Advance Pricing Agreements: Confidential Return Information or Written Determinations Subject to Release?

John L. Abramic
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INTRODUCTION

The globalization of markets, business, and economics consistently has spawned new challenges for the legal community. As international business becomes commonplace, conflicts or differences in the laws of many nations can create a variety of legal problems. In particular, the Internal Revenue Service ("IRS") began negotiating advance pricing agreements ("APAs") in 1991 to deal with taxation problems arising from differences in international taxation schemes.1 The APA system, however, creates a tension between the need for public oversight of the IRS versus a company's right to privacy and confidentiality.

An APA is a voluntary negotiation between the IRS and a company with international holdings that delineates the company's internal pricing scheme, which thereby determines its tax liability. During the course of negotiation, in order to secure a favorable pricing scheme, a company may divulge different types of proprietary information to the IRS. This leads to the question of whether the IRS should disclose APA records and, if so, to what extent?

Section 6103 of the tax code makes all taxpayer return information confidential, and therefore not fit for release to the public.2 Section 6110 of the tax code calls for the release of all IRS written determinations,3 and the Freedom of Information Act

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1. See Joint Committee on Taxation, JCT Describes Amendment to Extenders Bill, 1999 Tax Notes Today 186-13 (Sept. 27, 1999).
3. See id. § 6110.
("FOIA"), subject to certain exceptions, makes all governmental agency information available to the general public.

Since the APA program's inception in 1991, the IRS refused to require publication of APAs on the ground that to do so would violate taxpayer privacy and confidentiality rights. In 1996, the Bureau of National Affairs ("BNA") filed suit against the IRS in an effort to force the disclosure of APAs pursuant to section 6110 of the tax code and the FOIA. Proponents of disclosure fear that the IRS is building a secret body of law with respect to APAs and hope that disclosure will prevent the IRS from negotiating in an arbitrary and capricious fashion. The IRS fears that disclosure will invade the privacy and confidentiality of cooperating businesses and ultimately discourage participation in the APA process. After months of litigation, the IRS made the concession that APAs were written determinations subject to disclosure under section 6110, but the two sides still disagreed about the level of information that should be disclosed. In late 1999, after the IRS concession, Congress enacted legislation that classifies APAs as confidential return information under section 6103. The legislation prevents the publication of individual APAs and instead mandates the production and publication of an annual Treasury Department report containing generalized information about the APA system.

This Note will examine the law and policy involved with publication versus non-publication of APAs. Part I will provide a description of APAs and the recent developments surrounding attempts at forcing APA disclosure. Part II will discuss the relevant law involved: the FOIA, a comprehensive disclosure statute; section 6110 of the tax code which mandates the disclosure of IRS written

5. See id. § 552.
12. Id.
determinations; and section 6103 of the tax code which protects confidential return information from disclosure. The history of the relevant law provides a basis for understanding the tension between publication of IRS documents versus taxpayer confidentiality, and how Congress and the courts have attempted to address that tension. Part II then will analyze the relationships between the different sources of relevant law and reveal that for the purposes of APA disclosure, courts recognize no meaningful difference between the FOIA and section 6110. Part II finally will compare APAs with IRS written determinations and conclude that because APAs contain legal analysis, they fall under the definition of IRS section 6110 written determinations. Part III will explain that the BNA case, had it continued, would have resulted in the disclosure of redacted APAs. Part III then will describe the new legislation preventing APA disclosure and ultimately argue that redacted APAs should be released because they present no threat to participant confidentiality and because publication is necessary for adequate agency oversight.

I. ADVANCE PRICING AGREEMENTS

A. What Is an Advance Pricing Agreement?

It is increasingly common for companies to own facilities in multiple countries. A particular company may own manufacturing centers, service centers, or other subsidiaries situated in a number of different tax jurisdictions. Often companies prefer to establish subsidiaries rather than transact with independent agents because of the expectation that the former alternative “involve[s] lower transaction costs . . . and therefore higher profit[s]” result.\(^\text{13}\) In order to realize the desired low transaction costs, companies set up pricing schemes between themselves and their subsidiaries. This type of pricing scheme is referred to as transfer pricing.\(^\text{14}\) For example, if an American automobile manufacturer (e.g., Ford Motor Company) owns subsidiary X, a tire producer located in another country, Ford can set the tire price that subsidiary X charges the manufacturer. In addition, if Ford owns several other subsidiaries, possibly in other countries, it can set the price that those subsidiaries will pay for X’s


tires. The internal price fixing or pricing scheme is called transfer pricing.

In their quest for more attractive profit margins, companies operating in different tax jurisdictions sometimes create transfer pricing schemes structured in such a way to ensure that the subsidiaries in the lowest tax jurisdictions will maximize profits, thereby saving the company from quantifiable tax liability. For example, in the above hypothetical concerning Ford, if subsidiary X produces tires in a country with lower tax liability than the countries in which Ford’s other subsidiaries are located, Ford would create a transfer pricing scheme that charges a premium for X’s tires. By charging its subsidiaries a premium for X’s tires, Ford could maximize the profits of a subsidiary sitting in a low tax jurisdiction. This type of profit control or capital shifting may save a company large sums of money depending on the volume of business that is done internationally.

Section 482 of the tax code, however, provides that “[i]n any case of two or more organizations... owned or controlled... by the same interests,” the IRS can allocate gross income upon the determination that such allocation is necessary to “prevent evasion of taxes or clearly to reflect the income of any of such organizations.” Therefore, in the above hypothetical, if the IRS felt that Ford’s transfer pricing scheme was constructed in order to avoid federal taxes, the IRS could fix a pricing scheme, for tax purposes, that was not tax evasive.

