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Sharing Bank Deposit Information With Other Countries: Should Tax Compliance or Privacy Claims Prevail?

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By Cynthia Blum

A proposed regulation issued as one of the final acts of the Clinton Administration[1] would have required U.S. banks to routinely file with the IRS reports identifying nonresident alien individuals receiving payments of interest and the amount of such interest. U.S. bank deposit interest paid to nonresident aliens is exempt from U.S. tax,[2] and previously only payments to Canadians were required to be reported to the IRS.[3] Intense opposition[4] to this regulation was expressed by bankers[5] and other organizations, such as the Center for

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1. REG-126100-00, RIN 1545-AY62, Notice of Proposed Rulemaking, January 17, 2001.

2. IRC § 871(i)(2)(A). "Deposits" for this purpose include deposits with persons carrying on the banking business, certain deposits with savings and loan associations, as well as amounts held by an insurance company under an agreement to pay interest thereon. IRC § 871(i)(3). In order to qualify for the exemption the interest must not be effectively connected with a U.S. trade or business. Section 871(i)(2)(A). Withholding by the payor under § 1441 is not required. Section 1441(c)(10). A corresponding exemption from § 881 tax and § 1442 withholding applies to deposit interest paid to a foreign corporation. Section 881(d) (exempting any amount described in § 871(i)(2)); § 1442(a) (incorporating the rules of § 1441 and providing that "the references in § 1441(c)(10) to § 871(i)(2) shall be treated as referring to § 871(d)").

3. Generally, a person required to withhold a tax pursuant to § 1441 or 1442 on an amount paid to a nonresident alien individual or a foreign corporation is required to report that payment to the IRS on Form 1042-S. See Treas. Reg. § 1.1461-1(c)(1)(i). Bank deposit interest exempted from tax by § 871(i)(2)(A) or 881(d) is exempted from the information reporting on Form 1042-S. Treas. Reg. §1.1461-1(c)(2)(ii)(A). However, an exception is made for interest paid to an individual who resides in Canada with respect to a deposit maintained at an office within the U.S. Treas. Reg. §1.6049-8(a). See Treas. Reg. § 1.6049-4(b)(5) (Form 1042-S to be transmitted in the manner prescribed by § 1461 and the regulations thereunder); §1.6049-6(e)(4) (copy of 1042-S to be furnished to payee). The general requirement that a payor of interest report the interest to the IRS on Form 1099 is also inapplicable to bank deposit interest paid to a nonresident alien. See infra note 13.

4. See John E. Hembera, Jr., Witnesses Criticize Proposed Regs on Reporting Requirements for Deposit Interest Paid to Nonresident Aliens, 2001 TNT 121-4; Unofficial Transcript of IRS Hearing [June 21, 2001] on Proposed Regs on Reporting Requirements for Deposit Interest Paid to Nonresident Aliens, 2001 TNT 128-18. Present as witnesses were representatives of the Freedom and Prosperity Foundation, the Heritage Foundation, the Credit Union National Association, Institute of International Bankers, Florida Bankers Association, Bank of America, Banco Santander Central Hispano, the South Florida Area First Union Bank and a community bank in Miami.

5. See, e.g., Comment Letter of Patrick M. Frawley, Senior Vice President, Bank of America, Feb. 26, 2001, reprinted at 2001 TNT 162-25; Letter of Christopher L. Williston, President, Independent Bankers Association of Texas, to Paul O'Neill,

Freedom and Prosperity,[6] as well as by Governor Jeb Bush of Florida (where bank deposits are held by many residents of Latin America).[7] This opposition led the Bush Administration to withdraw the proposed regulation but to replace it with a similar proposed regulation applicable only to residents of 16 countries (12 member countries of the European Union, as well as Canada, Australia, New Zealand, and Norway).[8] While the new proposed regulation has also

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August 2, 2001, reprinted at 2001 TNT 159-30; Letter of Ken Guenther, President, Independent Community Bankers of America, to Paul O'Neill, July 30, 2001, reprinted at 2001 TNT 154-27 (negative impact particularly in California, Florida and Texas); Comment Letter of Steve Bartlett, President, The Financial Services Roundable, July 1, 2001, reprinted in 2001 TNT 138-35; Letter of Daniel A. Mica, President, Credit Union National Association, Inc., to Paul O'Neill, July 3, 2001, reprinted at 2001 TNT 134-36; Comment Letter of Mary Mitchell Dunn, Associate General Counsel, Credit Union National Association, Inc., May 31, 2001, reprinted in 2001 TNT 126-26; Comment Letter of Robert I. Gulledge, Chairman, Independent Community Bankers of America, Washington, D.C., May 15, 2001, reprinted in 2001 TNT 106-23; Comment Letter of Mark R. Baran, American Bankers Association, Washington, D.C., Feb. 27, 2001, reprinted at 2001 TNT 60-22; Letter of Lawrence R. Uhlick, Executive Director, Institute of International Bankers, N.Y., May 8, 2001, to Mark A. Weinberger, Assistant Sec'y of the Treasury for Tax Policy, reprinted in 2001 TNT 105-26 (regulation of concern to international banks that operate in the U.S. through branches)

6. Press Release of Center for Freedom and Prosperity, Nov. 6, 2001, reprinted at 2001 TNT 217-31 (39 groups including Heritage Foundation, Cato Institute, and Discovery Institute, oppose regulation). See Robert Goulder, "CFP condemns new U.S. interest reporting regs for nonresident aliens," 2001 TNT 50-6. See also Dan R. Mastromarco and Lawrence A. Hunter, "The 'U.S. Anti-Savings Directive,'" Tax Notes Int'l Magazine, Jan. 13, 2003, p. 159 (also available in 2002 TNT 247-28), detailing arguments against adoption of the regulation; Richard W. Rahn & Veronique de Rugy, "Threats to Financial Privacy and Tax Competition," Cato Institute Policy Analysis No. 491, Oct. 2, 2003, reprinted in 2003 TNT 197-28.

7. Letter of Governor Jeb Bush to Paul O'Neill, June 7, 2001, reprinted in 2001 TNT 120-22. See Letter of Rep. Dave Weldon, R-Fla., Dan Miller, R-Fla, et al, to Paul O'Neill, Feb. 27, 2001, reprinted in 2001 TNT 51-46 (letter signed by 15 members of House of Representatives from Florida); Letter of Miriam Lopez to Paul O'Neill, Oct. 1, 2001, on behalf of Florida International Bankers Association and Florida Bankers Association, reprinted in 2001 TNT 198-36 (Florida "could lose between $18 and $34 billion of NRA deposits"). The IRS also received negative comments on the regulation from a large number of individual banks in Florida. See, e.g., Comment Letter of Manuel Lucena, General Manager, Banco Comercial Portugues, Miami, Feb. 26, 2001, reprinted in 2001 TNT 162-27; Comment Letter of Joseph B. Shearouse, III, Senior Vice President, Fidelity Federal, West Palm Beach, May 30, 2001, reprinted in 2001 TNT 130-20; Comment Letter of Thomas H. Dargan, President, Peninsula Bank, Daytona Beach, May 25, 2001, reprinted in 2001 TNT 130-21.

8. REG-133254-02, RIN 1545-BA86, August 2, 2002. The EU countries are Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, Portugal, Spain, Sweden, and the United Kingdom. As discussed below, three of the current members of the EU were not listed in the regulation: Austria, Belgium, and Luxembourg. The EU will be adding ten new members, i.e., 8 Eastern European countries and Cyprus and Malta, in 2004.

attracted fierce opposition,[9] the Bush Administration has continued to defend it (but has not yet finalized it).[10]

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9. See Chuck Gnaedinger & Sarah Kirkell, "Witnesses Criticize New Proposed Regulations On Reporting Nonresident Aliens' Interest," 2002 TNT 235-1; Unofficial Transcript of IRS Hearing [Dec. 5, 2002] on Proposed Regs on Reporting Nonresident Aliens' Interest, 2002 TNT 241-60 (critical testimony by representatives of Office of Advocacy at the Small Business Administration, Conference of State Bank Supervisors, Small Business Survival Committee, Empower America, Americans for Tax Reform, Institute for International Bankers, Center for Freedom and Prosperity, Citizens for a Sound Economy Foundation, Institute for Research on the Economics of Taxation, Southeastern Legal Foundation, and National Small Business United). In addition, the IRS and Treasury received critical comments on the revised proposed regulation from, inter alia, Rep. Philip M. Crane, R-Ill., see 2002 TNT 191-12, Rep. Mark Foley, R-Fla., see 2002 TNT 193-23, Coalition for Tax Competition, see 2002 TNT 220-18, Rep. Ron Paul, R-Texas, see 2002 TNT 232-27, Rep. Jack Kingston, R-Ga., see 2002 TNT 232-28, Rep. Pete Sessions, R-Texas, see 2002 TNT 232-26, Mark R. Baran, American Bankers Association, see 2002 TNT 232-24, Mary Mitchell Dunn, Senior Vice President, Credit Union National Association, see 2002 TNT 232-23, Daniel J. Mitchell, Heritage Foundation, see 2002 TNT 237-29, Solveig Singleton, Competitive Enterprise Institute, see 2002 TNT 240-27, Robert R. Davis, Managing Director, America's Community Bankers, see 2002 TNT 245-10, Bruce Chapman, President, Discovery Institute, see 2002 TNT 245-8, Sen. Robert Bennett, R-Utah, see 2002 TNT 246-55, Rep. Don A. Manzullo, R-Ill., see 2002 TNT 246-56, Donald G. Ogilvie, President, American Bankers Association, 2002 TNTT 2-6, Rep. Robert Ney, R-Ohio, and sixteen other congressmen, see 2003 TNT 6-38, Alejandro M. Sanchez, Florida Bankers Association, see 2003 TNT 39-180, Rep. Spencer Bachus, R-Ala., see 2003 TNT 43-34, Sen. Mike Crapo, R-Idaho, see 2003 TNT 43-33, Sen. Sam Brownback, R-Kansas, see 2003 TNT 43-32, Sen. John Ensign, R-Nev, see 2003 TNT 46-59, 9 members of Senate Banking committee, see 2003 TNT 49-51, Sen. James M. Inhofe, R-Okla., see 2003 TNT 50-42, Phil Gramm, Vice Chairman UBS AG, see 2003 TNT 50-41, Sen. Conrad Burns, R-Mont., see 2003 TNT 50-39, Governor George Pataki, New York, see 2003 TNT 65-66, Sen. George Allen, R. Va., see 2003 TNT 65-65, Robert L. Livingston, Livingston-Solomon Group LLC, see 2003 TNT 99-36, Rep. Jeb Hensarling, R-Texas, and 14 other reps, 2003 TNT 99-35, 24 House members, see 2003 TNT 100-32. See also Letter by 29 U.S. Congressmen to President George Bush, 2003 TNT 12-31; Letter of Center for Freedom and Prosperity et al. to Secretary of the Treasury, John Snow, dated January 26, 2004, available at http://www.freedomandprosperity.org/ltr/ctc6/ctc6.shtml.

10. See Letter of Pamela F. Olson, Assistant Secretary (Tax Policy), Dept. of Treasury, to Senator Robert F. Bennett, dated December 22, 2003, reprinted in 2004 TNT 1-34, stating that "[t]his proposed regulation is just one element of our multi-faceted effort to protect the interests of honest taxpayers." See also Amy Hamilton, "U.S. Treasury Official Defends Nonresident Alien Interest Reporting Regs," Tax Notes International, May 12, 2003, p. 541; Statement of Pamela F. Olson, Assistant Secretary for Tax Policy, Treasury Department, before House Committee on Small Business, May 2, 2003, reprinted in 2003 TNT 85-20. But see Letter of Fred L. Smith Jr., President, Competitive Enterprise Institute, to Treasury Secretary John W. Snow, Sept. 26, 2003, reprinted in 2003 TNT 194-23, in which Mr. Smith thanks Secretary Snow for "our meeting in your offices," and states: "I understand that this proposal is opposed by Treasury and the IRS."

This article will explore some aspects of the controversy that continues to surround this proposed regulation. First, the article will discuss the chief justification for the regulation, i.e., to enhance and broaden efforts to exchange tax information with treaty partners. This part will explain that greater information sharing is needed as a means to counter the use of offshore bank accounts to facilitate tax evasion. In the next part, the article will assess the concern of many critics that the regulation will lead to unwarranted invasion of financial privacy. The article describes how Congress has already had to limit Americans' financial privacy in order to provide the IRS with adequate tools for verifying the accuracy of income tax returns. The article then argues that, assuming appropriate safeguards are in place, broader information exchange with our treaty partners will not significantly diminish the existing degree of privacy. The final part of the article suggests that some criticism of the proposed regulation may have the objective of replacing the income tax with another tax system that would afford greater financial privacy.

The article will not address the effects of the proposed regulation on the well-being of U.S. banks or on the U.S. economy nor will it address arguments that the Treasury may lack the authority to issue the regulation under current law.

I. The Rationale for the Regulation

A. The IRS Explanation

1. Detecting U.S. Taxpayers Posing as Foreigners

When the Clinton Administration issued the proposed regulation in 2001, it offered two justifications. The first was "to ensure voluntary compliance by U.S. taxpayers by minimizing the possibility of avoidance of the U.S. information reporting system (such as through false claims of foreign status)."[11]

A bank located in the U.S. that pays interest on deposits is generally required to report the amount paid and the recipient to the IRS on Form 1099.[12] However, under current law, no reporting is required if the bank has appropriate documentation that the recipient is a foreign payee (other than a Canadian resident).[13] Therefore, a U.S. citizen or resident can avoid a U.S. bank's filing

11. REG-126100-00, supra note 1, ¶ 19.

12. See IRC § 6049(a); Treas. Reg. § 1.6049-4.

13. Section 6049(b) provides that Form 1099 reporting is not required for an amount subject to withholding under § 1441 or 1442 or any amount that would be subject to such withholding but for the fact that such amount is described in § 871(i)(2).

a Form 1099 regarding interest paid to him if he falsely files with the bank a statement of his foreign status (on IRS Form W-8). There is no mechanism under current law that would block this type of perjurious action. The bank paying the interest is entitled to rely on a valid Form W-8 (if it does not know or have reason to know of the inaccuracy).[14]

Section 6049(b)(2)(C), (b)(5)(A),(B)(iv). See FSA 1998-381, August 24, 1992, available in 98 TNT 220-85. The regulations interpret this provision as making an exception from Form 1099 reporting for "payments that a payor can, prior to payment, reliably associate with documentation upon which it may rely to treat the payment as made to a foreign beneficial owner in accordance with § 1.1441-1(e)(1)(ii)." Treas. Reg. § 1.6049-5(b)(12). This exception to the filing requirement is not available, however, for interest on a deposit that is not effectively connected to a U.S. trade or business and is paid to a Canadian nonresident alien individual if the deposit is maintained at an office within the U.S. Treas. Reg. §1.6049-5(b)(12); §1.6049-8(a). See discussion in supra note 3.

14. Under Treas. Reg. § 1.1441-1(e)(1)(ii), a "withholding agent may treat a payment as made to a foreign person that is a beneficial owner if . . . the withholding agent can reliably associate the payment with a beneficial owner certificate. . . furnished by the person whose name is on the certificate." This certificate is "a statement by which the beneficial owner of the payment represents that it is a foreign person," and it is provided on IRS Form W-8. Reg. § 1.1441-1(e)(2)(i),(ii). According to the regulations, a "Form W-8 is valid only if its validity period has not expired, it is signed under penalties of perjury by the beneficial owner, and it contains all of the information required on the form." Treas. Reg. § 1.1441-1(e)(2)(ii). In addition, "the withholding agent. . . must not have been notified by the IRS that any of the information on the withholding certificate. . . is incorrect or unreliable." Treas. Reg. § 1.1441-1(e)(1)(ii)(B). According to Treas. Reg. § 1.1441-1(e)(4), a "withholding agent may rely on the information and certifications stated on withholding certificates or other documents without having to inquire into the truthfulness of this information. . . unless it has actual knowledge or reason to know that the same is untrue." The Form W-8BEN (rev. December 2000) includes a space for the beneficial owner's "permanent residence address" and states in bold "Do not use a P.O. box or in-care-of address." See also Instructions for Form W-8 BEN (Rev. January 2003), p. 4. However, the IRS publication relating to withholding of tax on nonresident aliens states: "Until further notice, you can rely upon Forms W-8 that contain a P.O. box as a permanent residence address provided you do not know, or have reason to know, that the person providing the form is a U.S. person and that a street address is available." IRS Publication 515 (rev. November 2002), p. 7. See generally Stephen E. Shay, J. Clifton Fleming, Jr., and Robert J. Peroni, "'What's Source Got to Do With It?' Source Rules and U.S. International Taxationn," 56 Tax Law Review 81 (2002), at 125, stating that "To avoid administrative burdens and excess withholding. . . , the final withholding regulations contain at least three important concessions that limit the identification of beneficial owners and the reach of disclosure."

However, under the original version of the proposed regulation, the bank relying on a Form W-8 to avoid Form 1099 reporting would nevertheless have to report the amount of interest and the name of the recipient to the IRS on Form 1042-S as deposit interest paid to a nonresident alien.[15] Whether this would serve as a greater deterrent to dishonesty by the U.S. taxpayer or would assist the IRS in detecting the deception by the U.S. taxpayer is not entirely clear.[16]

In any event, under the revised version of the regulation, Form 1042-S reporting of the interest would occur only if the recipient is a resident of one of 16 countries.[17] Thus, any U.S. taxpayer who under current law would falsely pose as a foreigner could easily avoid the impact of the new regulation by claiming residence in a country other than one of the sixteen listed in the regulation.[18]

Moreover, even if the proposed regulation were to be extended to all nonresident aliens (as under the original proposal), it does not require information reporting for payments made to foreign corporations.[19] Thus, a U.S. citizen bent on avoiding any reporting to the IRS could contribute the funds to

15. Under the proposed regulation, the payor was permitted to "rely upon a valid Form W-8 to determine whether the payment is made to a nonresident alien individual." If the payor did not have "either a valid Form W-8 or valid W-9, the payor [was required to] report the payment as made to a U.S. non-exempt recipient if it must so treat the payee under the presumption rules of § 1.6049-5(d)(2) and § 1.1441-1(b)(3)(iii)." Proposed Regulation § 1.6049-8(a).

16. See Mastromarco & Hunter, supra note 6, at 168 (questioning whether "the filing of the Form 1042-S [would] really have any effect on compliance").

17. See supra note 8.

18. Under the revised proposed regulation, the payor "may rely upon an applicable withholding certificate described in § 1.1441-1(c)(16) (Form W-8) that is valid to determine whether the payment is made to a nonresident alien individual who is a resident of one of the countries for which reporting is required." Proposed Regulation § 1.6049-8(a). But if there is not a valid Form W-8 or W-9, the payor "must report the payment as made to a U.S. nonexempt recipient if it must so treat the payee under the presumption rules of §§ 1.6049-5(d)(2) and 1.1441-1(b)(3)(iii)." Id.

19. See Treas. Reg. § 1.1441-1(c)(6), stating that "the beneficial owner means the person who is the owner of the income for tax purposes and who beneficially owns the income." See Shay, Fleming & Peroni, supra note 14, at 125-26, explaining that "the regulations treat a foreign corporation as the beneficial owner of its income, irrespective of whether it is located in a tax haven, and its owner(s) need not be identified." They state that "[t]his was a significant decision by the Service to limit the extent to which the withholding tax rules would be used as a means to catch U.S. tax evaders." Id. at 126.

be deposited to a wholly-owned foreign corporation and have the foreign corporation make the deposit in the U.S. bank.[20]

2. Facilitating Information Exchange with Other Countries

The second justification offered for the regulation by the IRS was that

> "several countries that have. . . agreements that provide for the exchange of tax information with the United States have requested information concerning bank deposits of individual residents of their countries. Because of the importance that the United States attaches to exchanging tax information as a way of encouraging voluntary compliance and furthering transparency. . . ., Treasury and the IRS believe that it is important for the United States to facilitate, wherever possible, the effective exchange of all relevant tax information with our treaty partners."[21]

Bilateral treaties entered into by the U.S. typically contain an article similar to Article 26 of the U.S. Model Income Tax Convention providing for "Exchange of Information and Administrative Assistance."[22] These agreements

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20. See Shay, Fleming & Peroni, supra note 14, at n. 171, noting that "A U.S. tax evader resident in the United States might arrange with a fiduciary in a country with confidentiality protections to organize a corporation to hold investment assets."

21. When the IRS replaced the proposed regulation with the new, more limited version, it explained: "The IRS and Treasury believe that limiting reporting to residents of these countries will facilitate the goals of improving compliance with U.S. tax laws and permitting appropriate information exchange without imposing an undue administrative burden on U.S. banks." REG-133254-02, supra note 8, at ¶ 25.

22. 1996 U.S. Model Income and Capital Tax Convention, Sept. 20, 1996, available at 96 TNI 186-16. See Richard Gordon, "Tax Havens and Their Use by United States Taxpayers - An Overview," IRS Publication 1150, Rev. 4-81, reprinted in 93 TNT 119-22 [hereinafter "Gordon Report"] at page 129, stating in 1981 that "United States treaties in force contain an article obligating this country and its treaty partner to exchange information on matters related to tax administration." For further discussion of information exchange under treaties, see Michael I. Saltzman and Jean-Claude M. Wolff, "The Growing Role of Information Exchange in U.S. Tax Treaties," 32 Tax Notes Int'l Magazine 943 (2003). Saltzman & Wolff note that the "IRS has five special programs for information exchange." Id. at 944, citing Internal Revenue Manual 4.60.1. One program is responding to specific requests of treaty partners for information, including "property ownership, financial records such as bank account information, verification of income tax return filing and filing status, and the types and amounts of income and expense reported." Id. A second program includes "routine exchanges of

would permit (but not require) routine or automatic exchange of information or a spontaneous sending of information without any request; they also mandate provision of information in response to a request regarding a specific taxpayer by the treaty partner.[23] If the revised regulation were put into effect, the U.S. would be in a position[24] to make an automatic exchange of information regarding bank deposit interest with the sixteen countries listed in the regulation. This would allow these countries to learn about interest paid by banks in the U.S. to their individual residents, thereby permitting these countries to impose their tax on such interest. Similarly, the U.S. would learn about interest paid by banks in those countries to U.S. taxpayers and could verify that the interest is reported on Form 1040.[25]

In addition, Treasury's adherence to the proposed regulation (as revised in August 2002) may be interpreted as an indication of willingness to participate in, and at least tacitly support, the recently adopted European Union Savings Directive. Under this Directive, interest paid within the EU to an EU resident would automatically be reported to the residence country. The twelve EU countries that have agreed to this routine sharing of information are all listed in the Treasury's proposed regulation, whereas the three EU countries that have not agreed to routine information sharing (Belgium, Luxembourg and

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information, such as dividend, interest, rents, and royalties, records of which are computerized and capable of being communicated without difficulty." Id. at 944-45.

23. See Gordon Report, supra note 22, at page 130; see David E. Spencer, OECD Model Agreement Is a Major Advance in Information Exchange (Part 2), 13 J. Int'l Tax'n 10, at text accompanying n. 8.

24. Although the IRS would be in a position to make an automatic exchange, the U.S. would not be required to do this under its existing treaties or information-exchange agreements. The IRS would merely be required to provide specific information when a request is made pursuant to such an agreement. Thus, it seems incorrect for the Cato Institute to say that "the proposed new regulation would be the equivalent of an automatic information-sharing agreement with other nations." See Rahn & de Rugy, supra note 6, at ¶ 33.

