

The secret attempt by the IRS to protect Hughes' tax rulings

Second of two articles

By Donald L. Barlett
and James B. Steele
Inquirer Staff Writers

© 1976, The Philadelphia Inquirer

Internal Revenue Commissioner Donald C. Alexander sent a letter to a congressional committee last summer seeking specific legislation to keep secret the tax favors that the IRS had granted over the years to the billion-dollar business empire of the late Howard Robard Hughes.

In his letter—a copy of which has been obtained by The Inquirer—Alexander asked that a special secrecy amendment relating to the Hughes empire be added to the tax-reform bill then under consideration in Congress.

In that letter, sent on June 23 to Dr. Laurence N. Woodworth, chief of the staff of the Joint Committee on Internal Revenue Taxation, Alex-

ander singled out The Inquirer as an example of a party to whom certain IRS rulings should not be disclosed.

For more than 18 months, The Inquirer has been investigating the special relationships between the Hughes organization and federal agencies such as the IRS, the Defense Department, the CIA and the State Department — special relationships that have continued since Hughes died in April.

The Inquirer disclosed yesterday that the president of a CIA-front organization interceded with President Richard M. Nixon's staff in 1971 in an effort to obtain preferential tax treatment for Hughes at the Treasury Department.

This year the organization seeking preferential treatment for Hughes was the IRS itself.

Alexander was unsuccessful in his attempt to gain special treatment for

Hughes' interests. But through a quiet, intense lobbying effort that lasted nearly a year, he did obtain from Congress a provision in the new tax law designed solely to keep secret the identity of persons who receive preferential tax rulings from the IRS.

The net effect of Alexander's lobbying efforts, found in the tax reform bill that was signed Oct. 4 by President Ford, is this:

The identities of all individuals corporations, businesses and tax-exempt organizations that have received in the past—or will receive in the future—special rulings from the IRS granting favorable tax treatment must be kept secret.

Interestingly, the tax-writing House Ways and Means Committee, the Senate Finance Committee and the Joint Committee on Internal Revenue Taxation all readily agreed to the disclosure.
(See IRS on 2-A)

Thursday, Oct. 28, 1976

Philadelphia Inquirer

IRS, From 1-A
mands of Alexander, who had some potent lobbying allies, including the American Bar Association.

The IRS, other executive departments and special-interest groups feared that under provisions of the Freedom of Information Act, the courts could order the IRS to make public the identity of individuals and businesses that received the preferential rulings.

By securing legislation barring the release of rulings unless all identifying information was deleted, Alexander avoided the unpleasant circumstances that were sure to follow such a court edict.

Not the least of those consequences would have been the embarrassing revelations growing out of the disclosure of the names of individual taxpayers, corporations and tax-exempt organizations that received letter rulings from the IRS.

Letter rulings are interpretations of tax laws that the IRS issues at the request of a taxpayer. A company, for example, sends a letter to the IRS outlining a planned business transaction. The IRS then issues a ruling to that company explaining the tax consequences of the proposed transaction. In effect, the ruling is a private tax law.

Over the years, the Hughes organization has received a number of special rulings.

Hughes exemption

While the precise nature of those rulings is unknown, at least one involved an IRS decision to exempt the Howard Hughes Medical Institute from the federal income tax laws. The institute owns 100 percent of the stock of Hughes Aircraft Co., one of the nation's 10 largest defense contractors.

In the years following the IRS ruling designating the medical institute a tax-exempt charitable organization—like the Boy Scouts or the YMCA—the institute gave more money to

Hughes in the form of interest payments on a loan and real-estate lease agreements than the institute spent on medical research, the purpose for which the IRS granted the tax exemption.

The IRS and Commissioner Alexander have argued strenuously against identifying individuals and businesses receiving the letter rulings, saying the privacy of the taxpayers must be protected.

Two such private rulings illustrate the importance the IRS attaches to maintaining secrecy.

In 1951, the IRS issued a secret ruling that had the effect of allowing American oil companies operating in Arab countries to treat payments they were making to those countries as foreign taxes rather than as royalties.

Because foreign taxes are creditable dollar-for-dollar against the U. S. income tax, companies such as the Exxon Corp., Texaco Inc., Mobil Oil Corp. and Standard Oil Co. of California have avoided paying billions of dollars in federal income taxes.

In another case, the IRS issued a secret ruling providing that stockholders would pay no taxes on income from a proposed merger of International Telephone & Telegraph (ITT) and the Hartford Fire Insurance Co.—a decision that would have allowed stockholders to avoid an estimated \$30 to \$50 million in federal taxes.