In an effort to simplify and facilitate proper tax liability reporting by companies using transfer pricing, the IRS created APAs. “An APA is a negotiated agreement between the IRS and a private corporation that sets forth the formulas and methods to be used when determining the tax on the corporation’s cross-border transactions.” The APA system is a cooperative process from which “taxpayers and the government derive significant benefits.”

15. See Ernst & Young LLP, Transfer Pricing: Risk Reduction and Advance Pricing Agreements, 10 Tax Notes Int’l 293, 299 (1995) (finding that of multinational corporations (“MNCs”) surveyed, 40% of British MNCs, 44% of German MNCs, 48% of Canadian MNCs, 50% of U.S. MNCs, 56% of Australian MNCs, 70% of Japanese MNCs, and 72% of Dutch MNCs considered transfer pricing to be the most important international tax issue they face).
uncertainties and costs of complex negotiations and litigation with the IRS, and the government ensures that it collects the appropriate amount of taxes while also avoiding a fight.\textsuperscript{19} APAs are the most significant determinant of the corporate tax liability for most major corporations because depending on IRS administration, tax liability can vary by as much as twenty-five percent.\textsuperscript{20} Some scholars believe that transfer pricing issues are some of the most important issues facing the government and business today.\textsuperscript{21} In fact, in a 1995 survey, approximately eighty percent of polled companies identified transfer pricing as the biggest issue facing multinational corporations.\textsuperscript{22} Many other countries have instituted programs similar to the IRS APA system,\textsuperscript{23} and, as a result, companies must sometimes negotiate to set pricing schemes with multiple countries.\textsuperscript{24}

\section*{B. Publication of Advance Pricing Agreements?}

Through the FOIA or section 6110, the IRS has been forced to release a variety of records.\textsuperscript{25} Most of the records published by the IRS that are relevant to the APA issue involve an IRS answer to a request from a taxpayer or an IRS field agent for a legal conclusion on a given set of facts or circumstances.\textsuperscript{26} For example, section 6110 mandates the release of private letter rulings ("PLRs").\textsuperscript{27} PLRs are memoranda issued by the IRS at the request of a taxpayer seeking advice as to the tax consequences of specific transactions.\textsuperscript{28} One particular example of a PLR involved a taxpayer, suffering from

\begin{itemize}
  \item \textsuperscript{19} Id.
  \item \textsuperscript{20} See Field, supra note 17.
  \item \textsuperscript{21} Id.; see also Arthur L. Nims, III, Tax Court Management of Jumbo Cases: The New Challenge, 38 Fed. B. News & J. 330 (1991) (projecting lost revenue ranging from $100 million to $10 billion). \textit{But see} Joint Committee on Taxation, supra note 1 (arguing that the future complexities of international business will make the current APA system impossible to administer).
  \item \textsuperscript{22} See Ernst & Young LLP, supra note 15, at 294.
  \item \textsuperscript{23} See, e.g., Timothy W. Cox, Australian Tax Office Releases Draft Ruling on Advance Pricing Agreements, 9 Tax Notes Int'l 1279 (1994); Albertina M. Fernandez, Mexico Issues First Maquiladora APA, 11 Tax Notes Int'l 1276 (1995).
  \item \textsuperscript{24} See, e.g., John Turro, IRS Inks Two Pricing Agreements in Derivative Products Area, 55 Tax Notes 725 (1992).
  \item \textsuperscript{26} Hickman, supra note 10, at 186-88 (comparing and contrasting APAs with other IRS records that are disclosed).
  \item \textsuperscript{27} 26 U.S.C. § 6110 (1994).
  \item \textsuperscript{28} Tax Analysts, 505 F.2d at 352.
\end{itemize}
AIDS with a poor prognosis, who wrote to the IRS for some guidance concerning the tax consequences of selling a life insurance contract to a viatical settlement company. The IRS issued a PLR to the taxpayer stating that although the tax code does exclude payments received under a life insurance contract from gross income, those payments are only excluded from gross income if they are paid by reason of the death of the insured. Therefore, if the taxpayer assigned his or her life insurance contract for consideration, the transaction would be classified as a sale of property for tax purposes and would be taxable. The taxpayer could then use the private ruling for guidance when considering the tax consequences of the proposed insurance contract assignment.

PLRs and other types of IRS written determinations typically include a summary of facts, recitation of the relevant law, and an application of the law to the facts. Lawyers are sure to recognize this format as the general standard for case law. Thus, just as bodies of law from other disciplines provide guidance to citizens concerning the application of the law to a wealth of different circumstances, IRS written determinations, if available to the public, may provide the citizenry with guidance concerning the application of the tax code to different transactions.

"It is well established that information which either creates or provides a way of determining the extent of substantive rights and liabilities constitutes a form of law that cannot be withheld from the public." Some scholars believe that APAs contain information that provides individual taxpayers with guidance for determining their rights under the tax laws with respect to APA negotiations and, therefore, that APAs should not be kept from the public.

In 1996, the IRS, under the authority of tax code confidentiality provisions, denied BNA's request for public release of APAs. On February 27, 1996, BNA filed suit in the District Court for the District

30. Id.
31. Id.
32. See generally P.L.R. 94-43-020 (July 22, 1994).
33. Tax Analysts, 505 F.2d at 353.
of Columbia to compel the release of APAs under section 6110 and later amended its complaint to include a disclosure request under the FOIA. BNA argued that APAs, like other published IRS records, "contain statements of policy and legal interpretation [and] should be published for the benefit of other taxpayers." The IRS argued against APA publication on the ground that APAs contain sensitive company information that is protected by FOIA exemptions and IRS confidentiality provisions. After months of litigation and disputes over discovery, the IRS conceded that APAs should be classified as written determinations under the disclosure provisions of section 6110 of the tax code. Following the IRS concession, the parties continued to squabble over which information should be disclosed and which information should be redacted for confidentiality purposes. Disclosure, though, was imminent.

