COLLATERAL COMPLIANCE

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As most of us are aware, the failure to comply with the tax law can lead to civil and criminal tax penalties. But tax noncompliance has other consequences as well. Collateral sanctions for tax noncompliance, which are imposed on top of tax penalties and are often administered by agencies other than the taxing authority, increasingly apply to individuals who have failed to obey the tax law. They range from denial of hunting permits to suspension of driver’s licenses to revocation of passports. Further, as the recent Supreme Court case Kawashima v. Holder demonstrates, some individuals who are subject to tax penalties for committing tax offenses involving “fraud or deceit” may even face deportation from the United States. Criminal law scholars have written dozens of articles on the collateral consequences of convictions. Yet tax scholars have virtually ignored collateral tax sanctions, even though their use by the federal and state governments is growing.

This Article offers a comprehensive analysis of collateral consequences in the taxation context. While many criminal law scholars have proposed ways to alleviate collateral consequences, this Article argues that, when applied in connection with violations of the tax law, collateral consequences may offer previously unappreciated social benefits. In many cases, collateral tax sanctions can promote voluntary tax compliance more effectively than additional monetary tax penalties, especially if governments increase public awareness of collateral tax sanctions. Governments should therefore embrace these sanctions as a means of tax enforcement and taxing authorities should publicize them affirmatively.

After considering the effects of collateral tax sanctions under each of the predominant theories of voluntary compliance, I propose principles that governments should consider when designing collateral tax sanctions. These principles suggest, for example, that initiatives to revoke driver’s licenses from individuals who have failed to pay outstanding taxes or professional licenses from individuals who have failed to file tax returns would likely promote tax compliance. However, whether the sanction of deportation for tax offenses involving fraud or deceit will have positive compliance effects is far less certain. Finally, I suggest how taxing authorities should publicize these sanctions to foster voluntary compliance.

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I. INTRODUCTION

Tucked in the corner of one of the dozens of strip malls along Ventura Boulevard in California’s San Fernando Valley, the Japanese cuisine restaurant Cho Cho San serves spicy tuna rolls, shrimp tempura and a menu of other entrées favored by the American palate. Its owners, Akio and Fusako Kawashima, arrived in the United States in 1984 in search of opportunity and, through hard work and good fortune, quickly established a profitable restaurant. Their business success, however, did not extend to their dealings with the Internal Revenue Service. In 1997, its agents determined that the couple underpaid taxes on their restaurant income by nearly a quarter million dollars over several years. Rather than face a criminal trial, the Kawashimas pleaded guilty to willfully making a false statement on a tax return, were sentenced to four months in prison and were ordered to pay back the taxes owed plus civil tax penalties and interest. Three years later, after reestablishing themselves as “exemplary” members of their community, the Kawashimas received an unexpected notice from the immigration authorities. As a result of their prior guilty pleas in their tax case, they would be forced to return to their native Japan and leave their children and their American lives behind them.

The story of Kawashima v. Holder, decided by the U.S. Supreme Court in 2012, illustrates a curious confluence of events. After incurring a tax penalty in the form of monetary penalties and prison time, the taxpayers faced the additional sanction of deportation as a result of the same tax offense. This added sanction can be described as a “collateral tax sanction.” It applied on top of monetary tax penalties and prison sentences, revoked a privilege provided by the government and was imposed by an agency other than the taxing authority.

While the application of a sanction for tax noncompliance by an agency other than the Internal Revenue Service in Kawashima may appear unusual to tax practitioners and tax scholars, collateral tax sanctions occur in many other contexts. In recent years, federal and state governments have applied

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2 Id., at 3-10.
3 Id.
4 Id. See also Brief for the Petitioners, Kawashima v. Gonzalez, 503 F.3d 997 (9th Cir. 2007).
5 Brief for the Petitioners, 17-20, Kawashima v. Holder, 565 U.S. ___, 132 S. Ct. 1166 (2012), appealing 615 F.3d 1043 (9th Cir. 2010).
myriad forms of collateral tax sanctions to combat tax delinquency, an offense that occurs when a taxpayer owes an established tax liability, but fails to pay the tax owed in a timely manner. For example, under current and proposed federal rules, the failure to pay taxes owed may result not only in civil and criminal tax penalties, but also in the loss of the ability to obtain federal employment, apply for Federal Housing Authority mortgages, enter contracts with the federal government, and hold U.S. passports. Likewise, several states suspend driver’s licenses and vehicle registration, revoke law and medical licenses, and deny hunting and gaming permits to residents who have failed to satisfy their tax obligations. Despite the recent proliferation of collateral tax sanctions as a response to tax noncompliance, tax law scholars have virtually ignored their existence, focusing instead on various aspects of the copious civil and criminal tax penalties that appear in the Internal Revenue Code.

Criminal law scholars, by contrast, have written dozens of articles on
the role that collateral consequences play in the justice system.\textsuperscript{16} Some of the most commonly discussed examples of collateral consequences include rules that prevent convicted felons from serving on juries,\textsuperscript{17} voting in elections,\textsuperscript{18} holding certain types of public and private sector employment\textsuperscript{19} and residing in states without participating in sex offender registration programs.\textsuperscript{20} The consensus view among criminal law scholars, and many policymakers as well, is that the proliferation of collateral consequences has had harmful effects on convicted individuals and society in general.\textsuperscript{21} They argue that collateral consequences impose “internal exile” by preventing the reintegration of former convicted individuals and are unfair because many defendants lack knowledge of their existence when they enter guilty pleas.\textsuperscript{22}

As a result, a wide array of initiatives which aim to reintegrate convicted individuals following incarceration and alert defendants of potential


\textsuperscript{17} See, e.g., Brian C. Kalt, \textit{The Exclusion of Felons from Jury Service}, 53 Am. U. L. Rev. 65 (2003) (criticizing statutes that ban felons from serving on juries).


\textsuperscript{19} See, e.g., New York State Bar Association, \textit{Re-entry and Reintegration: The Road to Public Safety}, 2006 (describing employment obstacles faced by convicted felons).

