailing standard thus would prevent self-assessment under any enforceable standard and thus prevent the IRS from fulfilling its mission to collect correct tax.

III. DUAL STANDARD FOR FLAGGED POSITIONS

A. Frivolousness Criteria

The Stark Task Force would allow a taxpayer to report tax relying on a position failing its 45-percent-of-the-weight-of-authority test if the position was not "frivolous," provided that the position was disclosed on a return. The nonfrivolous standard is a litigation standard, originating in the standard for when a citizen may bring a lawsuit without penalty. Frivolousness has been identified as less than a 10- to 20-percent chance of success on the merits it challenged.[43] The December 1988 draft of the Stark report had a "realistic possibility" standard for disclosed positions, drawn from the ABA and AICPA standards on when a professional may advise the client to take a position on a tax return, except that the ABA and AICPA do not require disclosure. The realistic possibility standard has been deemed to have a 30- to 35-percent chance of success,[44] although that seems high given that both nonfrivolousness and "realistic possibility" arise from a common litigation standard.

Although the ABA and AICPA statements do not require flagging aggressive positions, flagging seems an appropriate requirement for a litigation standard. Litigation anticipates an able adversary arguing against the moving party. The ABA and AICPA standard originates as a duty to opposing counsel. The value being protected is the taxpayer's right to access to a court. Disclosure in such a way as to encourage joinder of the issue by opposing counsel thus is an appropriate requirement.

Reporting tax under the basic reporting standard (whether 45-percent weight of authority or as likely as not) would remain the duty of the taxpayer, even with the lower standard with disclosure. The lower disclosure standard is protecting the taxpayer's right to get access to the Tax Court and IRS appeals officers and not protecting taxpayer's paying less tax without joinder of the issue by an IRS adversary.

B. Critique of the Disclosure Remedy

The proposed disclosure remedy is inadequate. It is not administratively feasible for the IRS to meet and litigate all positions disclosed by a taxpayer. A litigation standard implies that positions are met by able counsel. The IRS should no more let disclosed positions go uncontested than the government should default on million dollar lawsuits brought against it. Until the IRS can come closer to contesting all disclosures, the standard for disclosures needs to be higher than nonfrivolous. To use an accounting analogy, what counts is "earnings per share" (i.e., self-assessed, reported tax) and not the "footnotes" (i.e., the partially disclosed positions).

1. Inadequacy of Disclosure. Without 100-percent response to disclosures, the disclosure system alone is inadequate to prevent abuses. Even very clear disclosures commonly are not picked up by the IRS. There is, for instance, the story of the taxpayer who took protective claims for a single $100,000 bad debt in each of six successive years, because it was not clear in which year the debt went bad and each year had about a one-sixth chance of being the right year. Without taking the deduction in the right year, the taxpayer might have been barred by the statute of limitations from taking the deduction at all. After the first year, he clearly disclosed the prior deduction on each tax return. Nonetheless, none of the returns was ever audited or challenged and the taxpayer ended with $600,000 in deductions (and $420,000 in tax savings) from a single $100,000 loss! The procedure is not out of line: it is recommended, for instance, in a "Tax Saving" note by Prentice Hall Federal Taxes Para. 14,290. The IRS Service Centers do not handle stray pieces of paper very well, but disclosures such as that should not slip through.

The IRS should no more let disclosed positions go uncontested than the government should default on million dollar lawsuits brought against it.

Disclosing weak positions commonly is thought of in the bar as a way to get fraud insurance, at some low but acceptable risk of increasing audit likelihood. Others think that the risk of increasing audit outweighs the fraud insurance for aggressive positions, but that is a judgment call. Disclosure remedies in general are subject to being swamped by over-disclosure and by noninforming disclosures. A taxpayer who can avoid a penalty by disclosing information gains a game-position advantage by supplying a great deal of information without exercising any judgment as to the quality of the risks in the positions. A corporate taxpayer thus might deliver a box car of information, suggesting some doubt about the deductibility of wages expenses or cost of goods sold, just to camouflage the positions about which there is considerable doubt. The drafting of SEC prospectuses, moreover, has become in part a craft of writing statements that cover the

[43] Banoff, *supra* note 25, at 1188.
[44] *Id.*

risks sufficiently to avoid liability, without informing investors of the true risks that would dissuade them from investing. So, similarly, a taxpayer ordinarily would have a game-position advantage in writing disclosures that suffice as a matter of law, without alarming the IRS agent so as to trigger audit.