In response to confidentiality concerns from members of industry and current members of the APA program, Congress enacted legislation (Public Law No. 106-170) classifying APAs as confidential return information, thereby preventing APA disclosure. Debate continues over whether APAs, or some of the information contained in them, should be published, and whether there was adequate debate, prior to the enactment of APA legislation, on public policy objectives concerning the issue. This Note now will analyze the relevant law at issue prior to the enactment of Public Law No. 106-170 and conclude that the BNA lawsuit would have been successful regardless of the IRS concession. It then will compare APA publication with the disclosure mandated by the new legislation.

38. Hickman, supra note 10, at 184.
39. Id. at 185.
41. See Massey, supra note 9, at 2389.
42. Id. at 2389-90.
43. Id. at 2389.
II. RELEVANT LAW

A. The Freedom of Information Act

1. History

The FOIA's predecessor, section 3 of the Administrative Procedure Act,\(^44\) although enacted to give public access to governmental information,\(^45\) contained language that prompted administrative agencies to treat it as a withholding statute, or a statute that prevented disclosure.\(^46\) Congress enacted the Freedom of Information Act in 1966 as an amendment to the information section of the Administrative Procedure Act to promote governmental honesty and facilitate public access to information about governmental activities and policies.\(^47\) Legislators deemed public access to information as necessary to prevent arbitrary governmental action and also to nurture the development of an informed electorate.\(^48\) Although the FOIA improved the disclosure provisions of the Administrative Procedure Act, the 1966 Act still failed to accomplish its purpose of compelling substantially greater disclosure of agency information to the public.\(^49\) Congress then amended the FOIA in 1974 to better accomplish the goals of broad disclosure.\(^50\)

2. Scope of the FOIA

The FOIA imposes a duty on certain governmental agencies to publish, or make available for public viewing, certain agency records and information.\(^51\) In addition, the public may access agency information upon specific request,\(^52\) while the government has the burden of justifying non-disclosure.\(^53\) The agencies subject to disclosure duties under the FOIA include "any executive department, military department, Government corporation, Government controlled corporation, or other establishment in the executive

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46. Id. at 695-96.
48. See Fruehauf Corp. v. Internal Revenue Serv., 522 F.2d 284, 290 (6th Cir. 1975).
50. See Jordan v. United States Dep't of Justice, 591 F.2d 753, 755 (D.C. Cir. 1978).
51. 5 U.S.C. § 552(a)-(b).
52. Id. § 552(a)(3).
53. Id. § 552(a)(4)(B).
branch of the Government... or any independent regulatory agency. The FOIA is based on a broad policy of full disclosure, providing for the dissemination of information to all members of the public and applying to all governmental agencies.

Under the provisions of the FOIA, an agency must: publish in the Federal Register, descriptions of the organization, statements of the general course of functions and procedures, rules of procedure, and statements of substantive rules and general policy; make available to the public, final opinions and adjudication of cases, statements of policy not published in the Federal Register, administrative staff manuals, copies of records that have been submitted upon request and are "likely to become the subject of subsequent requests"; and upon request, submit to "any person," any records not described in (a) or (b) above, as long as the request reasonably describes the records and follows procedural rules.

Although the FOIA "creates a judicially enforceable policy that favors a general philosophy of full disclosure," courts must balance the public's right to agency information with certain governmental interests in prohibiting disclosure. Therefore, the FOIA provides nine categories of records that are exempt from disclosure. Those exemptions include, among others: matters specifically exempted from disclosure by statute, trade secrets, commercial or financial information, and privileged or confidential material. In addition, the statutory language suggests that courts construe these sole exemptions very narrowly. Furthermore, the exemption provision calls for the release of information that is segregable from portions

54. Id. § 552(f).
57. Id. § 552(f).
58. See id. § 552(a).
60. Id. at 78.
61. 5 U.S.C. § 552(b).
62. Id. § 552(b)(3).
63. Id. § 552(b)(4).
that are exempt. Therefore, a document requested under the FOIA, containing both protected and unprotected material, must be released after the redaction of the protected material.

B. Section 6103

1. Confidential Return Information

"In the wake of Watergate and White House efforts to harass" enemies, Congress amended section 6103 of the Tax Code in order to protect the "privacy interests of individuals and the investigatory and enforcement interests of the government." Section 6103 classifies return information as confidential and therefore prevents its public disclosure. Return information is defined by section 6103 of the tax code as:

A taxpayer's identity, the nature, source, or amount of his income, payments, receipts, deductions, exemptions, ... tax liability, ... or any other data, received by, recorded by, prepared by, furnished to, or collected by the Secretary with respect to a return or with respect to the determination of the existence, or possible existence, of liability (or the amount thereof) of any person under this title for any tax, penalty, interest, fine, or other imposition, or offense.

In addition, return information also includes any written determination, which is generally an IRS interpretation of the tax code as it applies to a specific circumstance, or any background file relating to such written determination not available to the public under section 6110 of the tax code. The courts have interpreted section 6103 broadly to include practically all data collected by the IRS that pertains to a taxpayer's tax liability.

65. See 5 U.S.C. § 552(b). This provision states that
Any reasonably segregable portion of a record shall be provided to any person requesting such record after deletion of the portions which are exempt under this subsection. The amount of information deleted shall be indicated on the released portion of the record, unless including that indication would harm an interest protected by the exemption in this subsection under which the deletion is made. If technically feasible, the amount of the information shall be indicated at the place in the record where such deletion is made.