\textsuperscript{20} See, e.g. Richard Tewksbury, \textit{Collateral Consequences of Sex Offender registration}, 21 J. Contemp. Crim. Just. 67 (2005)(finding that registered sex offenders experience “social stigmatization, loss of relationships, employment, and housing, and both verbal and physical assaults”).


\textsuperscript{22} See Demleitner, \textit{supra} note 21; American Bar Association Commission on Effective Criminal Sanctions, \textit{Internal Exile: Collateral Consequences of Convictions in Federal Laws And Regulations} (2009).
collateral consequences during the criminal settlement process has appeared over the past two decades.\textsuperscript{23}

The lack of a similarly robust discussion of collateral consequences in the tax context by tax scholars and federal and state taxing authority officials is surprising. Government officials have reported that collateral tax sanctions have encouraged delinquent taxpayers to settle their outstanding tax liabilities. While the potential loss of distinct government-provided benefits and services stemming from tax delinquency is a factor that could be relevant to the exploration of why individuals pay their taxes on time,\textsuperscript{24} scholars of tax compliance have not investigated their possible efficacy and taxing authorities usually do not highlight them in their internal directives or in their public communications with taxpayers.\textsuperscript{25} Further, as collateral tax sanctions are often administered by agencies other than the taxing authority, they should interest anyone who evaluates the consistency and coherence of tax penalties. And as the federal and state governments search for innovative strategies for collecting tax revenue, the use of this type of sanction is growing.\textsuperscript{26}

This Article offers a comprehensive analysis of collateral consequences in the taxation context. In exploring this overlooked aspect of tax enforcement, it considers several questions: Why do collateral tax sanctions appear to encourage individuals to pay their tax debts? Could collateral tax sanctions influence individuals’ tax compliance decisions regarding actions other than payment of outstanding tax liabilities? And how, if at all, should taxing authorities, as opposed to other government agencies, publicize the existence of collateral tax sanctions? While many criminal law scholars have proposed ways to alleviate collateral consequences, this Article argues that, when applied in connection with violations of the tax law, collateral consequences may offer previously unappreciated social benefits. In many cases, collateral tax sanctions can promote voluntary tax compliance more effectively than additional monetary tax penalties, especially if governments increase public awareness of collateral tax sanctions. Governments should therefore embrace these sanctions as a means of tax enforcement and taxing authorities should publicize them affirmatively.

To begin this investigation, I examine how collateral tax sanctions may affect the tax reporting behavior of individuals who are subject to different

\textsuperscript{23} See infra note 73 and accompanying text.
\textsuperscript{25} See infra note 369 and accompanying text.
\textsuperscript{26} See infra notes 83 – 135 and accompanying text.
tax compliance motivations that have been presented in the tax literature.\footnote{See infra notes 143 – 156 and accompanying text.}

In conducting this analysis, I contrast the likely effects of collateral tax sanctions with the exclusive use of formal tax penalties under each of these different motivations.


The loss of particular government-provided benefits, such as professional licenses or residency status, may be more salient to individuals than formal tax penalties, which individuals may simply view as part of their overall tax liability. Further, by targeting specific government-provided benefits and services for which individuals have developed feelings of entitlement, collateral tax sanctions may provoke individuals’ loss aversion bias, which causes individuals to desire to avoid incurring losses compared to acquiring gains.\footnote{See Daniel Kahneman et al., The Endowment Effect, Loss Aversion, and Status Quo Bias, 5 J. ECON. PERSP. 193, 197-201 (1991) (describing different psychological effects of losses versus gains); Amos Tversky & Daniel Kahneman, Rational Choice and the Framing of Decisions, in RATIONAL CHOICE: THE CONTRAST BETWEEN ECONOMICS AND PSYCHOLOGY, 74-75 (Robin M. Hogarth & Melvin W. Reder eds., 1987) (describing loss aversion bias).} Consequently, collateral tax sanctions could magnify the cost of tax noncompliance for individuals motivated by deterrence, leading them to pay their tax liability properly.

In addition to their deterrent effects, collateral tax sanctions may also increase individual tax compliance among taxpayers who are motivated by feelings of reciprocity. Under this theory, some taxpayers comply with the tax system only if they perceive that other taxpayers are complying as well. A disadvantage of traditional monetary tax penalties is that taxing authorities almost always apply them behind a curtain of taxpayer privacy,\footnote{I.R.C. § 6103.} preventing individuals who are motivated by reciprocity from viewing specific examples of the government’s detection and punishment of
individuals who have engaged in abusive tax activities. Certain types of collateral tax sanctions, on the other hand, may result in consequences that are not hidden by this curtain. For example, if a physician fails to pay her taxes for several years and, as a result, forfeits her medical license temporarily, her colleagues may learn of the suspension. If her colleagues are tax compliant, they may, upon hearing of this suspension, feel assured that they have not acted like “chumps” for paying their taxes honestly while others cheat. Collateral tax sanctions thus present governments with a unique opportunity to provide the public with vivid images of its tax enforcement capabilities.

Collateral tax sanctions may also have a beneficial influence on the tax reporting behavior of individuals who fear the negative signal of tax noncompliance. Certain collateral tax sanctions may force individuals to reveal to others that they have failed to pay their taxes. For example, individuals who must forfeit their driver’s licenses may seek transportation assistance from others, increase their use of public transportation options or share with others complaints about their loss of driving privileges. For individuals who are motivated by signaling, the possibility of collateral tax sanctions may enhance their willingness to calculate and pay their taxes correctly.