If a litigation standard is going to be allowed for disclosed positions, the IRS must meet every disclosed position with a 30-day and 90-day letter.

2. Flagged Position and Automatic Response. If a litigation standard is going to be allowed for disclosed positions, the IRS must meet every disclosed position with a 30-day and 90-day letter. The IRS has a fiduciary duty to the United States government to collect the correct amount of tax and thus it should ordinarily go forward on amounts identified as likely to yield an IRS victory. A litigation standard implies that a tax return is like a complaint in a lawsuit. Think of the malfeasance in office if an administrative officer allowed complaints in lawsuits to go to default judgment against the United States because they did not answer the lawsuit! The value being protected is the taxpayer's right to access to court. Disclosure in such a way as to encourage contesting of the issue by opposing counsel in court thus is a result implied by the standard.

The IRS also should sometimes litigate when it is less than likely to prevail in an attempt to bring current case law into conformity with good tax policy or administration. Less commonly, the IRS sometimes is right to settle cases it is likely to win because it has a test case that raises the issues more effectively or because of consideration of the normal hazards of litigation. Cases can be settled by the experienced IRS appeals officer or litigator to whom the disclosed positions are assigned after a 30-day or 90-day notice is given. But still all positions that a taxpayer has identified as giving the IRS a better than even chance of an IRS victory should be met automatically with an IRS 30-day notice claim for tax.

To facilitate automatic and efficient IRS meeting of all disclosed issues, the IRS will need a form or schedule for disclosures in order to identify and process the disclosures with dispatch and efficiency. The form should require the taxpayer to compute the taxable income and the amount at stake for each position for which the taxpayer judges he has a less than even chance of prevailing. From the face of the form, the IRS should be able to understand what issues are important sources of revenue and what issues are less material. In theory, a disclosure should be a program guide to a perfect audit.

Automatically meeting each disclosure with a demand for tax and notice of deficiency does not undermine the rights and values that a litigation standard was intended to protect. The procedure would allow the taxpayer to use the appellate procedures within the IRS to settle issues administratively and would allow access to the Tax Court to achieve judicial review without paying the contested tax. Since a litigation standard arises out of and is legitimated by adversary litigation, the litigation it engenders furthers the purpose of the standard. Reporting tax under the as-likely-as-not standard would remain the basic duty of the taxpayer, even with the lower flagged position standard. The lower disclosure standard is not protecting a taxpayer's paying less tax without counter on the issue by an IRS adversary. Given normal aversion to litigation, the nondisclosure standards would be the decided norm for reporting tax.

An automatic IRS 30-day letter would restrain the overclaiming of positions on the new Disclosure Statement form. If the taxpayer was unclear on the disclosure statement form, he would need to be clearer to convince the Tax Court on the merits of the position. A taxpayer is at his risk as to his excessive disclosures that a Tax Court judge would grow impatient over arguments about routine deductions and just disallow the deductions.

At very minimum, the IRS must be able to process disclosures enough to enter them into its Master File database and apply the Audit Discrimination program screens to the disclosures. If the disclosures are not automatically triggering audits, there is no resemblance between disclosure and litigation and the case for a lower standard to be applied to disclosed positions becomes very weak.

3. Raising the Disclosed Position Standard. Even under the most efficient IRS administration, flagging is unlikely to lead to full litigation with an able IRS adversary meeting every issue. Even if disclosures meet a less-than-full, but still reasonable, IRS response, the courts will be swamped by too much litigation, much of it nonmeritorious. A reasonable remedy is to raise the standards for positions litigated before payment of tax. The taxpayer might be required to have substantial authority for his position or considerable merit, or a 40-percent chance of success before relying on a position to pay no tax, even with flagging. Those taxpayers who want to pursue lesser chances of success would be able to continue to do so, but only by refund litigation. At common law, the only way to litigate tax issues was through refund litigation.[45]

In theory, a disclosure should be a program guide to a perfect audit.

IV. PENALTY STRUCTURE

The purpose of any penalty is to ensure that a taxpayer is better off complying with legal standards than breaching them. Penalties deter both the penalized taxpayer and other taxpayers. But penalties perceived to be fair also reinforce the personal ethics and social norms of the taxpayer. They validate the standard being enforced and remind the taxpayer of his duties.[46]

A. Stark Proposal for Three Tiers

The Stark Task Force proposed a three-tier penalty structure. There would be a 20-percent civil penalty if the taxpayer failed to exercise *reasonable care* that disclosed and undisclosed positions met the required standards. Individual tax underpayments of less than 10 percent of

[45] *Cheatham v. United States*, 92 U.S. 85 (1875) (prohibition on judicial review prior to paying tax is an ancient doctrine arising because taxes are "the very existence of the government").