25. An alternative to obtaining information regarding an American taxpayer from a foreign country is for the IRS to obtain such information directly from an foreign financial institution in which the American has an account and which has signed up to be a "qualified intermediary." See Marnin J. Michaels & Thomas A. O'Donnell, "The Death of Information-Exchange Agreements," 13 J. Int'l Tax'n 8 (August 2002), noting that "foreign financial institutions have signed up en masse for the Services's new qualified intermediary. . . program." The authors note however that under these agreements "the U.S. is allowing non-U.S. tax cheats to use the U.S. without obtaining information that it could exchange with the tax evader's home country." Id. at text accompanying n. 11. See discussion in Shay, Fleming & Peroni, supra note 14, at 124-25; Michael J. Graetz, Foundations of International Income Taxation 395-99 (2003).

Austria) are not listed in the regulation.[26] Although implementation of the EU Directive in 2005 has been made explicitly contingent on adoption of equivalent measures by certain other countries, the EU has already acknowledged that the U.S. cooperation has been adequate,[27] perhaps in part because of the proposed regulation.[28]

More generally, the Treasury's justification of the regulation suggests its desire to follow through with recent efforts to achieve greater information exchange with so-called tax havens. The efforts include the recent signing by the U.S. of bilateral information-sharing agreements with certain tax havens and the OECD initiative to compel tax havens to achieve greater transparency, both discussed below. By stating its own willingness to collect information about interest received by residents of other countries, the Treasury may seek to reassure tax havens that they will not be required to be more forthcoming in sharing information than the U.S. is willing to be.

In conclusion, the proposed regulation should be seen as part of a larger movement by the U.S. and its major trading partners toward greater sharing of

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26. Ten new countries are entering the EU in 2004. See supra note 8. These are not listed in the regulation.

27. In December 2002, the EU Commission concluded that while the U.S. "is not prepared at this stage to give a formal statement in relation to the [proposed EU] savings directive," the "Treasury remains clearly focused on a full and effective administration of taxes based on information exchange on a bilateral basis." Commission of the European Communities, Communication from the Commission to the Council, Report Concerning Negotiations with Third Countries on Taxation of Savings Income, Dec. 3, 2002, http://europa.eu.int/comm/taxation_customs/taxation/information_notes/taxation_package/taxpack_4.htm, last visited 10/20/03, at ¶¶ 20-26. However, in November 2002, two members of the Bush Administration, Larry Lindsey, director of the National Economic Council, and R. Glenn Hubbard, head of the U.S. Council of Economic Advisers, both apparently indicated that the Administration did not support the European Savings Tax Directive. See Cordia Scott, "White House Signals Lack of Support for EU Savings Tax Directive," Tax Notes International Magazine, Nov. 4, 2002, at 421-422; see also Edward Alden, Francesco Guerrera and Amity Shlaes, "U.S. Opposes Sharing Information on Savings Taxation - White House Advisers Come Out Against European Request For Data on Foreign-Held Accounts," Financial Times, Sept. 26, 2002, page 4. When the June 2003 agreement came out, its 2005 implementation was not conditioned on any further U.S. action. See infra notes 72-75 and accompanying text. For continuing uncertainty regarding the U.S. position, see Cordia Scott, "OECD Targets Additional Financial Centers in Expanded Tax Haven Crackdown," 2004 WTD 109-1.

28. See David R.Burton, "Financial Privacy and Individual Liberty," Discussion Draft/Working Paper, Austrian Scholars Conference, March 14, 2003, available online at http://www.mises.org/asc/2003/asc9burton.pdf, stating that "the proposed regulation is almost certainly the reason why the EU regards the U.S. as being in compliance with the EU Savings Tax Directive." Id. at 24 & n. 77.

information between countries as a means of improving tax compliance. This certainly appears to be a concern for many critics of the proposal. In fact, some critics have argued that this regulation will lead inevitably to a world tax clearinghouse for information. Because the regulation is part of a larger movement toward information sharing, it seems appropriate to consider, as a general matter, whether broader information sharing is really necessary and whether it brings too great a risk to the privacy of individuals.

B. Why the IRS Wants to Achieve Broader Information Sharing with Other Countries

1. The Prevalence of Tax Evasion through Offshore Arrangements

In responding to criticism of the proposed regulation, the Treasury has recently made clear the reason that it considers broader information-sharing to be necessary:

> "The offshore sector is an increasing problem in the enforcement of U.S. tax laws. . . . Addressing the potential for tax evasion through use of offshore accounts or entities is critical to maintaining the confidence of all Americans in the fairness of the U.S. tax system."[29]

The potential for tax avoidance or evasion through use of offshore entities or accounts has long been apparent. For example, in 1937, when Congress held hearings on the subject of "Tax Evasion and Avoidance," there was testimony regarding "the device of evading taxes by setting up foreign personal holding corporations in the Bahamas, Panama, Newfoundland and other places where taxes are low and corporation laws lax."[30] In 1970, a congressional report accompanying the passage of the Bank Secrecy Act of 1970 stated: "These days when the citizens of this country are crying out for tax reform and relief, it is grossly unfair to leave the secret foreign bank account open as a convenient avenue of tax evasion."[31]

More recently, in 1981, Richard Gordon, Special Counsel for International Taxation at the Treasury Department, wrote an extensive report

29. Treasury Thanks Lawmakers for Letter on NRA Interest-Reporting Rules, 2003 TNT 124-61 (letter sent by Pamela F. Olson, Assistant Secretary of the Treasury for Tax Policy, to 24 members of the House of Representatives).

30. Tax Evasion and Avoidance, Hearings before the Joint Committee on Tax Evasion and Avoidance, 75th Cong., June 17, 18, 22, 23, and 24, 1937, page 2, quoting from a letter to the President from Sec'y of the Treasury Henry Morgenthau, Jr., dated May 29, 1937. See Charles I. Kingson, International Taxationn 459-60 (1998).

31. H.R. Rep. No. 91-975, 91st Cong., 2nd Sess. (March 28, 1970), 1970 U.S.C.C.A.N. 4394, 1970 WL 5667 (Leg.Hist.).

entitled "Tax Havens and Their Use by United States Taxpayers – An Overview."[32] "Tax havens" were defined for this purpose as "countries having (1) low rates of tax when compared with the United States, and (2) a high level of bank or commercial secrecy that the country refuses to breach even under an international agreement."[33] In 1984, an updated report by the Treasury, entitled "Tax Havens in the Caribbean Basin," stated that "it seems reasonable to assume that a great deal of activities designed to violate the tax and other laws of the United States takes place in the Caribbean Basin tax havens."[34] A Senate report, entitled "Crime and Secrecy: The Use of Offshore Banks and Companies," was issued in 1985, and warned that "the effect has been to. . . thwart the collection of massive amounts of tax revenues."[35]

In the 1990's, the revelations by John Mathewson, the indicted former chairman of a Cayman Island bank, of how he helped numerous American tax evaders set up undisclosed offshore accounts and access their funds through credit cards, made it clear that the problem was continuing.[36] Advertisements in airline magazines, numerous websites, and self-help books, by authors such as Jerome Schneider and Terry Neal, offered U.S. taxpayers the "offshore advantage."[37] Books such as "The Cheating of America," and "The Great American Tax Dodge" gave detailed examples of instances of offshore tax evasion.[38] The fact that offshore accounts and entities can now be set up in the

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32. Gordon Report, supra note 22.

33. Id. at I., Overview of Findings and Options.

34. Treasury Dept., Tax Havens in the Caribbean Basin, January 6, 1984, quoted in Ex Parte Motion by Government To Search Offshore Credit Card Records, U.S. District Court for Southern District of Florida, Oct. 25, 2000, Declaration of Joseph C. West, Revenue Agent, ¶¶ 15-16, available at 2000 TNT 209-24 [hereinafter "Ex Parte Motion"].

35. Permanent Subcommittee on Investigations, Senate Committee on U.S. Government Affairs, "Crime and Secrecy: The Use of Offshore Banks and Companies," August 28, 1985, quoted in Ex Parte Motion, supra note 34, at ¶¶ 18-19.

36. U.S. Department of Justice Press Release, Former Chairman of Cayman Island Bank Sentenced for Nationwide, Multi-Million Dollar Offshore Banking Scheme, August 2, 1999, available in 1999 WTD 174-28; Letter of Faith S. Hochberg, United States Attorney, to Judge Alfred J. Lechner, Jr., District Judge, July 29, 1999, in U. S. v. John M. Mathewson, Crim. No. 96-353 (AJL), available in 1999 TNT 173-26; Barton Massey, "Convicted Bank Chairman Is Key to Dozens of Tax Haven Cases," 1999 WTD 172-2. See also Testimony of Jack A. Blum, Esq. before the Senate Finance Committee on Tax Schemes, Scams and Cons, April 22, 2002, reprinted in 2002 TNT 71-34.

37. Jerome Schneider is the author of "The Complete Guide to Money Havens: How to Make Millions, Protect Your Privacy and Legally Avoid Taxes," currently in a "Revised and Updated 4th Edition" published in 2001. Terry L. Neal is the author of The Offshore Solution (2001) and of The Offshore Advantage (1999). See Amazon.com, last visited on 07/09/03.

38. Charles Lewis, Bill Allison, & the Center for Public Integrity, The Cheating of America – How Tax Avoidance and Evasion by the Super Rich are Costing the Country Billions – and What You Can Do About it (NY 2002); Donald L. Bartlett &

privacy of one's home, through visiting websites on the Internet, raises further concern that this problem could become more widespread.

Beginning in 2000, the Government publicly set forth its case that taxpayers who held credit cards issued by offshore banks might well be engaged in tax evasion. On this basis, it convinced several federal district courts to permit it to serve summons on credit card companies and then on merchants to learn the identities of such holders.[39] After gathering this information, the IRS in 2003 offered taxpayers who had used offshore arrangements to improperly reduce taxes an opportunity to avoid the civil fraud penalty and criminal prosecution by coming forward voluntarily.[40] In July 2003, the IRS announced that 1,299 taxpayers had applied for the program, that it obtained information about 400 offshore promoters and that it had thus far collected $75 million in taxes.[41] In this same period, the Government obtained indictments against two leading promoters of offshore planning (who were also popular authors of self-help guides), Jerome Schneider[42] and Terry L. Neal.[43]

James B. Steele, The Great American Tax Dodge – How Spiraling Fraud and Avoidance are Killing Fairness, Destroying the Income Tax, and Costing You (Berkley 2000). See also Janet Novack, Forbes Magazine, "Are You a Chump?" p. 122 (March 5, 2001).

39. Internal Revenue Service, IRS Chronology on Credit Cards and John Doe Summons, January 4, 2003, available at 2003 TNT 10-12. See Ex Parte Motion, supra note 34 (request before U.S. District Court for Southern District of Florida). As of July 30, 2003, the IRS said there were 2,800 cardholders under audit or for which audit had been completed, $3 million in taxes assessed, and "dozens of cases" referred to Criminal Investigation. Internal Revenue Service, Offshore Compliance Program Shows Strong Results, July 30, 2003, available at 2003 TNT 147-12. See also David Cay Johnston, "IRS Says Offshore Tax Evasion is Widespread," The New York Times, March 26, 2002, at A1; Lavonne Kuykendall, "What's Behind Offshore Data Tug-of-War," The American Banker, p. 1, April 1, 2002, available on Lexis. See also "Motion to Quash Summons Based on IRS Offshore Credit Card Project Denied," 2004 TNT 33-5 (district court granted government's motion to enforce summons for bank records.)

40. Revenue Procedure 2003-11, available at 2003 TNT 10-7; IRS, IRS Unveils Offshore Voluntary Compliance Initiative; Chance for 'Credit-Card Abusers' to Clear Up Their Tax Liabilities, IR-2003-5, Jan. 14, 2003; IRS Revises Voluntary Disclosure Practice, IR-2002-135, Dec. 11, 2002. See also IRS, Offshore Voluntary Compliance Initiative has Month to go; People Need to Apply Directly to Receive Penalty Relief, IR-2003-35, March 17, 2003. See also Heather Bennett, "IRS Offshore Compliance Initiative Collects $170 Million So Far, Official Says," 2004 TNT 22-13.

41. IRS, Offshore Compliance Program Shows Strong Results, supra note 39. In October 2003, an IRS official predicted that the program would bring in about $150 million. Robert Goulder, "IRS Official Reviews Offshore Compliance Initiative Progress," 2003 TNT 210-5.

42. U.S. Attorney, Northern District of California, Press Release of Dec. 19, 2002, available at www.usdoj.gov/tax/usaopress/2002/2002_12_19_schneider.html. The indictment of Schneider and Eric J. Witmeyer was for "one count each of conspiracy to

2. How Offshore Arrangements Facilitate Tax Evasion

Although a taxpayer is expected to voluntarily report all his income to the IRS on Form 1040, the IRS has other means at its disposal for obtaining at least some of this information, at least when transactions are conducted within the U.S.

For example, many types of payments, most notably, wages, dividends, interest, unemployment compensation, and gross proceeds of security sales, must be reported by a U.S. payor or broker to the IRS as well as to the taxpayer.[44] If the taxpayer recipient has not provided his taxpayer identification number to the payor or broker,[45] then backup withholding of tax is required.[46] In addition, the IRS has authority to examine books or records which may be relevant to determining a taxpayer's liability, and to summon the taxpayer or other persons to produce such books or records, or to give testimony under oath relevant to such determination.[47] The U.S. District Court is authorized to

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defraud the IRS," and additional counts of wire and mail fraud. The charges were "in connection with their alleged marketing and sales to U.S. taxpayer investors of offshore international banks or corporations and causing those entities to be 'decontrolled' which is a process used by the defendants to attempt to conceal the U.S. taxpayer investor's ownership in the offshore bank or corporation."

43. Department of Justice Press Release, Alleged Promoters of Offshore Credit Card Schemes Indicted for Conspiracy to Defraud the IRS, April 23, 2003.

44. See, e.g., IRC § 6042 (dividends), § 6045 (returns of brokers), § 6049 (interest), § 6050B (unemployment compensation), § 6050N (royalties), § 6051 (wages). For provisions limiting reporting obligations to U.S. payors and middlemen, in the case of foreign-source income, see IRC § 6042(b)(2)(A)(i); Treas. Reg. § 1.6042-3(b)(iv) (dividends); Treas. Reg. § 1.6045-1(a)(1) (broker); IRC § 6049(b)(1)(D); Treas. Reg. § 1.6049-5(b)(6) (interest).

45. A U.S. citizen or resident opening a domestic bank account must provide his name, address and TIN on a form signed under penalty of perjury; a foreign person must provide his name, and address in his country of permanent residence on a form signed under penalties of perjury. OECD, Improving Access to Bank Information for Tax Purposes (2000) [hereinafter "OECD Bank Report"], Appendix I, ¶ 1.5.5.3.1. Nonresidents must provide a TIN in some cases. Id. at ¶ 1.5.5.3.3. The same rules apply to foreign branches and subsidiaries of U.S. financial institutions, except foreign persons may provide documentary evidence of foreign status rather than use the IRS form. Id., ¶ 1.5.5.3.1. In opening a bank account in the U.S., documentary evidence must be provided if a Currency Transaction Report is required. Id., at ¶ 1.5.3.3.2.

46. IRC § 3406(a).

47. IRC § 7602. See generally William M. Sharp, Sr. & Hale E. Sheppard, "Privilege, Work-Product Doctrine, and Other Discovery Defenses in U.S. IRS's International Tax Enforcement," 32 Tax Notes Int'l Magazine 377 (2003). For the historical background of the summons power under § 7602, see Bryan T. Camp, "Tax

compel compliance with the summons and to use the contempt power toward this end.[48] For example, the IRS can use a summons to a bank to obtain the complete banking records of an individual suspected of underreporting income.[49] Finally, U.S. banks are required to file Suspicious Activity Reports to report suspicious banking transactions, and Currency Transaction Reports with respect to currency transactions in amounts exceeding $10,000.[50] Banks are subject to audit and may incur civil or criminal penalties for noncompliance. These reports are available to the IRS. The purpose is to protect against money-laundering as well as tax evasion.[51]

Administration as Inquisitorial Process and the Partial Paradigm Shift in the IRS Restructuring and Reform Act of 1998," 56 Fla. L. Rev. 1, 31-52 (2004).

48. IRC § 7604. See § 7609, imposing special procedures, including notice, for a third-party summons.

49. Banks are required to keep certain records regarding their customers' accounts. See discussion in Matthew N. Kleiman, Comment: The Right to Financial Privacy versus Computerized Law Enforcement: A New Fight in an Old Battle, 86 Nw. U.L.Rev. 1169 (1992), at 1186. The Right to Financial Privacy Act establishes certain standards for bank secrecy but "an exception is made, pursuant to 12 U.S.C. § 3413(c), for financial records sought in accordance with the procedures set forth in Title 26 of the Code (i.e., the IRC)", including the administrative summons provided for in IRC § 7609. OECD Bank Report, supra note 45, Appendix I, at ¶ 1.3. Disclosure to the IRS of names and addresses of accountholders for purposes of withholding of tax on nonresident aliens is permitted by § 3413(k). Id. Other exceptions, e.g., §§ 3402, 3403(c)-(d), 3413 or 3414, involving "use of administrative or judicial subpoenas and search warrants," may also be available to the IRS. Id. at ¶ 1.3.

50. OECD Bank Report, supra note 45, Appendix I, ¶ 1.4, citing Reg. § 103.21-22. The Suspicious Activity Report (SAR) is on Form TD F 90-22.47, and the Currency Transaction Report (CTR) is on Form 4789. In addition, the Bank Secrecy Act requires filing of a Form 4790 by a person transporting currency or certain other monetary instruments in excess of $10,000 out of or into the U.S. See generally Treasury Department, A Report to Congress in Accordance with § 357 of the USA Patriot Act, April 26, 2002, available in 2002 TNT 84-19. See e.g., Joseph J. Darby, Confidentiality and the Law of Taxation, 46 Am. J. Comp. L. 577 (1998), stating that "Secrecy in banking is not protected in the United States. Au contraire, the Federal Banking Secrecy Act authorizes the Treasury Department to require financial institutions in the United States to keep certain records of financial transactions and to report certain domestic and foreign currency transactions directly to the Secretary of the Treasury." He notes that the statute's constitutionality was upheld in California Bankers Association v. Schultz, 416 U.S. 21 (1974).

51. OECD Bank Report, supra note 45, Appendix I, ¶ 1.6, citing 31 U.S.C. §§ 5331 and 5332. For a general survey on the practices of OECD member countries with respect to tax authorities' access to bank information, see OECD Bank Report, supra note 45, and OECD, Access for Tax Authorities to Information Gathered by Anti-Money Laundering Authorities – Country Practices, available online

By contrast, IRS information-reporting generally does not extend to foreign payors or brokers.[52] Moreover, some foreign countries, such as Liechtenstein, Switzerland, and the Cayman Islands, have held themselves out as places where investors and depositors can be sure that their identity and holdings are secret, places where confidentiality is assured.[53] In some cases, the government simply will not seek to collect information from banks; in other cases, the government may itself impose penalties on bank employees who breach secrecy. In any case, requests to the executive or judiciary of such a country for information related to taxes or to creditors' claims to collect debts will not be entertained. Apart from Switzerland, these are countries that do not have income tax treaties with the United States.

A U.S. citizen or resident who has an offshore account with a value exceeding $10,000 is legally required to acknowledge this on Schedule B of

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http://www.oecd.org/findDocument/0,2350,en_2649_33751_1_1_119663_1_1_37427,00.htm (results of survey as of February 2002). The Criminal Investigation Division of the IRS has on-line access to FINCEN's database of SARs. The Examination Division may "receive particular suspicious activity reports in connection with particular examinations following a name-specific request for such information to FINCEN." OECD, Access for Tax Authorities, supra. In the U.S., currency transaction reports filed by financial institutions, and reports required of persons entering the U.S. and transporting at least $10,000 in currency "[g]enerally. . . [are] available to federal tax authorities and [are] maintained on-line by both the Internal Revenue and Customs Services." Id. "The Bank Secrecy Act prevents the use of SARs for civil tax compliance." Id.

52. See supra note 44. As a result, compliance suffers. See Reuven S. Avi-Yonah, "Globalization, Tax Competition and the Fiscal Crisis of the Welfare State," 113 Harv. L. Rev. 1573, 1584-85 (2000), excerpted in Graetz, supra note 25, at 375-76, noting that when neither "withholding at the source or information reporting. . . is available. . . as in the case of foreign source income, compliance rates drop dramatically;" Michael J. Graetz, "Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies," 26 Brook. J. Int'l Law 1357, 1414 (2001), excerpted in Graetz, supra note 25, at 374-75, noting very significant underreporting of interest, dividends and capital gains on outbound portfolio investments.

53. See Lars P. Feld, "Swiss Bank Secrecy and International Taxation," Tax Notes International Magazine, Sept. 2, 2002, p. 1179; Robert Goulder, "Liechtenstein Defends Low Taxes and Fiscal Privacy," 2000 WTD 246-2 (Dec. 20, 2000). See also OECD Report, Improving Access to Bank Information for Tax Purposes: The 2003 Progress Report (2003), at 13-14, noting that Switzerland "had little or no access to [banking] information for civil tax purposes." . See generally OECD Bank Report, supra note 45, at 20-31, discussing the adverse consequences of bank secrecy.

Form 1040[54] and, separately, to file a report of the account with the Treasury Department.[55] However, the Treasury Department has, at least in the past, made little effort to enforce this requirement.[56]

Bank accounts in bank secrecy jurisdictions are ideal for concealment of illegally earned funds, funds to be used for terrorism or that are the product of political corruption, or funds that represent unreported income in the residence country. Even if the source of funds is completely legitimate, future earnings can be concealed from the home country's taxes. Finally, it may be impossible for the IRS or other creditors to collect debts against these assets.

3. Efforts to Break Down the Barriers of Secrecy Surrounding Tax Havens and How the Proposed Regulation Fits Together with These Efforts

As noted, the U.S. has not generally entered into tax treaties with tax havens, and thus has not had an mechanism for exchange of information with tax authorities in those countries. In 1984, when Congress passed the Caribbean Basin Initiative, Caribbean countries were offered the inducement of being able to host tax-deductible business conventions if they entered into agreements for the exchange of information. Section 274(h)(6) described the necessary

54. A taxpayer filing Schedule B to Form 1040 is asked to indicate whether he has a financial interest in a foreign account and, if the answer is yes, is referred to the filing requirements for Form TD F 90-22.1. 2002 Form 1040, Schedule B, Part III, Line 7a. See Treasury Department, A Report to Congress in accordance with § 361(b) of the USA Patriot Act, April 26, 2002, available at 2002 TNT 84-18. The 2002 Instructions for Schedule B explain that the "no" box is to be checked if the combined value of the foreign accounts is $10,000 or less during the whole year. However, the Instructions also state that the relevant accounts include foreign bank accounts owned by any corporation in which the taxpayer owns more than 50 percent of the stock.

55. The report is on Form TD F 90-22.1, entitled Report of Foreign Bank and Financial Accounts. Section 5314 of the Bank Secrecy Act (31 U.S.C. 5314) authorizes the Treasury to issue regulations requiring these reports. This provision was enacted in 1970. See Pub.L.91-508, 84 Stat. 1114, § 241, enacting 31 U.S.C. 1121; Pub. L. 97-258, 96 Stat. 997, revising 31:1121(a) as 31 U.S.C. 5314(a). The regulation is at 31 CFR 103.24. Under the Bank Secrecy Act, civil or criminal penalties may be imposed for failure to file. 31 U.S.C. 5321(5), 5322. A constitutional challenge to this filing requirement was rejected in California Bankers Assn. v. Shultz, 416 U.S. 21 (1974), at 56-63, 70-74.