67. See Raby, supra note 64.
69. Id. § 6103(b)(2)(A).
70. Id. § 6103(b)(2)(B).
71. See Lehrfeld v. Richardson, 954 F. Supp. 9, 13 (D.D.C. 1996) (noting that "return information is defined broadly by the statute to include almost any information compiled by the IRS in connection with its determination of a taxpayer's liability").
2. The Haskell Amendment

Although courts interpret section 6103 broadly, section 6103(b)(2), known as the Haskell Amendment,72 expressly excludes “data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.”73 Congress enacted the amendment to ensure that compilations of data and statistical studies prepared by the IRS using data disclosed to it by taxpayers, would remain subject to disclosure.74 Some courts have construed the provision to allow for disclosure following the redaction of identifying information,75 while others have found that it forces the IRS to reconfigure return information to conceal identity.76 It is clear that courts have construed the Haskell Amendment narrowly by erring on the side of secrecy, a practice that is consistent with the broad reading of section 6103 confidentiality provisions.77 In Church of Scientology of California v. Internal Revenue Service, the Supreme Court held that the mere removal of identifying language is not sufficient to justify the disclosure of return information.78 The Court reasoned that in light of the legislative intent, the Haskell amendment is to be construed narrowly and applies only to statistical studies and compilations of data by the IRS.79 Therefore, by classifying APAs as return information under section 6103, Congress prevented APA disclosure. Even the redaction of identifying information will not remove APAs from the protection of section 6103 unless APA information was used in some type of statistical compilation.

3. Relationship to the FOIA

“A definite tension exists between the policy interests of privacy embodied in [section 6103] and those of disclosure embodied in the FOIA.”80 A minority position that first arose in the courts in 1979, and met with some approval, found that section 6103 was self-

76. See King v. Internal Revenue Serv., 688 F.2d 488 (7th Cir. 1982).
77. See Church of Scientology of Cal., 484 U.S. at 16; see also Aronson v. Internal Revenue Serv., 973 F.2d 962 (1st Cir. 1992); King, 688 F.2d at 488; Currie v. Internal Revenue Serv., 704 F.2d 523 (11th Cir. 1983).
78. See Church of Scientology of Cal., 484 U.S. at 18.
79. Id. at 17.
80. See Raby, supra note 64.
governing and not subject to review under the FOIA. As a "self-governing" statute, section 6103 was not subject to the FOIA's disclosure standards. For example, under section 6103, the agency seeking to prevent disclosure only had to provide a rational basis for its decision to withhold, while the FOIA mandates a "heavy presumption favoring reviewability of agency action." These courts gave great deference to nondisclosure provisions, using an arbitrary and capricious standard of review when scrutinizing an agency's decision to withhold information instead of the de novo review now used for scrutinizing agency decisions to withhold under the FOIA.

A majority of courts, however, have held that section 6103 is subject to FOIA standards. Section 6103 can co-exist with the FOIA if it is recognized as a section 552(b)(3) exemption, which provides for the prevention of disclosure in cases where statutes specifically provide for non-disclosure. It is now well settled that return information classified by section 6103 is protected from disclosure by the (b)(3) FOIA exemption. Therefore, a party seeking disclosure of APAs could bring a suit demanding disclosure under the FOIA. A court would review an IRS decision to withhold using a de novo standard instead of the arbitrary and capricious standard.

81. In Zale v. Internal Revenue Serv., a taxpayer attempted to inspect government documents that related to an ongoing investigation. 481 F. Supp. 486, 487 (D.D.C. 1979). The court based its decision on the fact that section 6103 was enacted within a few weeks of the FOIA amendment. Id. at 488. The statute, a complex piece of legislation that attempts to balance privacy interests with the need for public disclosure of agency information, made no mention of the FOIA even though Congress was well aware of it at the time. Id. at 488-89. Other courts adopted the Zale approach and held that section 6103 was self-governing and therefore not subject to a FOIA analysis. See White v. Internal Revenue Serv., 707 F.2d 897 (6th Cir. 1983); see also King, 688 F.2d at 488; Green v. Internal Revenue Serv., 556 F. Supp. 79 (N.D. Ind. 1982), aff'd, 734 F.2d 18 (7th Cir. 1984).
82. See Zale, 481 F. Supp. at 489.
83. Id. at 490.
84. See Green, 556 F. Supp. at 83-84.
85. The first appellate court to rule on the relationship between section 6103 and the FOIA determined that section 6103 could be reconciled with the FOIA through the (b)(3) exemption which provides for the prevention of disclosure in cases where statutes specifically provide for nondisclosure. See Tax Analysts & Advocates, 505 F.2d at 353-54; Church of Scientology of Cal., 484 U.S. at 11 (stating that "[section] 6103 of the Internal Revenue Code is the sort of statute referred to by the FOIA in 5 U.S.C. § 552(b)(3) relating to matters that are 'specifically exempted from disclosure by statute.'"); Tax Analysts, 117 F.3d at 611; Grasso v. Internal Revenue Serv., 785 F.2d 70 (3d Cir. 1986); Linsteadt v. Internal Revenue Serv., 729 F.2d 998 (5th Cir. 1984); Long v. Internal Revenue Serv., 742 F.2d 1173 (9th Cir. 1984); Currie v. Internal Revenue Serv., 704 F.2d 523 (11th Cir. 1983); Mason v. Callaway, 554 F.2d 129, 131 (4th Cir. 1977), cert. denied, 434 U.S. 877 (1977).
86. 5 U.S.C. § 552(b)(3).
87. See Tax Analysts, 117 F.3d at 611.
88. For a discussion of the necessity of a de novo review in cases where the IRS relies on the nondisclosure provision, see Long, 742 F.2d at 1173. The Ninth Circuit explained that
would have to mandate disclosure unless a FOIA exemption excluded the information sought from disclosure. Because section 6103 is classified as a nondisclosure statute under the FOIA, any information classified under section 6103 would be protected from disclosure. However, because section 6103 is subject to FOIA standards, the IRS, in order to prevent disclosure, could not simply produce an affidavit expressing a need for nondisclosure.89 The IRS, when trying to prevent disclosure, must have some burden to prove to a court that requested materials fall under the statutory definition of return information. But, because in camera inspection of documents often is not practical due to limited judicial resources,90 a court will accept a detailed, itemized, and indexed affidavit with justifications for exemption claims that will allow the court to make a determination as to exemption.91

C. Section 6110

1. Scope

At the same time Congress enacted section 6103 with the intention of protecting taxpayer privacy and confidentiality, it enacted section 6110, a disclosure provision.92 Section 6110 provides for the disclosure of the text of any IRS written determination and related background file documents.93 As noted earlier, the records released under section 6110 generally involve IRS interpretations of the tax code as it applies to specific circumstances or contemplated transactions.

judicial review must involve more than simply relying on the findings of the agency. Id. at 1182-83.


