



OFFICE OF  
CHIEF COUNSEL

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

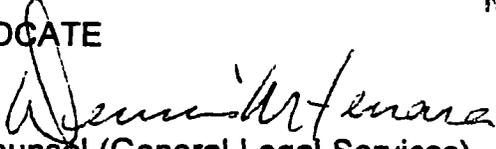
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COUNSEL TO THE  
NATIONAL TAXPAYER ADVOCATE  
INTERNAL REVENUE SERVICE

MEMORANDUM FOR VAL W. OVESON  
TAXPAYER ADVOCATE

NOV 03 1999

FROM:

Dennis M. Ferrara   
Assistant Chief Counsel (General Legal Services)  
Internal Revenue Service

SUBJECT:

Counsel Assistance with Activities Reports

You asked whether Office of Chief Counsel employees may, at your request, review and comment upon legislative recommendations that are to be submitted with your annual activities report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate. You also asked whether it would be feasible to wall off the attorneys reviewing the legislative recommendations from the rest of the Chief Counsel's and General Counsel's office to preserve both the appearance and fact of independence. The question arises in view of I.R.C. § 7803(c)(2)(B)(iii), which provides that such reports are to be *submitted directly* by you to these committees.

It is our opinion that Office of Chief Counsel attorneys can participate in the review of the legislative recommendations made in connection with your annual activities report, without violating I.R.C. § 7803(c)(2)(B)(iii). However, prudence dictates that certain structural separations be put in effect that will ensure the fact and appearance of the independence of that report.

I. THE STATUTE AND LEGISLATIVE HISTORY

A. The Current Statutory Language

As amended by the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98), I.R.C. § 7803(c)(2) provides that:

(ii) **ACTIVITIES.**—Not later than December 31 of each calendar year, the National Taxpayer Advocate shall report to the Committee on

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Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the activities of the Office of the Taxpayer Advocate during the fiscal year ending during such calendar year. Any such report shall contain full and substantive analysis, in addition to statistical information, and shall—

.....

(VIII) contain recommendations for such administrative and legislative action as may be appropriate to resolve problems encountered by taxpayers;

.....

(iii) **REPORT TO BE SUBMITTED DIRECTLY.**—Each report required under this subparagraph shall be provided directly to the committees described in clause (i) without any prior review or comment from the Commissioner, the Secretary of the Treasury, the Oversight Board, any other officer or employee of the Department of the Treasury, or the Office of Management and Budget.

I.R.C. § 7803(c)(2)(B). The National Taxpayer Advocate's (NTA's) responsibility and authority to submit directly to Congress an annual activities report, which would contain recommendations for legislation, was a feature introduced with the statutory creation of the Office of Taxpayer Advocate (OTA) by TBOR II. While certain categories of items to be reported were added and removed by RRA 98, the "independent reports" feature was adopted in both the House and Senate versions of H.R. 2676 with only very modest changes. Compare I.R.C. § 7802(d)(2)(B)(1997), with, I.R.C. § 7803(c)(2)(B). RRA 98 added a reference to the Oversight Board in clause (iii), which was present in the House bill and carried through to the Senate bill. The explanation of the revised provision in the legislative history clearly implies that the addition of the reference to the Oversight Board was viewed as a conforming change and a continuation of present law. H.R. Conf. Rep. No. 599, 105<sup>th</sup> Cong., 2d Sess. 213, 215 (June 24, 1998); accord S. Rep. No. 174, 105<sup>th</sup> Cong., 2d Sess. 22, 24 (April 22, 1998); H.R. Rep. No. 364 (Part I), 105<sup>th</sup> Cong. 1<sup>st</sup> Sess. 42-43, 137 (October 31, 1997). There was also a technical drafting change.<sup>1/</sup>

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<sup>1/</sup> A prior reference to the committees specified in clause (ii) was removed, apparently as surplusage. The committees referenced in clause (i)(which concerns the NTA's annual objectives report) are identical to those quoted above in clause (ii). The change occurred in the engrossed Senate amendment to H.R. 2676.

**B. The Stated Objective of TBOR II**

Consequently, the requirement that the NTA file the annual activities report "directly to the committees" and "without any prior review or comment from "other officer[s] or employee[s] of the Department" or OMB, in substance, dates back to TBOR II. The Congressional objective behind the provision was explained in the Ways and Means report on what became TBOR II:

To date, the Taxpayer Ombudsman has been a career civil servant selected by and serving at the pleasure of the IRS Commissioner. Some may perceive that the Taxpayer Ombudsman is not an independent advocate for taxpayers. . . . [I]n order to ensure that the Congress is systematically made aware of recurring and unresolved problems and difficulties taxpayers encounter in dealing with the IRS, the Taxpayer Ombudsman should have the authority and responsibility to make independent reports to the Congress in order to advise the tax-writing committees of those areas.

