K. DISCLOSURE OF TAX RETURN INFORMATION

by
Terrell Berkovsky and David Flavin

1. Introduction

The purpose of this discussion is to provide an awareness to exempt organization specialists of the background and law governing the availability of exempt organization information to the public. Although, for the most part, the actual administration of the various provisions governing disclosure is ultimately under the jurisdiction of the Office of Disclosure and the Assistant Chief Counsel (Disclosure Litigation), exempt organization personnel should be aware of the information that may be available to taxpayers. Having an understanding of what might be available to taxpayers can be useful in processing cases. It is also helpful in that, from time to time, exempt organization personnel may be asked for their recommendation as to the availability of particular documents.

The Freedom of Information Act, 5 U.S.C. 552, generally provides that any person has a right, enforceable in court, of access to federal agency records, except to the extent that such records (or portions thereof) are protected from disclosure by one of nine exemptions or by one of three special law enforcement record exclusions. In addition to the Freedom of Information Act, several sections of the Internal Revenue Code govern public disclosure of exempt organizations information. IRC 6103 generally provides for the confidentiality of tax returns and return information. IRC 6104 specifies rules concerning public disclosure of exemption applications, supporting documents, and annual returns. IRC 6110 provides for the disclosure of certain written determination letters, rulings, and technical advice memorandums.

2. Exceptions to the Confidentiality Rules Under IRC 6103

Unless otherwise specifically authorized, tax returns and return information may not be disclosed by individuals who have access to them. IRC 6103 defines the terms "tax return" and "return information" very broadly to include just about everything concerned with an individual's or organization's reporting and paying of federal taxes. However, "tax returns" and "return information" may be disclosed under limited circumstances. The most commonly encountered authorized disclosures in the exempt organizations area are: (See IRC 6103(c) through 6103(o))

1. A taxpayer's representative or designee, who holds a written power of attorney to represent the taxpayer on a specific matter, or written authorization to receive information, respectively, may have access to the returns or return information that relates to the matter at issue.

2. An agent of a state body may inspect tax returns in connection with the official administration of the state tax laws. This agent must hold written authorization from the interested state body.

3. Persons having a material interest in a tax matter may be provided with related tax information. This might include a spouse in the case of a jointly filed return, partner, trustee, executor, or administrator of an estate.

4. Disclosure may be made to certain congressional committees. The chairpersons of the House Ways and Means Committee, Senate Finance Committee, and the Joint Committee on Taxation may request and receive tax returns and tax return information.

5. The President may receive tax information in response to a written request. This applies to White House Employees and agency heads who are designated in the President's request. A report of these requests must be made by the Service to the Joint Committee on Taxation.

6. Officers and employees of a federal agency may receive tax returns to enforce a federal criminal statute, if the request is ordered by a federal district court judge.

7. The Service may release return information in a general non-identifying form to the Department of Commerce, the Federal Trade commission, and the Department of Treasury for use in making statistical compilations.

Any officer or employee of the United States who makes an improper disclosure of a tax return or return information (defined in IRC 6103(b)) may be guilty of a felony, punishable by a fine of up to $5,000 or imprisonment for 5 years, or both.

Chapter (49)00 of the Exempt Organizations Handbook (IRM 7751) provides further discussion of the provision of the law governing confidentiality of tax information under IRC 6103.

3. Disclosure under IRC 6104

IRC 6104(a) provides for public inspection of approved applications for recognition of exemption (Form 1023 and Form 1024 and supporting documents) and IRC 6104(b) provides for public inspection of exempt organization information returns (Forms 990, 990EZ, and 990PF). These disclosure requirements apply only to organizations determined to be exempt from tax. Applications under consideration by the Service or which have been denied are not subject to disclosure under IRC 6104(a). These disclosure requirements also apply to rulings, determination letters, and technical advice memorandums relating to approved exemption applications. When an organization's exemption has been revoked, the application is no longer subject to public inspection unless the organization continues to be recognized as exempt for some prior period.