56. In calendar year 2001, about 175,000 forms were filed. However, the IRS suggests that as many as 1 million taxpayers might have been required to file the report. Treasury Department, A Report to Congress in accordance with § 361(b) of the USA Patriot Act, April 26, 2002, reprinted in 2002 TNT 84-18, at ¶ 8.

agreements, and a draft agreement was developed. The U.S. entered into such agreements with certain countries.[57]

In 1998, the OECD launched a new assault on the secrecy of tax havens when it published a report entitled "Harmful Tax Competition – An Emerging Global Issue," addressing "harmful tax practices" in both member and non-member countries.[58] A follow-up report in June, 2000, listed 35 jurisdictions that were considered to be tax havens and that would have to make commitments to eliminate "harmful tax practices" to avoid being labeled "uncooperative tax havens."[59] The incoming Bush Administration was heavily lobbied to reject this initiative (as well as the proposed regulation on bank deposits),[60] and on May 10, 2001, Secretary of the Treasury Paul O'Neill

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57. See Rev. Rul. 2003-109, 2003 TNT 190-18, for an updated list of these countries.

58. OECD, Harmful Tax Competition – An Emerging Global Issue (1998) [hereinafter "1998 OECD Report"]. See "Tax Evaders Beware: Rich Countries Prepare for Crackdown on Havens," Wall St. J., May 21, 1998, page A12. For a thorough discussion of the report, see David E. Spencer, "OECD Report Cracks Down on Harmful Tax Competition," 9 Journal of Int'l Tax'n 26 (1998).

59. OECD, Progress in Identifying and Eliminating Harmful Tax Practices (OECD 2000). See discussion in David E. Spencer, Stepping Up the Pressure on Tax Havens: An Update (Part 1), 12 J. Int'l Tax'n 26 (2001). The 1998 report said that "[t]he necessary starting point to identify a tax haven is to ask (a) whether a jurisdiction imposes no or only nominal taxes. . . and offers itself. . . as a place to be used by non-residents to escape tax in their country of residence." 1998 OECD Report, supra note 58, at ¶ 52. It then goes on to list other "key factors," i.e., "(b) laws or administrative practices which prevent the effective exchange of relevant information with other governments on taxpayers benefitting from the low or no tax jurisdiction (c) lack of transparency and (d) the absence of a requirement that the activity be substantial, since it would suggest that a jurisdiction may be attempting to attract investment or transactions that are purely tax driven." Id. See also id. at ¶ 49, noting that "[t]ax havens serve three main purposes: they provide a location for holding passive investments ("money boxes"); they provide a location where "paper" profits may be booked; and they enable the affairs of taxpayers, particularly their bank accounts, to be effectively shielded from scrutiny by tax authorities of other countries."

60. The lobbying efforts were coordinated by Daniel Mitchell of the Heritage Foundation, and Andrew Quinlan, President of the Center for Freedom and Prosperity ("CFP"). See Anand Giriharadas, "The Treasury Coddles Tax Cheats – Sacred Havens," The New Republic Online, posted August 21, 2001 (describing various closed-door meetings of CFP lobbyists with Administration officials); Exhibits 11-15 to Hearings before Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs, July 18, 2001, reprinted in 2001 TNT 139-3 [hereinafter "Hearings"] (memorandum from the Prosperity Institute, and Special Alert, Strategic Memos and Press Statements of the CFP); "Avenue of the Americas: OECD Meets the XFL," Financial Times, Feb. 14, 2001 (describing lobbying against OECD initiative by

publicly expressed disagreement with any effort "to harmonize world tax systems."[61] As a result, the OECD initiative underwent modifications in June 2001[62] so that cooperation by tax havens required only that they commit to

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Andrew Quinlan "former amateur football player and inside-the-Beltway veteran" and "his more scholarly sidekick, Dan Mitchell") . The CFP also engaged in "an aggressive grassroots campaign, including "Internet advocacy" which "generated about 10,000 e-mails to members of Congress or the Treasury Secretary" and "a direct-mail crusade" in which it contracted for "100,000 pieces of mail to targeted citizens." See Exhibit 13 to Hearings, supra, Memorandum of Dan Mitchell to Leaders of Low-Tax Jurisdictions and Supporters of Tax Competition, Financial Privacy, and Fiscal Sovereignty, dated June 16, 2001. Girihandas mentions in particular meetings of CFP lobbyists with Mark Weinberger, Assistant Secretary of the Treasury for Tax Policy, and an April meeting of Secretary O'Neill with Ed Feulner, President of the Heritage Foundation. See also Lee A. Sheppard, News Analysis – It's The Bank Secrecy, Stupid, 91 Tax Notes 385 (April 16, 2001); Robert S. McIntyre, "The Taxonomist – Tax Cheaters' Lobby," The American Prospect, June 4, 2001, p. 12, available on Lexis, describing the mission of CFP as "to protect the God-given right of the rich and powerful to evade taxes."

61. Secretary of Treasury, Paul H. O'Neill, Department of Treasury News Release, May 10, 2001, available as Exhibit 2 to Hearings, supra note 60. He also stated that "the work of this particular OECD initiative. . . must be refocused on the core element that is our common goal: the need for countries to be able to obtain specific information from other countries upon request in order to prevent the illegal evasion of their taxes by the dishonest few. In its current form, the project is too broad and it is not in line with this Administration's tax and economic priorities." Id. Secretary O'Neill's concern was then conveyed in a letter to the G-7 Finance Ministers, dated June 7, 2001. See Exhibit 1 to Hearings, supra note 60. See discussion in David E. Spencer, "OECD Project on Tax Havens and Harmful Tax Practices: An Update (Part 1)," 13 J. Int'l Tax'n 8 (2002); A Retreat on Tax Havens, N.Y. Times Editorial, May 26, 2001, page A-12. The Administration's position was the subject of a July 18, 2001 hearing, entitled "What is the U.S. Position on Offshore Tax Havens?" led by Senator Carl Levin, D-Michigan, Chair of the Permanent Subcommittee on Investigations, Committee on Governmental Affairs. See Amy Hamilton, "O'Neill Says White House Is Pleased With OECD Tax Haven Sanctions Delay," 2001 TNT 139-3; Statement of Paul H. O'Neill before the Senate Committee on Governmental Affairs Permanent Subcommittee on Investigations, July 18, 2001, reprinted in 2001 WTD 139-20; Statement of Donald C. Alexander before Senate Committee on Governmental Affairs Permanent Subcommittee on Investigations, July 18, 2001, reprinted in 2001 TNT 139-54; Opening Statement of Carl Levin, before Senate Committee on Governmental Affairs Permanent Subcommittee on Investigations, July 18, 2001, reprinted in 2001 WTD 140-35, 2001 TNT 139-3. The hearings are described in Spencer, supra.

62. See "Accord is Reached by U.S. and Allies on Tax Havens, " Wall St. J., June 28, 2001, page A4; Statement of Paul O'Neill, supra note 61, ¶¶ 24-34. These modifications were incorporated in "The OECD's Project on Harmful Tax Practices: The 2001 Progress Report," Nov. 14, 2001, reprinted in 2001 WTD 221-14. The 2001 report confirmed that the "lack of substantial activities" criterion, described in the 1998

transparency and effective information exchange.[63] In April 2002, the OECD released its Model Agreement on Exchange of Information in Tax Matters, to reflect "the standard of effective exchange of information" for its tax haven initiative.[64] Thirty-two cooperating countries have agreed to engage in such exchange of information with respect to criminal tax matters, beginning January 1, 2004, and with respect to civil tax matters, beginning in 2006.[65]

At the same time that the OECD was pursuing this initiative, other complementary efforts were proceeding. In June 2000, the Financial Action Task Force on Money Laundering (FATF), established by the G-7, published its own list of 15 "uncooperative" countries.[66] The U.S. in turn, through FinCEN (the U.S. Financial Crimes Enforcement Network) issued advisories about these jurisdictions.[67]

The September 11 attacks focused new concern on the issue of money-laundering and inadequate supervision of bank accounts, onshore or offshore, because of their potential use by terrorists. In October 2001, Congress enacted

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report, would not be used "to determine whether or not a tax haven is uncooperative." In addition, the OECD would seek commitments "only with respect to transparency and effective exchange of information criteria." 2001 Report, ¶¶ 27-28.

63. In April 2002, the OECD cited seven "uncooperative tax havens:" Andorra, Liechtenstein, Liberia, Monaco, the Marshall Islands, Nauru, and Vanuatu. OECD, The OECD List of Unco-operative Tax Havens, April 18, 2002, reprinted in 2002 TNT 76-61. Vanuatu and Nauru were removed from the list in 2003. See Letter of Minister of Finance and Economic Management, The Republic of Vanuatu, to OECD Secretary General, May 7, 2003, online at www.oecd.org.; OECD, "Nauru is Removed from OECD List of Uncooperative Tax Havens," available in 2003 WTD 240-22.

64. OECD, Agreement on Exchange of Information on Tax Matters, ¶ 3, available at www.OECD.org, last visited 07-03-03. See discussion in David E. Spencer, "OECD Model Agreement Is a Major Advance in Information Exchange," 13 J.Int'l Tax'n 32 (2002) & (Part 2), 13 J. Int'l Tax'n 10 (2002); Graetz, supra note 25, at 389-91.

65. See OECD Report, Improving Access to Bank Information for Tax Purposes: The 2003 Progress Report (2003), at 18.

66. These were Bahamas, Cayman Islands, Cook Islands, Dominica, Israel, Lebanon, Liechtenstein, Marshall Islands, Nauru, Niue, Panama, Philippines, Russia, St. Kitts and Nevis, and St. Vincent and the Grenadines. David E. Spencer, "Stepping Up the Pressure on Tax Havens: An Update (Part 2)," 12 J. Int'l Tax'n 36 (2001), at n. 15. See also Jacqueline B. Manasterli, "Offshore Financial Centers and Harmful Tax Regimes Trigger Flurry of International Developments," Tax Notes International Magazine, Dec. 4, 2000, p. 2541.

67. Spencer, supra note 66, at n.16. During these same years, the U.S. was also cooperating in multilateral efforts to combat money-laundering in offshore accounts. See William F. Weschler, "Follow the Money," Foreign Affairs, July-August 2001. Mr. Weschler was Special Adviser to the Secretary of the Treasury from 1999 to 2001.

enhancements of the anti-money-laundering rules.[68] In addition, during 2001 and 2002, the Bush Administration negotiated exchange of information agreements with tax haven countries, such as the Netherlands Antilles, the British Virgin Islands, Bahamas, Antigua and Barbuda, and the Cayman Islands.[69]

In 2003, both the EU and the U.S. took further steps toward greater information exchange.[70] In January, the U.S. entered into an agreement with Switzerland designed to enhance tax information exchange under their existing

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68. The International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001, Title III, of the USA PATRIOT Act, Public Law No. 107-56, signed on Oct. 26, 2001. See Marnin J. Michaels and Thomas A. O'Donnell, "The Death of Information-Exchange Agreements?," 13 J. Int'l Tax'n 8, at n.8 (2002). See also Margaret R. Blake & Carrie J. DI Santo, "Guidance on Anti-Money Laundering Compliance Programs under USA Patriot Act," 13 Journal of Int'l Tax'n 35 (2002). Section 311 of the USA PATRIOT Act authorizes the Treasury to designate a foreign jurisdiction or financial institution as being "of primary money laundering concern" and to impose certain "special measures." The Treasury has exercised this authority with respect to Ukraine and Nauru. Treasury Dept., Press Release, December 20, 2002, available in 2002 TNT 247-20. In the case of Nauru, "U.S. financial institutions" are prohibited "from opening or maintaining correspondent accounts with Nauru-licensed financial institutions." Id. at ¶ 11. See Hudson Morgan, "Treasury's kid gloves," New Republic, p. 16, April 14, 2003, questioning Treasury's failure to use this authority with respect to Saudi Arabia.

69. During 2001 and 2002, the U.S. signed exchange of information agreements with the following countries: Columbia (03-30-01), Cayman Islands (11-27-01), Antigua & Barbuda (12-06-01), Bahamas (01-25-02), British Virgin Islands (04-03-02), Netherlands Antilles (04-17-02), Guernsey (09-12-02), Isle of Man (10-04-02), Jersey (11-04-02). In November 2003, the U.S. signed an exchange of information agreement with Aruba. See Kevin A. Bell, "U.S., Aruba Sign Tax Information Exchange Agreement," 2003 TNT 226-5. In the 1980's and early 1990's, the U.S. put into effect exchange of information agreements with the following countries: Barbados (1984), Jamaica (1986), Grenada (1987), Bermuda (1988), Dominica (1988), Dominican Republic (1989), Mexico (1990), Trinidad & Tobago (1990), St. Lucia (1991), Honduras (1991), Marshall Islands (1991), Costa Rica (1991), Guyana (1992), Peru (1993). All the latter agreements, except for those with Mexico, Peru and the Marshall Islands, qualify for the Caribbean Basin Initiative. John Venuti, Manal S. Corwin, Steven R. Lainoff, and Paul M. Schmidt, "Current Status of U.S. Tax Treaties and International Tax Agreements," 32 Tax Management International Journal 320, 325 (2003). See Marnin J. Michaels and Thomas A. O'Donnell, "The Death of Information-Exchange Agreements?," 13 J. Int'l Tax'n 8, at n. 1 (2002).

70. Earlier, in 1997, the Council of the OECD adopted recommendations for use of tax identification numbers in an international context and for a standard magnetic format for automatic exchange of information. C(97)29; C(97)30. See detailed discussion in David E. Spencer, "OECD Information Exchange Recommendations Are a Significant First Step in Resolving Tax Evasion," 8 Journal of Int'l Tax'n 353 (1997).

tax treaty.[71] In June 2003, the EU adopted its Savings Directive, providing generally for automatic information exchange on interest paid within the EU to a EU resident, but permitting Austria, Belgium and Luxembourg to impose a withholding tax (as a substitute for automatic information exchange).[72] In 2004, the EU fixed July 1, 2005 as the starting date for the Directive, after reaching agreement with the non-EU countries of Switzerland, Liechtenstein, San Marino, Monaco and Andorra,[73] as well as with the dependent or associated

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71. U.S. Treasury Press Release, KD-3795, January 24, 2003, attaching Mutual Agreement of January 23, 2003, regarding the administration of Article 26 (Exchange of Information) of the Swiss-U.S. Income Tax Convention of October 2, 1996, with Appendix. The treaty provides for the exchange of information "for the prevention of tax fraud or the like." The Mutual Agreement, inter alia, provides some elaboration of the term "tax fraud or the like." See infra note 195.

72. EU Council Directive 2003/48/EC of June 3, 2003, on Taxation of Savings Income in the Form of Interest Payments, released June 26, 2003, available at 2003 WTD 126-12 ["EU Savings Directive"], Art. 8, 9, 10, 11. The rate of withholding would be 15% for the first three years, 20% for the next three years and 35% thereafter. Seventy-five percent of the revenue is to be transferred to the country of residence. Id., art. 11.1, 12.1. See European Commission, IP/03/787, Taxation: Commission welcomes adoption of package to curb harmful tax competition, June 3, 2003, available at 2003 WTD 108-16; see also European Commission, Results of Council of Economics and Finance Ministers, Brussels, 21st January 2003 – Taxation, MEMO /03/13, reprinted in 2003 WTD 15-12. For earlier steps in this process, see Commission of the European Communities, Proposal for a Council Directive to ensure effective taxation of savings income in the form of interest payments within the Community, Brussels, 18.7.2001, COM(2001) 400 final, 2001/0164(CNS), at 3-4 , available at EU website, last visited July 7, 2003 (describing the November 2000 agreement). See discussion in David E. Spencer, "EU Agrees At Last on Taxation of Savings," 14 J. Int'l Tax'n 4 (2003); David E. Spencer, "Stepping Up the Pressure on Tax Havens: An Update (Part 1)," 12 J. Int'l Tax'n 26 (2001); Graetz, supra note 25, at 387-89.

73. See European Commission Release IP/04/958, Savings taxation: Commission welcomes Council Agreement on 1 July 2005 application date, July 19, 2004. The application of the Directive had been conditioned on reaching agreement with these non-EU countries. See EU Savings Directive, supra note 72, Art. 17.2. For the initialing of the agreement with Switzerland, see EU Release IP/04/803, EU-Switzerland: nine agreements to be initialed today, June 25, 2004. See also Chuck Gnaedinger, "EU Delays Start for Savings Tax Directive," 2004 WTD 122-1. For the prior history, see European Commission, IP/03/787, Taxation: Commission welcomes adoption of package to curb harmful tax competition, June 3, 2003, available at 2003 WTD 108-16, at ¶ 13. In that release, the EU Commission described a draft agreement with Switzerland for withholding of tax at the same rate, and under the same revenue sharing terms, as for Belgium, Austria and Luxembourg. The current Swiss withholding tax applies only to Swiss source income, but the agreement would apply the withholding to non Swiss source income. In addition, for "income covered by the draft Agreement, Switzerland [would] grant exchange of information on request for all criminal or civil

territories of the Netherlands and the U.K.,[74] for them to apply the same or "equivalent measures" (such as the withholding tax adopted by Austria, Belgium and Luxembourg) for interest paid to EU residents. In this way, the EU seeks to avoid its Directive merely resulting in capital shifting to other non-EU locations. Austria, Belgium and Luxembourg are required to institute automatic exchange of information only if and when Switzerland and the other non-EU countries listed above agree to an exchange of information regarding all interest, on request, in accordance with the OECD standard, and the U.S. is also committed to such exchange.[75]

II. THE COUNTERVAILING CONCERN FOR PRESERVING FINANCIAL PRIVACY

The argument that the Treasury's proposed regulation (as well the OECD anti-tax haven initiative and the European Union Savings Directive) represent too great a invasion of financial privacy has been forcefully presented by the report of a Task Force on Information Exchange and Financial Privacy, chaired by former Senator Mack F. Mattingly.[76] In order to evaluate this claim,

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cases of fraud or similar misbehavior on the part of taxpayers." On February 10, 2004, the European Commission published the text of a proposed agreement with Switzerland. See "EU Publishes Text of Savings Tax Agreement with Switzerland," 2004 WTD 30-8. On May 19, 2004, Switzerland confirmed "acceptance of [a] 13 May compromise on protecting bank secrecy in Luxembourg and Switzerland in exchange for Swiss participation in the EU savings tax directive." Chuck Gnaedinger, "EU, Switzerland Endorse Bilateral II Framework," 2004 WTD 98-1.

74. For the condition that these territories apply the same or equivalent measures, see EU Savings Directive, supra note 72, Art. 17.2. See Treasurey Department, Isle of Man Government, Taxation Strategy – Exchange of Information, Response to the EU Tax Package, June 10, 2003, reprinted in 2003 WTD 113-15 (Isle of Man will adopt a withholding tax on the same terms as Austria, Belgium and Luxembourg for interest paid to EU resident individuals, assuming all relevant dependent or associated territories and Switzerland and other specified third countries adopt the same or equivalent measures); John Burton & Andrew Parker, "Ultimatum to Caymans on EU tax directive: Caribbean territory urged to comply in crackdown on evasion," Financial Times, Dec. 1, 2003, p.1; Chuck Gnaedinger, "Cayman Islands Commits to EU Savings Plan," 2004 WTD 33-1.

75. EU Savings Directive, supra note 72, at Art. 10.2.

76. Task Force on Information Exchange and Financial Privacy, Report on Financial Privacy, Law Enforcement and Terrorism, March 25, 2002, available at 2002 TNT 65-54; see also Burton, supra note 28. Jack Kemp and former Attorney General Edwin Meese, III, were Senior Advisors to the Task Force. David R. Burton of the Prosperity Institute and the Argus Group was the Excecutive Director. The members of the Task Force were Dr. Veronique de Rugy of the Cato Institute, Stephen J. Entin, of

this part will begin by seeking to identify more specifically what is meant by the term "financial privacy" and why it is valuable.

A. Why We Want Our Financial Information to be Private

Privacy has been defined[77] by one observer as "a limitation of others' access to an individual." Under this approach, "[a] loss of privacy occurs as others obtain information about an individual, pay attention to him or gain access to him."[78] Financial privacy has been described as "about the ability, and what many consider the right, to keep confidential the facts concerning one's income, expenditures, investments and wealth."[79]

Most people, particularly Americans, do not feel comfortable speaking openly about these financial facts about themselves. For example, they do not generally talk about the dollar amount of their salaries or their net worth with friends, acquaintances, co-workers, household help, or their children.[80] Even

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the Institute for Research on the Economics of Taxation, James W. Harper of PolicyCounsel.com and Privacella.org, Dr. Lawrence A. Hunter of Empower America, J. Bradley Jansen of the Free Congress Foundation, Dan Mastromarco, of the Prosperity Institute and Argus Group, Dr. Daniel Mitchell of the Heritage Foundation, Andrew Quinlan of the Center for Freedom and Prosperity, Dr. Richard W. Rahn of the Discovery Institute, Solveig Singleton of the Competitive Enterprise Institute, Mark A. A. Warner, of Hughes, Hubbard & Reed LLP, and John Yoder of Burch and Cronauer. See also Rahn & de Rugy, supra note 6, at ¶¶ 63-68, supporting the Task Force proposals.

77. For an extensive discussion of the ways in which privacy has been conceptualized, see Daniel J. Solove, "Conceptualizing Privacy," 90 Calif. L. Rev. 1087 (2002) at 1099-1125.

78. Ruth Gavison, Privacy and the Limits of the Law, in Philosophical Dimensions of Privacy, ed. by Ferdinand David Schoeman (Cambridge 1984), at 350-51. She goes on to say that "[t]hese three elements of secrecy, anonymity, and solitude are distinct and independent, but interrelated." Id. at 351. See discussion in Solove, supra note 77, at 1104-06, arguing that this definition is too narrow in excluding "invasions into one's private life by harassment and nuisance and the government's involvement in decisions regarding one's body, health, sexual conduct and family life." He further contends that it may not cover some concerns about computer databases, i.e., "subjecting personal information to the bureaucratic process with little intelligent control or limitation, resulting in a lack of meaningful participation in decisions about our information." Id. at 1105 & n.83.

79. Richard W. Rahn, The Future of Money and Financial Privacy, in The Future of Financial Privacy-private choices versus political rules, The Competitive Enterprise Institute, ed. (2000), at 126, 132.

80. See Abby Ellin, "Want to Stop the Conversation? Just Mention Your Finances," The New York Times, July 20, 2003, at Business Section, page 9, noting that her friends renting a beach house together never discuss "salary, savings, or how much

these bare numbers (particularly in light of other information that the listener may already possess) may reveal a great deal about an individual's activities, social status, preferences and personality; and an individual's financial condition, may, justifiably or not, influence others' assessment of his "worth."[81]

Some people may avoid revealing facts about their financial condition out of a desire to avoid blatant comparisons (favorable or unfavorable) with others.[82] Some people may do so to avoid interference with, or scrutiny of, their decisions so as to protect creativity and autonomy[83] (although one commentator has questioned whether such a privacy claim is legitimate as it concerns financial information).[84] Some may fear that political or other enemies will make public revelation of their financial information in a manner designed to humiliate or embarrass.[85] In addition, some are concerned that their wealth

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is owed on the Visa card." She comments, however, that "[p]eople I know in parts of Europe and Latin America say it is common for friends to ask one another about their economic status." She quotes Pamela York Klainer, a workplace consultant, as saying that "Americans, over all, are far too secretive about money topics." Id.