The Taxpayer Advocate is required to make two annual reports to the tax-writing committees. . . . The second report is on the activities of the Taxpayer Advocate during the previous fiscal year. The report must . . . contain a summary of at least 20 of the most serious problems which taxpayers have in dealing with the IRS [and] include recommendations for such administrative and legislative action as may be appropriate to resolve such problems . . . .

The reports submitted to Congress by the Taxpayer Advocate are not subject to prior review by the Commissioner, the Secretary of the Treasury, any other officer or employee of the Department of the Treasury, or the Office of Management and Budget. The objective is for Congress to receive an unfiltered and candid report of the problems taxpayers are experiencing and what can be done to address them. The reports by the Taxpayer Advocate are not official legislative recommendations of the Administration; providing official legislative recommendations remains the responsibility of the Department of Treasury.

H.R. Rep. No. 506, 104<sup>th</sup> Cong. 2d Sess. 23-25 (March 28, 1996)(on H.R. 2337). <sup>2/</sup>

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<sup>2/</sup> TBOR II passed on a voice vote in the Senate, without any competing Senate bill and without being sent to the Senate Finance Committee. See 142 Cong. Rec. S7753 (daily ed. July 11, 1996)(remarks of Senator Lott). Identical "direct submission"

**C. Hearings Leading to the Passage of TBOR II**

The "filtering" of legislative recommendations through the Treasury legislative coordination and clearance process had been discussed in hearings that had occurred the year earlier on various predecessor taxpayer rights bills, which included the independent reporting provision. The then-Deputy Assistant Secretary for Tax Policy, Cynthia Beerbower, took exception to the provision in prepared statements, and the following colloquy ensued:

**Chairman JOHNSON.** Your testimony suggests on page 10 that you oppose the provision of these reports to the committee.

**Ms. BEERBOWER.** We oppose the provision of legislative tax from proposals [sic] going directly from the ombudsman to the committee without the review that is institutional in the Office of Tax Policy -- the revenue estimating, the balancing, the input, the conflicts with other provisions-- and without filtering that through the Secretary of the Treasury and ultimately the President in order to speak with one voice on tax legislation.

**Chairman JOHNSON.** I appreciate your concern with the Treasury having a single voice. I hope you will think this over and discuss it with us in the days ahead, because I think there is some merit, frankly, to that discussion going on publicly, to the ombudsman having the responsibility to report things as he sees it to us, and our having the responsibility to work with you and listen. I think certainly the Nation does need one voice on tax policy.

But particularly in today's world, it is important that some of those controversies be discussed and the resolution be a matter of public process. And so I hope you will work with us to reconsider that position on your part.

Exploring the Development of Taxpayer Bill of Rights II Legislation, Hearing Before the Subcommittee on Oversight of the Ways and Means Committee, 104<sup>th</sup> Cong., 1<sup>st</sup> Sess. 77 (March 25, 1995)(considering H.R. 390, S. 258, H.R. 661, and Title V of H.R. 11).

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provisions, offered on comparable rationales, had been introduced in prior taxpayer rights bills. See, e.g., H.R. Rep. No. 280(II), 104<sup>th</sup> Cong. 1<sup>st</sup> Sess (October 17, 1995)(on section 13301(a) of H.R. 2491); H.R. Conf. Rep. No. 1034, 102d Cong., 2d Sess. (October 5, 1992)(on section 5001(a) of H.R. 11).

We understand from discussions with former Taxpayer Advocate Lee Monks that informal reporting to Congress was started in 1992 at the request of Chairman Pickle, wherein a report to the Ways and Means Committee dealing only with the "most serious problems" was institutionalized. See I.R.C. §7803(c)(2)(B)(III). According to Mr. Monks, the practice was suspended when the Chairmanship passed to Rep. Nancy Johnson, and was resumed in a more elaborate form with TBOR II.