90. Id. at 88.

91. See Vaughn v. Rosen, 484 F.2d 820 (D.C. Cir. 1973), cert. denied, 415 U.S. 977 (1974). The affidavit described by the Rosen case is commonly referred to as a Vaughn Index. A Vaughn Index satisfies the following criteria:

(1) The Index should be contained in a single document complete in itself;
(2) must adequately describe each withheld document or deletion from a released document; and
(3) must state the exemption claimed for each withheld document or deletion and explain why the exemption applies.

See Segal, supra note 89, at 88.


93. Id.
Two FOIA lawsuits, successful at requiring the IRS to disclose PLRs, formed the basis for section 6110. Proponents of disclosure argued that IRS PLRs were developing into a secret body of law known only to a limited group of people in the tax profession. After the court ordered the release of PLRs, questions remained as to the specific types of information that should be disclosed. Congress then enacted section 6110, which attempts to define the types of IRS memoranda that should be disclosed.

Courts have classified the following IRS documents as written determinations subject to disclosure under section 6110: PLRs, issued to the taxpayer upon request; Technical Advice Memoranda, issued during an audit at the request of an IRS agent; General Counsel’s Memoranda, detailed analysis of an area of tax law written by the Office of Chief Counsel to other IRS personnel; Actions on Decisions, IRS responses to court decisions; and Field Service Advice Memoranda ("FSAs"). These documents may vary in their level of detail and may be intended for different audiences ranging from taxpayers to various IRS personnel. However, IRS written determinations follow the same general "caselaw" format described in Part I.B of this Note.

While section 6110 provides for the disclosure of many IRS documents, it also, like the FOIA, contains a list of exemptions.

96. See Joint Comm. on Tax’n, supra note 94.
98. See Fruehauf Corp., 566 F.2d at 577; Tax Analysts & Advocates, 505 F.2d at 352-53.
100. See Tax Analysts, 117 F.3d at 615.
102. The disclosure exemptions outlined in section 6110 are similar to those outlined in the FOIA. Section 6110 exemptions include:

(1) the names, addresses, and other identifying details of the person to whom the written determination pertains . . . ;
(2) information specifically authorized under criteria established by an Executive order to be kept secret in the interest of national defense or foreign policy . . . ;
(3) information specifically exempted from disclosure by any statute (other than this title) which is applicable to the Internal Revenue Service;
(4) trade secrets and commercial or financial information obtained from a person and privileged or confidential;
(5) information the disclosure of which would constitute a clearly unwarranted invasion of personal privacy;
(6) information contained in or related to examination, operating, or condition
Those exemptions include, among others, identifying details of the person to whom the written determination pertains,\textsuperscript{103} trade secrets, and privileged or confidential commercial or financial information.\textsuperscript{104} Therefore, even if a court classified APAs as written determinations subject to disclosure under section 6110, information determined by the IRS to be confidential or identifying must be redacted prior to release. The question then becomes, if confidential and identifying information is protected under disclosures mandated by both the FOIA and section 6110, what is the difference between the two statutes as they relate to APA publication?

2. Relationship with the FOIA

When BNA sued to force the disclosure of APAs, it brought an action under the FOIA and also under section 6110.\textsuperscript{105} Congress enacted section 6110 to provide for the disclosure of certain IRS documents without the need for the FOIA.\textsuperscript{106} In fact, section 6110 is the only vehicle that may be used to force disclosure of IRS “written determinations.”\textsuperscript{107} A Maryland district court, in 1978, held that “[s]ections 6103 and 6110 effectively displace the FOIA with respect

\begin{itemize}
\item reports prepared by, or on behalf of, or for use of an agency responsible for the regulation or supervision of financial institutions; and
\item (7) geological and geophysical information and data, including maps, concerning wells.
\end{itemize}

26 U.S.C. § 6110(c). The exemptions outlined in the FOIA are information:

\begin{itemize}
\item (1) established by an Executive order to be kept secret in the interest of national defense or foreign policy . . . ;
\item (2) related solely to the internal personnel rules and practices of an agency;
\item (3) specifically exempted from disclosure by statute . . . ;
\item (4) trade secrets and commercial or financial information obtained from a person and privileged or confidential;
\item (5) inter-agency or intra-agency memorandums or letters which would not be available by law to a party other than an agency in litigation with the agency;
\item (6) personnel and medical files and similar files the disclosure of which would constitute a clearly unwarranted invasion of personal privacy;
\item (7) records or information compiled for law enforcement purposes . . . ;
\item (8) contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions; or
\item (9) geological and geophysical information and data, including maps, concerning wells.
\end{itemize}


104. Id. § 6110(c)(4).
105. The court in BNA never ruled on the matter but also never indicated that a FOIA action could not be brought to compel the release of APAs. See Bureau of Nat’l Affairs, 24 F. Supp. 2d at 40.
106. See Fruehauf Corp., 566 F.2d at 577.
to written determinations of the IRS.\textsuperscript{108} In application, however, courts have not drawn a clear distinction between a lawsuit brought under the FOIA and section 6110 of the tax code.\textsuperscript{109}