81. Marc Linder, "Tax Glasnost for Millionaires: Peeking Behind the Veil of Ignorance Along the Publicity-Privacy Continuum," 18 N.Y.U. Rev. L. & Soc. Change 951, 971 (1990/1991). He states that "in the United States a person's income level plays a crucial part in determining 'worth,' that is, others' estimation of her economic, social and moral value as a human being and in turn shapes her self-worth and self-image." Id. He explains that his article "challenges the underlying reality and desirability of this set of interlocking assumptions." Id.

82. Ellin, supra note 80. Ms. Ellin quotes a Silicon Valley worker as saying, "Showing off one's fancy car, P.D.A. with integrated MP3 player, summer house, or throwing an elaborate party, is a classier way of communicating monetary status." Id.

83. See Julie E. Cohen, "Examined Lives: Information Privacy and the Subject as Object," 52 Stanford L. Rev. 1373 (2000), at 1424-25, arguing that "Autonomy in a contingent world requires a zone of relative insulation from outside scrutiny and interference – a field of operation within which to engage in the conscious construction of self." She explains that "[t]he opportunity to experiment with preferences is a vital part of the process of learning, and learning to choose, that every individual must undergo."

84. See Linder, supra note 81, at 973-74, arguing that: "If the ethical, cognitive and moral developmental underpinnings of personhood are made the focus of a right to privacy, then it becomes very difficult to apply a protective shield to such mundane material matters as income." He further notes "[t]he incongruity inherent in assimilating the annual results of the most successful individual encounters with mammon with the more ethereal aspects of personhood qua sanctuary." Id. at 974.

85. See Solove, supra note 77, at 1145, arguing that "there is no overarching value of privacy," but that "we must focus specifically on the value of privacy within particular practices." He notes that "one of the most important reasons for protecting privacy is to prevent stifling exercises of power employed to destroy or injure individuals." Id. at 1149. Solove gives as an example General Motors' "campaign of harassment, surveillance, and investigation" of Ralph Nader. See id. at 1149-51.

makes them susceptible to requests for donations, or gifts to friends or family, or raises for employees. Many may seek to avoid commercial solicitations, e.g., by purveyors of luxury goods or investment management.[86] There may also be a fear that information about the amount of their wealth may make the wealthy a target of thieves, scam artists, or other criminals, including kidnappers seeking a ransom.[87] Disclosure of financial information may facilitate identity theft, or may allow advantage to business competitors.[88] Finally, information about an individual's assets allow creditors to enforce monetary obligations, such as contractual debts, tax liability, obligations of support, tort liability or criminal fines.[89]

Detailed information about an individual's receipts or expenditures (i.e., the amount, timing, name of payee or payor) may reveal considerable additional information about a person's activities, material possessions, spending or saving habits, obligations, occupation, abilities, associations, beliefs, interests, and personality. For example, a record of expenditures could include payments to a political party or charity, payments for a particular brand of clothing or auto, payments of child support or alimony or of a gift, payment of a mortgage, or payment for an airline ticket or for a hotel in a particular location.[90] Justice Douglas, dissenting in California Bankers Ass'n v. Schultz,

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86. For example, lottery winners, whose accession to wealth is publicly announced, often face these concerns. See, e.g., Peggy Y. Lee, "Lotto Pots Hold Joys, Trials for Big Winners," Los Angeles Times, Jan. 25, 1993, at B1; Roy Bragg, Winning & losing; scam artists, jealous neighbors and lousy investments – what's so great about hitting the lottery, anyway?" San Antonio Express-News, August 9, 2003, p. 10H; Tina Moore, "Experts Tell Lottery Winners to Protect their Privacy First," Pittsburg Post-Gazette, Dec. 29, 2002, pg. C-3.

87. See e.g., R.Posner, The Economics of Justice 234-35 (1983), suggesting that people "conceal an unexpectedly high income to avoid the attention of tax collectors, kidnappers, and thieves; [and] fend off solicitations from charities and family members," cited by Linder, supra note 81, at 970-71.

88. See Joint Committee on Taxation, Study of Present-Law Taxpayer Confidentiality and Disclosure Provisions as Required by § 3802 of the IRS Restructuring and Reform Act of 1998, JCS-1-00, Volume 1, reprinted in 2000 TNT 21-8, at ¶ 362 [hereinafter 2000 JCT Report]. See also Peter P. Swire, Financial Privacy and The Theory of High-Tech Government Surveillance, 77 Wash. U. L. Q. 461, 470 (1999), noting that making financial transactions "highly traceable" increases the risk of "identity theft."

89. For discussion of the use of offshore asset protection trusts to prevent creditors from reaching assets, see Stewart E. Sterk, "Asset Protection Trusts: Trust Law's Race to the Bottom?" 85 Cornell L. Rev. 1035 (2000).

90. Thus, one might be able to determine to what "groups and associations. . . the individual belongs. . . the social causes the individual supports. . . books and publications an individual buys. . . and the material items an individual purchases."

416 U.S. 21 (1974), stated that "the banking transactions of an individual give a fairly accurate account of his religion, ideology, opinions and interests."[91]

B. How Financial Institutions Serve as Necessary Stewards of Financial Information

Financial privacy can never be absolute because institutions, such as banks, credit card companies, and brokerage firms that assist individuals in the conduct of their financial transactions necessarily have access to financial information about their customers. Most individuals (particularly those with greater income) utilize such institutions as intermediaries to conduct financial transactions despite the loss of privacy entailed. They do so because of the practical benefits that these institutions offer.[92]

In addition, the loss of privacy may seem relatively tolerable because of limitations on the "degree of accessibility" of the financial information.[93] Knowledge on the part of the employees of a financial institution seems relatively unobtrusive because of the fact that one's contact with the employees is purely on a business level, and for a particular purpose, and may take place over the phone, by mail or internet (rather than in person). One does not expect to see or deal with these employees in any other role or context, and although they know your name, they have no particular interest in knowing any details about your life. Entertainers, politicians, athletes and other who are publicly

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Kleiman, supra note 49, at 1176, citing David F. Linowes, Privacy in America: Is Your Private Life in the Public Eye? (1989) at 103.

91. California Bankers Ass'n v. Schultz, 416 U.S. 21, 85 (dissenting opinion). Some financial records might allow "interested observers to recreate a financial 'snapshot' of the individual [by reference to stocks and bonds, insurance, real estate, retirement funds, cars, homes, personal property, mortgage loans, alimony, and child support." Kleiman, supra note 49, at 1176, citing David F. Linowes, Privacy in America: Is Your Private Life in the Public Eye? (1989) at 103. In addition, through credit cards, one "can trace individuals in their every physical movement – to different countries, states, or cities, and even to restaurants, to stores, to airline travel, and to hotels." Id.

92. See generally, Michael S. Barr, Banking the Poor, 21 Yale J. on Regulation 121 (2004), at 135-42 (disadvantages of being unbanked).

93. "Perfect privacy" in the sense of complete "secrecy [or] anonymity" is not attainable. See Gavison, supra note 78, at 351. Therefore, issues of privacy involve the appropriate "degree of accessibility of information." Solove, supra note 77, at 1152. As explained by Professor Anita Allen, "[i]nformational privacy obtains where information actually exists in a state of inaccessibility." The idea that privacy consists of control over one's own personal information does not take into account that some people exercise that control by "making themselves informationally and physically more accessible to others." Anita L. Allen, Commentary: Privacy-as-Data Control: Conceptual, Practical and Moral Limits of the Paradigm, 32 Conn. L. Rev. 861, 868-69 (2000).

known obviously cannot rely on anonymity to shield them from scrutiny. They may perhaps prefer to rely on private banking arrangements that include extra safeguards for their privacy.

Secondly, one may assume that the bank will not share the information with others.[94] In order to make the use of a bank palatable to potential customers, bankers generally have a tradition or practice of maintaining the confidentiality of customer information.[95] Some courts have recognized an implied contract of confidentiality, though subject to exceptions,[96] including one for "legitimate law enforcement inquiry."[97] In other countries, such as Switzerland, this tradition has been even stronger.[98] As we have seen, in the U.S. information in financial accounts is directly accessible to the federal government, particularly the IRS, by a number of methods.[99]

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94. Thus, it has been noted that "our financial records are commonly understood as private matters even though third-parties may have access to (or even possess) that information." Solove, supra note 77, at 1152. He goes on to say: "We expect privacy because we do not expect unauthorized persons to delve through this information. Indeed, we often share information in various relationships, such as those between attorney and client. . . In contrast to the notion of privacy as secrecy, privacy can be understood as an expectation in a certain degree of accessibility. This is not the only way to conceptualize privacy, but it is more appropriate as an account of modern practices, where cumulatively, we disclose a tremendous amount of data in various settings and transactions." Id.

95. See ACLU Feature, Defending Financial Privacy, available at http://archive.aclu.org/issues/privacy/Financial_Privacy_feature.html. The ACLU webpage states that "[f]or centuries, bankers used to pride themselves on being discreet and confidential about their customers' business. But today that tradition. . . is breaking down. . . ." Id.

96. See Robert S. Pasley, Privacy Rights V. Anti-Money Laundering Enforcement, 6 N.C. Banking Institute 147, 174-90 (2002) (discussing the case law). In Tournier v. National Provincial and Union Bank of England, 1 K.B. 461 (1934), an English court found that nondisclosure was "an implied term of the contract," but with various exceptions. See Pasley, supra, at 174. An Idaho court found an agency relationship resulting in a "duty to the customer not to use or communicate information confidentially given him by the customer." Peterson v. Idaho First Nat'l Bank, 367 P. 2d 284, 289-90 (Idaho 1961), described in Pasley, supra, at 175-76.

97. Indiana National Bank v. Chapman, 482 N.E. 2d 474, 482 (Ind. Ct. App. 1985), quoted in Pasley, supra note 91, at 181.

98. See Erich I. Peter, "Reasonable Limits of Transparency in Global Taxation: Lessons from the Swiss Experience," Tax Notes Int'l Magazine, Nov. 11, 2002, 591, at 615-16.

99. See supra notes 44-52 and accompanying text. In U.S. v. Miller, 425 U.S. 435 (1976), the U.S. Supreme Court held that a bank depositor "takes the risk, in revealing his affairs to another, that the information will be conveyed by that person to the Government," and that the obtaining of those records by the U.S. Attorney's office

Recently, many have expressed concern that banks and other financial institutions in which they have accounts have been selling their personal information to others and that legislation adopted by Congress in 1999 that addressed this privacy issue was not sufficiently protective.[100] Concerns that have been raised about this type of information sharing are that it "leads to annoying telemarketing calls, e-mail spam, and other unwanted marketing. . . increases the power and leverage of insurance companies and other big corporations over individuals. . . makes it easy for companies called data aggregators to compile huge dossiers of detailed information about American citizens. . . and allows personal information to be gathered by the government."[101]

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by a grand jury subpoena was not an "intrusion upon the depositors' Fourth Amendment rights." In reaction to that decision, Congress enacted the Right to Financial Privacy Act of 1978. 12 U.S.C. 3401-22. See discussion in Kleiman, supra note 49, at 1187-90. However, the limitations contained in this statute do not apply to an IRS summons. See U.S. v. MacKay, 608 F. 2d 830, 834 (10th Cir. 1979). See supra note 49.

100. See ACLU Feature, Defending Financial Privacy, available at http://archive.aclu.org/issues/privacy/Financial_Privacy_feature.html. The ACLU webpage states that the "tradition" of bankers' maintaining confidentiality "is breaking down. . . . The problem lies not just with banks, but also insurance companies and many other corporations who gather details about the financial lives of Americans, and increasingly see those details as a valuable resource to be mined for profit." Id. The Gramm-Leach Bliley Act, enacted in 1999, provided in Title V for certain privacy protections for the customers of financial institutions. These protections largely take the form of requiring the financial institution to provide notice of its information-sharing practices and offering an opportunity to opt-out of sharing of information with non-affiliates. See Statement of Mr. Edmund Mierzwinski, Consumer Program Director, U.S. Public Interest Research Group, Sept. 19, 2002, before Senate Banking, Housing and Urban Affairs Committee, available in Lexis, Federal Document Clearing House Congressional Testimony. The legislation, however, allowed states to adopt stronger privacy requirements. Alaska, Connecticut, Illinois, Maryland, Vermont, and North Dakota have stricter rules. In June 2002, more than 70% of voters on a ballot measure in North Dakota in effect reinstated stricter state protections requiring that consumers "opt-in" before certain information is shared. Id. See ACLU Congratulates People of North Dakota for Defending their Privacy, June 12, 2002, Press Release, available on ACLU website. See also Statement of Professor H. Cate, Indiana University School of Law, Sept. 19, 2002, before Senate Banking, Housing and Urban Affairs Committee, available in Lexis, Federal Document Clearing House Congressional Testimony, noting that "[t]he available published information indicates that fewer than 5 percent of consumers responded to the deluge of notices [required by July 1, 2001, under the Gramm-Leach legislation] by opting out of having their financial information shared with third parties." Id.

101. ACLU Feature, Defending Financial Privacy, available at http://archive.aclu.org/issues/privacy/Financial_Privacy_feature.html.

C. How Congress has also made the IRS a Custodian of our Financial Information

Despite their desire for financial privacy, Americans not only choose to utilize financial institutions (which thus obtain access to financial information) but also tolerate massive collection of financial information by the IRS.[102] This information includes not only the source and amount of an individual's income but also information about expenditures that may form the basis for various deductions and credits. For example, one's Form 1040 may show the amount of interest paid on a home mortgage, the amount of alimony paid, the amount one has given to particular charities, the dependents living in one's household, gambling winnings and losses, the amount of loans to friends or relatives that have become worthless, amounts spent for childcare, tuition, business entertainment, or medical expenses. This information obviously may reveal a great deal about the taxpayer's activities and personality.[103]

Collection of such information by the IRS is presumably accepted because it is necessary to the enforcement of the tax system that Congress has enacted. Since the adoption of the 16th Amendment in 1913, the Congress has consistently imposed on U.S. citizens and residents an obligation to pay income taxes annually. Congress has defined "gross income" in section 61 of the Internal Revenue Code as including "all income from whatever source derived, including . . . compensation for services. . . gross income derived from business . . . gains derived from dealings in property. . . interest. . . rents. . .royalties. . .

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102. Dan Mitchell, Ph.D, Tax Reform: The Key to Preserving Privacy and Competition in a Global Economy, Policy Report 171, Feb. 2002, IPI (Institute for Policy Innovation), available online at http://www.ipi.org. Mitchell states that "the personal income tax requires individuals to either disclose or make available upon demand almost every shred of their personal financial data to the Internal Revenue Service. . . Individuals have to reveal their personal savings, their financial assets, their personal wealth, their profits and losses, and other intimate details of their existence." Id. at 1. He further notes that "Divulging private data to the government. . . is a compulsory activity that will result in the loss of income and/or assets." Id. See 2000 JCT, supra note 88, at ¶¶ 35-42, 357-59, at ¶ 357, stating that "Through the filing of tax returns, information received from third parties, and its own audits and investigations, the IRS has 'a data source of unparalleled detail and completeness.'"

103. See Privacilla.org, Assessing Threats to Privacy: The Government Sector – Greatest Menace to Privacy By Far (September 2000) [hereinafter "Privacilla report,"] at 7, stating that "when Americans file tax returns with the [IRS], they must reveal a great deal of personal information, much of which is private or at least sensitive. . . . [including] name, address, phone number, Social Security number, income, occupation, marital status, parental status, investment transactions, home ownership, medical expenses, foreign assets, charitable gifts. . . . If anyone ever needed to compile a dossier on our behavior, the IRS would be a good place to start."

dividends . . .alimony. . . annuities. . .pensions. . . income from discharge of indebtedness." In addition, Congress has determined that a variety of "personal" deductions (e.g., for charitable contributions or medical expenses) should be permitted.[104]

Given such an income tax system, it seems to be a necessary corollary that the IRS should have access to financial information regarding each potential taxpayer. Denying the IRS such access would mean that taxpayers would essentially be on the "honor system." A taxpayer would, in the privacy of his or her home, determine his sources of income and his deductions and credits, apply the rules of the Code, compute the tax, and send to the IRS merely a check for the amount of his self-computed tax liability; the only job of the IRS would be to deposit the check and perhaps offer the taxpayers a reminder of when the check is due. There would be no way for the IRS to verify the accuracy of the amount computed as tax liability of the taxpayer.

Obviously, this would not be a practical way for Congress to raise revenues. There would be no motive other than a sense of patriotism for a taxpayer to compute his own tax accurately; even a patriotic citizen might well hesitate to pay the correct amount of tax when he knew that many other taxpayers would not do the same. Therefore, it seems inevitable that Congress would establish a method by which the correct amount of a taxpayer's tax liability would be verified and, if necessary, collected by the IRS. Apart from administering a lie detector test to each taxpayer to determine if his computation of tax was at least intended to be accurate, the IRS can verify the accuracy of the tax liability only by obtaining information about all the taxpayer's items of income and all his expenditures eligible for deduction or credit.

To this end, Congress has required that each taxpayer file a tax return annually, which lists his income by source and also lists his allowable deductions and credits.[105] Congress has sought to insure that the taxpayer provides information that is accurate and complete by imposing civil or criminal penalties for a taxpayer's failure to do so.[106] But if a taxpayer's failure to provide accurate information is to be detected, the IRS must have some other

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104. See id., stating that "the list [of personal information provided to the IRS] is very, very long because politicians are addicted to social engineering through tax policy."

105. IRC § 6012.

106. If the taxpayer willfully makes statements on the return that she does not believe to be true and correct as to every material matter, she is guilty of a felony (and subject to a fine of not more than $100,000 and/or imprisonment of not more than 3 years). IRC § 7206(1). This assumes that the return contains a written declaration that it is made under penalties of perjury, which the current Form 1040 does. The Code also provides civil penalties for inaccuracy. IRC §§ 6662 and 6663.

source of the relevant information for comparison with the information provided by the taxpayer.

A very important source of information for the IRS is the requirement, imposed by Congress, that many types of payments, most notably, wages, dividends, interest, unemployment compensation, and gross proceeds of security sales, be reported by the payor or broker to the IRS (as well as to the taxpayer).[107] This allows the IRS to run a very efficient check of these items for many or all taxpayers, without making any prior determination that a particular taxpayer is suspected of having filed inaccurately. The taxpayer, knowing that the IRS has a ready source of information for checking his tax return (and having also received the same information from the payor), has very little incentive to provide other than accurate information on his return. Thus, the GAO has estimated that for 1992 taxpayers reported on their returns 99.1% of their true net income from wages, 97.7% of their true net income from interest, 92.2% for dividends and 92.8% for capital gains.[108]

Congress has given the IRS a further means of verifying information provided by a taxpayer about whose return the IRS has suspicions. Even though the IRS does not have probable cause to believe that a wrongdoing has occurred, the IRS has authority to examine books or records which may be relevant to determining a taxpayer's liability and to serve a summons on the taxpayer or other persons to produce such books or records, or to give testimony under oath relevant to such determination. The U.S. District Court is authorized to compel compliance with the summons and to use the contempt power toward this end.[109]

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107. See supra note 44.

108. Joel Slemrod & Jon Bakija, Taxing Ourselves: A Citizen's Guide to the Great Debate over Tax Reform (2d ed. MIT Press 2000), Table 5.1, id., at 154, showing GAO compliance estimates for certain types of personal income in 1992. By contrast, the percentages are 18.6% for "informal suppliers" and 67.7% for other sole proprietors. Slemrod & Bakija note that "[f]or types of income subject to information reporting, and especially for those with tax withholding at the source of payment, evasion is much less prevalent." Id. at 160-61. They also note that "[e]ach year, the IRS receives one billion information reports, most of them on magnetic tape or transmitted electronically." See id. at 157 & n. 50, citing IRS Data Book, 1997, Table 19.

109. IRC §§ 7602 and 7604. See supra notes 48 and 99. The U.S. Supreme Court discussed the standard that must be met by the IRS for enforcement of a summons in United States v. Powell, 379 U.S. 48 (1964). It explained that the Commissioner "need not meet any standard of probable cause to obtain enforcement of his summons . . . . he must show that that investigation will be conducted pursuant to a legitimate purpose, that the inquiry may be relevant to the purpose, that the information sought is not already within the Commissioner's possession, and that the administrative steps required by the Code have been followed." Id. at 57-58. "The Powell standards have been liberally construed by U.S. courts and as a result banks routinely comply with IRS

In sum, Congress in imposing an income tax, recognized that its enforcement required that the IRS have detailed knowledge of a taxpayer's financial affairs, and Congress provided the IRS with the tools to obtain that information. Thus, it seems fair to say that our current tax system simply does not contemplate that an individual should be able to exclude the IRS from knowledge about his financial affairs.[110] The IRS's access to financial information of individuals is essential not only to enforcement of the income tax, but also to the citizenry's efforts to monitor and debate the government's tax policy. Knowledgeable debate of the income tax requires knowing the

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summons without requiring judicial enforcement." OECD Bank Report, supra note 45, Appendix I, ¶ 3.2. For further discussion of the *Powell* decision, see Camp, supra note 47, at 53-59. In reviewing the Supreme Court's interpretations of § 7602, Camp concludes that "the Supreme Court has consistently interpreted the Service's summons power expansively, using inquisitorial logic. . . [meaning that] the Court based its decision on one or more of the following rationales: (a) an expansive interpretation was necessary to preserve the Service's role as decision-maker or evidence-gatherer; (b) Truth trumped Autonomy as the value promoted by the statute; and (c) potential abuse should be or was actually limited through internal bureaucratic controls." Id. at 53.

110. For example, Professor Anita Allen explained: "[I]t might seem innocuous to make the assertion that people should be able to control personal financial data, until one realizes that our political obligations to our country and fellow citizens make that impossible. As James Rule and Lawrence Hunter have observed, 'if governments are expected to tax income or commerce. . . citizens can hardly expect control over information about their personal finances.'" Anita Allen, supra note 93, at pp. 7-9, n. 46, citing James Rule & Lawrence Hunter, Towards Property Rights in Personal Data, in VISIONS OF PRIVACY: POLICY CHOICES FOR THE DIGITAL AGE, at 168, 169-70 (Colin J. Bennett & Rebecca Grant eds., 1966). See also Swire, supra note 88, at 485, noting that "[t]he government has a strong interest in receiving data relevant to its financial affairs, such as collection of taxes and distribution of benefits. . . . For the government, when collecting taxes, access to financial records helps correct for the sometimes overwhelming human temptation not to pay all of the taxes due by law. . . . The[se] arguments do not give a reason, however, for the IRS. . . to share information with agencies that do not need the information to assist in the government's financial affairs." Id. at 486. Another reason for rejecting a citizen's claim to conceal sources of income from his own government is that the government through its "massive. . . economic-protective intervention in the form of infrastructure, government contracts, regulation, licensing, and insurance," is already "involved" in one's financial affairs. Linder, supra note 81, at 974-75. See also Camp, supra note 47, at 16, arguing that "in order to maintain a voluntary tax reporting system, the government must have access to enough information about the taxpayer's transactions to monitor, verify, and enforce the law."

extent to which the income tax is, in fact, paid by those that the Code purports to tax.[111]

Concern for open public debate and government accountability has led some to conclude that not only the government, but even one's fellow citizens should have access to the information on one's tax return.[112] For example, in the 1920's and 1930's, the Progressives sought to institute public inspection of tax returns.[113] However, the view that tax returns should be made public has not prevailed (although tax return information does become public when a taxpayer challenges the IRS determination of his tax liability in the Tax Court).[114] Congress has recognized that taxpayers have an important interest in the privacy of the financial information about them collected by the IRS[115] even

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111. See Julie Roin, "Competition and Evasion: Another Perspective on International Competition," 80 Geo L. J. 543 (2001), at 599-600, discussing the importance of "transparency" and how "self-help methods of tax reduction made available through the use of tax havens" are an obstacle to making "[p]ublic officials. . . properly accountable for their actions." See further discussion at infra notes 201-02 and accompanying text.

