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THE PRIVACY ACT OF 1974: ITS IMPACT ON  
TAXPAYERS AND THE INTERNAL REVENUE SERVICE

Introduction

Taxpayers, their lawyers and accountants found a new half-page of verbage with the heading "Privacy Act Notification" when they came to prepare their Form 1040s this year. The Privacy Act Notification was but one of a host of changes which the Privacy Act of 1974<sup>1/</sup> brought to the collection, maintenance and use of taxpayer information.

Before turning to a detailed analysis of the origins and impact of the Privacy Act on taxpayers and the IRS, it is useful to dwell briefly on the development of Congressional policy towards the disclosure of taxpayer information.

Developing Congressional Policies on  
Disclosure of Taxpayer Information  
before Passage of the Privacy Act

1789-1946

From the very beginning of our republic, Congress has debated and enacted legislation affecting the disclosure of information collected by government agencies and departments, including the tax collection authorities.

In 1789, the head of each department of the federal government was authorized to prescribe regulations dealing with the "custody, use and preservation of the records, papers and property appertaining to it."<sup>2/</sup> There is little evidence over the next 100 years of the extent to which the so-called "housekeeping" provision of 1789 affected the disclosure or non-disclosure of information falling under the control of federal tax collection agencies.

In 1870, however, Congress specifically denied tax collectors the right to publish tax returns.<sup>3/</sup> Then, under the Income Tax Act of 1894, the Congress went a step further and established penalties for the disclosure of income tax return information. The Tariff Act of 1909 briefly opened corporate tax records to the public, but the next year, the Appropriations Act of 1910 restricted this disclosure policy by requiring that corporate returns not be available for public scrutiny unless the President or the Secretary of the Treasury so provided.

The secrecy of tax records was debated by the Congress regularly from 1913 to 1924, with the secrecy of tax records generally maintained.

A shift in this policy occurred upon passage of the Revenue Act of 1924, which provided for public listing of taxpayers and their incomes. The negative reaction to this reversal in

policy was swift, and in 1926, the publication of taxpayers and their incomes was prohibited by Section 257 of the Revenue Act of that year.

Herbert Hoover, in an Executive Order issued in 1931, for the first time authorized disclosure of individual income tax returns to state tax officials. In 1935, the Congress limited such disclosures by making them solely for the purpose of state or local tax purposes. At this time, Congress also repealed its 1934 "pink slip" provision which would have authorized disclosure of individual income tax information at the discretion of tax collectors.

Section 55 of the Internal Revenue Code, adopted by the Congress in 1939 (carried forward as section 7213 of the Internal Revenue Code of 1954, as amended), provided for criminal penalties to be levied against state or federal officials guilty of unauthorized disclosure of federal income tax data.

#### The Administrative Procedure Act of 1946

The Administrative Procedure Act of 1946,<sup>4/</sup> in its Section 3, reflected a significant attempt to make governmental records more available to the public. The section reflects the philosophy that governmental operations and procedures should not be hidden from public view where there is no substantial reason for

non-disclosure. Section 3 also contained, however, sufficient loopholes to permit non-disclosure where there was involved "any function of the United States requiring secrecy in the public interest" or where there were records "required for good cause to be held confidential." In 1958, these loopholes resulted in the Congress passing the Moss-Hennings Amendment to the 1789 "house-keeping" provision. The amendment stated: "This section does not authorize withholding information from the public or limiting the availability of records to the public."<sup>5/</sup>

#### The Freedom of Information Act of 1966

Since even this amendment resulted in no fundamental shift in opening general government records, including tax records, to public view, the Congress after extensive debate passed the Freedom of Information Act of 1966.<sup>6/</sup> The Freedom of Information Act established that disclosure of information held by the government would be the general rule not the exception, and that all individuals would have equal right to access to such information. The structure of the Freedom of Information Act made it a "disclosure law" not a "withholding statute." For the first time, the act required agencies of the federal government to publish in the Federal Register statements of policy and interpretations, administrative staff manuals and instructions to staff that affect

members of the public, except where such materials were promptly published and offered for sale to the public.

