

## Written Testimony for Hearing on “Taxpayer Fairness”

U.S. House of Representatives  
Committee on Ways and Means  
Subcommittee on Oversight

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October 13, 2020

Chairman Pascrell, Ranking Member Kelly, Members of the Oversight Subcommittee, and Members of the Ways and Means Committee:

Thank you for inviting me to participate in today’s hearing. I am a professor at Washington University, where I work on issues of government ethics, legal ethics, the law of whistleblowing and national security law.

In this testimony, I will discuss:

- (1) the conflict faced by IRS employees who audit the President’s taxes, and how increased transparency can mitigate that conflict;
- (2) why we need to know how much the President owes, and to whom he owes it; and
- (3) the need for new legislation to address gaps in our financial disclosure system for the President and other federal officials.

### **The conflict of interest faced by IRS officials who review and audit the President’s tax returns**

Internal Revenue Service (IRS) employees who review and audit the president’s taxes face an inherent conflict of interest. On the one hand, the employees handling the President’s tax returns have a duty to treat the President the same way they would treat an ordinary taxpayer. On the other hand, these employees may feel pressure to treat the President more favorably than they would an ordinary taxpayer. This conflict results from the structure of our government – the fact that IRS employees are part of the executive branch, and the President sits at the top of the executive branch. The President is in some sense ultimately the boss of the IRS employees who review the President’s tax returns.

This conflict is not just a theoretical or academic matter. History demonstrates that in the past, IRS employees treated a President more favorably – and that once this favorable treatment came to light, it could not withstand public scrutiny. As I am sure you know, one of the biggest scandals in the history of the IRS stemmed from the IRS’s favorable treatment of President

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<sup>1</sup> The views expressed are my own and should not be attributed to my employer, Washington University.

Nixon's tax returns.<sup>2</sup>

During President Nixon's first term (1969-1972), he paid a surprisingly low average tax rate (7 per cent) on the more than \$1 million in income he received over that time. His returns for those years contained some highly questionable deductions that would likely have triggered an audit for an ordinary taxpayer, including his claimed \$576,000 charitable deduction for donating his vice presidential papers. In processing Nixon's tax returns, the IRS did not initially raise questions about this or his other deductions.

But in June of 1973, by happenstance, the public learned that President Nixon had claimed this large charitable deduction. The gift was revealed during a deposition in a lawsuit related to Watergate, and a Washington Post journalist wrote a series of articles about it. Tax experts contended that the deduction was not legal, and that Nixon's success in claiming it stemmed from the conflict felt by IRS officials:

It is obvious that Internal Revenue Service agents and their superiors throughout the Internal Revenue Service would be extremely reluctant to audit the tax returns of the President of the United States as if he were an ordinary taxpayer.<sup>3</sup>

In the fall of 1973, a newspaper published information -- leaked by an IRS employee -- that Nixon paid less than \$900 in taxes in 1970 and 1971 even though he had more than \$200,000 in income each year. Only after this leak, did the IRS re-review Nixon's tax returns and conclude that his claimed deductions were untenable.

In 1977, the IRS adopted a policy to automatically audit the tax returns of the sitting President and Vice President. This policy has the advantage of ensuring a second review by the audit staff. By mandating an audit, the policy removes any discretion on *whether* to conduct an audit. But what remains in place is discretion on *how* the agency conducts the audit.

Since the conflict of interest described above is inherent in the structure of our government, IRS employees under any administration might feel some degree of pressure. But the pressure to give the President favorable treatment has likely increased during the Trump administration because of this administration's record of retaliating against officials who have insisted on following the law, even where that works to President Trump's detriment.

Here are a few examples of executive branch officials who have experienced retaliation after following the law despite pressure from President Trump not to do so:

- President Trump retaliated against Attorney General Jeff Sessions for following an ethics

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<sup>2</sup> The following paragraphs about Nixon's tax returns are based primarily on two sources: William D Samson, *President Nixon's Troublesome Tax Returns*, TAX NOTES (April 11, 2005) and Joseph J. Thorndike, *JCT Investigation of Nixon's Tax Returns* (February 2016).

<sup>3</sup> Joseph J. Thorndike, *JCT Investigation of Nixon's Tax Returns* (February 2016) (quoting Ira L. Tannenbaum, "Income Tax Treatment of Donation of Nixon Pre-Presidential Papers, TAX NOTES (30 July 1973)).

regulation requiring Sessions to recuse from the investigation into Trump's campaign.<sup>4</sup> Despite the clear legal standard requiring Sessions' recusal, Trump berated Sessions in private and public, even asking Sessions to resign. Trump believed the role of an Attorney General is to protect the President, and was angered that Sessions' followed the law rather than protecting him.

- The Trump administration retaliated against Pentagon official General Elaine McCusker for warning political appointees that the President's hold on military aid to Ukraine violated the Impoundment Control Act – an assessment later confirmed by the Government Accountability Office. President Trump had earlier nominated McCusker to become the Defense Department Comptroller, but after impeachment, the White House withdrew her nomination because she tried “to thwart” the president's agenda.<sup>5</sup>
- This administration allegedly retaliated against a government scientist, Rick Bright, who resisted efforts to broaden the use of hydroxychloroquine, an unproven treatment for COVID-19 that President Trump had repeatedly promoted. The administration removed Bright as head of the federal agency that develops vaccines, transferring him to a position with little responsibility.