112. See Linder, supra note 81, recommending that the tax returns of millionaires be made public to foster public debate about income disparities and redistribution. He argues that this "would vindicate the principle that in a highly interdependent economy and a democratic state 'there should be no secrecy in the transactions between any citizen and his Government.'" Id. at 976 & n.157, quoting 67 Cong. Rec. 892 (1925) (statement of Rep. Griffin). For a recent proposal for disclosure of corporate returns, see Theodore S. Sims, "Corporate Tax Returns: Beyond Disclosure," 96 Tax Notes 735 (July 29, 2002). He suggests that such disclosure "could pave the way for bringing non-governmental energies to bear on the effort to police corporate tax shelters, through a system of rewards to private auditors who brought such schemes to light and to heel." Id.

113. See Linder, supra note 81, at 962-65. He notes that "for two decades after 1913, Progressives in Congress used the enactment of every revenue act to debate the issue of publicity of income tax returns." Id. at 963. For further discussion of this history, see Marjorie E. Kornhauser, "More Historical Perspective on Publication of Corporate Returns," 96 Tax Notes 745 (July 29, 2002) (describing debates of 1934-35).

114. See generally, Diane M. Ring, "On the Frontier of Procedural Innovation: Advance Pricing Agreements And The Struggle to Allocate Income For Cross Border Taxation," 21 Mich. J. Int'l L. 143 (Winter 2000), at 208, noting that "[i]n litigation,. . . most taxpayer information may be released in the form of court opinions and other litigation documents." She explains that one reason for this is "a powerful vision about the importance of a public judicial process, as well as the likelihood that taxpayer data revealed in a case will usually be at least several years out of date."

115. By contrast, Linder argues that, at least as far as the tax returns of millionaires are concerned, "no legitimate privacy interest exists that would require accommodation." Linder, supra note 81, at 969. His article begins with the following quotation: "As far as taxation is concerned, there ought to be nothing 'private' about the

though that interest must yield when it conflicts with the government's need to accurately determine and collect the income tax.

Thus, Congress has adopted a compromise position. The IRS may have access to financial information required to enforce the tax; however, since 1976,[116] Congress has declared in IRC section 6103[117] that tax return information "shall be confidential" and may not be disclosed by the IRS except in certain situations expressly defined in the statute.[118] Confidentiality is viewed not only as a taxpayer's entitlement in light of the compulsory nature of the

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amount of any man's income, or the aggregate of all forms of his property, inasmuch as every man has a right to know, that all his neighbors are contributing pro rata with himself to support that Government, which is common to him and them. . . . [L]east of all should there be anything private in the matter of public taxes, since in bearing up the burdens of Government all the citizens are like copartners, and. . . for this purpose each has a right to demand a look into the books of all the others." A. Perry, Principles of Political Economy 552 (1890), quoted in Linder, supra note 81, at 951.

116. Prior to 1976, tax returns were formally classified as "public records," subject to disclosure by the order of the President or pursuant to regulations approved by him. See 2000 JCT Report, supra note 88, at ¶¶ 754-776, discussing the history from 1862 through 1975. The degree of actual disclosure varied. The Revenue Act of 1924 called for public lists with the taxpayer's name, post office address, and the amount of tax paid. Id. at ¶ 766. But the Revenue Act of 1926 eliminated the listing of the amount of tax paid. Id. at 768. The Revenue Act of 1934 called for a taxpayer's gross income, total deductions, net income and tax payable (shown on a so-called "pink slip") to be open for public inspection but "Congress repealed the provision before it took effect." Id. at ¶ 770. The requirement of public lists was repealed in 1966. Immediately prior to 1976, "the regulations provided access to returns and return information for persons with material interest. . . the heads of departments for official business upon written request detailing why inspection was necessary, and use in legal proceedings where United States was a party to the proceedings." Id. at 774. For further discussion of this history, see Linder, supra note 81, at 961-66; Kornhauser, supra note 113; Joe Thorndike, "Historical Perspective: Promoting Honesty by Releasing Corporate Tax Returns," Tax Notes, July 15, 2002, p. 324; Richard D. Pomp, "The Disclosure of State Corporate Income Tax Data: Turning the Clock Back to the Future," 22 Capital U. L. Rev. 374 (1993).

117. For a detailed discussion of IRC § 6103, its background, and subsequent amendments, see 2000 JCT Report, supra note 88, at ¶¶ 754-844. For a similar view that the government should act as "confidante and not broadcaster," see Allen, supra note 93, at 874, referring to the court's interpretation of the Freedom of Information Act in Wine Hobby USA, Inc. v. United States, 502 F.2d 133 (2d Cir. 1974).

118. For a thorough description of these authorized disclosures, see 2000 JCT Report, supra note 88, at ¶¶ 38-153. One authorized disclosure is for statistical use of information in anonymous form. See I R C § 6103(j).

disclosure on the tax return,[119] but also as a necessary precondition if the taxpayer is to feel comfortable making full disclosure on his return.[120]

Congress apparently believed that citizens would generally feel secure in providing financial information to the IRS if the information would be held in confidence and used for the sole purpose of collecting taxes.[121] The taxpayer would find assurance in the fact that the employees in the IRS having access to the information are strangers, anonymous bureaucrats in unfamiliar places, such

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119. "Taxpayers have a justifiable expectation of privacy in the extensive information they furnish to the IRS under penalty of fine or imprisonment." 2000 JCT Report, supra note 88, at ¶ 359. See Joint Committee on Taxation, General Explanation of the Tax Reform Act of 1976 (December 29, 1976), at 314-315, explaining that: "Questions were raised and substantial controversy created as to whether the extent of actual and potential disclosure. . . to other Federal and State agencies for non-tax purposes [under prior law] breached a reasonable expectation of privacy on the the part of the American citizen with respect to such information. This, in turn, raised the question of whether the public's reaction to this possible abuse of privacy would seriously impair the effectiveness of our country's very successful voluntary assessment system, which is the mainstay of the Federal tax system. . . . . With respect to each of the [areas in which disclosure was permitted], the Congress strove to balance the particular office or agency's need for the information involved with the citizen's right to privacy and the related impact of the disclosure upon the continuation of compliance with our country's voluntary tax assessment system." See also Nina E. Olson, "Sugarman Lecture: The Relationship between the Taxpayer and her Government," available in 2003 TNT 202-34, at ¶ 16, stating that "taxpayers have a right to expect that information related to their tax affairs is confidential and used for tax administration purposes only."

120. See 2000 JCT Report, supra note 88., at ¶¶ 359-361, citing Statement of Senator Haskell, 122 Cong. Rec. S 12589 (July 27, 1976). See supra note 119. The JCT Report notes that "one study showed an increase in nonfiling by those taxpayers whose refunds had been offset for child support the year before." Id. at ¶ 361. But it notes that a 1991 GAO study concluded that "these results may have been overstated." Id. at n. 542. For the view that publicity of corporate tax returns could lead to more complete enforcement, see Sims, supra note 112.

121. In part, this may because the taxpayer sees a practical benefit in revealing information that will permit claiming a deduction or credit. But in general, the disclosure of information to the IRS on a tax return is not only compulsory (with little room for bargaining) but also without direct benefit to the taxpayer. See Letter by James W. Harper, Editor, Privacilla.org, to Subcommittee on Commercial and Administrative Law, House Judiciary Committee, May 24, 2002, available online at Privacilla.org, at 2, noting that "[b]usinesses may lose customers if they ask for too much information . . . . Governments, on the other hand, can demand information on tax forms,. . . without losing 'customers' if they collect too much." He also explains that "[u]nlike businesses, governments do not lose the value of information they hold if they abuse it. . . . So, where a business must make tactful and intelligent use of scarce information, a government has few similar incentives." Id. at 2. See also Privacilla Report, supra note 103, at 10.

as Holtsville, NY, whom the taxpayers do not expect to see or deal with in any other role or context. Although an IRS employee handling a taxpayer's return may know the taxpayer's name, the taxpayer would expect that the IRS employee has no particular interest in knowing any of the details of the taxpayer's life (except to carry out the employee's duties). By contrast, a taxpayer would likely be outraged if his own financial information were disclosed publicly or used by IRS employees, or their friends or superiors, to satisfy curiosity, to achieve financial[122] or political advantage, or to oppress disfavored groups.

The danger that tax return information will be misused has been magnified by the advent of the computer.[123] In the 1990's, Congress received much evidence[124] that IRS employees were perusing tax records of friends,

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122. See Swire, supra note 88, at 493-94, discussing how government officials with a database of financial information might use such information for "financial gain." First, the information "might reveal confidential business information or otherwise give officials an advantage in choosing their own investments." Second, "officials might get money from people who do not want their financial transactions revealed." This could take the form of their being bribed or their practicing extortion. Third, they "might benefit financially by sharing the data with outside parties," with whom they might make a joint investment.

123. See generally Kleiman, supra note 49, at 1177, stating that "modern advances in computer technology and use have escalated the potential for abuse [by governmental prying] in exponential degrees."

124. In 1993, an internal IRS report, showing that 350 employees had improperly accessed tax accounts through the IRS's Integrated Data Retrieval System led to a hearing before the Senate Governmental Affairs Committee, chaired by John Glenn, D-Ohio. See Rita L. Zeidner, "Lawmakers Blast Service for Confidentiality Breaches," 93 TNT 163-48; Stephen Barr, "Probe Finds IRS Workers Were 'Browsing' in Files; Computer Security Review Points to Fraud," Washington Post, August 3, 1993, page A1; Stephen Barr, "Glenn Calls IRS Lax on 'Browsing;' Senator Says Agency Was Aware of Risk," Washington Post, August 4, 1993, page A4; Stephen Barr, "Accused of Failing to Protect Data, IRS Says It Will Buttress Safeguards, Washington Post, August 5, 1993, page A6; Editorial, "Snoops (and Crooks) at the I.R.S.," New York Times, August 5, 1993. A follow-up hearing in July 1994 showed that in the previous 10 months more than 500 such cases were investigated by the IRS. The IRS installed an Electronic Audit Research Log, in an effort to monitor employees. Stephen Barr, "1,300 IRS Workers Accused of Snooping at Tax Returns; Employees Used Computers to Peek at Friends' Files," Washington Post, July 19, 1994, page A1; see also Robert D. Hershey Jr., "I.R.S. Staff Is Cited in Snoopings," New York Times, July 19, 1994, page D1; Stephen Barr, "IRS Vows 'Zero Tolerance' For Snooping in Tax Records; Budget Cut Could Delay Computer Safeguards," Washington Post, July 20, 1994, page A4. Nevertheless, in 1997, the GAO concluded that the "IRS is not effectively addressing electronic browsing." See GAO Testimony before the Subcommittee on Treasury and General Government, Committee on Appropriations, United States Senate, Statement

enemies, acquaintances, relatives or celebrities.[125] Congress responded by enacting the Taxpayer Browsing Protection Act of 1997. This legislation makes unauthorized inspection of a tax return by an IRS employee a criminal offense, if willful, and also authorizes a suit for civil damages.[126] This has apparently not

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of Dr. Rona B. Stillman, Chief Scientist, Computers and Telecommunications Accounting and Information Management Division, April 15, 1997, reprinted in 97 TNT 73-42. See Robert D. Hershey Jr., "Snooping by I.R.S. Employees Has Not Stopped, Report Finds," N.Y. Times, April 9, 1997, page 16A; John Godfrey, "IRS Finds More Cases of Browsing, Falls Short on Sanctions," 97 TNT 68-2; Editorial, "Tax Snoops," The Washington Post, April 10, 1997. See also Statement of Laurence Summers, Deputy Treasury Secretary, before the Subcommittee on Treasury, General Government, Civil Service, Committee on Appropriations, U.S. Senate, April 15, 1997, 97 TNT 73-39, acknowledging that the IRS policy against browsing "was NOT effectively designed or implemented and penalties are neither sufficiently consistent nor severe to put an end to unauthorized access." See also discussion of IRS browsing in Swire, supra note 88, at 495.

125. In a statement before the Senate Finance Committee, an unidentified GS 12 Revenue Officer stated that he had personally witnessed browsing "to check on prospective boyfriends," browsing to see if ex-husbands had increased income available to pay child support, browsing with respect to taxpayers "with whom IRS employees were having some kind of personal disagreement," browsing of records of "locally prominent or newsworthy individuals, public figures – even team coaches," browsing "out of simple curiosity about a friend, a relative or an employee's neighbor" or accessing information on "individuals who are perceived as critical of the IRS." In addition, the witness said that he had seen cases of institutional abuse, such as accessing tax records of potential witnesses or jurors in tax cases. Unofficial Transcript of Finance Hearing on IRS Abuses, September 25, 1997, 97 TNT 191-52, Witness #3, at ¶¶ 191-203.

126. Public Law 105-35, signed into law on August 5, 1997. The Act added new IRC § 7213A imposing a criminal penalty of a fine not to exceed $1,000 or imprisonment of not more than one year, or both. The Act also added new IRC § 7431 providing civil damages; in addition, this provision requires the IRS to notify a taxpayer if an employee is criminally charged with unauthorized inspection of the taxpayer's return. Section 7431(e). See H. R. Rep. No. 105-51, April 14, 1997, reprinted in 97 TNT 74-16; Herman Ayayo, "President Signs Anti-Browsing Bill," 97 TNT 153-2.

put an end to such browsing,[127] and Congress continues to debate further measures to combat it.[128]

Most cases of unauthorized browsing by IRS employees that have been investigated have apparently not involved fraud.[129] However, the potential for malicious attacks on the IRS computer systems by outside hackers, including attacks designed to perpetrate identity theft, does exist. Accordingly to a report recently submitted to Congress, the IRS has made considerable progress in improving the security of its computer systems, but serious vulnerability is still present.[130]

The possibility that the White House might conspire to misuse information held by the IRS, e.g., to harm political enemies,[131] was a focus of

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127. In the two years following the statute's enactment, the Treasury substantiated 198 cases of unauthorized browsing. 2000 JCT Report, supra note 88, at n. 778 and accompanying text. The reports states that these cases involved the following kinds of employees: "auditors and tax examiners (77), collection (48), Taxpayer service (31), clerical (19), Criminal Investigation Division (3), Management (6), Professional/Technical (2) and other (12)." Id.

128. In 2003, the House of Representative's passed a bill that would classify unauthorized inspection of returns as being a serious form of IRS employee misconduct requiring discipline, and would call for annual IRS reporting regarding investigations and prosecutions of unauthorized browsing; in addition a taxpayer would have to be notified whenever the Treasury Inspector General for Tax Administration substantiates that his return has been unlawfully accessed. Taxpayer Protection and IRS Accountability Act of 2003, H.R. 1528, § 331(a), amending IRC § 7804A, and § 347(a),(b), reprinted in House Passes Bill Revising '10 Deadly Sins,' 2003 TNT 127-80. The offenses described in §7804A, Disciplinary Actions for Misconduct, are referred to colloquially as the "10 Deadly Sins." The IRS acknowledges that in the short-term its computer system is not capable of modification to prevent and immediately detect unauthorized browsing. 2000 JCT Report, supra note 88, ¶¶ 512-13.

129. Id. at ¶¶ 501-506. But cf. Kleiman, supra note 49, at n. 47, describing a 1991 FBI arrest of "16 government 'insiders' on charges of stealing confidential personal information from government computer databases and brokering the information to customers. . . in the private sector."

130. GAO, Report to the Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform, House of Representatives, May 2003, INFORMATION SECURITY: Progress Made, but Weaknesses at the Internal Revenue Service Continue to Pose Risks, reprinted in 2003 TNT 106-12, at ¶¶ 6-7. See generally Swire, supra note 88, at 497, noting that "the Defense Department reports hundreds of thousands of successful intrusions into military computers per year. . . . The possibility of intrusions. . . is a powerful argument against allowing unlimited government access to sensitive personal information of any kind." Id.

131. See Swire, supra note 88, at 494-95, for a discussion of how government officials with access to a government databases might "misuse [the data] for political gain." First, "the data may be an inexpensive and effective form of opposition research." In addition, "officials might use the inside information to extract concessions from targets of surveillance," as J. Edgar Hoover is alleged to have done, and finally

Congressional concern in the 1970's. The Articles of Impeachment against President Nixon, voted by the Judiciary Committee in 1974, alleged that the President "endeavored to obtain from the [IRS]. . . confidential information contained in income tax returns for purposes not authorized by law, and to cause. . . income tax audits. . . to be initiated. . . in a discriminatory manner."[132] To protect against further abuse by the White House, Congress in 1976 required that requests by the White House for taxpayer information be signed by the President personally and that the President make a quarterly report to the Joint Committee on Taxation regarding any tax returns that he requested to see and the reasons therefor.[133]

While Congress appears to have focused its concern on curbing such specific abuses of power, some commentators appear to have a more generalized concern about the huge amount of financial information that comes into the hands of the IRS and its effect on liberty.[134] They suggest that when

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"political officials might benefit from sharing the data with friendly outside parties." Id. at 494.

132. Articles of Impeachment Adopted by the Committee on the Judiciary, July 27, 1974, available at http://watergate.info/impeachment/impeachment-articles. President Nixon allegedly asked his aide John Dean to request that the IRS Commissioner audit taxpayers on his "enemies list." See George Lardner Jr., "Nixon Sought 'Ruthless' Chief to 'Do What He's Told' at IRS; Tape Includes Mention of Pursuing Enemies," Washington Post, January 3, 1997, page A01. According to the article, Commissioner Johnnie Walters, with the backing of Treasury Secretary George P. Shultz, refused this request transmitted by Dean. Id. Nixon, in turn, complained that there had been a probing audit of his own tax return in 1963, initiated by the Kennedy Administration. Id. President Kennedy is said to have shared tax return information regarding J. Paul Getty and H.L. Hunt with Ben Bradlee of the Washington Post. See John Berlau, "JFK Used Audits to Silence His Critics," Insight on the News, p. 21, Sept. 29, 2003, available on Lexis. See also Senate Comm. on the Judiciary, S.Rep. No. 1227, 93rd Cong., 2d Sess. 23 (Oct. 4, 1974), stating that the IRS had a "secret political intelligence unit known as the Special Service Staff which was responsible for compiling political intelligence data on at least 11,000 individuals and organizations deemed to be 'activist. . . ideological, militant, subversive or radical.'" In August 1973, the unit was disbanded. Id. This episode is referred to in Kleiman, supra note 49, at n. 46. For further discussion of the "SSI," see David M. Alpern with Anthony Marro and Evert Clark, "At Sea with the IRS," Newsweek, p. 32 (Oct. 13, 1975) (subjects of files included Mayor John V. Lindsay and Linus Pauling); Prepared Statement of Shelly L. Davis before the Senate Finance Committee-Oversight Hearing on the Internal Revenue Service, Federal News Service, Sept. 24, 1997, available on Lexis.

133. See IRC § 6103(g)(1),(5), added by P.Law 94-455, Sec. 1202. Such reports need not include requests for returns of an official in the executive branch of the federal government. Section 6103(g)(5). Separate rules are also established for information regarding Presidential appointees. See 6103(g)(2).

134. See Privacilla Report, supra note 103, at 7, stating that "[g]overnment databases and collections of information are a threat to privacy in and of themselves because governments can change or ignore the privacy laws that apply to them. Even the United States government, one of the most solicitous of privacy and the rule of law in

government obtains so much information about citizens, serious abuse is inevitable. They further argue that for government even to possess such information gives it a power that runs counter to our Founders' vision of limited government. Government monitoring of citizens,[135] in this view, inevitably moves our society in the direction of totalitarianism,[136] such as is described in George Orwell's book entitled "1984."[137]

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the world, has done this." See also Swire, supra note 88, at 507, suggesting that: "In our most pessimistic moments, we might even contemplate how tracking of all financial transactions. . . might contribute to an increased risk of tyranny in a society. . . If a society repeatedly opts for surveillance rather than privacy, then the nature of that society may change over time." See also Privacilla Report, supra note 103, noting that census information was used to identify Americans of Japanese ancestry and carry out their internment during World War II. The report explains: "Census Bureau employees opened their files and drew up detailed maps that showed where Japanese Americans were located and how many were living in given areas." He states: "Nearly 112,000 people were captured and sent to internment camps with the help of the census." See also Letter of James W. Harper, supra note 121, at 3.

135. Recently, concern about excessive government spying against Americans caused Congress to block a proposed Defense Department anti-terrorist initiative called Total Information Awareness, that would have used sophisticated data-mining and profiling technologies on an integrated database, created from existing government databases combined with financial, education, travel and medical records. See Adam Clymer, "Congress Agrees to Bar Pentagon From Terror Watch of Americans," N.Y. Times, p. A1, Feb. 12, 2003; Adam Clymer, "Senate Rejects Pentagon Plan to Mine Citizens' Personal Data for Clues to Terrorism," N.Y.Times, p. A12, January 24, 2003; John Schwartz, "Planned Databank on Citizens Spurs Opposition in Congress," N.Y.Times, p. A16, Jan. 16, 2003; Jeffrey Rosen, "The Year in Ideas; Total Information Awareness," N.Y. Times Magazine, p. 128; William Safire, N.Y. Times, Editorial Desk, p. A41, Feb. 13, 2003.

136. See Burton, supra note 28, at 15, explaining that: "Free people are not required to report their whereabouts or their actions to their governments. Governments in free societies do not monitor law-abiding citizens unless they are suspected of criminal acts and then can do so only under strict safeguards because all citizens are presumed innocent until the state has proven otherwise in a court of law. Invading private spaces requires authority from an independent judiciary that enforces legal restrictions on police action." He further states that: "[i]n contrast, totalitarian governments constantly monitor their citizens. . . . Virtually all aspects on one's life is known and controlled by the state. . . financial transactions must be conducted through state financial institutions. . . .Systems are established to systematically collect, analyze and act on information about individuals. The information collected enhances the power of the state to control the lives of those living under its control. . . . The very fact that U.S. citizens are being required to report so much information to the federal government, whether for tax, regulatory or simply monitoring purposes would, the author believes, shock the founding generation. . . Even relatively responsible governments, such as our own, can be expected to misuse and abuse information collected from time to time." Id. at 15-16.

137. George Orwell, 1984 (1949). See Kleiman, supra note 49, at 1176, referring to "Orwell's chilling vision of a nation where the 'powers that be' can monitor the who, what, where and how of every individual's life." In that book, the Party

Congress, however, has not endorsed this view. Not only has Congress allowed the IRS to collect the massive amount of information required to enforce the income tax, it has also sanctioned disclosure by the IRS of such information to a variety of other agencies of the federal and state governments for purposes other than federal tax administration.[138] Pursuant to section 6103, the IRS may make disclosure, for example, to *state* tax officials for purposes of state tax administration,[139] to congressional committees and the GAO in certain

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"criminalizes thoughts which are not in accord with the party line. . . [and] enforces this law by constant surveillance of the individual." Kleiman, supra note 49, at n. 45. But c.f. Alan Ehrenhalt, "The Misguided Zeal of the Privacy Lobby," Governing Magazine, May 1999, p. 7, stating that "[o]f all the dangers that this society faces. . . one of the most remote is the risk that America will become an Orwellian police state, watching everything citizens do and taking down every word that they say. . . . Those of us who lay awake at night in America in 1999 worrying about the government's desire to snoop on them are mostly (1) paranoid or (2) guilty of something." He further claims: "In America in the 1990's, the obsession with privacy. . . is a reflection of the hyper individualism to which the political system has succumbed in the past generation or so." Id. See also Amitai Etzioni, The Limits of Privacy, Basic Books 1999, at p. 127, arguing, in connection with a proposal for a mandatory national ID card, that "libertarian concerns about totalitarianism confuse cause with consequence. . . Totalitarian governments do not creep up on the tails of measures such as ID cards. They arise in response to breakdowns in the social order when basic human needs, such as public safety and work opportunities, are grossly neglected;" Michael Lind, "Solving the privacy puzzle; Thinking Aloud, " The New Leader, Vol. 85, p. 15, Jan. 1, 2002, suggesting that "[t]he fear that the convergence of high technology with law enforcement and business practices is about to rob us of our privacy has the hallmark of a classic, irrational moral panic." He argues that "the new privacy crusaders" consist mainly of "elite men." For an argument in favor of "transparency," in contrast to privacy, see David Brin, The Transparent Society (1998). But see "No Hiding Place," The Economist, January 25, 2003, arguing that Brin's solution of "mutually assured surveillance" is "one that most people would be unwilling to live with."