The disclosure policy of the Freedom of Information Act did not reverse the historical policy of maintaining the secrecy of tax records, however. The act included a section authorizing the non-disclosure of information which would otherwise be a "clearly unwarranted invasion of personal privacy." Further, the act did not reverse the effects of other federal statutes specifically forbidding the disclosure of various categories of governmental information.

If one looks back at the history of our country's policy towards the disclosure or non-disclosure of governmental information generally, and taxpayer-related information specifically, it can be seen that the clear thrust has been towards non-disclosure. The Freedom of Information Act of 1966 reflected a sharp turn towards disclosing broad categories of information concerning government agencies and departments, and their conduct of the public's business, but taxpayer privacy was not thereby eroded.

It was in this historical context that other developments in the 1960's and early 1970's brought about the climate leading to the passage of the Privacy Act of 1974.

## The Privacy Act of 1974

### Origins

Increasing computerization of government records and files during the decade of the 1960's, coupled with the Watergate revelations of abuses by the IRS and other agencies, combined to set the stage for passage of the Privacy Act.

By 1974, the politically conservative Liberty Lobby was telling the Congress, "The IRS is not only the tax collector, but also the Eye of Big Brother; it is the American Gestapo . . ."<sup>7/</sup> President Ford was noting, "What a person earns . . . is his own personal business and should not be spread around without his consent."<sup>8/</sup> Senator Charles H. Percy (R. Ill.), a co-sponsor with Senator Sam Ervin (D. N.C.) of much privacy legislation, jumped on the bandwagon, "What about malicious, politically-motivated invasion of privacy? One of the most insidious abuses is attempted use of Internal Revenue Service data for political purposes."<sup>9/</sup>

Thus, in retrospect, passage of the Privacy Act can be attributed in part to computer salesmen, for the great headway which they made in selling their wares to the federal government, and in part to former President Richard M. Nixon, whose IRS "enemies list" politically catalyzed Congressional liberals, moderates and conservatives to enact privacy legislation.

Publication of IRS File Systems Relating to Individuals

The Privacy Act was passed by the Congress on December 31, 1974, and became effective on September 27, 1975. Prior to the effective date, the act provided that every federal agency, including the IRS, publish in the Federal Register a list of each "system of records" under its control from which information can be retrieved by the name of an individual or by some other identifier assigned to an individual (such as their social security number).<sup>10/</sup> Thus, on August 26, 1975, the Department of the Treasury on behalf of the IRS published in the Federal Register notice of the existence of over 200 separate IRS systems of records falling within the definition of the act.<sup>11/</sup> In all, 8,000 separate systems of records containing files on millions of individuals were identified by federal agencies.<sup>12/</sup>

According to the IRS, it maintained files on individuals in the following categories: Public Affairs; Accounts, Collection and Taxpayer Service Accounts and Data Processing; Collection; Administration; Fiscal Management; Facilities Management; Personnel; Audit; Appellate; Intelligence; Office of International Relations; Inspection; Planning and Research; Technical; Office of Chief Counsel; as well as a catch-all category entitled "General Items Not Otherwise Numbered."

Typical of the specific systems of records within these categories are: System 22.011, Card Index File of Erroneous Refunds; System 22.055, Tax Practitioner, Extension-of-Time Card File; System 42.012, Tax Shelter Program File; System 46.005, Electronic Surveillance File; System 60.002, Bribery Investigation File.

In a triumph of bureaucratic euphemism, the infamous IRS "enemies list," which helped prompt passage of this kind of legislation, became soothingly metamorphosed into System 26.023, Defunct Special Service Staff File Being Retained Because of Congressional Directive.