Last, collateral tax sanctions may have a greater ability than formal tax penalties to strengthen the norm of compliance among individuals who are motivated by a sense of duty arising out of their citizenship. Some individuals obey the tax law because they believe that it is their duty as citizens to pay their taxes in exchange for government benefits. Governments struggle to establish “expenditure-revenue links” convincingly, leading some tax scholars to propose a variety of public communication methods. When governments apply collateral tax

31 Conversely, tax privacy also prevents them from viewing specific examples of the government’s tax enforcement weaknesses. See Blank, supra note 28.
33 See Eric Posner, Law and Social Norms: The Case of Tax Compliance, 86 Va. L. Rev. 1781 (2000) (arguing that an individual complies with the tax law to avoid sending a signal to others that he is a “bad type”).
34 For further discussion, see infra notes 216 – 231 and accompanying text.
35 See infra notes 232 – 242 and accompanying text.
sanctions, they confiscate valued benefits from individuals who fail to pay their taxes. This act of confiscation may enable governments to preserve, and even expand, the perception that tax dollars indeed fund important benefits and services.

After considering the compliance benefits of collateral tax sanctions and potential drawbacks under each of the predominant theories of voluntary compliance, I propose principles that governments should consider when designing collateral tax sanctions. Specifically, I argue that collateral tax sanctions are most effective as a means of promoting tax compliance where (1) the tax offense results from a violation of a tax rule, not a tax standard, (2) the taxing authority, as opposed to another government agency, determines that a taxpayer has committed the tax offense and (3) the collateral tax sanction is proportionate to the tax offense.

I then apply this proposed framework to determine whether a variety of specific tax offenses, including offenses other than non-payment of taxes, should subject offenders to collateral tax sanctions. These principles suggest that initiatives to revoke professional licenses from individuals who have failed to file their tax returns would likely promote voluntary compliance. However, whether the threat of deportation as punishment for tax offenses “involving fraud or deceit,” the collateral tax sanction at issue in Kawashima, will have positive effects on voluntary compliance is far less certain. In addition, I consider the role that the taxing authority should play in publicizing collateral tax sanctions.

The remainder of this Article proceeds as follows. Part II introduces the concept of collateral tax sanctions and offers illustration of their current application. Part III investigates the reasons why collateral tax sanctions appear to promote individual tax compliance more effectively than additional monetary tax penalties. Part IV proposes principles that governments should consider when designing collateral tax sanctions and addresses publicity strategies that taxing authorities should adopt. Part V concludes.

revenue links); The White House, Your 2010 Federal Tax Receipt, available at http://www.whitehouse.gov/issues/taxes/tax-receipt (providing detailed allocation of individual tax payments to government programs and services).

38 See infra notes 262 – 297 and accompanying text.
39 See infra notes 299 – 366 and accompanying text.
41 See infra notes 299 – 366 and accompanying text.
42 See infra notes 367 – 394 and accompanying text. This Article focuses exclusively on the potential tax compliance effects of state-sponsored collateral tax sanctions. It does not address the collateral consequences of tax noncompliance that may be imposed by private actors, such as private sector employers, creditors, and personal associates.
II. THE RISE OF COLLATERAL TAX SANCTIONS

If you ask most people what will happen to them if they decide not to pay their taxes, they will probably provide one or more responses: audits, tax penalties, maybe even prison. While these are familiar possibilities to much of the population, a host of additional sanctions that are administered by agencies other than the taxing authority may also apply. Scholars are well aware of the concept of collateral consequences of criminal convictions, yet they have not explored the rise of these consequences for civil and criminal acts of tax noncompliance. This Part briefly reviews the criminal law literature on collateral consequences generally, introduces the concept of collateral tax sanctions and offers examples of these sanctions applied by governments today.

A. Collateral Consequences Generally

Collateral consequences are the indirect penalties, restrictions and “legal disabilities” that an individual faces as a result of being subject to a formal sanction for committing an offense. They can be automatic or discretionary. They can be administered by the state through administrative government agencies. And they may also be applied by private actors, such as employers, lenders and even family and friends. Regardless of the specific type, collateral consequences apply in addition to the formal sanction that an offender receives for committing an offense.

The most common examples of collateral consequences stem from criminal convictions. The federal government alone revokes dozens of benefits and opportunities from individuals who are convicted of certain

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43 For discussion of popular perceptions of formal tax penalties, see Blank, supra note 28 at 299; Lawrence Zelenak, Six Decades of the Federal Income Tax in Sitcoms, 117 TAX NOTES 1265 (2007) (reporting results of television sitcom episodes involving tax compliance and finding that 50% of the episodes studied featured criminal tax penalties, including prison).
44 See supra note 16.
46 For example, in New York, certain convictions mandatorily prevent certain individuals from gaining licenses to serve as bail bondsmen, alcoholic beverage wholesalers and others. See New York State Bar Association, supra note 19 at 88-93.
felony and misdemeanor offenses. For example, when an individual is convicted of a felony drug offense, he may receive a prison sentence (a formal sanction), but upon release from prison, he may also be denied admission to public housing (a collateral consequence). And as a result of federal rules and regulations, he may also, for varying periods of time, forfeit the ability to serve on a federal grand or petit jury; hold a passport; enlist in any branch of the military; receive a commercial motor vehicle license; serve in certain leadership roles in a labor organization; work as a federal law enforcement officer; register as a commodities dealer; work for a hospice; receive a broadcast license; work at a federal insured depository institution; serve as a foster or adoptive parent; qualify for certain federal higher education grants or loans; receive food stamps or temporary assistance to needy families; obtain or sell firearms; among many others. State government agencies may also impose their own additional restrictions upon an individual convicted of a federal drug offense, such as by suspending his driver’s license. Commentators have noted that over the past two decades, Congress has granted federal agencies increasing autonomy to determine whether to deny or revoke a benefit as a result of an individual’s prior criminal conviction.