138. In addition, Congress has authorized disclosure to private contractors for purposes of federal tax administration. Section 6103(n). For an argument that disclosure of tax return data to other agencies is unwise, see Swire, supra note 88, at 498, arguing that such disclosure involves the dangers of "mission creep. . . [i.e.,] the risk that initial and justifiable government actions, such as collecting tax information or having a limited mission in South Vietnam, can evolve into unjustified and potentially tragic actions. If mission creep continues unchecked, tax returns might become essentially public documents." He notes that "[i]f the government. . . already has fifteen uses for a category of data, it may be impossible politically to stop the sixteenth or seventeenth uses, even where those additional uses would never have been approved at the time the data collection system was first instituted." Id. at 499. See also Linder, supra note 81, at 966, noting that under the 1976 Act, "the exceptions [to confidentiality] remain quite extensive, especially the massive use of individually identifiable returns by the Bureau of the Census."

139. Section 6103(d)(1).

cases,[140] to a federal, state or local agency administering various welfare or government assistance programs,[141] to the U.S. Customs Service,[142] to federal, state and local child support enforcement agencies,[143] and to certain federal officials for the nontax criminal investigations.[144] Once the IRS has collected its vast stores of information, use of this information by other government agencies has the advantage of efficiency.[145] Of course, just as Congress has sought to prevent abuse of taxpayer information by the IRS, it has also established a system of safeguards surrounding IRS disclosures to other government agencies.[146]

In summary, Congress's actions show its willingness for the IRS to obtain extensive financial information about citizens to enforce the federal income tax and even to share this information with other government agencies for certain specified purposes. This suggests that Congress is relatively sanguine that misuse of taxpayer financial information can be held in check and

140. Section 6103(f),(i)(8).

141. Section 6103(l)(7). The information is to be used for purposes of determining eligibility and the correct amount of benefits. Id. For a proposal to amend § 6103(l)(13) to permit disclosure of taxpayer information to the Department of Education to permit income verification in determining eligibility for student financial aid, see Dept. of Treasury, Office of Tax Policy, Report to the Congress on Scope and Use of Taxpayer Confidentiality and Disclosure Provisions (Oct. 2, 2000), available at 2000-TNT 192-7, at ¶¶ 344-50; Michael Brostek, General Accounting Office, Report to the Senate Finance Committee, Taxpayer Information, Increased Sharing and Verifying of Information Could Improve Education's Award Decisions, available at 2003 TNT 160-17.

142. Section 6103(l)(14).

143. Section 6103(l)(6)(A).

144. Section 6103(i)(1),(2),(3),(5),(7).

145. See Swire, supra note 88, at 497, explaining that: "Once the costs of the database and infrastructure are already incurred for initial purposes, then additional uses may be cost-justified that would not otherwise have been. . . . An efficiency argument can. . . be made that additional uses of [tax return] data, such as protecting against welfare fraud, should be authorized where the costs of gathering and organizing the comprehensive tax data would not have been justified solely to protect against welfare fraud." Id. at 497-98.

146. See § 6103(p)(4),(5),(6) (relating to disclosures to federal, state and local agencies). See also Reg. § 301.6103(n)-1(d), relating to disclosures under § 6103(n). However, thus far it is not clear that these safeguards have been adequately implemented. See, e.g., Deputy Inspector General for Audit, Treasury Inspector General for Tax Administration, Final Audit Report, dated Dec. 19, 2002, Improvements Are Needed to Prevent the Potential Disclosure of Confidential Taxpayer Information, reprinted in 2003 TNT 12-22.

that Congress does not believe that extensive government knowledge about its citizens is incompatible with a free society.[147]

III. THE INTERNATIONAL CONTEXT

Accepting the basic structure of the federal income tax precludes the argument that the Internal Revenue Service has no right to know the details of one's financial information. And the Congressional scheme for automatic reporting of dividends, interest, and sale proceeds of U.S. taxpayers to the IRS cannot be reconciled with the view that bank reporting of interest to tax authorities should be limited to cases of suspected wrongdoing.[148]

Why then is it controversial for the Treasury to seek to develop a system of routinely exchanging information about interest paid on bank accounts with other countries? This scheme obviously involves some new elements: some of the reporting will be done by foreign banks, some information will be conveyed to, and transmitted by, foreign countries, and some of the reporting will be of interest paid to nonresident aliens, who are not subject to U.S. tax thereon. Should the introduction of these new elements raise concerns to a new level?

*A. The Privacy Claims of Nonresident Aliens with U.S. Bank Account*s

Unless and until the proposed IRS regulation is issued, nonresident aliens (other than Canadians) are able to open U.S. bank accounts in the knowledge that will be no routine reporting of interest paid on the account to the IRS or their home country's tax authorities. Under the regulation's original version, the IRS was to receive information annually about interest paid to all nonresident alien depositors; under the revised version, the IRS is to receive information only about interest paid to residents of 16 countries. Particularly under the original version of the regulation, there was concern that nonresident aliens would no longer wish to have deposits in U.S. banks.

One potential concern of a nonresident could be that the IRS itself would have routine access to information about her bank account. This might seem objectionable in that the IRS has no need for the information in order to impose its own tax. On the other hand, the IRS's role in collecting information from U.S. banks is indispensable to the ultimate objective of conveying that information to the tax authorities of the depositor's residence country. A U.S.

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147. For arguments supporting this belief, see supra notes 110 and 137.

148. See Roin, supra note 111, at n. 193, asking whether Richard Armey, who criticized the OECD tax competition initiative as destructive of privacy, "holds a similar view of employer-based wage reporting."

bank cannot be expected to convey information directly to each residence country of its depositors. Moreover, as previously discussed, it is fairly unlikely that information held by the IRS will be abused by it or disclosed[149] without statutory authorization.[150] (The likelihood is sufficiently low that Congress is willing to subject U.S. citizens, as well, to this risk.) And the political stability of the U.S. government may be one of the reasons that the depositor has chosen a U.S. bank account in the first place.

The more significant concern of a nonresident depositor is that the IRS will convey the information to the tax authorities of her residence country, pursuant to the authorization in IRC section 6103(k)(4) for disclosure pursuant to a treaty or information exchange agreement.[151] This could lead to dire consequences if the residence country's government is oppressive, corrupt, unstable, or otherwise irresponsible. The government might use this financial information about its resident to carry out illegitimate acts such as expropriation

149. IRS Considers Giving Data to Law Enforcement Agencies, The Boston Globe, Sept. 26, 2003, stating that IRS officials have recently "approached the [Ways & Means] committee for discussions of how certain confidentiality laws could be reinterpreted to expedite the sharing of taxpayer records with the Justice Department, the FBI, INS and the Securities and Exchange Commission." IRS apparently wants to share "information compiled under its individual taxpayer identification number program, which requires foreigners with earned income in the United States and awaiting citizenship to comply with US tax laws." Id. See also Thomas F. Field, "Taxpayer Privacy: An Appeal to the Commissioner," 2003 TNT 218-48, requesting that the IRS clarify its position.

150. It might be possible to argue that because the nonresident alien individual is not subject to U.S. tax with respect to the bank deposit interest (and may not have any other item that is taxable by the U.S.), he or she is not a "taxpayer" for purposes of § 6103(b)(2). In that case, the information about the nonresident alien's interest may not be "return information" and thus may not be protected by the confidentiality rule of § 6103(a). Section 6103(b)(2) defines "return information" as "a taxpayer's identity, the nature, source, or amount of his income, payments, receipts. . . whether the taxpayer's return was, is being, or will be examined. . . or any other data, received by. . . or collected by the Secretary with respect to a return or with respect to the determination of the existence, or possible existence, of liability. . . of any person under this title for any tax, penalty. . . or offense." Although this interpretation is possible, it is not likely that the IRS would press this interpretation.

151. Section 6103(k)(4) provides that: "A return or return information may be disclosed to a competent authority of a foreign government which has an income tax or gift and estate tax convention or other convention or bilateral agreement relating to the exchange of tax information with the United States but only to the extent provided in, and subject to the terms and conditions of, such convention or bilateral agreement." For a discussion of this statutory provision and of provisions of bilateral agreements providing for such exchange of information, see 2000 JCT Report, supra note 88, at ¶¶ 162-198.

or persecution; or they could deliberately or through corruption or insufficient safeguards, let the information fall into the hands of criminals,[152] who might then rob, or kidnap for ransom, the innocent bank depositor.[153] (On the other hand, in the case of corrupt governments, it may be even more common for the leaders and their friends and relatives to secrete funds in offshore accounts to

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152. Opponents of the tax return publicity bill passed by Congress in 1934, see supra note 116, argued that "kidnappers and other criminals would use returns to pick their next (wealthy) victims. In light of the Lindbergh baby kidnapping two years before, this alleged consequence of publicity received an enormous amount of attention." Kornhauser, supra note 113. Senator Norris noted that this argument was "made on the floor of the Senate by a number of Senators. . . [and] it has had a great influence" in the statute's repeal. 79 Cong. Rec. 54427 (April 11, 1935), quoted in Kornhauser, supra. She notes that "Norris was justly cynical" about these arguments in that context. Kornhauser, supra.

153. See Task Force, supra note 76, at ¶ 122, recommending that information-exchange be limited to "governments that: 1. are democratic; 2. respect free markets, private property, and the rule of law; 3. can be expected to always use the information in a manner consistent with U.S. national security interest; [and] 4. have in place (in law and in practice) adequate safeguards to prevent the information from being obtained by hostile parties or used for inappropriate commercial, political or other purposes." See Mitchell, supra note 102, at 15, stating that "privacy. . . makes it harder for criminals to select victims." He states that "[m]any citizens, particularly those from the developing world, want confidentiality so they are less likely to be targeted for kidnaping and other violent crimes." Id., citing Testimony of Amy Elliot before the Permanent Subcommittee on Investigations of the Committee on Governmental Affairs, U.S. Senate, Nov. 9, 1999. He further states that the "ability to have private offshore accounts also enables people to protect themselves from financial instability and expropriation." Id., citing Testimony of Antonio Giraldi before the Permanent Subcommittee on Investigations of the Committee on Governmental Affairs, U.S. Senate, Nov. 10, 1999. See also Swire, supra note 88, at 471-72, expressing concern about "how an authoritarian or totalitarian government might use and abuse information about citizens' financial transactions." He notes that some "countries lack the democratic history and judicial oversight that exist in the United States." Id. He suggests that "United States deployment of [surveillance] technologies can embolden authoritarian regimes to deploy the same technologies and weaken U.S. complaints against authoritarianism." Id. at 503. He notes for example that, "Other countries often do not offer the legal protection to individuals that match those within the United States . . . [such as] a warrant requirement and other judicial oversight of investigations and prosecutions. Many countries give their officials greater access to data than is permitted in the United States. In some countries, there is a greater likelihood of corrupt officials." Id. at 504. See also Swire, supra note 88, at 473, stating that "The harms from surveillance of all financial transactions are even easier to imagine in a police state. In the absence of effective checks on official powers, those in control might use the information for their economic or political advantage. Political opponents, disfavored minorities, and powerless people generally could be targeted for exploitation by government officials." Id.

hide them from the populace.)[154] The bank depositor's human rights are surely violated by a government that misuses the information in this way or allows the information to be misused by criminals.

Many of the governments that might meet this description, e.g., those of Nigeria or Bulgaria,[155] have neither an income tax treaty nor an exchange of tax information agreement with the U.S.,[156] so disclosure of taxpayer information to tax authorities of such countries would be barred by section 6103. On the other hand, there may also be treaty or information-exchange partners of the U.S. that would not handle tax information responsibly; examples might include China, Egypt, Pakistan, Morocco, Russia, Tunisia and

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154. See Roin, supra note 111, at 598, arguing that "secrecy laws abet the discriminatory application of facially neutral tax rules" in that "[t]he politically favored may be given advance warning of changes in tax rules, and allowed the opportunity to hide their money." In addition, "bank secrecy laws and tax haven entities encourage corrupt administration and corrupt administrators." Id. at 598-99.

155. See Burton, supra note 28, at 27, stating that "Bulgaria, Colombia and Nigeria have major corruption problems." The U.S. signed an exchange of information agreement with Colombia on March 30, 2001, but there has not yet been an exchange of notes so that it is not yet in force. John Venuti, Manal S. Corwin, Steven R. Lainoff, and Paul M. Schmidt, "Current Status of U.S. International Tax Treaties and International Tax Agreements," 32 Tax Management International Journal 375, 380 (July 11, 2003). See also Task Force, supra note 76, at ¶ 122 stating that "[c]ertain NATO allies, most notably Greece and Turkey, do not currently provide adequate safeguards with respect to information and also have inordinate difficulties with corruption and protecting civil rights." See generally Burton, supra note 28, at 16, stating: "The idea of sharing banking, credit card and tax information relating to U.S. citizens or benign foreigners with most governments on the planet should cause most Americans to shudder. Most governments are corrupt. Most governments are not interested in preserving freedom. Most governments are more than willing to use such information to oppress their political opponents or disfavored ethnic or religious minorities. Most governments are more than willing to confiscate the property of their opponents. Few governments have meaningful controls on information, so unscrupulous government employees can misuse information even if its not a matter of state policy. For example, banking information has routinely been used in Columbia to identify potentially profitable kidnap victims." He also asserts that "French intelligence services are known to spy for commercial purposes" and that "the Greek and Turkish governments have intelligence services that used such information for domestic political oppression." Id. at 17 n. 60. See also Mitchell, supra note 102, at 15, stating that "[f]inancial privacy historically has been viewed as 'an essential safeguard of the citizen against the power of dictatorship.'" Mitchell cites Christopher Adams, "Nowhere to Hide," the Financial Times, June 26, 2000.

156. See Venuti, Corwin, Lainoff, & Schmidt, supra note 155, at 375-76, 380.

Turkey.[157] Treaty provisions providing for exchange of information typically provide that information received is to be disclosed only to person involved in tax administration and is to be used solely for such purposes.[158] However, this restriction may be difficult to enforce after the information has already been conveyed.

A nonresident alien depositing funds in a U.S. bank account deserves assurance that information about the account will not be transmitted to an irresponsible government that may misuse the information (or allow it to be used) in a way violating the alien's human rights. This suggests that an amendment of IRC section 6103(k)(4) is needed so that IRS transmittal of tax information is restricted to countries[159] that can provide assurance that the

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157. For a survey of the extent of political rights and civil liberties (from 1 as "best" and 7 as "worst") in the various countries of the world, see Freedom House, The World's Most Repressive Regimes 2003, A Special Report to the 59th Session of the United Nations Committee on Human Rights, Geneva, 2003, Appendix A, available online, at www.freedomhouse.org/research/mrr2003.pdf, last visited Oct. 18, 2003. The sixteen countries listed in the proposed regulation, see supra note 8, all have the highest score of 1 or political rights and 1 for civil liberties, except for Greece, which has a score of 1 for political rights and 2 for civil liberties. Other countries or territories with scores of 1 in each criterion are: Andorra, Austria, the Bahamas, Bermuda, Barbados, Belgium, British Virgin Islands, Cayman Islands, Cyprus, Dominica, Iceland, Isle of Man, Kirbati, Liechtenstein, Luxembourg, Malta, Marshall Islands, San Marino, Slovenia, Switzerland, Tuvalu, and Uruguay. The U.S. has tax treaties with the following countries that lack the highest (1,1) rating: Armenia (4,4), Azerbaijan (6,5), Belarus (6,6), China (7,6), Czech Republic (1,2), Egypt (6,6), Estonia (1,2), Georgia (4,4), Hungary (1,2), India (2,3), Indonesia (3,4), Israel (1, 3), Jamaica (2,3), Japan (1,2), Kazakhstan (6,5), Korea (2,2), Kyrgyzstan (6,5), Latvia (1,2), Lithuania (1,2), Mexico (2,2), Moldova (3,4), Morocco (5,5), Pakistan (6,5), the Philippines (2,3), Poland (1,2), Romania (2,2), Russia (5,5), Slovakia (1,2), South Africa (1,2), Tajikistan (6,5), Thailand (2,3), Trinidad & Tobago (3,3), Tunisia (6,5), Turkey (3,4), Turkmenistan (7,7), Ukraine (4,4), and Uzbekistan (7,6), Venezuela (3,4). The U.S. has an exchange of information agreement with the following countries or territories that lack the highest rating: Colombia (4,4), Antigua & Barbuda (4,2), Netherlands Antilles (1,2), Jamaica (2,3), Grenada (1,2), Dominican Republic (2,2), Mexico (2,2), Trinidad & Tobago (3,3), St. Lucia (1,2), Honduras (3,3), Costa Rica (1,2), Guyana (2,2), Peru (2,3). (The "freedom" ratings for territories are for the year 1999-00 and are found at http://www.freedomhouse.org/ratings/related.htm#top.)

158. See, e.g., U.S. Model Income Tax Convention of Sept. 20, 1996, Article 26.1; 2000 JCT Report, supra note 88, at ¶¶ 179-202, describing provisions in treaties with Germany, Canada, Japan, and the U.K.

159. In fact, the IRS may well have been sensitive to these issues in formulating its revised version of the proposed regulation for reporting of bank deposit interest of nonresident aliens. The 16 residence countries listed in the regulation are stable democracies, whose safeguards of the confidentiality of government information may

information will be safeguarded and will be used only for the purposes intended.[160] On the other hand, a foreign government that demonstrates its actual adherence to appropriate standards for handling and using tax information should not be denied such information merely because it does not meet Western standards for political democracy;[161] in some cases, securing a stable revenue source may be a necessary step in progress toward greater political rights and rule of law.

Many nonresident alien depositors in U.S. bank accounts may have a different concern about the proposed information-sharing. Rather than fearing that the information will be put to unintended purposes, they might fear that the information will be used by the residence government, *as intended*, to enforce the residence country's tax laws against the depositor. The depositor may sincerely believe that the tax which his residence country seeks to impose is grossly unfair to him. Does the depositor have the right to be assured that when he secretes his funds in another country, that country will not report the deposits to the tax authorities in his home country? For example, one commentator has recently presented such an argument:

> "In a number of European countries, governments are elected from time to time on a platform of explicit class warfare. . . . When there is a significant chance of a [such a] government being elected. . . government is no longer the neutral body that law-abiding citizens should obey at all times[,] it is an instrument of depredation and plunder. In order to protect themselves against such looting, it is right and proper that the professional classes should have access to an offshore bank

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well equal or exceed those in the U.S. See, e.g., Kleiman, supra note 49, at 1215-19, discussing the "independent privacy watchdog" used to insure protection of personal privacy in Sweden, West Germany and France, as potential models for the U.S. The one possible exception in this list is Greece. See supra notes 155, 157.

160. The Code already provides that in cases where information is shared with federal or state agencies or independent contractors pursuant to § 6103 the recipients must maintain certain procedures to safeguard the confidentiality of the information and that these are subject to audit by the General Accounting Office. IRC § 6103(p).

161. By contrast, under the Draft Convention proposed by the Task Force on Information Exchange and Financial Privacy, see supra note 153, information would be exchanged only with "governments that: 1. are democratic; 2. respect free markets, private property, and the rule of law; 3. can be expected to always use the information in a manner consistent with U.S. national security interest; [and] 4. have in place (in law and in practice) adequate safeguards to prevent the information from being obtained by hostile parties or used for inappropriate commercial, political or other purposes." Task Force, supra note 76, at ¶ 122. Under this draft Convention, however, information would be exchanged only for national security purposes, or to combat terrorism, or serious ordinary law crimes (defined so as not to include tax evasion). See infra note 197.

> account system, with banking secrecy that cannot be broken by agents of the looter government. Without such access, there is no security of property, and we are reduced to the law of the jungle."[162]

In general, each country is considered to have the right to make its own decisions[163] (through its own political system) about taxing its residents; these decisions require reaching a consensus about what level of government services should be provided and how the burden thereof should be distributed, and views on these matters often vary between (as well as within) countries.[164] Any scrutiny of such decisions by the international community would be quite limited; there is no international consensus regarding the appropriate level or distribution of taxes; only in extreme cases (usually involving discrimination on the basis of race, sex, ethnicity, religion or political views), would substantive rules of taxation[165] be considered to involve a violation of human rights.[166] If the residence country's tax system does not have flaws of such an

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162. See, e.g., Martin Hutchinson, UPI Business and Economics Editor, Bank secrecy – key civil liberty, United Press International, Oct. 4, 2001, available on Lexis.

163. See Roin, supra note 111, at 597, noting that "[w]hether rational or not, most countries consider the design of tax systems to be a national prerogative, and foreign influences thereon to be an intolerable intrusion."

164. See Roin, supra note 111, at 552, noting that "[i]n a simple world consisting of a single jurisdiction, that jurisdiction would choose its tax system and its tax levels based on its residents' (or leaders') evaluation of the social needs and desires of the populace;" id. at 557, noting that "residents of different countries may have different preferences regarding the mix between publicly and privately supplied services that affect the level (and thus the cost) of maintaining their public sectors;" id., at 581, arguing that "the whole point of the political process is to aggregate [the variety of] views to reach a collective 'consensus' according to which the society can function."

165. See Roin, supra note 111, at n. 180, noting that "[i]ndividuals' definitions of 'oppressive and confiscatory' may differ."

166. Recently, Philip Baker has written an analysis of 240 cases involving taxation that were decided by the European Commission on Human Rights and the European Court of Human Rights during period 1959-2000. Philip Baker, Taxation and the European Convention on Human Rights, British Tax Review, 211-377 (2000). These decisions interpret the European Convention on Human Rights, including protocols. See Convention for the Protection of Human Rights and Fundamental Freedoms, signed at Rome on November 4, 1950 (ETS No. 5), and Protocol No. 1, March 20, 1952 (ETS No. 9). There are 44 parties to the Convention. See http://www.coe.fr. Article 1 of Protocol No. 1 is entitled the Protection of Property. It provides: "Every natural. . . person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law. The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it

extreme nature, then the depositor is not entitled to assurance that information about his deposit will be kept from the tax authorities of his residence country.[167]

Critics of the Treasury's proposed regulation suggest that this initiative will inevitably lead to indiscriminate sharing of tax information with all countries (necessarily resulting in some misuse of information). They note that the Treasury left open the possibility of adding to the list of 16 countries in the future,[168] and they view the proposed regulation, the EU Savings Directive, and the OECD information-exchange initiative as leading to widespread, automatic information sharing,[169] epitomized by the so-called "international tax

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deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties." Baker explains that "all taxation must satisfy the principles underlying the Convention: it must be imposed according to law, it must serve a valid purpose in the public or general interest, and the provisions adopted must be a reasonable and proportionate means to achieve that end." Id. at 220. He notes that of the 65 cases seeking relief under this Article, only two have been successful, both involving tax *enforcement* measures. Id. at 220 and 226-28. A much larger number of successful taxation cases were raised under Article 6 of the Convention, dealing with the Right to a Fair Trial. Id. at 228. There were six successful taxation cases brought under Article 14, Prohibition of Discrimination; five involved discrimination on the basis of sex and one "involved unjustified discrimination on grounds of residence." Id. at 249. Two successful taxation cases were brought under Article 8, Right to Respect for Private and Family Life; both involved "information-seeking by revenue authorities where there were inadequate judicial safeguards." Id. at 253. In one case a search of premises was made by French customs officers; in the other, the taxpayer's phone was tapped by the French government. Id. at 254-55. Finally, six successful cases were brought under Article 5, Right to Liberty and Security. Id. at 260-61.