[46] Stark Task Force, ch. III.

tax (*and* less than $5,000) could not be subject to the first tier penalty. For corporations, underpayments of less than 10 percent of tax (*and* less than $10,000) would be immune. There would be a 50-percent gross negligence penalty if the taxpayer took a frivolous position or *willfully* failed to meet the weight of authority test for undisclosed positions and there would be a 100-percent civil penalty on "*fraud*," defined without change from current law. The first tier penalty would be waived if the taxpayer nonnegligently failed to identify an issue, but not if the taxpayer nonnegligently overestimated the changes of success.[47]

Systems that let the taxpayer get out of standards if the taxpayer tries hard enough in fact encourage the taxpayer to give less than his best effort to accomplish the standard.

The Task Force concluded that viewed from an economic perspective, effective deterrence requires that the rates for penalties be extremely high. With audit rates of two percent, for instance, penalty rates have to get to 4,900 percent just to "break even," that is, leave the taxpayer with no incentive to underreport.[48]

The Stark Task Force proposal would liberalize current law in that each penalty would be targeted to only that part of an underpayment of tax for which a standard was breached. Once the IRS had established a breach of standard as to part of a tax underpayment, taxpayers could avoid penalty on another portion of their underpayment if they establish that the conditions of the penalty were not present as to that portion.[49] Under current law, negligence (or fraud) as to part poisons the entire underpayment and makes it subject to the percentage penalty.[50] To prevent piling up of penalties, moreover, only the most severe applicable penalty could be collected.

B. An Automatic Penalty

There is need in the penalty structure for a small five-to seven-percent automatic penalty to reinforce the legal standard. A taxpayer who has breached his obligation to pay the correct tax or to report under some objective standard can be subject to some penalty reminding him of his obligation, even though subjectively he thought his behavior was not censurable.

To create a penalty structure that will ensure that a taxpayer is better off meeting a standard than breaching it, it is sometimes necessary to impose a penalty because the standard was not met, rather than because the taxpayer did not try hard enough. Systems that let the taxpayer get out of standards if the taxpayer tries hard enough, in fact encourage the taxpayer to give less than his best effort to accomplish the standard. The taxpayer has just to convince the finder of fact that he tried; that may be considerably cheaper than actually accomplishing the standard. A taxpayer will work harder to meet a standard he must meet than he will to meet a standard from which he can get excused.

[47] *Id.* at VIII-42-45.
[48] *Id.* at VIII-29.
[49] *Id.* at VIII-26, 45.
[50] *Commissioner v. Asphalt Products Co.*, 107 S.Ct. 2275 (1987).

Litigation about the taxpayer's good faith effort always is inherently unsatisfactory. Facts about the taxpayer's mind are difficult to establish and taxpayers sometimes can lie with impunity about their purely subjective intent. The taxpayer has an affirmative duty to report tax on a 50-percent chance standard. His sin may be a sin of omission rather than commission, so no one should have to look for or prove he committed some positive fault.

The single best objective evidence as to whether a taxpayer was more likely than not to prevail when he reported his tax usually is that he did not prevail in the end. A court sometimes can see that it has modified the law against taxpayer positions since the return was filed and the IRS sometimes will litigate in the face of authority, making it likely that it will lose in order to try to effect better tax policy. A taxpayer also can be exempted from penalty if he relies on an opinion by a practitioner who takes responsibility for accuracy and to whom all the facts have been given. But absent such circumstances, a decision against the taxpayer is sufficient evidence in the civil context that he was not more likely to win when the return was filed.

Minor penalties are not socially stigmatizing nor a sign of moral turpitude. But like parking tickets and minor moving violations, they are reminders to the taxpayer that the law intends that ordinary law-abiding taxpayers follow the standard and take it seriously.