As to each of these systems of records, there was disclosed in accordance with the act: the name and location of the system; the categories of individuals on whom records are maintained in the system; the categories of records in the system, the routine uses of the records contained in the system, including the categories of users and the purpose of such use; the policies and practices of the IRS recording storage, retrievability, access, controls, retention and disposal of records; the title and business address of the IRS official responsible for the system, the procedures by which an individual can obtain notice if the system of records contains information pertaining to him; and the



procedures by which an individual can obtain access to and contest the content of a record in the system.<sup>13/</sup>

Standards Imposed on Collecting Information Concerning Taxpayers

The act also codifies standards concerning the collection, maintenance and use of taxpayer information. To the extent it did not before, the IRS now is to maintain only such information about an individual as is relevant and necessary to accomplish the purpose for collecting the information established by statute or executive order.<sup>14/</sup> The IRS also must now maintain all records with such accuracy, relevance, timeliness and completeness as may be necessary to insure fairness to the individual.<sup>15/</sup>

Further, the obligation was imposed upon the IRS to inform every individual whom it asks to supply information of the authority which authorizes the solicitation, the principal purpose for which the information is intended to be used, the routine uses to be made of the information and the effects on the individual, if any, of not providing all or any part of the requested information.<sup>16/</sup> Thus, it was that Form 1040 came to have its second page taken up with the "Privacy Act Notification."

Those who took the trouble to read the notice discovered, hardly to their surprise, that the principal purpose for soliciting tax return information is to administer the Internal Revenue

laws of the United States. They also learned that the Internal Revenue Code provides penalties for: failure to file a return; failure to supply information required by law or regulations; failure to furnish specific information required on return forms; or for furnishing fraudulent information. Routine uses of tax return information were specified as including disclosures: to the Department of Justice in connection with actual or potential criminal prosecution or civil litigation; to other federal agencies; to states, the District of Columbia, the Commonwealth of Puerto Rico or possessions of the United States to assist in the administration of their tax laws; to other persons in accordance with and to the extent permitted by law and regulations; and to foreign governments in accordance with treaties with the United States.

#### Disclosure of Information on Individual Taxpayers

With certain limited exceptions, the act prohibits the IRS from disclosing information concerning individuals to any outside party without that individual's consent.<sup>17/</sup> The major exceptions include: disclosures which are compatible with the purpose for which the information was collected; disclosures for statistical research which do not involve identification of the individual involved; disclosures to the National Archives; disclosures to other agencies or state and local tax authorities for civil or

criminal law enforcement activity; and disclosures pursuant to court order.

Also, the IRS is now under an obligation to keep an accurate accounting of the date, nature and purpose of each disclosure of a record made to another agency and, except where civil or criminal prosecutions are involved, the IRS must make this accounting available to the individual upon his request.<sup>18/</sup>

The Privacy Protection Study Commission and Federal Tax Return Confidentiality

The act also established a Privacy Protection Study Commission with seven members. The Commission was authorized and directed to report to the President and Congress at a later date "whether the Internal Revenue Service should be prohibited from transferring individually identifiable data to other agencies and to agencies of State Governments."<sup>19/</sup> Thus, the act at least opened the door for limiting even further presently permissible disclosures.

The Commission published draft recommendations in this area on February 8, 1976. The recommendations, if enacted into law, would prohibit disclosure of tax return information without the prior written consent of the individual taxpayer involved, except for disclosures made:

estates. Finally, the American Bar Association suggested that tax returns not be made available to the Department of Justice or other federal agencies for non-tax investigations, notwithstanding the fact that a judicial warrant might otherwise issue for the returns.

A decision from the Commission on its final recommendations is not expected until sometime this summer.

New Rights for Individual Taxpayers to Examine and Amend Information Concerning Them

Under the Privacy Act, individuals now have the right to request access to records pertaining to them. They have the right to review the records, have copies made, and they also have the right to request correction of records which they believe are inaccurate, irrelevant, untimely or incomplete.<sup>20/</sup> If such a correction is refused, reasons must be given,<sup>21/</sup> and the individual has the right to request an internal review of such refusal.<sup>22/</sup>

If an individual taxpayer still is unsatisfied, he has the right to bring a civil action in a United States District Court to seek an order directing the IRS to amend the record.<sup>23/</sup> Should the taxpayer prevail, he will be entitled to recover the costs of the court action, attorneys' fees and not less than \$1,000 in actual damages.