167. In the case of countries party to the European Human Rights Convention, discussed supra note 166, one could further argue that in light of the opportunity for redress before the European Court of Human Rights, protective action by a third country, such as the U.S., should be viewed as an unnecessary intrusion.

168. Burton, supra note 28, at p. 13: "As a prelude of things to come, the Treasury presages it may expand upon this list of countries. The Service intends to collect this information in a central repository, so that it can be made available to unspecified authorities in the enumerated foreign nations." See CFP, "Key Lawmaker Condemns IRS Regulation: Florida Banks Are Ultimate Target," Oct. 3, 2002, reprinted in 2002 TNT 193-24, arguing that, if the regulation is not withdrawn, "it will be just a matter of a few short years before the IRS imposes a reporting requirement for depositors from all nations."

169. See Burton, supra note 28, at 21, arguing that "The logic of the OECD proposal is the total abolition of financial privacy and a world where all governments can access the financial information . . . of any individual living anywhere in the world;" id., at 25: "The larger concern is that U.S. legal protections guaranteeing taxpayer

organization" proposed in a 2000 U.N. Report.[170] These critics are correct to stress the dangers of indiscriminate sharing of tax information. But they seem to be unduly pessimistic in predicting the IRS cannot maintain limitations on information-sharing in order to protect depositors against irresponsible governments.

The U.S. and other countries seeking to stem offshore tax evasion by their respective residents can so do without agreeing to provide information to irresponsible governments that would abuse such information. For one thing, these countries are generally not countries in which Americans or other tax evaders would seek to establish offshore accounts and thus there may be no need to negotiate for information exchange with those countries. Second, even if the U.S. did need information about U.S. bank accounts in one of those countries, it could negotiate a bilateral agreement to receive information from that country without agreeing, as part of the bargain, to provide information about U.S. bank accounts to that country. An example of a one-way tax sharing agreement is the U.S.– Bahamas Tax Information Agreement, signed on January 25, 2002.[171] Of course, such one-sided agreements require that the U.S.

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confidentiality would be undermined by the automatic information exchange that is the EU's ultimate goal. The United States is in a position to derail the entire EU Savings Tax Directive process if it withdraws the proposed bank deposit interest regulation." See also Task Force, supra note 76, at ¶ 138, stating that the OECD initiative on harmful competition "represents a major step toward the unrestricted disclosure of private financial and tax information, including from the U.S. and other OECD countries, to a wide array of countries that can be expected to misuse the information for commercial, political or intelligence purposes."

170. See Burton, supra note 28, at 6-7, citing Report of the High Level Panel on Financing for Development to the General Assembly, pp. 27-28, 64-66. The report proposed a "mechanism for multilateral sharing of tax information, like that already in place with OECD, so as to curb the scope for evasion of taxes on investment income earned abroad." Burton, at 6, quoting U.N. report, at 28; see also Task Force, supra note 76, at ¶¶ 56-59. See also Cordia Scott, "U.N.'s Annan Presses To Create Global Tax Commission," 2003 WTD 211-1, stating that, on October 29, 2003, the Secretary General "suggested that the current 25-member U.N. ad hoc group of experts on international tax policy should be transformed into an intergovernmental body."

171. See William M. Sharp Sr., William T. Harrison III, Rachel A. Lunsford, and Scott A. Harty, "The U.S. Tax Information Exchange Agreements: A Comparative Analysis," 2002 TNT 219-45, at n.4 and accompanying text. They note that the agreement "does not require the United States to tender any requested information to the Bahamas," whereas the U.S. could be required to provide information under the agreements with the Cayman Islands and British Virgin Islands, signed in 2001 and 2002, respectively. However "it seems unlikely that the Cayman Islands or the BVI will request this information." Id. at n. 4.

offer the other party some incentive to enter the agreement other than reciprocity of information exchange.[172]

This section has focused on whether a nonresident alien depositor in a U.S. bank has the right to assurance that his deposit information will be kept secret from his home government. My conclusion is that the nonresident alien's claim to secrecy is convincing only if the home government is likely to misuse (or allow misuse of) the information, and not if the home country can insure that the information is used solely to enforce the tax obligation of the depositor to his home country. This does not answer the question of whether the country where the deposit is made (e.g., the U.S.) has any reason, or obligation, to help the home country enforce its taxes (which may be too high in the view of the U.S.).[173] I will turn to this question in part C. below.

B. The Privacy Claims of U.S. Citizens or Residents who have Offshore Accounts

If one accepts that a U.S. person banking with a U.S. bank will have his receipt of interest payments reported to the IRS on a Form 1099 (and that this does not pose an intolerable risk that the information will be misused), is there any basis to argue that a U.S. person banking with an *offshor*e bank has a right to avoid such reporting to the IRS?

It could be argued generally that a U.S. citizen should be able to avoid the reach of the U.S. government when his actions occur wholly outside the U.S. But in this context this argument would be in direct conflict with decisions made by Congress. Congress has determined that the gross income of U.S. citizens or residents should generally include income from foreign as well as U.S. sources,[174] and the permissibility of this rule has been confirmed by the

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172. One of the incentives for the Bahamas to sign the agreement may be the provision in Article 5 confirming that the limitations on deductions for expenses of attending a convention outside the North American area under § 274(h)(1) will not apply to a convention in the Bahamas in light of § 274(h)(6) (Bahamas is a beneficiary country under the Caribbean Basin Economic Recovery Act that has in effect a bilateral agreement with the U.S. for exchange of information). See id. at text accompanying notes 131-36.

173. Mastromarco & Hunter, supra note 6, at 167 suggesting that, the EU and OECD efforts to expand information-reporting "would enable governments to impose high extraterritorial taxes with impunity – taxes that have driven the funds the EU is chasing offshore in the first place."

174. Sections 1; 61. Section 911 provides an exclusion, however, for a certain amount of foreign *earned* income. For this purpose "earned income" is defined as "wages, salaries, or professional fees, and other amounts received as compensation for personal services." Section 911(d)(2).

U.S. Supreme Court in Cook v. Tait.[175] Congress has not only made plain that interest paid by a foreign bank is taxable to a U.S. citizen or resident, but has also authorized the Treasury to require a U.S. citizen or resident to file a report of any offshore financial accounts that he owns or controls.[176] And, it has authorized the IRS to obtain the records of a taxpayer's domestic bank accounts without any showing of probable cause that any criminal or civil wrong has occurred.[177] Thus, Congress's failure to require reporting of the interest by the foreign bank to the IRS can be assumed to be based not on concern for the privacy of the depositor but on a lack of jurisdiction to impose this reporting requirement on the foreign bank.[178]

The exchange of information meant to be facilitated by the proposed regulation would involve transmittal of information about an offshore bank account of a U.S. citizen first to the government of the country where the bank is located and then by that government to the IRS. This might be considered a more serious invasion of privacy than the transmittal of information directly from a bank to the IRS (as in the case of a U.S. bank account). However, the American depositor himself chooses the foreign country in which to make the deposit, and therefore presumably should be able to insure that the foreign government can be relied upon to keep the information confidential (except for conveying it to the IRS).

C. The Claims of Tax Havens to be Entitled to Provide Privacy

Thus far, I have sought to establish that a taxpayer secreting funds in a bank account outside his residence country has no entitlement to have the host

175. 265 U.S. 47 (1924).

176. 31 U.S.C. 5314. See supra note 55.

177. See supra note 109 and accompanying text. Thus, there would seem to be no reason why the IRS should be required to show "probable cause" in seeking information regarding a foreign bank account. But see Burton, supra note 28, at 20-21, stating that: "The OECD MOU provides for the total abolition of financial privacy in the 41 targeted countries as it relates to the 30 OECD member countries. The targeted countries would be under an obligation to routinely share banking, tax, and other financial information with OECD member countries. . . . There would be no requirement for the recipient country to show probable cause for belief that a crime had been committed in either country. . . [or even] a requirement to show that some civil wrong had been committed or was even suspected. The information would simply be routinely sent to any OECD country that asked for it. There are absolutely no restrictions on the use to which the information may be put."

178. On the other hand, the IRS has taken advantage of the willingness of foreign financial institutions to provide certain information by voluntary agreement under the "qualified intermediary" program. See supra note 25.

country refrain from providing that information to his residence country (unless the residence country is expected to misuse or allow misuse of the information).

In this part, I will address the claim that a host country should be permitted to choose the role of the tax haven (i.e., to provide privacy to nonresident investors seeking to evade taxes in their home countries) and that, because it is a sovereign nation, the host country's choice should be respected by residence countries. Tax havens defend this claim with a number of arguments: First, there is no affirmative obligation of one country to help another enforce its own tax law. Providing such assistance has an administrative cost to the host country, and, more importantly, may damage or destroy the tax haven's financial services industry (which may be its only profitable industry).[179] Maintaining bank secrecy not only serves a tax haven's economic self-interest, but , in some cases, is an expression of the tax haven's culture and political values (such as, protection of an individual's privacy and freedom from government interference). Thus, for residence countries to seek to force a tax haven to give up bank secrecy is a violation of the tax haven's sovereignty. In this view, coordinated efforts by rich and powerful, developed countries to eradicate bank secrecy in poor, weak, undeveloped countries is a reprehensible form of bullying, particularly when developed countries have not fully renounced bank secrecy themselves. One commentator has likened the OECD to "twenty-first century pirates" who have "robbed fourteen CARICOM countries of their tax and economic policy sovereignty."[180]

It is true that international law has not as yet recognized any universal obligation of host countries to assist in enforcement of tax imposed by residence countries. Currently such an affirmative obligation only comes into being by agreement of the host country. This, however, does not establish that it is inappropriate for a residence country to seek to convince a host country to take on such an obligation.

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179. It may well be that giving up bank secrecy will have dire effects on the economies of a number of Caribbean counries. See Vaughn E. James, "Twenty-First Century Pirates of the Caribbean: How the Organization for Economic Cooperation and Development Robbed Fourteen CARICOM Countries of their Tax and Economic Policy Sovereignty," 34 U. Miami Inter-Am. L. Rev. 1, 33-39, concluding that "[a]ll the blacklisted countries have been severely affected by their inclusion on the OECD List of Tax Havens." See also Roin, supra note 111, noting that some tax haven countries argue that "their economies will collapse if they cannot provide investors with secrecy-leveraged tax advantages." Professor Roin notes that this argument was made by the Netherlands Antilles in an effort to ward off repeal by the U.S. of the withholding tax on interest. She suggests that "[s]ympathy for European countries such as Switzerland, Luxembourg, and Monaco may be even greater."

180. James, supra note 179, at 33-39.

In addition, the lack of a generalized obligation for a host country to assist a residence country in enforcing its tax law probably rests on the assumption that the host country has not participated in creating any obstacles to such enforcement, i.e., it is merely an innocent bystander. However, a tax haven adopts bank secrecy rules with the deliberate intent to attract banking transactions of nonresidents seeking to evade their home country's taxes; the tax haven's role is to facilitate such tax evasion. Thus, the tax haven can be viewed as an accomplice in thwarting another country's legitimate efforts to tax its own residents. The harm to the residence country is significant; it includes not only the taxes evaded by by those with offshore accounts, but also the resulting loss of confidence in its tax system and likely decline in voluntary compliance or even in respect for government.[181] In the view of the residence country, the tax haven is not being asked for assistance but merely to refrain from interfering in the residence country's affairs.

In many cases where this conflict occurs, the tax haven is a poor, undeveloped country that is highly dependent on its financial services industry and the residence country is a rich, developed country. Many would recognize an obligation of the richer country to provide economic aid to the smaller country. Allowing the tax haven to profit by facilitating tax evasion on the part of residents of the richer country may be viewed as an indirect form of economic aid. However, even if rich countries should accept an obligation to help poorer countries, they have no obligation to offer assistance *in this form*. As Professor Julie Roin has pointed out, more efficient means for providing financial assistance to poor countries can be devised.[182]

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181. See Roin, supra note 111, at 597, stating that arguments about infringement of sovereignty "lack much force in [the] contexts" of "bank secrecy and proposals for the exchange of tax information," by comparison to the context of "[m]andated tax uniformity." She explains: "[i]t is one thing to argue that a country should be able to use the tools at its disposal – tools that impose costs on the local population – to attract investment and tax revenues. It is another to attract investment (or launder the profits generated by investment elsewhere) by using tools that impose costs only on outsiders (including outside governments)." Id.

182. See Roin, supra note 111, at n. 196, commenting that a "simple transfer of money from the treasuries of the residence countries to those of the haven countries would be cheaper if the only goal is to provide foreign aid. The recipient country could use this money to encourage activity more productive than training people how to launder money." Id. She concludes: "Surely more productive, and less open-ended methods of foreign aid can be designed." Id at 602. She also notes that "[a]s it stands, the residence countries have very little control over the amount of foreign aid being transferred to tax haven countries." Id. at n. 197. Moreover, this form of aid is inefficient in that not all the benefits are captured by the tax havens; they must be shared with their customers, the tax evaders.

In some cases, the residence country whose tax enforcement efforts are thwarted is not a wealthy, developed country. As discussed in a recent Oxfam report,[183] it may be a relatively poor developing country (even a tax haven)[184] which is struggling to establish a working tax system. A country such as Brazil[185] should not be viewed as having an obligation to forego revenues by

183. Oxfam GB Policy Paper, Tax Havens: Releasing the Hidden Billions for Poverty Eradication. The report asks "If revenue authorities in Britain and Germany feel threatened by offshore activity, how much more severe are the problems facing countries with weak systems of tax administration?" Id. at 2. See also id. at 7, stating: "Tax authorities, particularly in developing countries, rarely have an effective means of knowing about the income their residents earn from abroad. . . In some developing countries, the tax regime permits or even encourages the non-payment of tax on foreign income. Even where this is not the case and tax treaties do contain adequate exchange of information agreements, the option of tax havens ensures that savers always have a way of escaping detection." The report seeks to quantify the revenue loss, as follows: "By 1990, the stock of capital flight from developing countries was estimated at around U.S. $700 billion. . . . Supposing a rate of return of 10 per cent and a tax rate of 22 per cent, tax on interest income from the U.S. $700 billion in capital flight could be contributing to developing country tax revenues to the tune of around U.S. $15.4 billion each year." Id. at 10.

184. See Bruce Zagaris, "Tax Compliance Initiative in Antigua and Barbuda Illustrates New Approach to an Old Problem," Tax Notes International Magazine, Feb. 3, 2003, 521, pointing out that the 2002 Budget Statement of the Prime Minister "focused on the culture of tax avoidance and evasion that has limited his government's ability and capacity to deliver vital services to citizens." Id. at 521. Zagaris notes that "[a]nother mechanism that Antigua and Barbuda will soon have to assist in its tax initiative is the proposed tax information exchange agreement" with the U.S. He explains that "TIEAs can help developing countries combat the ease with which taxpayers may use globalization to manipulate their financial affairs for the purpose of evading taxes." Id. at 524-5.

185. See David Roberto R. Soares da Silva, "Brazil Considers Tax Amnesty for Undeclared Investments Abroad," 2003 WTD 23-2, noting that "the [Brazilian] government estimates that more than U.S. $30 billion in undeclared, legally earned funds have been deposited abroad by Brazilian taxpayers;" Moises Naim, The Fourth Annual Grotius Lecture: Five Wars of Globalization, 18 Am. U. Int. L. Rev. 1 (2002), describing the five wars of globalization as including the "war against money laundering." He states that "developing countries lose about $50 billion a year in taxes through" tax evasion. He notes that "In 1998, $74 billion were transferred from Russian banks to overseas accounts. Of that amount, $70 billion went to accounts to banks in the small island-state of Nauru." Id. at 11-12. See Jennifer L. Franklin, Other International Issues: Tax Avoidance by Citizens of the Russian Federation: Will The Draft Tax Code Provide A Solution, 8 Duke J. Comp. & Int'l L. 135 (1997), at 153 fn. 117, noting that one method of tax avoidance in the Russian Federation has been "sending money abroad," citing Vincent Boland, Russian Maifa Has $10 billion in Swiss Bank, Financial Times, Feb. 14, 1997, at 3. See also Iurie Lugu, "Russia to Negotiate Information

allowing a Caribbean tax haven to use bank secrecy to attract tax evaders from Brazil.

Moreover, the country offering its services as a tax haven is not always a poor country with few alternatives for lifting its economy. For example, the United States and Switzerland do not fit this description.[186] Critics of the proposed regulation appear to argue that the United States has a greater self-interest as a tax haven country that attracts foreign capital by offering anonymity, than it does as a residence country seeking to prevent tax evasion by Americans using offshore accounts.[187] A quantitative comparison of these two competing interests of the United States is difficult because it is hard to quantify the damage to voluntary compliance that results from the widespread use of tax havens. In any event, neither the U.S. nor Switzerland could be expected to suffer an economic collapse if bank deposits in their banks were made subject to information reporting to the home country.

Exchange Agreements," 2003 WTD 146-5, noting that Russian tax authorities planned to enter into information exchange agreements with six additional countries and believed that exchange of information was "one of the principal factors in determining how effective [they are] are in preventing tax offenses and crimes." See also Cristian E. Rosso Alba, Argentine Revenue Service Empowered to Exchange Tax Information, 2003 WTD 195-6, (this authorization is "part of an antifraud package the administration proposed to uncover Argentine tax residents' accounts and offshore corporations in tax havens and foreign jurisdictions"); Michael Casey, "Argentina Is Taxing on Tax Dodgers," Wall Street Journal, June 25, 2003, at B5C, noting that "[t]here is. . . a broad consensus in Argentine society that the enormous tax-evasion problem needs to be fixed. Revenue lost to tax dodgers is estimated at 33 billion pesos (about $12 billion) each year, about half the federal government's budget;" "U.S. Colombia To Sign Pact To Share Tax Information," 2001 WTD 63-7 (Colombian official stated that the new agreement "would encourage Colombian taxpayers to take advantage of an amnesty that lets funds sent. . . overseas, without the knowledge of the tax authorities,. . . come back into the country").

186. The per capita GDP of the U.S. is $37,600, the second in the world after first-place Luxembourg, which has a per capita GDP of $44,000. Bermuda and the Cayman Islands are respectively third and fourth, while Switzerland is seventh, with per capita GDP of $31,700. Liechtenstein is number fifteenth, with per capita GDP of $25,000. At the bottom (number 231) is East Timor, with per capita GDP of $500. See The World Factbook, Rank Order - GDP per capita, available at http://www.odci.gov/cia/publications/factbook/rankorder/2004rank.htm, last visited on Oct. 8, 2003.

187. See Task Force on Information Exchange, supra note 76, at 142, recommending that the U.S. reject the EU Savings Tax Directive because: "The United States is a capital-inflow country. It is not in America's interest to facilitate foreign taxation of U.S.– source income." For an attempt to quantify this comparison, see Mastromarco & Hunter, supra note 6, at 171-72, citing testimony of Stephen J. Entin.

Of course, if small, poor countries with undiversified economies are expected to give up bank secrecy on the grounds that it is harmful to residence countries, it will be viewed by them as hypocritical and unfair for residence countries making that request, e.g., the United States, to themselves serve as tax havens in order to attract capital.[188] But the fact that the U.S. currently is a tax haven is not a good reason for the U.S. to continue to thwart the tax enforcement efforts of other countries. It is circular to argue that the U.S. (in its role as tax haven) should maintain bank secrecy (i.e., should not adopt the proposed regulation) because the U.S. (in its role as residence country) has no right to criticize Caribbean bank secrecy because the U.S. (in its role as tax haven) maintains bank secrecy itself.

Further, it has been argued that the OECD has acted to "impose [its] own cultur[e] on others."[189] Some tax havens defend bank secrecy as a form of human rights protection. For example, Switzerland claims to provide a haven for individuals who are persecuted by their own governments[190] on the basis of

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188. See Task Force, supra note 76, at ¶ 99, stating that "[i]t is wrong for the U.S. to be demanding that the small targeted countries [labelled as tax havens by the OECD] live by tax and financial privacy rules by which the U.S. itself is not willing to abide." See also Burton, supra note 28, at 20 stating that the U.S., U.K. and Switzerland "could also be on the OECD blacklist except the OECD members were excluded." See also Marshall J. Langer, "Harmful Tax Competition: Who Are the Real Tax Havens?" 2001 TNT 19-66, stating that "It is obvious that the United States, Britain, and many of the other OECD member states are significant tax havens." Id. at ¶ 42. To demonstrate that the U.S. meets the definition of a tax haven in the so-called Gordon Report, supra note 22, he points out: "The United States, the United Kingdom, and many other OECD countries have local laws and practices that deny information to other countries and that are at least as abusive as those of the so-called tax havens. . . . The United States still does not tax interest on bank deposits of foreigners, nor does it generally require any reporting of these deposits except those paid to Canadian residents. Therefore it cannot and does not give information concerning such deposits to any country other than Canada. The United States now also exempts portfolio interest and capital gains. . . other than real estate gains." Id. at ¶ 3. For discussion of the 1984 enactment of the portfolio interest exemption, see Graetz, supra note 25, at 376-80.

189. Langer, supra note 188, at ¶ 42 and n. 246, describing speech by Neville Nicholls, president of the Caribbean Development Bank, at a consultation between the OECD and CARICOM in Barbados in January 2001.

190. See Roin, supra note 111, at 597-98, noting that "[b]ank secrecy laws and laws forbidding cooperation with foreign tax authorities traditionally have been justified as a necessary protection against the ability of oppressive governments to strip members of political, racial or religious minorities of their assets under the guise of taxation or other laws." Id at 597 & n. 178, citing Allaire Urban Karzon, International Tax Evasion: Spawned in the United States and Nurtured by Secrecy Havens, 16 Vand. J. Transnat'l. L. 757, 781 (1983); Jeffrey I. Horowitz, Comment, Piercing Offshore Bank Secrecy Laws Used to Launder Illegal Narcotics Profits: The Cayman Islands Example, 20 Tex.

their religion, politics or race and who may be unfairly deprived of their assets.[191] Ironically, the bank secrecy laws of Switzerland proved to be a barrier to efforts by Holocaust survivors or their heirs to reclaim amounts deposited in Swiss banks while the Nazis were in power.[192] In any event, as discussed above,

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Int'l L.J. 133, 134-35 (1985); Feld, supra note 53, at 1182 (stating that "[h]istorically Swiss bank secrecy was created by private bankers in Geneva when French Protestants had hidden their remarkable wealth from the access of Catholic French kings in the banks of their brothers in faith in Geneva"). Professor Roin notes that "Switzerland's protection of the assets of European Jews during the Hitler era was routinely cited as the paradigmatic example of the beneficent quality of such behavior." Id. at 598, citing Senate Comm. on Gov'tal Affairs, Crime and Secrecy: The Use of Offshore Banks and Companies, S. Rep. No. 130, at 33 (1985); Karzon, supra, at 781. But she notes that "that particular canard has been laid to rest." Roin, supra, at 598.