For example, in 1997, in \textit{Tax Analysts}, a nonprofit corporation brought an action under the FOIA to compel the disclosure of FSAs. FSAs are written legal guidance prepared for IRS field service personnel, usually with respect to a specific taxpayer’s situation.\textsuperscript{110} “Each FSA includes a statement of issues, a conclusions section, a statement of facts, and a legal analysis section.”\textsuperscript{111} FSAs were not listed as written determinations under section 6110, but the nonprofit corporation was entitled to bring suit under the FOIA since the FOIA mandates the release of any agency record.\textsuperscript{112} In response to the IRS invoking a FOIA exemption\textsuperscript{3} by arguing that FSAs are confidential return information under section 6103,\textsuperscript{4} the court noted that section 6103 clearly falls within the third FOIA exception.\textsuperscript{5} It then distinguished the legal interpretations and analysis portions of FSAs from information protected from disclosure under section 6103.\textsuperscript{116} The court concluded that because of the similarities between FSAs and other section 6110 determinations—mainly that both contained legal analysis that was not personal to any particular

\textsuperscript{108} “Written determinations not open to public inspection under Section 6110 are confidential and non-disclosable under section 6103 and therefore exempt from the FOIA. The legislative history of the Tax Reform Act reveals that the Act was meant to supplant the FOIA in this case.” Grenier v. Internal Revenue Serv., 449 F. Supp. 834, 840-41 (D. Md. 1978).

\textsuperscript{109} \textit{See Fruehauf Corp.}, 566 F.2d at 577 (holding that section 6110 was the exclusive vehicle for obtaining the release of IRS written determinations). \textit{But see Taxation with Representation Fund}, 485 F. Supp. at 263 (requiring, under the FOIA, the release of general counsel’s memoranda, technical memoranda, and actions on decisions); \textit{Tax Analysts}, 117 F.3d at 609 (forcing the release of field service advice memoranda in an action under the FOIA).

\textsuperscript{110} \textit{See Tax Analysts}, 117 F.3d at 607-09.

\textsuperscript{111} \textit{Id.} at 609.

\textsuperscript{112} 5 U.S.C. § 552(a)(3) (mandating the disclosure of any agency record).

\textsuperscript{113} \textit{Id.} § 552(b)(3) (exempting information protected by other statutes from disclosure).

\textsuperscript{114} The IRS, relying on the broad reading of section 6103 contained in \textit{Church of Scientology of California}, also argued that all portions of the FSAs fell under the definition of section 6103 confidential return information. \textit{See Tax Analysts}, 117 F.3d at 611. The district court disagreed and found that the portions of the FSAs containing discussion of tax law principles, legal analysis, or possibly other types of nonfactual information not unique to any particular taxpayer, may not fall under the scope of section 6103. \textit{Id.}

\textsuperscript{115} \textit{See Tax Analysts}, 117 F.3d at 611.

\textsuperscript{116} \textit{Id.} at 614-16 (determining whether legal interpretations and analysis contained in FSAs fell under the definition of “any other data, received by, recorded by, prepared by, furnished to, or collected by the Secretary with respect to a return”). The court based its decision, in part, on the fact that each of the specific items mentioned in the beginning of section 6103(b)(2)(A) “is not only factual but unique to the specific taxpayer.” \textit{Id.} at 614. While the court does accept the Supreme Court’s broad reading of section 6103 as pertaining to the nondisclosure of any information that falls under the scope of the statute, the D.C. circuit court makes it clear that legal analysis and possibly other types of nonfactual information not unique to any particular taxpayer, may not fall under the scope of section 6103. \textit{Id.}
taxpayer—and because FSAs were not in existence when section 6110 was enacted,117 FSAs should be classified as written determinations and subject to disclosure.118

One outcome of the Tax Analysts case is that there seems to be no distinction between the disclosure protection afforded IRS documents under the FOIA and section 6110. Although the lawsuit in Tax Analysts was brought under the FOIA, the court found that FSAs were written determinations under section 6110.119 One scholar tries to make a distinction between a FOIA and section 6110 action to require APA publication.120 Kristin Hickman predicts that in the event of a FOIA action requesting APA publication, Tax Analysts seems to suggest that a court would only allow the release of “segregable legal analysis” portions of APAs.121 Hickman then notes that a different case can be made for APA publication under section 6110 as opposed to the FOIA by attempting to classify APAs as 6110 written determinations.122 However, when contrasting APAs with other IRS section 6110 documents, Hickman explains that FSAs, the subject of the Tax Analysts litigation, are distinguishable from APAs and classified as written determinations because they “contain a segregable legal analysis section.” Hickman therefore argues that the FOIA mandates the disclosure of APAs to the extent they contain segregable legal analysis, and then suggests that APAs may be classified as 6110 written determinations if they contain segregable legal analysis. This would indicate that regardless of whether a suit to compel the disclosure of APAs was brought under FOIA or section 6110, the critical determination rests on whether APAs, like other section 6110 documents, contain segregable legal analysis. Therefore, in order to determine whether or not the law requires APA disclosure,123 one must make a comparison between APAs and other publicly available IRS documents that contain legal analysis.

117. If FSAs were in existence at the time section 6110 was enacted, Congress would have included them. Id. at 616.
118. Id.
119. Id.
120. See Hickman, supra note 10, at 186-88.
121. Id.
122. Id. at 186.
123. This is referring to the law in place prior to the enactment of legislation defining APAs as confidential return information.
III. HOW SHOULD APAS BE CLASSIFIED?

A. APAs As Written Determinations

In order to compel the release of APAs, the best strategy would involve a comparison of APAs to other IRS determinations that are disclosed under the authority of section 6110. As explained earlier, the records released under section 6110 generally involve IRS interpretations of the tax code as it applies to specific circumstances or contemplated transactions.