Both the oil industry ruling and the ITT-Hartford merger ruling eventually were made public. An embarrassed IRS subsequently reversed itself and revoked the ITT ruling.

For the most part, though, the identities of taxpayers receiving special rulings have remained a closely guarded secret.

Erosion of secrecy

In the last two to three years, however, that secrecy has been gradually eroded, due entirely to the Freedom of Information Act signed by President Lyndon B. Johnson in 1967.

Public-interest groups and newspapers were slow to make use of the new law in seeking documents from the IRS. For its part, the IRS delayed the process by forcing individuals to file a lawsuit to obtain the material sought.

By the summer of 1975, though, as a result of such lawsuits, the IRS had been ordered to release the material requested.

(It should be pointed out that the material involved was not personal income tax information, but statistical data concerning the IRS' inequitable enforcement of the tax laws, as well as information on the letter rulings.)

(In at least two cases, as a result of legal action, the IRS released the letter rulings identifying the companies that received the rulings, as well as the internal documents justifying the IRS' reasons for granting the ruling.)

Formal request

It was against this background, then, that The Inquirer, in a letter to IRS Commissioner Alexander on May 1, 1975, made a formal request under provisions of the federal Freedom of Information Act to examine certain IRS documents relating to Hughes.

Specifically, the newspaper asked to examine "all IRS letter rulings issued since Jan. 1, 1955, relating to . . . Howard R. Hughes, Hughes Aircraft Co., Howard Hughes Medical Institute, Hughes Tool Co., Hughes Air West and Summa Corp."

over

In a letter dated May 28, 1975, the IRS said that similar requests were the subject of lawsuits and that "until the legal issues are resolved by the courts, the Service cannot determine whether or not your request should be granted or denied."

The Inquirer then submitted an administrative appeal of that decision to Commissioner Alexander, as provided under the Freedom of Information Act.

Alexander's response, dated July 14, 1975, was similar to the original letter from the agency. He said the agency would "defer action" on the appeal, but added that The Inquirer could file a lawsuit challenging his decision.

In fact, Alexander said that he wanted the courts to determine whether letter rulings should be considered public records. "The Internal Revenue Service is hopeful that the matter of the availability of its unpublished letter rulings will be finally settled by the pending litigation," he wrote.

So in August 1975, The Inquirer filed suit against the IRS in U. S. District Court in Washington, seeking the release of the letter rulings concerning Hughes.

But at the same time Alexander was telling the newspaper that he wanted the courts to decide whether the rulings should be made public, other IRS officials began working with the staff of the Joint Committee on Internal Revenue Taxation on Capitol Hill, drafting legislation that

would prohibit release of the rulings.

Months dragged by. The IRS stalled proceedings in the newspaper's lawsuit. Congress debated a series of reforms that were to be included in the proposed tax package.

Possible loophole

Then, last summer, when the tax reform bill was undergoing final revisions, Alexander noticed that the legislation contained a possible loophole: In the case of lawsuits filed before Jan. 1, 1976, the IRS would have to comply with any court decision granting the release of information about the letter rulings.

No one knows, of course, whether the courts will ever make such a decision. Nonetheless, seeking to close what he considered a tiny potential loophole in the legislation, Alexander wrote to Woodworth, chairman of the staff of the Joint Committee on Internal Revenue Taxation:

"In two of the five pending requests which would be subject to this rule, the Freedom of Information Act claimant has requested certain rulings by asking for the rulings pertaining to a certain taxpayer.

"For example, in Philadelphia Newspapers Inc., rulings issued to Howard Hughes, Hughes Aircraft, etc., are sought to be disclosed.

"Therefore, disclosure would reveal identity in this case, and, in effect, the Service would be honoring a request for documents that identifies the material sought on the basis of identity. I believe that this result was unintended since the legislation provides for the deletion of identity.

Alexander then suggested that a phrase be added to the tax legislation specifically prohibiting the release of rulings in which the taxpayer was identified by name, regardless of whether a lawsuit had been started prior to passage of the bill.

In other words, Alexander was proposing a special amendment to protect the Hughes interests.

Exactly what happened next is unclear, except that the clause Alexander objected to was incorporated in the tax bill finally passed by Congress in September and signed by President Ford on Oct. 4.

For the IRS, however, it was simply a matter of losing a battle but winning the war, because the tax bill did contain a provision barring the IRS from releasing any rulings that identify an individual or company receiving the ruling — a provision that IRS lobbied for intensely.

Thus, unless a federal court ultimately sustains The Inquirer's request, the preferential tax rulings issued to the empire of Howard Robard Hughes will remain forever secret.