191. See Jennifer A. Mencken, Note: Supervising Secrecy: Preventing Abuses within Bank Secrecy and Financial Privacy Systems, 21 B.C. Int'l & Comp. Law Rev. 461, 467-68 (1998) explaining that: "After coming to power in 1933, the Nazi government enacted a regulation requiring all German nationals to declare assets held outside of Germany, with non-compliance punishable by death. When three Germans were executed the following year, the Swiss government codified the secrecy customs of Swiss bankers." Germany was concerned with capital flight resulting from "hyperinflation and exchange controls caused by World War I." Id. at 467. She notes that: "Prior to the creation of numbered accounts by Swiss bankers, the Gestapo would routinely target low level Swiss bank employees for asset information concerning certain individuals." Id. at 471.

192. See Mencken, supra note 191, at 461, providing as an example the case of Jacob Friedman. Friedman at age 16 smuggled his father's funds from Romania to a numbered Swiss bank account, but his father and the rest of his family died at Auschwitz; in the 1970's Friedman sought to retrieve the funds from the Swiss bank was turned away because he did not have the secret account number. This story is recounted in Sean MacCarthaigh, Swiss Held to Account, IRISH TIMES, March 8, 1997, available in Lexis. In December 1999, a commission sponsored by the Swiss Bankers' Association and the World Jewish Congress and chaired by Paul Volcker, which conducted a three-year investigation, identified 53,000 Swiss bank accounts that might have belonged to Holocaust victims. The report stated that: "The handling of these funds was too often grossly insensitive to the special conditions of the Holocaust and sometimes misleading in intent and unfair in result." David E. Sanger, 54,000 Swiss Accounts Tied to Nazis' War Victims, New York Times, Dec. 7, 1999, at A15. See also Elizabeth Olson, Swiss Holocaust Accounts Reportedly Have $250 Million, Near York Times, Dec. 3, 1999, page A5; Elizabeth Olson, Swiss Embrace Report; Banks are Tarnished, New York Times, Dec. 7, 1999, at A15. Class action suits brought in federal court in Brooklyn resulted in a 1998 settlement of $1.25 billion against a group of Swiss banks, for which final court approval was given in 2000. Alan Feuer, Final Approval on Swiss Holocaust Claims, New York Times, July 27, 2000, at A8; see David Barstow, Plan for Swiss to Pay Nazi Victims, New York Times, Sept. 13, 2000, at A3; Elizabeth Olson, Swiss to List Bank Accounts Unclaimed Since Holocaust, New York Times, Nov. 26, 2000, § 1, p. 28; Elizabeth Olson, Swiss Banks Find $10 million from

protection from government persecution does not seem an adequate justification for a blanket rule of bank secrecy. Rather, it would seem to justify special measures on the part of the country in which a bank is located to insure that information about residents is provided only to countries that will hold it in confidence and will put it to appropriate uses.[193]

Some tax haven countries, such as Switzerland, are said to have a different view than most developed countries about issues of government, privacy and taxes.[194] For example, some countries do not view tax evasion as

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Holocaust, New York Times, Oct. 12, 2001, at A9. In March 2002, a commission of historians, led by Swiss historian, Jean-Francois Bergier, completed a five-year investigation of Switzerland's wartime activities and concluded that Swiss "authorities cooperated unduly with the Nazis and failed to return assets to their rightful owners when the war ended." The panel "criticized the banks' failure to return Jewish assets after 1945, but said it resulted from poor judgment and a desire to safeguard Swiss banking secrecy rather than pure profiteering." Elizabeth Olson, Commission Concludes That Swiss Policies Aided the Nazis, New York Times, March 23, 2002, at A4; see also Elizabeth Olson, Swiss Were Part of Nazi Economic Lifeline, Historians Find, New York Times, Dec. 2, 2001, at § 1A, p. 24; Nostra Culpa, The Economist, March 30, 2002, available on Lexis, noting the Commission's conclusions that "After the war, banks and art galleries were negligent about restoring property. Decades of pressure from Hitler's victims or their heirs seeking to recover the assets bore real fruit only in the late 1990's, with the help of Jewish groups, lawyers and the American government." See also Judith Mandelbaum Schmid, "Bankers don't tell: The Swiss government and banks say they have no plans to alter the secrecy code. But given recent damage to the banks' reputation and a changing financial landscape, they may have no choice," Swiss News, May 1, 2002, at p. 10, available on Lexis, stating of the Swiss bankers actions after the war: "The problem was not that they breached rules – it was that they followed the rules blindly (and in their own financial interests) without considering moral issues . . . they took cover under their own, perfectly legal rules of bank secrecy and did nothing, under the pretext that they were protecting their clients' confidentiality." Id. For more recent developments, see William Glaberson, "Holocaust Fund Official Says Many People May Not Get Paid – Swiss banks are withholding information, a report says," N. Y. Times, p. B1, Oct. 8, 2003.

193. See Roin, supra note 111, at 598, stating that "the time has come to distinguish between secrecy that serves. . . meritorious ends and secrecy that instead contributes to various forms of tax and nontax related illegal and abusive behavior by governments, bankers and their clients."

194. See Feld, supra note 53, at 1182, stating that "Switzerland perceives itself as protecting free individuals from government access. . . The Swiss government and the Swiss people obviously believe that bank customer secrecy reflects their liberal values to a very strong extent." Professor Feld is a professor of public finance at the Philipps-University of Marburg. He notes that a recent poll showed that "77 percent of Swiss citizens support the existence of Swiss bank secrecy laws." Id. at 1184. See Erich I. Peter, "Reasonable Limits of Transparency in Global Taxation: Lessons from the Swiss

a serious crime if it merely involves secrecy and not the use of false documentation.[195] They may view tax evasion as a citizen's natural response to

Experience," Tax Notes International Magazine, Nov. 11, 2002, at 591, 614, stating that bank customer secrecy in Switzerland "is not only rooted in long legal tradition but also [is] a part of the self-conception of the Swiss people;" Judith Mandelbaum Schmid, "Bankers don't tell: The Swiss government and banks say they have no plans to alter the secrecy code. But given recent damage to the banks' reputation and a changing financial landscape, they may have no choice," Swiss News, May 1, 2002, at p. 10, available on Lexis, stating that "The tradition of bank secrecy [in Switzerland] is inseparable from two national prerogatives: the inviolability of the individual's right to making personal decisions about paying taxes and the right to privacy." She notes that "the confederation of Swiss cantons was formed in 1291 primarily as a means to avoid paying the exorbitant taxes demanded by the Habsburg emperor [and that s]ince then the Swiss have always voted on all taxes." She quotes Hans Geiger, professor of economics at the University of Zurich, who says that "Tax evasion is not a crime in Switzerland. It is only a minor offence." Id. Although cantonal tax authorities cannot demand bank information about a suspected tax evader, this may not be necessary because banks levy a 35% withholding on interest (except from retirement funds). Id. She notes that "Switzerland has the lowest rate of tax evasion in Europe." Id. See also Rahn & de Rugy, supra note 6, at ¶¶ 10-12.

195. See Feld, supra note 53, at 1183, noting that that Switzerland distinguishes between "tax evasion" which is not a crime and "is treated as contravention of regulations and punished in an ordinary civil administrative process like parking violations," and "tax fraud," which is a crime. He explains that "[t]ax fraud exists if false documents are used to cheat the tax authority," e.g., a forgery, "while tax reporting forms are no document in this sense." Id. In his view, "[t]axes in Switzerland are perceived and constructed as prices for public services," and there is a "partnership between the state and its citizens. . . . Less severe cases of tax evasion are. . . accepted as mistakes that might occur in such a partnership. Nobody's perfect and cheating a little bit does not undermine the basis of the state." By contrast "[t]ax fraud. . . is actively breaching the tax contract with the government." Id. See also Erich I. Peter, "Reasonable Limits of Transparency in Global Taxation: Lessons from the Swiss Experience," Tax Notes International Magazine, Nov. 11, 2002, at 591, 601-02, describing the distinction between tax evasion and tax fraud under Swiss law. In January 2003, the U.S. and Switzerland agreed that certain hypothetical conduct would constitute "tax fraud or the like" within the meaning of Article 26.1 of the Swiss-U.S. Income Tax Convention of Oct. 2, 1996, and thus require exchange of information. See Mutual Agreement of January 23, 2000, Regarding the Administration of Article 26 (Exchange of Information of the Swiss-U.S. Income Tax Convention of Oct. 2, 1996. One of the examples was of an individual who maintained a bank account in the other country into which he deposits income taxable in his residence country. The taxpayer does not file an income tax return. He uses a credit card issued in the name of a corporation to withdraw substantial amounts form the account to pay his living expenses. Tax officials in the first country determine that a credit card tied to the bank account was used to purchase numerous personal items delivered to the taxpayer. "When these officials ask the individual

a country's imposition of excessively high taxes. Thus, such countries may consider that automatic information sharing is an excessive invasion of privacy when used to identify "mere" tax evasion.[196] Such a country might find it distasteful to engage in automatic information sharing regarding American or European taxpayers with the respective home government and may argue that it is under no obligation to do so.[197]

In some cases, one might question whether a particular tax haven country sincerely holds this view or whether this is merely a convenient justification for actions taken out of economic self-interest. In any event, the tax haven does not have a convincing reason for refusing to exchange information routinely with a residence country with a democratic political system and a constitution that limits government powers and is interpreted by an independent judiciary, such as the United States.

Reasonable people may differ as to whether the U.S. government should subordinate the privacy rights of its taxpayers to the needs of tax enforcement by requiring routine reporting of their bank deposit interest. But

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whether he owns or controls the bank account, the individual does not acknowledge any interest in the corporation or the bank account, and provides no explanation regarding the source of the funds in the bank account." Id., Hypothetical 12. See Robert Goulder, "Former Treasury Official Notes Problems with Swiss Information Exchange," Tax Notes International Magazine, May 19, 2003, 663, pointing out that the new agreement "does not provide for Swiss cooperation in civil tax matters, and fails to cover all criminal tax matters."

196. See Peter, supra note 194, at 635, arguing that "there should be no exchange of information in a case of mere tax evasion since this offense does not represent a crime under Swiss law." See also Task Force, supra note 76, at ¶ 129, stating that: "The dual criminality principle should be honored. . . Countries that honor requests for information about criminals and terrorists should not be harassed or sanctioned because they honor financial privacy in civil controversies or matters that are not a crime in their jurisdictions (e.g., tax evasion)." See also Burton, supra note 28, at 18, 27.

197. The Convention of Privacy and Information Exchange proposed by the Task Force on Information Exchange and Financial Privacy, see supra note 76, would provide that information obtained under the convention be used by a Member government for no purpose other than "national security," defense against terrorism or "to detect, prevent or defend against serious ordinary law crimes and to apprehend persons who have committed serious ordinary law crimes." Article III, ¶ (1). The convention defines a Serious Ordinary Crime as "conduct that (a) constitutes an offence in all Member States and (b) is punishable by a maximum deprivation of liberty of four years or more in all Member States." Art. 4, ¶ 6. The penalty under IRC § 7206(1) for willfully making statements on a tax return that the taxpayer does not believe to be true is a fine of not more than $100,000 and/or imprisonment of not more than 3 years. However, "a person who willfully attempts in any manner to evade or defeat. . . tax. . . or the payment thereof," is subject to a penalty of not more than $100,000 and/or imprisonment of not more than 5 years or both. Section 7201.

there surely is no international consensus that the U.S. approach is a violation of human rights, which would justify outside intervention. Moreover, aggrieved U.S. individuals have opportunities to debate and challenge the U.S. government's approach through the American political or legal system. Instead, tax havens offer the U.S. depositor with a means to bypass the IRS information system silently and with impunity.[198] In this light, the tax haven's refusal to exchange information represents an unwarranted interference in the relationship between the U.S. government and its citizens or residents.

A similar argument should preclude tax havens from arguing that bank secrecy is a salutary means to prevent Western European countries from imposing confiscatory rates of tax on high income individuals. The argument that "political sovereignty" justifies the tax havens claim to impose low rates of tax also justifies the Western European country's claim to impose high rates of tax.[199] The high-tax countries in Western Europe are recognized as having democratic governments, and there is thus no reason not to view such a country's decisions about its own tax system as legitimate. Moreover, these countries have subscribed to the European Convention on Human Rights, and thus have provided a means for taxpayers to seek redress for oppressive or discriminatory taxation in a forum outside the taxing country.[200]

Professor Roin has suggested that in some cases a residence country may be content to have its residents (or a favored groups of its residents) use tax havens to avoid high taxes imposed by the residence country. In that case, the tax haven is assisting the residence country's government to obscure its true tax policy and avoid accountability under its own political system.[201] Moreover, an unscrupulous government might utilize this means to subject unfavored

198. See Roin, supra note 111, at 600, arguing: "If open tax reductions cannot be sustained politically, then the hidden version of such reductions, effected through the use of tax havens should not be allowed either. Eliminating the secrecy surrounding such transactions would be a step in the direction of putting such policies to the necessary political test."

199. See Roin, supra note 111, at n.181, discussed at supra notes 163-65.

200. Since 1959, at least 240 cases challenging improper substantive or procedural aspects of European tax systems have been brought before the European Commission on Human Rights or the European Court of Human Rights. See supra note 166. Switzerland is one of the countries that has ratified the European Convention on Human Rights (including Protocols 6 & 7), although it has not ratified Protocols 1 & 4. See http://www.echr.coe.int/Eng/EDocs/DatesofRatification.htm. Currently, M. Luzius Wildhaber of Switzerland is the President of the Court.

201. See Roin, supra note 111, at 597-601. Roin argues that when countries "fail to provide openly for. . . rate reductions through domestic legislation. . .[and] rely instead on. . . informal, uneven, and unpoliced self-help methods of tax reduction. . . [this] suggests a disconnect between those parties effectively making tax policy and those that are supposed to determine that policy."

groups to discriminatory or harsh treatment, while alerting more favored groups (such as family and friends of the leaders) to the need to secrete funds.[202] Thus, the tax haven's justification for withholding tax information from the residence country may not be as strong as it first appears even when the residence country is relatively undemocratic. If bank secrecy allows the governments' tax treatment of its own citizens to be hidden, there is little opportunity for the government's tax policy to be subject to democratic control.

D. The Argument that Fighting Non-Tax Crime and International Terrorism Should Take Priority

Among the arguments raised by the Task Force on Information Exchange to counter proposals for broader tax information exchange is that priority should be given to investigation of international terrorism or "serious ordinary law offenses."[203] Thus, the Task Force asserts:

> "Countries that honor requests for information about criminals and terrorists should not be harassed or sanctioned because they honor financial privacy in civil controversies or matters that are not a crime in their jurisdictions (e.g., tax evasion). Misguided efforts like the OECD initiative against harmful tax competition should not be allowed to impede efforts to obtain information about terrorists."[204]

This argument is in part a restatement of the arguments addressed in Part C. above. But, in addition, the Task Force is contending that U.S. efforts to obtain tax information from tax havens jeopardizes its efforts to obtain information about terrorism and other serious crimes from such havens and that the need for the latter information is much greater.

202. Id.

203. The Convention of Privacy and Information Exchange proposed by the Task Force on Information Exchange and Financial Privacy, see supra note 76, would provide that information obtained under the convention be used by a Member government for no purpose other than "national security," defense against terrorism or "to detect, prevent or defend against serious ordinary law crimes and to apprehend persons who have committed serious ordinary law crimes." Article III, ¶ (1). See supra note 197 for the definition of serious ordinary law crimes.

204. Burton, supra note 28, at 27; Task Force, supra note 76, at ¶ 129. See also Rahn & de Rugy, supra note 6, at ¶ 22, arguing that "[a] more constructive approach to fighting terrorism would be to move away from all-embracing information-gathering towards much more narrowly focused money-laundering laws."

Assuming, for sake of argument, that fighting terrorism and serious non-tax crimes is much more important than enforcing the tax law, there is still a question as to whether pressuring tax havens with respect to tax information will in fact jeopardize tax havens' cooperation with respect to terrorism and other serious crimes. A tax haven's refusal to cooperate in the latter enterprise is likely to cost it dearly in terms of its standing in the international community. Thus, it is by no means clear that fighting terrorism or other crime is a good reason for the IRS to abandon its efforts to obtain tax information from tax havens.

IV. QUESTIONING OUR CURRENT TAX SYSTEM

The above defense of the Treasury's efforts to institute automatic information sharing regarding bank deposit interest accepted certain features of our current tax system as a given: Under the current Internal Revenue Code, U.S. citizens or residents on taxed on their income from worldwide sources and are allowed certain deductions or credits. The taxpayer is expected to compute his own tax liability. At the same time, the IRS is to have various sources of financial information regarding taxpayers in order to verify that the tax is accurately determined. Thus, the taxpayer is required to file a complete and accurate tax return, as well as a return detailing any foreign accounts that he owns or controls. U.S. payors of various types of income, e.g., wages, dividends, interest, and royalties, are required to report these payments to the taxpayer and the IRS as a means to insure compliance. In addition, the IRS may issue a summons for bank records of a taxpayer in order to verify the accuracy of his tax return without establishing probable cause to believe that the return is false.

Given these features of our current tax system, Treasury's effort to expand automatic information sharing to cross-border payments of bank deposit interest seems not to represent much of an additional invasion of privacy and seems clearly warranted by the needs of the system. Thus, it seems plausible that much of the criticism of the proposed regulation is actually directed at the larger goal of replacing the federal income tax with a new tax system. The criticism may be designed to serve two alternative purposes: If the criticism succeeds in derailing the proposed regulation and the Treasury's efforts to broaden information exchange, then income tax compliance and taxpayer morale may decline further and the need for a replacement of the tax system will become apparent. If the proposed regulation is finalized despite the criticism, the criticism will at least have highlighted the degree to which privacy is necessarily sacrificed under the income tax and may help to convince citizens of the need for a less invasive alternative.

For example, Dr. Daniel J. Mitchell of the Heritage Foundation, who is one of the members of the Task Force on Information Exchange and

Financial Privacy, has written: "The reduction of government prying is sufficient reason to scrap the Internal Revenue Code."[205] He points out that under the "flat tax," the only income that individuals (in contrast to businesses) would be required to report would be wages; dividends and interest would not be reported on an individual's return.[206] Employers, as under the current system, would be responsible for reporting and withholding tax from an individual's wages, so compliance would be fairly well assured. Assuming also that deductions, such as medical expenses and mortgage interest, are not allowed, the IRS would appear to have no need to obtain extensive financial information about individuals (apart from their ownership of businesses).[207]

On the other hand, a number of other federal programs require financial information about individuals, such as the Social Security disability program, college loan assistance, medicare benefits and food stamps.[208] In addition, state

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205. See Mitchell, supra note 102 , at 2. He notes that "[d]uring America's early years. . . tax collectors were not even allowed to enter homes." Id., citing Charles Adams, For Good and Evil: The Impact of Taxes on the Course of Civilization (New York: Madison Books: 1993). See also Rahn & de Rugy, supra note 6, at ¶ 13, noting that "[u]ntil 1913 [when the Sixteenth Amendment was ratified,] the government did not have constitutional authority to invade financial privacy."

206. See Mitchell, Tax Reform, supra note 102, at 9-11; see John O. Fox, If America Really Understood the Income Tax (Westview Press 2001), at pp. 260, 263, showing tax forms required under the flat tax.

207. See discussion in GAO/GGD-98-37, U.S. General Accounting Office, Potential Impact of Alternative Taxes on Taxpayers and Administrators, January 14, 1998, Appendix Vii, reprinted in 98 TNT 11-10 & 11-11. Similarly, it has been suggested that a national retail sales tax would avoid the need for information about an individual's finances to be provided to the IRS. See Mitchell, supra note 102, at 11-12, stating that the IRS would have no need to track wages or individual savings, stockholdings or bondholdings of individuals. Further, although the government would have to keep track of sales, "the compliance burden would fall on sellers rather than buyers." However, he notes that "[p]urchases of goods made overseas would be taxable, so consumers would have to divulge those purchases when returning to the United States." Id. at 12. By contrast, a cash-flow tax may not offer greater privacy because of the need to track amounts added to savings and amounts withdrawn from savings. Id. at 13.

208. See e.g., Mitchell, supra note 102, at 12 & n. 9, noting that although a national sales tax would not entail any tracking of individuals' salaries by the IRS, "[t]here may be other reasons for the government to obtain this data, including: 1. calculation of Social Security taxes and/or benefits, and 2. determination of eligibility for various government programs." Id. at n. 9; see Privacilla Report, supra note 103, at 7-8, noting that the SSA keeps records of "individuals' earning histories over their entire lives." This report further notes that the Census Bureau questionnaire asks for "a detailed breakdown of income, how people get to work. . . how many toilets families have, and how much they pay annually for electricity, gas water, sewers, oil, coal,

and local governments require such information for their own income taxes and other programs. Moreover, there is the question of whether a new federal program would be instituted to replace the earned income credit.[209] If the current IRS information-reporting system for income other than wages were dismantled, the same information might nevertheless be sought by government agencies, but the information actually collected might prove to be less accurate. Thus, there is need for considerably more analysis before one could conclude that enhancing the privacy of Americans would be sufficient justification to replace the federal income tax system with a flat tax.[210]

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kerosene and wood." Id. at 8. The bureau "is a repository of massive amounts of sensitive personal information about Americans." He notes that "In the modern welfare state, governments use copious amounts of information to serve up various entitlements and benefits as well. Any program that doles money out to citizens based on their condition or status must know that condition or status is, often in comparison to the condition or status of the population at large. A program to provide medical care, as an example, requires the government to collect the beneficiary's name, address, telephone number, sex, age, income level, medical condition, medical history, providers' names, and much more." Id. at 9. In addition "the government sector makes [use] of personal information. . . to investigate crime and enforce laws and regulations. Governments' ability to do these things correlates directly to the amount of information they can collect about where people go, what they do, what they say, to whom they say it, what they own, what they think, and so on. We rely on government to investigate wrongdoing by examining information that is often regarded as private in the hands of the innocent." Id. at 9. See also Allen, supra note 93, at 7-9, explaining: "A sense of moral responsibility for one's conduct and a desire for morally responsive public policies might lead to abandonment of enhancing individual data control as the central objective of privacy policy. . . It would seem unwise to prohibit the constitutionally mandated decennial census-takers from collecting personal information about household income. Welfare, Social Security, disaster relief, student loans – all of these public benefits should be available, but surely require moral accountability in the form of personal financial disclosures."

209. See David A. Weisbach, Ironing Out the Flat Tax, 52 Tax L. Rev. 599 (2000), explaining that if the income tax were replaced with a flat tax and the earned income credit was to be retained, then there would be an issue as to whether to retain the partial phase-out based on overall income (as contrasted with wages). To eliminate this phase-out would allow the EIC to be claimed by "those living off investments with low wages," but to retain the phase-out would be putting "those who claim the EIC, at least in part, back in an income tax system." Id. at 658-59. He notes that "[m]oving the EIC out of the tax system to the welfare system does not change the analysis at all." In addition, he points out that "[o]ne in five families now collects the EIC." Id. at 658.

210. This topic will be explored further in a future article.

V. CONCLUSION

This article has examined the Treasury's recent efforts to expand exchange of bank deposit information with other countries and, in particular, the criticism that these efforts involve a serious erosion of privacy. Privacy, especially from scrutiny by the government, is an important value, but one that Congress has balanced with other important objectives in fashioning the current tax system. Under the current system, the Treasury's efforts to broaden information-sharing by the U.S. with other countries is critical to the goal of achieving an acceptable level of tax compliance (and of being sure of what level of compliance is actually being achieved).

Critics of the Treasury's information-sharing initiative are right to call for strong safeguards to insure that tax information is not transmitted to governments that will misuse it (or permit misuse by others). But, with such safeguards in place, it will be time for some of Treasury's critics to acknowledge that their arguments are directed not at improving the income tax, but at undermining and replacing it.