V. PRACTITIONERS AND PREPARERS

A. Stark Proposals

The Stark Task Force generally would conform the standards of behavior applied to practitioners and tax return preparers with the standards required of taxpayers themselves. A practitioner thus would be required to exercise reasonable care that undisclosed positions meet the newly required standard for taxpayers. Tax return preparers also would be required to exercise reasonable care, but "the custom of the profession and the facts surrounding the matter at issue [are to] guide the valuation of reasonable care."[51] Whereas the Stark Task Force standard for taxpayers was expected to be an "objective" test for taxpayers, practitioners would be subject to penalty only if they failed to exercise reasonable care themselves.[52] A practitioner could be referred to the Director of Practice for possible discipline only because of his own behavior and not because of the behavior of his client. Disbarment or suspension would arise only for egregious misconduct and not for isolated incidences of mere negligence.[53]

Minor penalties are not socially stigmatizing or a sign of moral turpitude.

B. Monetary Penalties

There need to be monetary penalties, short of disbarment or suspension, that better meet practitioner breaches of their standard. Loss of the ability to practice before the IRS often is tantamount to loss of livelihood

[51] Stark Task Force at VIII-45.
[52] *Id.* at VIII-46.
[53] *Id.* at 42, 46-47.

for a practitioner. For what may be only a moderate fine for the client, the practitioner could be subject to the "capital punishment" of the field.

For what may be only a moderate fine for the client, the practitioner could be subject to the 'capital punishment' of the field.

Penalties enforcing taxpayer standards should fall primarily on taxpayers, rather than on their representatives. Tax practitioners and return preparers generally are loyal agents of the taxpayer. If the penalty structure allows the taxpayer to be in a better position by breaching standards than by paying tax, a competent and loyal agent normally can be expected to tell the taxpayer and thus to encourage breaches. The system can get some leverage over the taxpayer by threatening to punish the adviser, but ultimately, the tax adviser is paid by the client and has a place in the system only because he is perceived as loyal and competent by the client. If the separate penalties on the adviser get so high as to force the adviser to be disloyal to the client, the adviser will be forced out and the government will have to try to collect tax, under a complicated system, without any help from tax professionals. On the other side of the coin, if the penalty structure is adequately designed and adequately severe so that it is in the client's interest to meet a specific standard, the tax adviser will serve the system by informing the client of his self-interest and will help him meet the standard. If the penalties on the taxpayer are sufficient, added penalties on a competent adviser rarely will arise. Taxpayers, moreover, have the ultimate responsibility for the completeness and correctness of their returns and only they have full knowledge of all of the relevant facts.

The practitioner, however, is not always an innocent party when standards are breached. Abusive shelters often were created by the lawyer writing the legal opinion, rather than by the general partner selling the investment. Indeed, in some tax shelters the investors were buying a legal opinion rather than any real economic resource. Practitioners who publicly and formally advise taxpayers to take positions to which they are not legally entitled do the system considerable harm by their own actions. If the practitioner's conduct does independent harm, it is difficult to see why it should be immune from penalty.

Disbarment sometimes may be appropriate, but since that remedy is so severe, it is unlikely to be invoked in many cases, if ever. Monetary penalties, perhaps on a three-tier structure like those that the Stark Task Force would make applicable to a taxpayer, would be more effective to cover the breaches that are less serious than a felony.

Reliance on a practitioner often is a defense against penalties for the taxpayer. If a taxpayer has a formal written opinion from a practitioner or authority absorbing responsibility, to whom all facts had accurately been revealed, that the position was an as-likely-as-not-to-prevail position, the taxpayer should not be penalized even if the position did not prevail. Where that defense is successfully invoked, it would be rational to shift penalties from the taxpayer and onto the practitioner. The practitioner and client, who act as a single bound unit of agent and principal, should not be able to bootstrap on each other to make penalties disappear. Under normal legal damage principles, moreover, a practitioner who is responsible for harm to the government because of his breach of a legal duty would be responsible for the foreseeable harm that his breach causes. Too many formal opinions are rendered with the practitioner confident that there is no risk or penalty for being too optimistic about the client's position. Again, a monetary remedy would be warranted.