Why are convicted individuals subject to so many restrictions in addition to their formal punishments? The most convincing explanation for

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56 42 C.F.R. § 418.144.
57 47 C.F.R. § 73.4280.
60 20 U.S.C. § 1091(r).
61 21 U.S.C. § 862a(a) (lifetime ban on food stamps due to felony drug conviction).
62 18 U.S.C. § 922(g)(9)
63 For a comprehensive list of collateral consequences, see American Bar Association Commission on Effective Criminal Sanctions, Internal Exile: Collateral Consequences of Convictions in Federal Laws and Regulations (2009).
65 For discussion, see Pinard, supra note 16 at 634-647.
the existence of collateral consequences is that government officials revoke or deny a benefit when they believe that there is a relationship between an individual’s past offense and the particular benefit at issue. For instance, states presumably rescind a convicted drug dealer’s driver’s license in order to prevent the individual from transporting and distributing drugs with ease. Some commentators have argued that collateral consequences are actually part of a defendant’s punishment and should be treated that way for legal purposes, an interpretation which could implicate the information that a defendant must receive prior to sentencing. Courts have rejected this argument, however, holding that collateral consequences are merely civil restrictions imposed by agencies outside of the judicial system.

Despite this ostensible purpose, many have argued that the proliferation of collateral consequences that attach to felonies and misdemeanors should be reconsidered. The consensus view is that the accumulation of collateral consequences that apply under current federal and state law is detrimental to convicted individuals, their families and the rest of society as well. The primary objections of opponents of the current state of collateral consequences can be grouped into two overarching categories and are described briefly below.

**Obstacle to Reentry.** The first principle objection to collateral consequences is that they present to convicted individuals an unjustifiable obstacle to reentry into the community following their conviction. By preventing certain convicted individuals from residing in public housing or participating in civic engagement, such as by voting or serving on juries, collateral consequences, critics argue, alienate these individuals from others. They further assert that this ostracism leads to recidivism among offenders, and several studies support this claim.

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68 See, e.g., Olivares et al., *supra* note 16; Pinard, *supra* note 16; Pinard & Thompson, *supra* note 16; Chin; *supra* note 16; Mauer and Chesney-Lind, *supra* note 16; Karlan, *supra* note 18; Tewksbury, *supra* note 20.


Lack of Advance Notice. The second principle objection is that defendants lack adequate notice of the future application of collateral consequences when entering into plea agreements with prosecutors. Many commentators have noted that discussion of the potential collateral consequences rarely occurs between defendants, their lawyers and prosecutors before defendants enter a guilty plea.\textsuperscript{71} With few exceptions, however, courts have rejected general claims that defendants’ due process rights are violated if they are not informed of the collateral, in addition to the direct, consequences of convictions.\textsuperscript{72}

As a result of these concerns, government officials, advocacy groups and scholars have proposed a range of reforms to the criminal justice system that endeavor to reduce the adverse effects of collateral consequences of criminal convictions.\textsuperscript{73}

B. Collateral Tax Sanctions Defined

The discussion of collateral consequences by commentators thus far has focused almost exclusively on the extra-judicial effects of convictions for felony criminal offenses such as drug possession and distribution, illegal weapons possession, robbery, rape, assault and other violent crimes. Yet,

\textsuperscript{71} See, e.g., Priscilla Budeiri, \textit{Collateral Consequences of Guilty Pleas in the Federal Criminal Justice System}, 16 HARV. C.R.-C.L. L. REV. 157 (1981); Pinard & Thompson, \textit{supra} note 16 at 590-593; Archer & Williams, \textit{supra} note 69.

\textsuperscript{72} See, e.g., Commonwealth v. Duffey, 639 A.2d 1174, 1175 (Pa. 1994) (holding that there is no due process requirement that defendant who has pled guilty to driving under the influence be informed of collateral consequences, such as the suspension of his driver’s license); French v. United States, 408 F.2d 1027 (5th Cir. 1969) (holding that defendant lacks due process right to information regarding “legal disadvantages and collateral consequences of his conviction”). In 2010, however, the U.S. Supreme Court held that lawyer has engaged in deficient performance by failing to inform a defendant that a guilty plea may subject him to automatic deportation. Padilla v. Kentucky, 130 S.Ct. 1473 (2010).

\textsuperscript{73} For example, during his 2004 State of the Union address, President George W. Bush proposed, and Congress subsequently enacted, the allocation of $300 million in federal grants to organizations that provide employment assistance, substance abuse treatment and housing to individuals upon their release from incarceration. President George W. Bush, State of the Union Address, Jan. 20, 2004. On April 9, 2008, then-President George W. Bush signed the Second Chance Act of 2007, which authorized grants to government agencies and nonprofit groups to provide re-entry assistance to convicted individuals. Pub. L. 110-199 (2008). Another set of proposals has focused on increasing defendants’ knowledge of potential collateral consequences during plea negotiations with prosecutors. National Conference of Commissioners on Uniform State Laws, Uniform Collateral Consequences of Conviction Act (2010).
collateral consequences occur in other legal settings, including tax
noncompliance. As this Subpart reveals, the imposition of “collateral tax
sanctions” for acts of tax noncompliance has flourished in recent years
under federal, state and local law. Before proceeding, however, it is
necessary to define collateral tax sanctions and to distinguish them from
formal tax penalties.

The tax law contains an abundance of formal tax penalties that apply to
different acts of tax noncompliance. At the federal level, the Internal
Revenue Code contains more than 130 different tax penalties that apply to
civil tax offenses. Some of the most commonly known civil tax penalties
include delinquency penalties, where taxpayers who fail to pay their taxes
on time owe an additional penalty equal to up to 25% of the tax liability;
accuracy penalties, where taxpayers who underpay their tax through various
acts, such as negligence, owe an additional tax penalty equal to 20% of the
tax liability; and civil fraud penalties, where taxpayers who intentionally
underpay taxes owe an additional penalty equal to 75% of the tax liability.
The federal tax law also includes numerous criminal sanctions, including
prison sentences, which apply to offenses such as tax evasion, willful
failure to collect or pay taxes and declarations of false statements.

Collateral tax sanctions, on the other hand, are additional penalties that
occur outside the tax system. To use a fictional example, imagine that if
you fail to pay your taxes on time, your local board of elections will
prohibit you from voting in any federal, state or local election. In this
case, when you eventually pay this tax liability, you will likely owe a
formal tax penalty in the form of a delinquency tax penalty. But in addition
to the formal tax penalty, you will also have been subject to a collateral tax
sanction by forfeiting your right to vote.