An APA is based on the IRS’s interpretation of the tax code as it applies to the specific situations presented by each participating company. Hickman, however, argues that APAs are distinguishable from other 6110 documents, such as PLRs and FSAs. PLRs, as explained above, are memoranda issued by the IRS at the request of a taxpayer seeking advice as to tax consequences of specific transactions. FSAs provide legal guidance to IRS field personnel with respect to specific taxpayer situations. Hickman explains that these two types of 6110 documents are distinguishable from APAs because they are “one sided issuances of opinion from the IRS: The taxpayer or field agent requests a legal conclusion for a given set of facts, and the IRS responds with its answer.” However, although an APA is a negotiated agreement, the IRS’s negotiating position stems from its interpretation of the tax code as it applies to the information presented by a participating company. In essence, when a company negotiates an APA with the IRS, it is requesting a legal interpretation for a particular set of facts or circumstances. The set of facts or circumstances in the case of an APA may be any type of a participating company’s information relating to its income, including pricing schemes, product details, manufacturing processes, intellectual property, overhead costs, labor issues, market forces, etc. The actual agreement between the IRS and the company is an application of the tax code to the specific set of facts offered, much like other 6110 documents.

Hickman also attempts to distinguish APAs from other 6110 documents by suggesting that APAs tend to focus more on the specific facts and circumstances surrounding the agreement instead of the legal analysis they contain. While it is true that an APA

124. See Hickman, supra note 10, at 186.
125. Id. at 187.
126. Id.
agreement requires the digestion of an inordinate amount of facts, the application of the law to those facts is not diminished by the importance or volume of the facts. A large collection of facts is useless to APA participants without the IRS’s interpretation of the law. When an IRS field agent requests a FSA from his or her superiors, the agent is not only interested in an analysis of facts and circumstances, but is trying to obtain a prediction of how the tax code will be applied to a specific situation. Likewise, when a company negotiates an APA, although the negotiations may center on interpretations of fact, the ultimate goal of the company is to obtain an agreement that is based on the application of the tax code to a specific transfer pricing scheme.

Therefore, although APAs may be distinguished from other types of 6110 documents, just as all 6110 documents can be distinguished from each other, APAs share a component with all 6110 documents: the application of the tax code to a particular set of facts or circumstances. As explained in the previous section, and by the court in *Tax Analysts*, legal analysis contained in IRS written determinations is subject to disclosure. This Note will now predict that because of the similarities between APAs and section 6110 documents, BNA’s attempts to compel APA disclosure through the D.C. federal court system would have prevailed.

**B. Redacted APAs**

When speculating as to the result of the BNA case, assuming the IRS never had made a concession that APAs should be classified as written determinations, one would expect the D.C. District Court to closely follow the analysis performed in *Tax Analysts*, which mandated the disclosure of legal interpretations included in FSAs. In fact, the court for the BNA case suggested as much by noting that in *Tax Analysts*, “a most significant development... casts a most significant light on whether the documents in this case [APAs] are exempt under FOIA.” In addition, the court noted that for purposes of legal analysis, FSAs “are similar to APAs in the sense that they involve the application of a section of the Internal Revenue Code to a given set of facts and a resulting legal analysis and conclusion.” Since the BNA court indicated that the *Tax Analysts*

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127. See *Tax Analysts*, 117 F.3d at 616.
128. See Bureau of Nat’l Affairs, 24 F. Supp. 2d at 92.
129. Id. at 93.
case, which mandated disclosure, was likely to have such influence over the BNA court's decision, the BNA court probably would have followed the analysis of the Tax Analysts decision.

Assuming that the D.C. district court would have treated APAs in the same, or similar, fashion that it treated FSAs, the court initially would have distinguished taxpayer-specific information from the legal conclusions or policy statements contained in APAs. The court then would have mandated the disclosure of APAs that were subject to the redaction of identifying taxpayer information, trade secrets, and other confidential information. Therefore, if Congress had not enacted legislation protecting the confidentiality of APAs, the IRS likely would have been forced to release redacted APAs. This Note now will examine the new APA legislation and the effects it will have on taxpayer access to APA information.

C. Public Law No. 106-170

Following the IRS concession classifying APAs as IRS written determinations, and amidst the impending disclosure of thousands of APAs, business leaders, industry representatives, and members of the APA program lobbied Congress to prevent disclosure of APAs. Congress responded by enacting legislation that explicitly classifies APAs as confidential return information under section 6103. The legislation also provides that APAs and related background information are not written determinations as defined by section 6110. In an effort to remedy the problem of agency review that results with the nondisclosure of APAs, the statute also requires the Treasury Department to prepare and publish an annual report on APA status. The report must include information about the APA office; copies of model APAs; statistics regarding APA requests and applications; general descriptions of related organizations involved with APAs; and generalized, assimilated information on the criteria

130. See Tax Analysts, 117 F.3d at 614-16.
131. Id.
132. This is surely the case considering the IRS concession to classify APAs as written determinations under section 6110.
133. See Masscy, supra note 9, at 2389-90.
135. Id. This provision has significance considering the fact that the text of section 6110 seems to exclude section 6103 material as exempted from disclosure, although this Note has already argued that the D.C. district has suggested that section 6110 material is subject to section 6103 provisions.
and methods used to determine appropriate transfer pricing schemes.\textsuperscript{137}