Detailed rules and regulations governing the procedures by which individual taxpayers may assert their rights under the Privacy Act have been published in the Federal Register and are now a part of the Code of Federal Regulations.<sup>24/</sup>

#### New Forms

Generally, where there is a new act affecting a federal agency, there are new forms. The Privacy Act is no exception to this rule. Individual taxpayers wishing to assert their rights under the act can do so by filling out the new Form 5394, Request for Notification and Access--Systems of Records.

#### Exemptions to File Access by Individuals: No Hope for the Mafia

The right of individual taxpayers to have access to and amend portions of systems of records containing information concerning them is limited by the act's provision for exempt systems of records. Among the exempted systems are those pertaining to the enforcement of criminal laws or record systems otherwise containing investigative material compiled for law enforcement purposes.<sup>25/</sup>

Thus, Mafia members wondering if the feds are on to them need not bother trying to gain access to files such as System

42.009, Strike Force (Exempt). Other exempt record systems are so specified in the Federal Register:

The Privacy Act: How  
Much of a Real Difference

It is still too early to determine the long-term effect of the changes wrought by the Privacy Act of 1974. The IRS and other federal agencies have been forced to look within their own houses and place on the public record evidence of the files they maintain on individual Americans. Those individuals, in turn, now have the right to examine much of this information and correct it where it proves inaccurate. How many individuals will actually avail themselves of their new rights in the years ahead is hard to tell, although to date there has certainly been no stampede by citizens for access to IRS records that pertain to them.

With the increasing complexity of our society and our government, citizens' concerns over the files the government maintains on them has grown. The Privacy Act has been burdensome for federal bureaucracies, including the IRS. They have had to examine their operations and devise new procedures in order to comply with the Privacy Act. However, this burden seems minor when balanced against the fact that individuals now can find out what the government knows about them and can complain and correct inaccurate

information. Further, the Privacy Act means that "enemies lists" are out and civil and criminal remedies have been established to insure this remains the case.

The English writer George Orwell foresaw that advances in technology could give Uncle Sam a descendant named Big Brother. Big Brother, as Orwell envisioned in his novel 1984, would be in a position to stifle individuality and dominate the lives and thoughts of citizens in our post-industrial society. At the very least, passage of the Privacy Act of 1974 has helped push the 1984 timetable back a bit.

## F O O T N O T E S

1. P.L. 93-579, 5 U.S.C. §552(a)-(q).
2. 5 U.S.C. §22 (1789).
3. For a fuller description of the history of disclosure policies 1870-1935, see "Disclosure History," Midwest Revenews, October/November 1975, pages 3-4.
4. 5 U.S.C. §1002 (1946).
5. PL 85-618 (1958). The statute as it presently exists is now codified as 5 U.S.C. §301.
6. 5 U.S.C. §552.
7. Joint hearings before the Ad Hoc Subcommittee on Privacy and Information Systems of the Committee on Government Operations and the Subcommittee on Constitutional Rights of the Committee on the Judiciary, United States Senate, 93rd Congress, 2nd Session, June 18, 19 and 20, 1974, Part I, page 184.
8. Id., Part II, page 1811.
9. Id., Part II, page 1636.
10. 5 U.S.C. §552(e)(4).
11. Federal Register, Vol. 40, No. 166, pages 37,681-37,765, August 26, 1975.
12. Speech by David F. Linowes, Chairman, Privacy Protection Study Commission, November 18, 1975.
13. 5 U.S.C. §552(e)(4)(A)-(I).
14. 5 U.S.C. §552(e)(1).
15. 5 U.S.C. §552(e)(5).
16. 5 U.S.C. §552(e)(3)(A)-(D).



17. 5 U.S.C. §552(b)(1)-(11).
18. 5 U.S.C. §552(c).
19. P.L. 93-579, Privacy Act of 1974, §5(c)(2)(B)(ii).
20. 5 U.S.C. §552(d)(2)(B)(i).
21. 5 U.S.C. §552(d)(2)(B)(ii).
22. 5 U.S.C. §552(d)(3).
23. 5 U.S.C. §552(g).
24. Federal Register, Vol. 40, pages 45,684-45,692, October 2, 1975; Code of Federal Regulations, Title 31, Subtitle A, Part I, Subpart C.
25. 5 U.S.C. §552(j), (k).