Collateral tax sanctions, as I shall define them, possess three primary
characteristics: (1) they apply in addition to formal tax penalties; (2) they
rescind or deny a government-provided benefit or privilege; and (3) they are

of number of assessments of each penalty for a single fiscal year, see National Taxpayer
75 I.R.C. §§ 6651(a)(1), (2).
76 I.R.C. §6662.
77 I.R.C. §6663.
78 While criminal tax penalties are probably most prominent in the public
consciousness, nearly all enforced tax penalties relate to civil tax offenses. See National
79 The deprivation of voting rights may raise Constitutional concerns. See Cipriano
v. City of Houma, 395 U.S. 701 (1969)(striking requirement that voters in a general
bond election be “real property taxpayers”); Hill v. Stone, 421 U.S. 289 (1975)(striking
requirement property tax payment condition to voting).
usually enforced by an agency other than the taxing authority. These characteristics mirror the features of nearly all of the non-tax collateral consequences described above, such as restrictions on the right of certain convicted individuals to serve on juries or qualify for public housing. Applying this definition to the voting example, the revocation of the right to vote as a result of an outstanding state tax bill is a collateral tax sanction because it (1) applies in addition to a formal tax penalty, the monetary tax delinquency penalty, (2) revokes a government-provided benefit, the right to vote and (3) results from an action by a government agency other than the taxing authority, the board of elections.

Collateral tax sanctions are akin to tax expenditures, except that they operate in reverse. Tax expenditures refer to tax credits, deductions, exemptions and other mechanisms that the taxing authority administers in order to achieve a non-tax revenue-related public policy objective. As one example out of hundreds, the federal government encourages support of charities by allowing individuals to make tax-deductible contributions to a number of qualifying charitable organizations. The IRS must monitor these deductions to ensure that they comply with the relevant statutory provisions. Collateral tax sanctions, by contrast, require agencies other than the taxing authority, such as the board of elections in the example above, to participate in tax enforcement by rescinding or denying a government benefit as a result of an individual’s tax noncompliance.

C. Examples

With this definition in hand, it is possible to identify collateral tax sanctions. Below are several illustrations of collateral tax sanctions that have been proposed or enacted by the federal government and by state and local governments.

1. Federal Examples

a. Passports

Each year, the U.S. Department of State issues hundreds of thousands of passports to United States citizens who, collectively, owe the federal

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81 See Gov’t Accountability Office, Government Performance and Accountability: Tax Expenditures Represent a Substantial Commitment and Need to Be Reexamined (Sept. 2005).
82 I.R.C. § 170(a)(1).
government billions of dollars in unpaid tax. In 2012, the United States Senate passed a measure designed to encourage tax delinquent individuals to pay their tax outstanding tax bills. Under the legislation, the U.S. Department of State would be required to deny a request for a new passport or renewal of an existing passport from any individual owing more than $50,000 in “seriously delinquent” tax debt, tax debt for which the IRS has filed a notice of federal tax lien, and would be authorized to revoke the outstanding passport of any individual owing this amount of tax who attempts to re-enter the U.S.

The announcement of the passport denial proposal generated heated public debate. Opponents argued that denying passports to tax delinquent individuals would violate their due process rights by restricting an individual’s ability to travel based on a non-judicial determination of tax liability. Sponsors of the legislation responded that the provision would only apply to tax debt where the IRS had filed a notice of lien in public records. Further, they asserted that, if enacted, the proposal would raise over $740 million in tax revenue over a ten-year period. While the passport denial provision was passed by the U.S. Senate in 2012, it has not been adopted by the U.S. House of Representatives.

b. Residency

In *Kawashima v. Holder,* the U.S. Supreme Court addressed another
A collateral tax sanction with significant implications for lawful permanent residents in the U.S. who may have engaged in certain abusive tax activities. In this case, two lawful permanent residents, Akio and Fusako Kawashima, failed to pay nearly $250,000 in taxes attributable to their Japanese-food restaurants. In 1997, the Kawashimas pled guilty to willfully filing a false tax return, a felony under Section 7206(1) of the Internal Revenue Code. In addition to civil tax penalties, they received a four-month prison sentence and one year of supervised release.

In August 2000, three years after entering their guilty pleas and serving their prison sentences, federal immigration officials determined that the Kawashimas were subject to deportation back to Japan as a result of committing an “aggravated felony” under the Immigration and Nationality Act. Specifically, this statute provides that an aggravated felony includes an offense that “(i) involves fraud or deceit in which the loss to the victim or victims exceeds $10,000 or (ii) is described in section 7201 of title 26 (relating to tax evasion) in which the revenue loss to the Government exceeds $10,000.” While the Kawashimas did not plead guilty to tax evasion under Section 7201 of the Internal Revenue Code, the immigration authorities held that they had committed an act involving fraud or deceit which imposed a loss of more than $10,000 on a “victim”—the federal government itself—because they willfully filed false tax returns.

The U.S. Supreme Court upheld the Kawashimas’ deportation in a 6-3 decision in 2012, holding that the willful filing of a false tax return necessarily involves “fraud or deceit” under the aggravated felony statute. Whether the federal immigration authorities will expand the use of the collateral tax sanction of deportation following this decision remains to be seen.

c. Housing Assistance

Since the Great Depression, low-income individuals have received access to funds to purchase a home by borrowing a mortgage this is insured

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91 Brief for the Respondent, 5-12, Kawashima v. Holder, 565 U.S. ___, 132 S. Ct. 1166 (2012), appealing 615 F.3d 1043 (9th Cir. 2010).
92 Id.
93 Id.
94 Id.
96 Brief for the Petitioners, 5, Kawashima v. Holder, 565 U.S. __ (2012), appealing 615 F.3d 1043 (9th Cir. 2010).
97 Id.
by the Federal Housing Administration (FHA).\textsuperscript{99} Unlike conventional mortgages, an FHA-insured loan is a low-payment obligation that requires a very low down payment from the borrower.\textsuperscript{100} This federal program has offered housing assistance to millions of Americans. Under current law, however, if an individual is delinquent in paying any federal taxes or has been subject to a tax lien by the federal government, the individual may not participate in the FHA loan program until entering into a written repayment plan with the IRS.\textsuperscript{101} Denial of this federal benefit applies in addition to any formal tax penalties and is applied by the U.S. Department of Housing and Urban Development.