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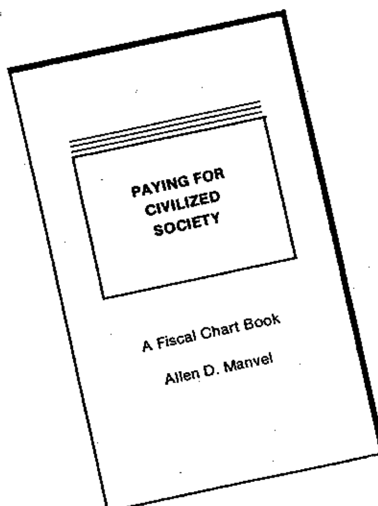

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GAO REPORTS

IRS EXPANSION OF ELECTRONIC FILING SYSTEM NEEDS FURTHER REVIEW, GAO SAYS. The IRS electronic filing system is in need of a significant review before it can proceed with proposed expansions, says a May 5 General Accounting Office (GAO) study (GAO/IMTEC-89-33). Because the Service believes that electronic filing saves significant amounts of time and money, they are anxious to increase the number of electronically filed returns well beyond the 583,000 returns processed in 1988. Yet their system has been plagued by major technical problems. These problems, according to the GAO report, have been exacerbated by the IRS' failure to "define critical performance requirements for the software" and by the insufficient amount of time that has been allotted to quality assurance testing.

The Service has proposed improving and expanding the current electronic filing system, so as to handle a projected 1997 volume of 36 million returns; yet the current system was initially adopted only as a two-year interim measure. The GAO expressed concern over this, and said that the Service "will not know whether the current system being proposed by the electronic filing project office is the best approach for accommodating expansion until it clearly defines system requirements and evaluates the costs, benefits, and technical feasibility of other approaches."

Full Text Citations: AccServ & Microfiche: *Doc 89-4837*

GAO RECOMMENDS IMPROVEMENTS IN UNEMPLOYMENT INSURANCE TAX COLLECTION. The General Accounting Office (GAO), in a study of the tax collection process for the unemployment insurance (UI) system, has concluded that delinquency and debt write-offs have been on the rise recently and that increased Federal assistance could help change this. The GAO report, Unemployment Insurance—Opportunities to Strengthen Tax Collections" (GAO/HRD-89-5), argues that better "oversight and guidance" are necessary by the Department of Labor to effectively monitor and improve the UI collection systems.

Delinquency increased to over $1.3 billion by September 1987, a figure, the report notes, that is 60 percent above the $830 million delinquency of three years earlier. Present state monitoring by the Department of Labor is too limited, the GAO argues, and improvements could increase its ability to provide guidance as well as its potential to find violators. Labor should create state guidelines for "establishing court and administrative procedures" and for "systematically reviewing state UI legislative proposals." Furthermore, the GAO recommends that Labor designate an organization to oversee collection techniques and that it establish a national program to identify employers who should pay UI tax. These national systems should have primary responsibility for overseeing state programs, with only secondary help from the less effective state single audit results.

Full Text Citations: AccServ & Microfiche: *Doc 89-4699*

GAO REPORTS DECLINE IN SINGLE PREMIUM LIFE INSURANCE CONTRACTS. The General Accounting Office (GAO) has issued an interim report on the economic consequences of the tax treatment of life insurance contracts designed primarily for investment. Congress intended the Tax Reform Act of 1986 to limit the tax advantages of such insurance contracts. The interim report suggests that single premium life insurance policies, which increased relative to both total disposable personal income and to all other life insurance from 1980 to 1987, suffered a sharp decline starting in March 1987, and continuing through 1988.

Jennie S. Stathis, Director of Tax Policy at GAO, stated that she had met with staff from the House Ways and Means Committee and the Joint Committee on Taxation and they all agreed that 1988 data on ordinary life insurance and annuity sales and early 1989 data on single premium life insurance were required before reasonable conclusions could be drawn. This data should be available within a few months, Stathis said.

Full Text Citations: AccServ & Microfiche: *Doc 89-4729*; Electronic: *89 TNT 124-9*

CONGRESSIONAL HEARINGS

RIEGLE ANNOUNCES HEARING ON THE UNINSURED. Senate Finance Committee member Donald W. Riegle, Jr., D-Mich., announced on June 9, that the Subcommittee on Health for Families and the Uninsured will hold a hearing on June 19, to consider proposals to provide universal access to health care. The hearing will be at 10:00 a.m. in Room SD-215 of the Dirksen Senate Office Building.

"I've called this hearing to focus on developing a solution that will provide universal access to health insurance for all Americans," said Riegle in a press release. "Today we have about 37 million persons in this country with no health insurance; tragically, 12 million of these are children, the most vulnerable of our society," he added. "High quality, affordable health care should be available for all Americans and their families," Riegle said, adding that "one of my priorities is to see that all Americans have access to health care when they need it."

Full Text Citations: AccServ & Microfiche: *Doc 89-4831*