Form 4720, Return of Certain Excise Taxes on Charities and Other Persons under Chapters 41 and 42 of the Internal Revenue Code, is disclosable unless filed by a disqualified person as defined in IRC 4946(a). The Service is required to disclose this information upon proper application and private foundations are required to disclose their annual returns, by publishing a notice of their availability in a newspaper serving the area where the principal office is located.

IRC 6104(c) provides for notifying appropriate State officials of certain determinations made by the Service under IRC 501(c)(3), including denials, failures to establish, and revocations. It also describes the State officials who are entitled to notification and to the inspection of various returns and other documents.

IRC 6104(d) places certain limitations on the material that may be disclosed. The organization may request that information relating to any trade secret, patent, process, style of work, or apparatus of the organization be withheld from disclosure. If the Commissioner determines that disclosure of such information would adversely affect the organization, it will be withheld from the public inspection file. This is also true of information that the Commissioner determines would adversely affect the National defense. Also, the names of contributors to public charities are withheld from public inspection. The amount of contributions is open to the public unless disclosure can identify any contributor.

IRC 6104(e)(1) provides for all organizations described in IRC 501(c) and (d) and exempt from taxation under IRC 501(a) that are not private foundations to make copies of their annual returns (Forms 990 and 990EZ) available for public inspection for a three-year period beginning on the date the return is due. The returns shall be made available for inspection during regular business hours by any

individual at the principal office of the organization and, if the organization maintains regional or district offices having 3 or more employees, the returns shall be made available also at such regional or district office.

IRC 6104(e)(2) requires all organizations exempt from taxation under IRC 501(a) that filed an exemption application, to make a copy of the application for recognition of exemption together with a copy of any papers submitted in support of such application and any letter(s) or other document(s) issued by the Service with respect to such application, available for inspection during regular business hours at the principal office or at such regional or district offices as applicable. IRC 6652(c)(1) provides that persons who fail to meet the requirements relating to public inspection of returns and applications must pay a penalty of $10 per day as long as the failure continues.

Chapters (49)00 and (50)00 of the Exempt Organizations Handbook (IRM 7751) provide further discussion of the provision of law governing disclosure of tax information under IRC 6104. Chapter 900, Exempt Organizations, of the Disclosure of Official Information Handbook (IRM 1272) provides the rules and procedures for disclosing material under IRC 6104. Notice 88-120, 1988-2 C.B. 454, specifies what an exempt organization, other than a private foundation, must allow to be inspected under the provisions of IRC 6104(e)(1).

4. Disclosure under IRC 6110

A. Public Inspection of Written Determinations:

IRC 6110 provides for the disclosure of the reasoning and legal discussion in private letter rulings to the public. Letter rulings, written determinations, and technical advice memoranda issued by the National Office are made available by the National Office Freedom of Information Reading Room upon specific requests. Determination letters issued by districts are made available to the public in regional reading rooms.

Rulings, determination letters, and technical advice memoranda involving the following are subject to the provision of IRC 6110:

1. Applicability of Chapter 42 provisions;

2. Applicability of the unrelated business income tax provisions of IRC 511 through 515;

3. Applicability of IRC 527(f) regarding political activity of IRC 501(c) organizations;

4. IRC 509(a) status of nonexempt charitable trusts;

5. IRC 6033 regarding filing requirements;

6. Lobbying provisions of IRC 4911 and 501(h);

7. Qualification of prepaid legal plans under IRC 120.

B. Support of Deletions

Rev. Proc. 92-4, 1992-1 I.R.B. 66, explains what a taxpayer is required to submit when requesting written guidance from the Assistant Commissioner (Employee Plans and Exempt Organizations). Rev. Proc. 92-5, 1992-1 I.R.B. 90, explains what statements are required to identify the information to be deleted from public inspection with regard to technical advice requests under the jurisdiction of the Assistant Commissioner (Employee Plans and Exempt Organizations). Ruling requests, determination requests, and requests for technical advice that are subject to the provisions of IRC 6110 must include the following special submissions:

1. A copy of the request and supporting documents on which are indicated, in brackets, those portions the taxpayer suggests be deleted in accordance with IRC 6110(c). In lieu of these copies, a statement may be submitted indicating that no deletions need be made except names, addresses, and taxpayer identifying numbers.