d. Government Contracts and Employment

Individuals and businesses that desire to enter into valuable contracts with the federal government may be prevented from doing so if they have failed to comply with certain tax rules. In 2011, the Government Accountability Office revealed that 3,700 federal contractors who received economic stimulus funds during the Obama Administration collectively owed nearly $760 million in outstanding federal tax liability.\textsuperscript{102} In response, Congress ultimately enacted legislation that bars the award of a government contract worth more than $5 million unless the service provider can certify that it has filed all federal tax returns during the prior three years, has not been convicted of a tax crime and does not owe any outstanding federal tax debt.\textsuperscript{103}

In addition, in 2012, the U.S. House of Representatives passed legislation that would deny federal employment to tax delinquent individuals. Under the legislation, all federal agencies would be required to deny employment to any individual with a “serious” federal tax delinquency and to terminate any existing federal employee who is “seriously” tax delinquent.\textsuperscript{104} The legislation defines tax delinquency as serious whenever the IRS has filed a Notice of Federal Tax Lien with


\textsuperscript{100} See id.


\textsuperscript{102} Gov’t Accountability Office, Thousands of Recovery Act Contract and Grant Recipients Owe Hundreds of Millions in Federal Taxes, April 2011.


respect to the tax debt, regardless of the amount of the obligation. As the sponsor of this legislation has described its justification, “[e]mployees who consciously ignore the channels and processes in place to fulfill their tax obligations must be held accountable.” This provision has not yet been passed by the U.S. Senate.

2. State and Local Examples

a. Driver’s Licenses and Vehicle Registration

Several states have created policies that revoke one of the most significant benefits that they provide, the license to drive. In 2011, California enacted legislation that requires the Department of Motor Vehicles to suspend the driver’s license of any individual on a list of the top 500 taxpayers who owe income taxes or on another list of the top 500 taxpayers who owe sales taxes. The license suspension remains in effect until the taxpayer has made arrangements to satisfy the outstanding tax liability. Other states that also rescind driver’s licenses from tax delinquent residents include Massachusetts, Maryland and South Carolina.

Similarly, several states deny renewal of vehicle registration to individuals who are delinquent in paying a variety of state and local taxes. For example, many municipalities in Rhode Island impose an annual “car tax” based on the value of automobiles owned by residents. If an individual is delinquent in paying the car tax on any of his cars, the

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105 Id., at § 2(a).
109 Id.
110 Mass. Gen. L. Part I, Title X, Ch. 60A, § 2A (“Nonpayment of taxes; collection; nonrenewal of driver’s license and vehicle registration”).
112 South Carolina Code § 12-37-2740 (suspension of driver’s license for failure to pay personal property tax on vehicle).
113 See, e.g., Rhode Island General Laws § 31-3-6 (“Denial of registration”); Connecticut, CT Motor Veh. Ch. 246, § 14-33; South Carolina, S.C. Code § 12-37-2740 (suspension of vehicle registration; for failure to pay personal property tax on vehicle);
114 Rhode Island General Laws § 31-3-6 (“Denial of registration”).
Rhode Island Department of Motor Vehicles blocks the renewal of vehicle registration for all cars owned by the individual. Not only does the individual owe the original car tax and formal delinquency tax penalties, but the individual may also lose the use of the car that was subject to the tax and any other cars that he owns as well.

b. Professional Licenses

Many states condition the grant of various professional licenses held by individuals and by businesses upon compliance with state and even federal tax laws. Like all collateral tax sanctions, they revoke a government-provided benefit, the license to engage in a particular profession, in addition to formal tax penalties that may result from tax noncompliance.

Medical Licenses. When considering whether to grant or renew medical licenses, state medical licensing boards often consider tax compliance as a factor relevant to the question of whether a physician possesses moral character sufficient to establish a patient’s trust. In Minnesota, for instance, if the state taxing authority informs the medical licensing board that a physician is delinquent in paying taxes, civil tax penalties or interest or has simply failed to file tax returns at all, the medical licensing board may deny or suspend the physician’s license.

Law Licenses. In the same vein, many state bars consider certain tax noncompliance to be an act of “moral turpitude” that may justify denial or suspension of a license to practice law. For example, in 2011, a prominent New York attorney pled guilty to two counts of failing to file U.S. income tax returns for 2004 and 2006 and two counts of willfully failing to pay income taxes in 2005 and 2007. He paid formal tax penalties and received a criminal sentence of 28 months of incarceration,

115 Id.
117 See Minn. Stat. § 270C.72 (mandating revocation of medical license if individual owes taxes, penalties or interest and the taxing authority notifies the medical licensing board); Mo. Rev. Stat. § 324.010 (Missouri); 32 V.S.A. § 3113(f) (Vermont). For discussion see Arthur H. Coleman, Suspension of Medical License for Tax Evasion, 55 J. NAT’L MED. ASSOC. 255 (1963)
118 See, e.g., California Rules Proc. of State Bar, tit. IV, Stds. for Atty. Sanctions for Prof. Misconduct, std. 1.4(c)(ii) (revoking law license for acts of moral turpitude, including failure to pay taxes).
followed by one year of supervised release. In addition to incurring these formal tax penalties, the disciplinary committee of the New York bar suspended the attorney’s law license as a result of his willful failure to file tax returns even though this was a misdemeanor offense and involved federal, not state, tax returns.