Mr. Monk's recollection is confirmed by hearing testimony on early TBOR II legislative proposals. This hearing testimony also shows former Taxpayer Ombudsman Damon O. Holmes being vigorously encouraged by Congressman Anthony to provide his legislative proposals directly to the subcommittee for the record. The request followed Chairman Pickle's observation of concerns being raised that "your office is unable to bring taxpayers' problems and perhaps legislative remedies to the attention of Congress without first getting the approval of the IRS or the Treasury." The request was also preceded by questioning about how the Ombudsman made legislative recommendations within the administrative policy chain and by Mr. Holmes' expressing concerns about providing recommendations directly to Congress due to "restrictions that might be there in the Treasury legislative proposal process." Relevant testimony abstracted from that hearing is presented as Attachment A. See Reforms to Establish Taxpayer Safeguards and Protect the rights of Taxpayers Under the Internal Revenue Code, Hearings Before the Subcommittee on Oversight of the Ways and Means Committee, 102d Cong., 1<sup>st</sup> Sess. 260-264 (July 18 and September 25, 1991)(hearings prior to H.R. 11 as reported by Ways and Means, containing the relevant provision). The administrative proposals for statutory revision were ultimately provided for the record of the hearing. See id. at 27, 81-259.

## II. PRIOR PRACTICE

As a matter of practice, we understand from OTA employees involved in the creation of activities reports, both before and after RRA 98, that Counsel review of draft legislative recommendations was not sought. Lee Monks advised that his failure to seek Counsel review of the legislative recommendations in the activities report was not because he viewed clause (iii) as *necessarily* precluding such review at the time, rather, it was because he thought such a review was a sensitive issue and ultimately not necessary. Mr. Monks offered that Counsel usually had the opportunity (at one time or another before the report was drafted) to comment on ideas that were later recommended by him through the report (e.g., interest capping, changes to offer in compromise). He stated that he did not feel bound by those comments.

We also heard from Mr. Monks and current employees that Counsel *input* for the report is solicited for certain items and that, in the past, Legislative Affairs was consulted on matters of style. Mr. Monks stated that he viewed this type of interaction as within the intention of clause (iii), which he understood to insulate his office from the strictures of the normal Treasury coordination and clearance process and simply require a true "product of the Advocate."

### III. DISCUSSION

#### A. The Language Cannot Be Taken Literally.

The language of clause (iii), taken literally, would preclude the National Taxpayer Advocate from sharing drafts of the activities report with "any other officer or employee of the Department of the Treasury," which would include his staff.<sup>3/</sup> Such a literal construction is simply implausible and impracticable. Therefore, we look to the legislative history to ascertain legislative intent.

#### B. The Purpose of the Provision is to Insulate the Taxpayer Advocate from the Normal Coordination and Clearance Process for Purposes of the Report and to Assure an Independent Report.

The purpose of the provision was twofold: to provide Congress with "an unfiltered and candid report of the problems taxpayers are experiencing and what can be done to address them" and to ensure the appearance of independence of both the report and the Advocate. As regards legislative recommendations, this unfiltered and independent report must be distinguished from the formal process of making legislative recommendation in the Department, which involves mandatory and sometimes copious reviews and clearance within the Department and beyond. As a general matter, the Office of Management and Budget coordinates and clears the legislative programs of Executive agencies under OMB Circular A-19. Within the Department:

Draft legislation, proposed Executive Orders, legislative reports, legislative comments, legislative programs, and congressional testimony prepared within the Departmental Offices or Treasury

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<sup>3/</sup> RRA 98 established OTA "in the Internal Revenue Service" and excludes service as an employee of OTA from the preemployment restriction on National Taxpayer Advocate incumbents. I.R.C. §§ 7803(c)(1)(A),(B)(iv). This restriction normally prevents appointment if the incumbent was an IRS employee within the preceding 2 years. Thus, for these reasons and others, OTA employees must be regarded as IRS employees and, therefore, employees of the Department.

bureaus that express the official views of the Department or any office or bureau shall, consistent with law, be reviewed and coordinated within the Department prior to transmittal to the Congress, Office of Management and Budget, any other agency or department of the Federal Government or otherwise being made public.

TO 113-02 ¶ 1 (July 25, 1990). This order applies, without exception, to all offices and bureaus of the Department. Procedures to be followed by Departmental offices and Treasury bureaus for coordinating and clearing proposed legislation and other defined legislative items (including a "recommendation or proposal for specific legislative action") are further prescribed in TD 28-02 (July 26, 1990). In sum, the relevant orders and directives provide for Executive and Departmental coordination, clearance, and transmission of draft tax legislation proposed by bureaus, including recommendations for specific legislative action, except where such coordination and clearance are inconsistent with law. The House report distinguishes the Advocate's legislative recommendations from legislative recommendations that would be subject to these processes (in the absence of statutory language to the contrary). In effect, Congress sought to ensure that the legislative recommendations of the Advocate were made without interference (or "filtering") from these other offices, whose program and other interests might differ from those of the Advocate.