2. A statement in support of the deletions suggested, indicating which specific exemption provided by IRC 6110(c) applies to each bracketed portion.

3. For rulings and determinations and any additional facts submitted by the taxpayer, a "penalties of perjury" declaration, signed by the taxpayer.

The types of information that must be deleted before the text of any written document is open to public inspection are described in Reg. 301.6110-3. The basic deleted information includes:

1. Identifying details (names, addresses, identifying numbers, etc.);

2. National defense and foreign policy information;

3. Information exempted by other statutes and agency rules;

4. Trade secrets and privileged or confidential commercial or financial information;

5. Information within the ambit of personal privacy;

6. Information concerning agency regulation of financial institutions; and

7. Geological information concerning wells.

C. Determinations That Include IRC 6110 and 6104 Issues:

Some determinations may include issues that are subject to the provisions of IRC 6110 and the provisions of IRC 6104. For example, a technical advice request may have an exemption issue and an unrelated business income issue. Whenever possible the issues should be segregated so that one determination can be written on the issues subject to IRC 6110 and another determination written on issues subject to IRC 6104. If it is not possible to segregate the issues, preparation and issuance of the document should be handled as though the entire determination were subject to IRC 6110.

An initial application involving a determination under IRC 501(c)(3) and advance approval of grant making procedures under IRC 4945(g) is not treated as subject to the provisions of IRC 6110. In this situation, IRC 6104 will apply to such a request.

D. Third Party Contact:

A record must be made of any communication (whether written, by telephone, at a meeting, or otherwise) received by the Service prior to the issuance of a written determination, from any person other than the person to whom the determination pertains or such person's authorized representative. A notation of such communication must be placed on the determination when it is released to the public. The notation will consist of the date of the communication and the category of person making the communication, such as: Congressional, White House. The "Third Party Contacts" and the "Uniform Issue Numbers" should be placed on the top left side of the ruling letter and be included on all copies, including the deleted copy.

IRM 7(16)00 and Section 5.1 of the Exempt Organizations Technical Division Operating Procedures provide guidance on the preparation of section 6110 written determinations. Chapters 800 and 900 of the Disclosure of Official Information Handbook (IRM 1272) further explain the rules and procedures for disclosure of written determinations. "Uniform Issue Numbers" are in the Office of Chief Counsel, Uniform Issue List, IRS Publication 1102.

5. Freedom of Information Act

A. Exemptions from Disclosure

The Freedom of Information Act, 5 U.S.C. 552, is an independent disclosure statute. While IRC 6103, 6104, and 6110 relate only to tax information, the FOIA is applicable to all departments, agencies, and commissions in the federal government. It creates a right, beyond other disclosure provisions, to obtain information about government actions. The basic purpose of the FOIA is to ensure an informed citizenry. The Supreme Court emphasized that "official information that sheds light on an agency's performance of its statutory duties falls squarely within that statutory purpose." Department of Justice v. Reporters Comm. for Freedom of the Press, 489 U.S. 749, 773 (1989). Under the structure of the FOIA, virtually every record possessed by a federal agency must be made available to the public in one form or another, unless it is specifically exempted from disclosure or specifically excluded from the Act's coverage.

The nine exemptions of the FOIA ordinarily provide the only basis for nondisclosure and are discretionary, not mandatory. (See 5 U.S.C. 552(b).) In other words, unless disclosure is prohibited by IRC 6103 or 6104, or other qualifying statute, the government is not required to invoke an exemption to deny access to a document. The current Service policy is to claim an exemption only if it can be demonstrated that disclosure will result in a significant harm to tax administration. Dissatisfied record requesters are given a remedy in the U.S. district courts, where the government bears the burden of sustaining its nondisclosure actions.