Liquor Licenses. When restaurant owners have failed to pay established tax liability, the state agency responsible for issuing liquor licenses may suspend the restaurant’s license to serve alcoholic beverages to customers. The responsible agency often publicly posts a notice of suspension or revocation of a restaurant’s liquor license at the entrance of the restaurant, informing all customers that they will not be able to purchase alcoholic beverages at this establishment. As a result of this sanction, not only will the restaurant owner face formal tax penalties for not paying outstanding tax liabilities, but, without a liquor license, may also lose significant business income.

c. Recreational Licenses

Last, several states and municipal governments suspend licenses to engage in recreational and entertainment activities from individuals who are delinquent in paying state and local taxes.

Hunting and Fishing Licenses. Whether the target is deer, bass or even alligators, recreational hunting and fishing in Louisiana, the “Sportsman’s Paradise,” is often described as a “way of life.” Since 2004, however, if a Louisiana resident owes over $500 in state taxes, the

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120 Id.
121 Id.
122 See, e.g., Minnesota Statutes § 270C.725 (describing how all businesses with licenses to sell liquor, beer or wine must be placed on the “Tax Delinquency List” if they owe state taxes); Assembly Bill 1424, California, The Delinquent Taxpayer Accountability Act (Oct. 4, 2011).
123 For example, in 2011, the California Department of Alcohol Beverage Control posted a “Notice of Suspension” sign in the window of 3rd & U Café, located near the University of California-Davis campus, because the restaurant owners owed outstanding tax liability. Angela Swartz, Cafe is left dry following liquor license suspension, THE CALIF. AGGIE, Nov. 14, 2011.
124 As one disappointed student commented in response to the closing of the 3rd & U Café, “For me it sucks…alcohol is a huge part of their business….” Id.
126 This slogan has appeared on Louisiana license plates since 1958. See Louisiana Office of Motor Vehicles, Vehicle Services, available at http://omv.dps.state.la.us/.
127 James A. Robichaux, Gator hunting is way of life for some, StMaryNow.com, Sept. 5, 2012.
Louisiana Department of Wildlife and Fisheries will suspend all hunting and fishing licenses held by that individual and will deny requests for renewal until the individual has satisfied the outstanding tax liability.\footnote{128} Despite initial controversy over the measure, Louisiana state officials have reported that this license suspension program has significantly enhanced its ability to settle outstanding tax debts.\footnote{129}

**Entertainment Events.** Finally, some state and local governments have barred tax noncompliant individuals from participating in entertainment activities. In Minnesota, the annual state fair boasts attendance rates that are among the highest of such events in the United States.\footnote{130} In keeping with its description as the “Great Minnesota Get-Together”,\footnote{131} participation in the fair includes enjoyment of carnival rides and live music,\footnote{132} but also operation of educational booths, such as one offering attendees the opportunity to “milk” a fiberglass cow\footnote{133} or witness a live animal birth.\footnote{134} While the state fair is an annual community ritual, if an individual owes more than $500 in Minnesota state taxes or has not filed state tax returns, he will not be permitted to operate a concession, ride or booth at the fair.\footnote{135}

### III. Why Collateral Tax Sanctions Promote Compliance

Despite the apparent popularity of collateral tax sanctions among federal and state government officials, sponsors of these sanctions have not offered a coherent theoretical or empirical basis to justify why they should be applied as tax collection tools. Neither the tax compliance nor criminal

\footnote{128} Louisiana Revised Statutes § 47:296.3.
\footnote{129} See Louisiana Dep’t of Rev., Suspension, Revocation, Denial of Licenses Now in Effect, 24 TAX TOPICS 1 (2004) (describing initial results of hunting license revocation program).
\footnote{131} This is the official slogan of the fair. See Minnesota State Fair, available at http://www.mnstatefair.org/_assets/pdf/Printable_12_New_Foods.pdf.
\footnote{134} See Minnesota State Fair, 2012 CHS Miracle of Birth Center, available at http://www.mnstatefair.org/entertainment/ag_exhibits/chs_mob.html (described as the “birthplace of approximately 200 animals including calves, lambs and piglets during the fair’s 12-day run”).
\footnote{135} Minn. Stat. § 270C.72, Subd. 2(c) (defining “license” as authorization to operate “concessions or rides” at “Minnesota State Fair”).
law literature presents a theory of why the collateral consequences of formal penalties may prevent individuals from violating the law. However, before we can determine whether governments should deploy collateral tax sanctions, and in what contexts, we must examine the reasons why they may promote voluntary compliance.

It is not surprising that criminal law scholars who have studied the collateral consequences of convictions have not explored their effects on an individual’s initial decision to commit a crime. Imagine that an individual is considering robbing a bank using a shotgun. If the individual is convicted for committing this crime, under federal law, he may receive a prison sentence of up to twenty years.\(^{136}\) In addition, after serving the prison sentence, he may also be barred from working in a variety of jobs, ranging from barber\(^ {137}\) to airline employee\(^ {138}\) to officer in a labor organization\(^ {139}\). If the threat of a 20-year prison sentence does not prevent this individual from robbing the bank, however, it is highly improbable that the future loss of professional opportunities following the conviction will deter this individual either. An explanation for the lack of discussion in the criminal law literature of affirmative uses of collateral consequences, thus, is that the formal penalties for many criminal offenses are often of greater magnitude than the associated collateral consequences.\(^ {140}\)

Collateral consequences may play a more significant role in influencing an individual’s decisions in the tax compliance context. Nearly all enforced tax penalties are civil rather than criminal.\(^ {141}\) At both the federal and state level, the offense of tax delinquency results in the imposition of additional monetary penalties and interest, but, absent fraud, it usually does not result in jail time.\(^ {142}\) It is possible that collateral tax

\(^{136}\) See 18 USC § 2113(a).


\(^{139}\) See 29 U.S.C. § 504.

\(^{140}\) Further, several scholars have commented that government officials do not apply collateral consequences to serve a deterrence purpose because most defendants are unaware of most of these consequences at the time when they enter a guilty plea, let alone commit the original offense. See, e.g., Demleitner, supra note 16 at 161 (1999) (“the relatively low visibility of collateral consequences makes them unlikely deterrents to crime”); Pinard, supra note 16 at 508 (“there are reasons to doubt that deterrence explains the proliferation of collateral consequences in recent decades”).


sanctions may promote compliance where the threat of criminal sanctions does not exist. Put differently, collateral tax sanctions may represent an intermediate tax penalty, one that is more significant than traditional monetary tax penalties, but less severe than incarceration.