C. The Statute Can Be Honored with the Participation of Counsel.

It would be nearly impossible to comply with the literal language of clause (iii), and so you must comply with the language as informed by its purpose, which is to create an independent, unfiltered, and candid report and set of recommendations. We think this can be accomplished with Counsel assistance structured in the manner that you have suggested. We distinguish this type of Counsel assistance from the compulsory review and clearance of legislative proposals set forth in TO 113-02 and TD 28-02. These types of "review" clearly could compromise your independence as institutional author and result in a "filtered" product, even if "filtering" only means that competing values would be introduced into consideration, if not the text. By contrast, the review in question is at your request and continues at your sufferance. You are under no obligation, legally or administratively, to accept the comments or suggested revisions made by these Counsel employees, and may submit report text as originally provided to them, if you please. While not beyond all doubt, with the appropriate procedures in place, we believe that the intentment of clause (iii) will be met, the statute complied with, and the product made better by Counsel assistance.

#### D. Prudence Dictates the Use of Structural Separations.

To assure that there is not even the potential for collateral or indirect influence on your report, we agree that an attorney or attorneys from Counsel reviewing the recommendations should be "walled off" from the rest of Counsel, including Counsel supervisors, for the sole purpose of reviewing legislative recommendations.<sup>4/</sup> The object of such a procedure in this case is just the opposite of more typical "walling off" procedures, which exist as screening mechanisms employed by law firms, accounting firms, and brokerage houses to avoid imputed disqualification.<sup>5/</sup> Such walls are typically erected around a member or employee of a legal or other organization to keep that person's personal, economic, or professional interest or knowledge in a matter or matters from being imputed to the organization, thereby disqualifying the firm from working on the same matter or matters. By contrast, what is necessary here is a procedure that insulates the employing organization from working on or influencing a matter, a "black box" in effect, where the attorney or attorneys working on the review of the NTA's legislative recommendations are isolated from the control, review, and supervision of other Departmental components and officers (including their legal organization) to assure that Departmental policy interests (other than those represented by the NTA) are not allowed to impact the report and that the normal institutional arrangements are not allowed to appear to compromise NTA's independence.

#### IV. RECOMMENDED TERMS FOR AGREEMENT

Such a "black box" should be crafted to allow Counsel attorneys to work directly on behalf of the NTA with respect to the review of legislative recommendations. These attorneys, while remaining employees of the Office of Chief Counsel, would not be under the supervision, direction, authority, or responsibility of other Office of Chief Counsel officials or employees with respect to the work being performed on behalf of the NTA. Rather, with respect to such work, these attorneys would be under the direct supervision of the NTA, subject to the general restriction that they would not be placed into situations of ethical conflict. The structure of the "black box" should allow the attorneys to be free to review, provide advice on, and support NTA positions that may be contrary to those established by the Departmental Offices,

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<sup>4/</sup> Another effective procedure would be to detail a Counsel (or other attorney) to your office for this particular engagement.

<sup>5/</sup> Sometimes referred to as a "Chinese Wall," the firm's screening device serves as an elaborate and extraordinary, yet effective and impregnable, barrier against transgression, as did the Great Wall of China.

the Commissioner, or the Chief Counsel. The attorneys in the "black box" would also be in the position to professionally support the policy result preferred by the NTA, subject to the applicable laws, the canons of ethics, and the rules of conduct.

[REDACTED]

- [REDACTED]

DP

- [REDACTED]
- [REDACTED]
- [REDACTED]

DI-

V. CONCLUSION

It is our opinion that Office of Chief Counsel attorneys can participate in the review of the legislative recommendations made in connection with your annual activities report, without violating I.R.C. § 7803(c)(2)(B)(iii). However, prudence dictates that certain structural separations be put in effect that will ensure the fact and appearance of the independence of that report.

Should you have any questions or concerns, please do not hesitate to phone me.

Attachment(s): 1

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[REDACTED]

DP

ATTACHMENT A (GLS-116374-99)

*Abstracts from*

Reforms to Establish Taxpayer Safeguards and Protect the rights of Taxpayers Under the Internal Revenue Code, Hearings Before the Subcommittee on Oversight of the Ways and Means Committee, 102d Cong., 1<sup>st</sup> Sess. (July 18 and September 25, 1991)

Chairman PICKLE [continuing]. . . .

Now, some concerns have been raised that because the Ombudsman position was not statutorily created, your office is unable to bring taxpayers' problems and perhaps legislative remedies to the attention of Congress without first getting the approval of the IRS or the Treasury. In the overall view of problems we have, that we are going to be discussing today, what, in your judgment, are the 10 most significant problems encountered by taxpayers?