Under the FOIA structure two categories of information must automatically be disclosed. Subsection (a)(1) of the FOIA requires publication in the Federal Register of information such as descriptions of agency organization, functions, procedures, substantive rules and statements of general policy. (5 U.S.C. 552(a)(1).) Subsection (a)(2) requires that materials such as final opinions rendered in the adjudication of cases, specific policy statements, and certain administrative staff manuals routinely be made available for public inspection and copying. (5

U.S.C. 552(a)(2)). Generally, this means having the IRM and other publications available in a public reading room. These records are commonly referred to as "reading room" materials and serve to guard against the development of agency secret law known to agency personnel but not to members of the public who deal with agencies.

Under subsection 5 U.S.C. 552(a)(3), unless otherwise exempted or excluded, all records are subject to disclosure upon an agency's receipt of a proper access request from any person. "Any person" as defined in 5 U.S.C. 551(2) encompasses individuals (including foreign citizens), partnerships, corporations, associations and foreign or domestic governments. FOIA requests can be made for any reason, with no showing of relevancy required. As such, the FOIA has been invoked successfully as a substitute for or supplement to discovery in both civil, Jackson v. First Fed. Sav., 709 F. Supp. 887, 889 (E.D. Ark. 1989), and criminal, North v. Walsh, 881 F.2d 1088, 1096 (D.C. Cir. 1989), litigation contexts.

The FOIA specifies only two requirements for access requests: that they "reasonably describe" the records sought, and that they be made in accordance with agencies' published procedural regulations. The standard is that a professional agency employee familiar with the subject areas be able to locate the record with a "reasonable amount of effort." However, an agency "must be careful not to read the request so strictly that the requester is denied information the agency well knows exists in its files, albeit in a different form from that anticipated by the requester." Hemenway v. Hughes, 601 F. Supp. 1002, 1005 (D.D.C. 1985).

The Supreme Court has articulated a basic, two-part test for determining what constitutes an "agency record" under the FOIA: "Agency records" are documents which must be (1) either created or obtained by an agency, and (2) under agency control at the time of the FOIA requests. Department of Justice v. Tax Analysts, 492 U.S. 136, 144-45 (1989). Certain records maintained by agency employees may qualify as "personal" rather than "agency" records. In Sibille v. Federal Reserve Bank of New York, Civil No. 90-5898, slip op. at 11 (S.D.N.Y. July 9, 1991), the court found that handwritten notes of meetings and telephone conversations taken by employees for their personal convenience and not placed in agency's files were not "agency records". Also American Fed'n of Gov't Employees v. Department of Commerce, 632 F. Supp. 1272, 1277 (D.D.C. 1986), aff'd., 907 F.2d 203 (D.C. Cir. 1990), held that employee logs created voluntarily to facilitate work were not to be "agency records" even though containing substantive information.

An agency in receipt of a proper FOIA request is required to inform the requester of its decision to grant or deny access to the requested records within ten working days from the date of the request. The FOIA provides for extensions of such time limits for several specific situations: (1) the need to search for and collect records from a separate office; (2) the need to examine a voluminous amount of records required by the request; and (3) the need to consult with another agency or agency component. A requester must file a written appeal with the Commissioner of Internal Revenue within 35 days after (1) the date of a determination to withhold records or, (2) if some records are released at a later date, the date the last records were released. If the request for records is denied on appeal, or if the requester does not receive a timely response, a complaint may be filed in an appropriate U.S. District Court.

The FOIA requires that "any reasonably segregable portion of a record" must be released after appropriate application of the nine exemptions. (5 U.S.C. 552(b).) Where nonexempt material is so "inextricably intertwined" that disclosure of it would "leave only essentially meaningless words and phrases", the entire record can be withheld. Neufeld v. IRS, 646 F.2d 661, 663 (D.C. Cir. 1981). The agency, not the requester, has the right to choose the format of disclosure, so long as the agency chooses reasonably under the circumstances presented.