While it is not possible to remove entirely the conflict faced by IRS employees, Congress could mitigate the conflict by increasing transparency. If we required public disclosure of both the President's tax returns and the IRS audit of those returns, the IRS would be publicly accountable for the way it handles this conflict of interest. The Nixon tax episode demonstrates the power of transparency, as the IRS decided to re-evaluate Nixon's returns only after information about those returns was leaked to the press.

### **Why we need to know what the President owes, and to whom he owes it.**

The New York Times expose on President Trump's taxes indicated that President Trump has more than \$300 million in debt that will come due in the next four years.<sup>6</sup> Yet we do not have a clear idea of exactly how much President Trump owes, and to whom he owes it.

Public disclosure of a President's debts is important for several reasons. A person who owes so much debt that they are unable to pay it off easily is subject to pressure by creditors, or subject to influence by a third party who offers to help pay the debt. A heavily indebted person may also be more likely to engage in risky or criminal behavior to earn the money to pay off the debt. For these (and other) reasons, excessive debt is a common reason for denying security clearances, and is a common characteristic among U.S. persons who have committed espionage.<sup>7</sup>

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<sup>4</sup> 28 CFR § 45.2(a) (prohibiting an employee from participating “in a criminal investigation or prosecution if he has a personal or political relationship with ... [an] organization substantially involved in the conduct that is the subject of the investigation or prosecution”).

<sup>5</sup> Steven Nelson, *White House expected to drop Pentagon nominee Elaine McCusker amid Ukraine fallout*, N.Y. POST (Feb. 11, 2020).

<sup>6</sup> Russ Buettner, Susanne Craig and Mike McIntire, *Long-Concealed Records Show Trump's Chronic Losses and Years of Tax Avoidance*, N.Y. TIMES (Sept. 27, 2020).

<sup>7</sup> KATHERINE L. HERBIG, *THE EXPANDING SPECTRUM OF ESPIONAGE BY AMERICANS, 1947–2015* vi

While in theory, anyone might be influenced by an offer of financial gain, social science shows that people are generally more motivated not to lose something they already have rather than they are motivated to gain something they do not have. This “loss aversion” may explain why a person with excessive debt is seen as more vulnerable to an offer of financial gain.

President Trump’s ability to pay his debts may depend on his ability to refinance his loans. Thus, his creditors – or others who could offer refinancing -- may have leverage over him. And in light of his position at the head of the executive branch, his creditors and others may have leverage over the U.S. government.

### **Recommended legislative reforms**

Congress needs to address several gaps in our current system of financial disclosure for the President and other high-level government officials.

- **Require disclosure of a President’s tax returns and the IRS’s audit of those returns**

As described above, IRS officials face a conflict of interest when they process and audit the President’s tax returns. Congress should mitigate that conflict by requiring the President to disclose his tax returns and requiring the IRS to disclose its audit of those returns.

- **Clarify that business-related debts must be disclosed**

The Office of Government Ethics has interpreted the financial disclosure statute so that Presidents and other executive branch officials do not need to disclose business-related debts.<sup>8</sup> Business-related debts can cause the same concerns as other debt, and disclosure of such debt is necessary to have a complete picture of an official’s finances. Congress should clarify that the financial disclosure statute requires disclosure of business-related as well as other debt.

- **Increase maximum threshold for amount of assets and liabilities**

The Ethics in Government Act requires the disclosure of finances, but does not mandate the precise amount of assets and liabilities. Instead, a filer must indicate whether the asset or liability falls into a range of amounts, such as “greater than \$15,000 but not more than \$50,000” and “greater than \$50,000 but not more than \$100,000.”<sup>9</sup> The highest category is “greater than \$50,000,000,” an amount so high that very few office holders have any assets or liabilities in that category.<sup>10</sup> But more than a third of the debts that President Trump lists on his financial disclosure form fall into the highest category, and the form does not reveal whether those

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(2017) (“Money is the most common motive for committing espionage-related offenses”).

<sup>8</sup> OFFICE OF GOVERNMENT ETHICS, PUBLIC FINANCIAL DISCLOSURE GUIDE 268 (July 2016) (“You are not required to report assets and liabilities of a trade or business, unless those interests are unrelated to the operations of the business.”).

<sup>9</sup> 5 U.S.C. App. § 102(d)(1)(B) and (C).

<sup>10</sup> *Id.* at § 102(d)(1)(J).

liabilities are \$51 million, \$500 million or greater.<sup>11</sup>

In order to provide an accurate financial picture of office holders and candidates with massive assets and liabilities, Congress needs to increase the maximum threshold for public disclosure of assets and liabilities.

- **Require disclosure of business partners**

Our current system for financial disclosure does not require office holders to disclose the identity of business partners, even though those relationships may require a government official to recuse from particular matters involving those partners.<sup>12</sup> Congress should expand the financial disclosures to mandate disclosure of business relationships, including the identity of partners and co-venturers.

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<sup>11</sup> OGE Form 278e for President Donald J. Trump (July 31, 2020) at 35 (5 of the 14 liabilities listed are “over \$50,000,000”).

<sup>12</sup> See 5 C.F.R. § 2635.502 (recusal standard for a matter involving a person “with whom the employee has or seeks a business, contractual or other financial relationship”).