. . . .

Chairman PICKLE. Now, have you in the past informed the Congress of these specific items that you think are the outstanding problems that we ought to work on or try to correct?

Mr. HOLMES. Well, I have talked to members of the committee's staff, and we have talked about problems in general. I don't think I have listed them in exactly that way. We have talked about some specific problems.

Chairman PICKLE. Have you listed them in any way with respect to a written listing of these items?

Mr. HOLMES. Not to this committee, no Sir.

Chairman PICKLE. Has the Congress asked you to submit this type of data or these kind of questions?

Mr. HOLMES. No sir, they have not.

Chairman PICKLE. Has this committee had any conversation with you and asked you to submit this general listing to us?

Mr. HOLMES. I am not aware of such a request. I have made annual reports to the Congress on treatment of taxpayers under the Bill of Rights requirement. Those are made jointly with the Assistant Commissioner of Taxpayer Services, but I am not aware of any specific formal request for issues, no sir.

Chairman PICKLE. Well, let me ask you then, why haven't you submitted a list of these main items that are contentious and troublesome so that this committee or the Congress could look at it?

Mr. HOLMES. Well, I can't really say, I guess, why I haven't done that specifically. I have routinely raised problems inside the Service and worked to get them solved. I think that in a lot of the areas I mentioned, we are actually doing things as a result of the activities of my office, and the problems are being addressed, generally.

I do have, of course, proposed legislation, if you are talking about that. The reasonable requirement, in my opinion, at the present time, is for Treasury to exercise its responsibilities in the policy area. That would require that legislative proposals come from there.

Chairman PICKLE. Have you made a listing of these serious problems to the Treasury? Has Treasury or the IRS objected or had a policy against you sending these suggestions to this committee or to the Congress?

Mr. HOLMES. That kind of conversation has not occurred, sir. What has happened is that I have presented, in our normal process, ideas to our legislative liaison, and that office then packages those suggestions into a format that goes through the Commissioner, Treasury, and OMB to this committee or to others.

Chairman PICKLE. Well, would you personally object if, when you make your annual report to the Congress, you list these items and specifically point out in detail what they are and what we perhaps can do to correct them or to make them more functional, more efficient, and more fair?

Mr. HOLMES. I can't at the moment think of any reason to object to that.

....

Mr. ANTHONY. Thank you, Mr. Chairman. Mr. Holmes, have you in fact sent specific ideas to the Commissioner for the improvement of the operation of the Service?

Mr. HOLMES. I have sent specific problems that I think need addressing. In some cases, I may have suggested the direction of an improvement, but what I mainly have done is identify problems that need to be solved so that other people can help find ways to solve them.

In some cases, I might suggest a direction I think it ought to go, but mainly what I am doing in those situations is pointing out systems that I think are unfair or difficult to understand, that sort of thing.

Mr. ANTHONY. Can you share those with us for the record? I assume they are not in your testimony?

Mr. HOLMES. No sir, they are not in my testimony, and I have given them to, as I said, to the Legislative Liaison for presentation. I am willing--

Mr. ANTHONY. Can you give them to us--

Mr. HOLMES. Sir?

Mr. ANTHONY. Can you give them to us so that we can put them in the record of this hearing?

Mr. HOLMES. I am not sure, really, of the restrictions that might be there in the Treasury legislative proposal process, Mr. Anthony. I have no opposition to giving you the ideas. I am not --

Mr. ANTHONY. Then why don't you do this. Why don't you give them to us unless somebody at Treasury tells you that you are not allowed to do it. Is that fair enough?

Mr. HOLMES. Yes, sir. I think that is fair enough.

Mr. ANTHONY. Fine. The Commissioner is put on notice and the Treasury is put on notice that we are requesting it, and if they do not want it done, then they will specifically have to tell you not to do it, and I will ask the staff to followup with you in that regard.

Mr. HOLMES. Yes, sir.

Mr. ANTHONY. In other words, I don't want it to be your responsibility not to do it. I want somebody above you who has the authority and responsibility to say no, that it cannot be done. Then we can ask that person why it can't be done.

So I am assuming that you can. I want it on the record, and we will put the burden on them to stop it.

Reforms to Establish Taxpayer Safeguards and Protect the rights of Taxpayers Under the Internal Revenue Code. Hearings Before the Subcommittee on Oversight of the Ways and Means Committee, 102d Cong., 1<sup>st</sup> Sess. 260-264 (July 18 and September 25, 1991)(hearings prior to H.R. 11 as reported by Ways and Means, containing the relevant provision).