The FOIA provides for nine specific exemptions from disclosure of information. For the purposes of exempt organizations the primary exemptions are: (1) Records, such as tax returns and tax return information, specifically exempted from disclosure by statute other than FOIA, 5 U.S.C. 552(b)(3); (2) Trade secrets and commercial or financial information obtained from a person and considered privileged or confidential, 5 U.S.C. 552(b)(4); (3) inter-agency or intra-agency memorandums or letters which would not be available to a party other than an agency in litigation with the agency, 5 U.S.C. 552(b)(5); and (4) records or information compiled for law enforcement purposes, but only to the extent that the production of such law enforcement records or information could reasonably be expected to interfere with enforcement proceedings, could reasonably be expected to constitute an unwarranted invasion of personal privacy, or could reasonably be expected to disclose the identity of a confidential source, 5 U.S.C. 552(b)(7)(A), (C), or (D).

Exemption (b)(5) protects "inter-agency or intra-agency memorandums or letters which would not be available by law to a party. . . in litigation with the agency." As such, it has been construed to exempt documents normally privileged in the civil discovery context. NLRB v. Sears, Roebuck & Co., 421 U.S. 132, 149

(1975). The three most frequently invoked privileges are the deliberative process privilege (sometimes referred to as "executive privilege"), the attorney work-product privilege, and the attorney-client privilege. The issue remains unsettled as to documents generated in the course of settlement negotiations.

The most commonly invoked privilege is the deliberative process privilege, the general purpose of which is to "prevent injury to the quality of agency decisions." Three policy purposes have been consistently held to constitute the basis for this privilege: (1) to encourage open and frank discussion on matters of policy between subordinates and superiors; (2) to protect against premature disclosure of proposed policies before they are finally adopted; and (3) to protect against public confusion that might result from disclosure of reasons and rationales that were not in fact ultimately the grounds for an agency's action.

There are two fundamental requirements that must be met in order for the deliberative process privilege to be invoked. First, the communication must be predecisional. Second, the communication must be deliberative, i.e., a direct part of the deliberative process in that it makes recommendations or expresses opinions on legal or policy matters. Vaughn v. Rosen, 523 F.2d 1136, 1143-4 (D.C. Cir. 1975). Documents that are commonly encompassed by the deliberative process privilege include advisory opinions, recommendations, and deliberations comprising part of a process by which governmental decisions and policies are formulated, the release of which would be likely to stifle honest and frank communication within the agency. This also includes "briefing materials" that summarize issues and advise superiors, as well as "drafts". The primary limitation on the scope of the deliberative process privilege is that it ordinarily is inapplicable to purely factual matters, or to factual portions of otherwise deliberative memoranda.

Documents generally recognized as part of the deliberative process, include drafts, workpapers, and memos for file. National Office personnel should follow Operating Procedure, Assembly of Case Files, paragraph 3D.6, to purge file folders of all unnecessary documents.

National Office General Counsel Memorandums (GCM's) and Actions on Decisions (AOD's) that relate to IRS cases are not subject to exemption (b)(5). After such documents have been deleted of all taxpayer identifying information, they are made available to the public through the FOIA Reading Room and commercial tax services.

The second traditional privilege incorporated into exemption (b)(5) is the attorney work-product privilege, which protects documents and other memoranda prepared by or under the direction of an attorney in contemplation of litigation. The privilege includes civil proceedings, administrative proceedings, and criminal proceedings. Litigation need never have been actually commenced, so long as specific claims have been identified which make litigation probable. However, the mere possibility that litigation may occur at some unspecified time in the future will not ordinarily be sufficient to protect attorney-generated documents. The attorney work-product privilege also has been held to cover documents "relating to possible settlements" of litigation. (U.S. v. Metropolitan St. Louis Sewer Dist., Civil No 88-543-C, Slip op. at 2-3 (E.D. Mo. Jan. 14, 1992 (appeal pending); Cities Serv. Co. v. FTC, 627 F. Supp. 827, 832 (D.D.C. 1984), aff'd, 778 F.2d 889 (D.C. Cir. 1985).)

The third traditional privilege incorporated into exemption (b)(5) concerns "confidential communications between an attorney and his client relating to a legal matter for which the client has sought professional advice." Unlike the attorney work privilege, the availability of the attorney-client privilege is not limited to the context of litigation. This applies to facts divulged by a client to his attorney and any opinions given by an attorney to his client based upon those facts, as well as communications between attorneys which reflect client-supplied information. In the exempt organizations context, this privilege would include communications to and from Chief Counsel. Such communications may include specific information regarding a taxpayer as well as legal advice based upon such information.