\textbf{D. Confidentiality}

Because the IRS had never released APAs to the public prior to the \textit{BNA} litigation, the IRS concession ending the \textit{BNA} case and classifying APAs as 6110 documents surprised some participants of the APA program.\textsuperscript{138} Parties originally told that their APAs would remain confidential argued that by allowing APA publication, the IRS changed "the terms of the confidentiality agreement retroactively and without consulting the affected parties."\textsuperscript{139} Internationally operating businesses participated in the APA program with "the expectation that their confidential business information [would] not be exposed to any risk of being made public."\textsuperscript{140} Therefore, after the IRS announced its intention to publish redacted APAs, APA participants filed amicus curiae briefs in the \textit{BNA} lawsuit arguing to keep APAs confidential.\textsuperscript{141} In addition, APA participants lobbied the IRS, the Treasury Department, and Congress to devise a legislation scheme that would protect APAs from disclosure.\textsuperscript{142} Furthermore, tax officials from other countries indicated that they may be reluctant to participate in the APA program if Congress did not pass legislation protecting the confidentiality of APA participants.\textsuperscript{143}

Although lobbying ultimately was successful in getting legislation passed to protect APAs from disclosure, the policy behind the legislation's enactment, business confidentiality, is poorly founded. As explained earlier, both the FOIA and section 6110 contain disclosure exceptions that protect confidentiality. Prior to APA release, the IRS would redact any company trade secrets, privileged commercial and financial information, and any information that would identify the taxpayer. Like other 6110 documents, only legal analysis portions of APAs would be subject to disclosure. Therefore, the disclosure of redacted APAs would not compromise the

\textsuperscript{137} Id.
\textsuperscript{138} See Patton & Ackerman, \textit{supra} note 8, at 100-20.
\textsuperscript{139} Id.
\textsuperscript{141} See Massey, \textit{supra} note 9, at 2390.
\textsuperscript{142} See id.
confidentiality of APA participants as long as the IRS does a thorough job of redacting confidential information. While there may be concerns about the IRS's ability to redact confidential information from APAs, the IRS has been releasing redacted 6110 documents, such as PLRs, for years, "and there have been no problems with disclosing PLRs." In fact, a PLR may provide an answer to a relatively complex transfer pricing tax issue while protecting taxpayer confidentiality.

Opponents of APA disclosure may correctly argue that certain APAs contain much more identifying and confidential information than other forms of 6110 documents. For example, certain transfer pricing issues could be highly product specific, causing an APA to refer to a product that may, on its own, identify a particular taxpayer. Other aspects of the APA negotiation may depend on the intricacies of a proprietary process, or another form of identifying information. While disclosure opponents may be correct in asserting that APAs may contain a higher level of confidential information, section 6110 mandates that all identifying and confidential information be redacted from IRS publications. Therefore, APA disclosure does not threaten taxpayer confidentiality.

E. Treasury Report v. Redacted APAs

Proponents of Public Law No. 106-170 argue that the annual treasury report mandated by the legislation will be more beneficial to taxpayers than redacted APAs. Robert Ackerman, the first director of the APA program, believes the treasury report contains information that would not be available through redacted APAs. As explained earlier, the treasury report must include, among a wealth of other information, copies of model APAs; statistics regarding APA requests and applications; general descriptions of related organizations involved with APAs; and generalized, assimilated information on the criteria and methods used to

144. See Massey, supra note 9, at 2390.
145. For example, one PLR made a ruling on the tax consequences of advance payments made by a taxpayer for a particular product manufactured by affiliated companies. See P.L.R. 99-49-027 (Dec. 10, 1999), 1999 WL 1129413. In the PLR, the IRS replaced identifying information with more general, nonidentifying language. Id. For example, the PLR states, "Taxpayer is the principal United States operating subsidiary of Parent, a Country A corporation engaged in research, design, manufacturing, marketing and servicing of Product A worldwide." Id.
146. See Triplett, supra note 140.
147. See Massey, supra note 9, at 2390.
determine appropriate transfer pricing schemes.\textsuperscript{148} While it may be true that the treasury report offers benefits that redacted APAs could not provide, and this Note will not argue otherwise, redacted APAs provide for better agency oversight than a generalized report.

The treasury report gives taxpayers APA information in a disassembled format instead of showing how the IRS applied the tax code to a discrete, specific set of facts.\textsuperscript{149} Therefore, the treasury report gives the IRS more leeway to apply the tax code in an arbitrary manner than redacted APAs would. Without APA disclosure, no party is reviewing IRS application of the tax code to specific factual scenarios. The disassembling of APA data for the purposes of generating the treasury report may hide arbitrary or even devious application of the tax code. The lack of oversight provided by the treasury report will place the IRS in an uneven bargaining position, especially for less sophisticated taxpayers. Although participants in the APA program generally are business savvy and well advised,\textsuperscript{150} the globalization of the world economy makes publication of APAs more important today than in the past. As more and more companies operate internationally and advances in communication make international business easier, the continuum of the business sophistication of internationally operating companies grows larger. Therefore, in order to provide all taxpayers with the information necessary to effectively negotiate APAs with the IRS, it is important for taxpayers to have access to individual APAs.

CONCLUSION

As businesses begin international operations and countries become industrialized, the IRS has a greater incentive to ensure they are collecting appropriate taxes. The APA is the vehicle the IRS uses to ensure tax code compliance of internationally operating companies. Therefore, the IRS must do everything in its power to persuade taxpayers to participate in the APA program. Sacrificing agency oversight, however, is not the appropriate method of persuasion. The IRS should be compelled to release redacted APAs. They provide better agency oversight than the annual treasury report mandated by Public Law No. 106-170. In addition, the most repeated argument in favor of Public Law No. 106-170, APA participant

\textsuperscript{148} Id.
\textsuperscript{149} Id. at 2391.
\textsuperscript{150} Id.
confidentiality, is not well-founded. The confidentiality protections provided by the FOIA and section 6110 exemptions would prevent access to confidential or proprietary business information. The citizens and businesses of the United States have a fundamental right to review the actions of their government. APAs should be released to allow public review of IRS actions.