Exemption (b)(7) of the FOIA protects from disclosure "records or information compiled for law enforcement purposes, but only to the extent that the production of such law enforcement records or information (A) could reasonably be expected to interfere with enforcement proceedings, (B) would deprive a person of a right to a fair trial or an impartial adjudication, (C) could reasonably be expected to constitute an unwarranted invasion of personal privacy, (D) could reasonably be expected to disclose the identity of a confidential source, (E) would disclose techniques and procedures for law enforcement investigations or prosecutions, or would disclose guidelines... if such disclosure could reasonably be expected to risk circumvention of law, or (F) could reasonably be expected to endanger the life or physical safety of any individual."

To make a determination under exemption (b)(7)(A), a two-step analysis must be made to determine (1) whether a law enforcement proceeding is pending or prospective and (2) whether release of information about it could reasonably be

expected to cause some articulated harm. Such proceedings include criminal actions, civil actions, and regulatory proceedings. This subpart is used to protect material that is part of an ongoing exam or a pending exam. After any investigation is closed such exemption may be applicable if disclosure could be expected to interfere with a related, pending litigation.

Exemption (b)(7)(C) provides protection for personal information in law enforcement records. This exemption includes withholding information that identifies third parties. To make a determination under this exemption, one must first identify and evaluate the privacy interests implicated in the requested records. Exemption (b)(7)(C) is regularly applied to withholding references to identities of e.g., lower level Service employees, witnesses, individual taxpayers.

Exemption (b)(7)(D) of the FOIA protects against disclosure of information pertaining to confidential sources. This exemption is crucial to ensuring that "confidential sources" are not lost through retaliation against the sources for past disclosure or because the sources fear future disclosure. The term "source" includes a broad variety of individuals and institutions, such as: crime victims, citizens providing unsolicited allegations of misconduct, or citizens who respond to inquiries from law enforcement agencies. The term "confidential" signifies that the information was provided in confidence or in trust, with the assurance that it would not be disclosed to others.

Exemption (b)(7)(E) affords protection to all law enforcement information which would disclose techniques and procedures for law enforcement investigations or prosecutions, or would disclose guidelines for law enforcement investigations or prosecutions if such disclosure could reasonably be expected to risk circumvention of the law. The general requirement for this exemption is that the technique or procedure not be already well known to the public. Non-investigatory law enforcement records, such as the Law Enforcement Manual, to the extent that they can be fairly regarded as reflecting techniques or procedures, and law enforcement guidelines that satisfy the "could reasonably be expected to risk circumvention of law" standard such as tolerances, are entitled to protection under this exemption.

Exemption (b)(7)(F) permits the withholding of information that could "endanger the life or physical safety of law enforcement personnel." 5 U.S.C. 552(b)(7)(F). Courts have applied this protection to withhold the "names and identifying information of federal employees, and third persons who may be unknown" to the requester. (Luther v. IRS, Civil No. 5-86-130, slip op. at 6 (D.

Minn. August 13, 1987). Under this exemption, Courts have also included the identity of informants who have been threatened with harm.

B. Reasonably Segregable Portions

Although portions of some records may be denied, the remaining portions must be released when the meaning will not be distorted by deletion of the denied portions, and when it can be reasonably assumed that a skillful and knowledgeable person could not reconstruct the excised information.

When non-exempt material is so inextricably intertwined that disclosure of it would leave only essentially meaningless words and phrases or where editing required for proper disclosure would be so extensive as to effectively result in the creation of new records, the entire records can be withheld.

Chapter (13)00, Disclosure of Official Information Handbook, IRM 1272, provides a detailed examination of the requirements that must be met before disclosure of records may occur. The annual publication, Freedom of Information Case List is an excellent source of information interpreting the meaning of each exception under the FOIA. Copies may be obtained through the Department of Justice, Office of Policy Development, Office of Information and Privacy.