In this Part, I argue that as a result of significant differences between collateral tax sanctions and traditional tax penalties, the use of collateral tax sanctions may promote compliance among individuals more effectively than the imposition of additional monetary tax penalties. My primary claim is that an individual may be more likely to choose to pay outstanding tax liabilities when faced with the risk of losing a salient government benefit, such as a professional or, even, recreational license, than when faced with the threat of being subject to additional monetary tax penalties. After addressing arguments for why collateral tax sanctions may be successful in the tax delinquency context, we can consider whether and how collateral tax sanctions should be applied to tax offenses other than tax delinquency.

A. Why Do People Pay Taxes?

In the United States, most people pay their taxes. According to the latest statistics released by the federal government, approximately 83% of all tax dollars owed to the federal government are paid correctly and in a timely manner each year.

In light of the complexity of the federal tax law and its reliance on individual taxpayers to correctly self-assess and report income, government officials, commentators and scholars have lauded this compliance rate as high.

The other side of the voluntary compliance coin is the gross federal tax gap, the amount of true tax liability that is not paid on time each year. According to the most recent government reports, this amount is $450 billion, or approximately 17% of taxes owed. Noncompliance by

This number represents 0.00086% of the total individual tax returns filed in 2009. See Individual Complete Report (Publication 1304), Table 1.6, SOI Tax Stats—Individual Statistical Tables by Size of Adjusted Gross Income, available at http://www.irs.gov/taxstats/indtaxstats/article/0,,id=96981,00.html (140,494,127 individual tax returns filed in 2009).

143 Int. Rev. Serv., Tax Year 2006 Tax Gap Estimate – Summary of Estimation Methods, 1, January 2012 (describing voluntary compliance rate of 83.1%).


146 Id. at 1 (describing gross federal tax gap of 16.9%).
individual taxpayers, as opposed to corporations or other entities, represents the largest component, $296 billion, of the gross federal tax gap.\textsuperscript{147} And within the federal tax gap, certain forms of tax compliance occur at levels far lower than the overall voluntary compliance rate, such as reporting of income by small business owners who are not subject to information reporting or withholding.\textsuperscript{148}

There is no single answer to the question of why some individuals comply with the tax law and others do not.\textsuperscript{149} Over the past several decades, legal scholars and economists have offered a number of theories that may explain why individual taxpayers are motivated to comply with the tax law, other than rules that require mandatory withholding of tax liability by third parties. Some of the most prominent of these possible motivations of compliance include fear of sanctions;\textsuperscript{150} the perception that others are reciprocating one’s tax compliance;\textsuperscript{151} a desire to avoid the negative signal of tax noncompliance;\textsuperscript{152} and the belief that payment of taxes is a duty of citizenship.\textsuperscript{153}

In addition to these theories of individual tax compliance, tax scholars have observed that cognitive biases and heuristics may also influence individuals’ decisions.\textsuperscript{154} As a general matter, these biases cause people to draw incorrect conclusions based on memorable events, anchor themselves to initial values, overvalue losses and exhibit other seemingly irrational

\textsuperscript{147} U.S. Gen. Acc. Office, Sources of Noncompliance and Strategies to Reduce It, 4, April 2012. Underreporting of income by individuals represents most of this portion of the individual tax gap, but underpayment and non-filing represent $61 billion, or 20%, of the gross individual tax gap. \textit{Id.}

\textsuperscript{148} Only 44% of income that is subject to little or no information reporting, such as cash income, rents, royalties and farm income, is properly reported and paid to the federal government each year, where 99% of income that is subject to third party information reporting and withholding rules, such as wages, that is properly reported and paid. \textit{Id.} at 6 (Figure 1).


\textsuperscript{151} See Ernst Fehr & Simon Gächter, \textit{Reciprocity and Economics: The Economic Implications of Homo Reciprocans}, 42 EUR. ECON. REV. 845 (1998) (applying reciprocity theory to economics scenarios); Kahan, \textit{supra} note 32 (discussing the reciprocity model).

\textsuperscript{152} See Posner, \textit{supra} note 33 (applying signaling model to tax compliance).


\textsuperscript{154} See generally, \textit{Thaler & Sunstein, supra} note 28; Tversky & Kahneman, \textit{supra} note 28; McCaffery, \textit{supra} note 28 (describing cognitive biases).
Several tax scholars have explored the ways that cognitive biases may influence individuals’ tax planning and compliance decisions.  

B. Collateral Tax Sanctions and Motivations of Compliance

In this Subpart, I investigate how the current uses of collateral tax sanctions by the federal and state governments, which primarily have targeted the offense of tax delinquency, may promote tax compliance among individuals. In conducting this analysis, I contrast the use of collateral tax sanctions in addition to formal tax penalties with the exclusive use of formal tax penalties, taking into account the perceived major motivations for tax compliance and individuals’ well-known cognitive biases.

1. Deterrence

Individuals who are motivated by deterrence may assign greater weight to collateral tax sanctions than to traditional monetary tax penalties. Deterrence theorists posit that individuals act rationally when deciding whether to engage in tax avoidance or evasion by comparing the expected benefit of a particular tax position (the tax savings, discounted by the probability that the taxing authority will detect the position) against the expected cost of claiming the tax position (tax penalties and interest, discounted by the probability that the taxing authority will not detect the position). Behavioral law and economics expands on this model by revealing that when individuals weigh costs and benefits, they often make errors in calculating their values as a result of inherent cognitive biases.

An explanation for the success that governments have experienced when threatening to apply collateral tax sanctions is that these sanctions trigger individuals’ salience biases and loss aversion and endowment effect biases.


156 See supra note 28.

157 See JEREMY BENTHAM, THE THEORY OF LEGISLATION 325 (C.K. Ogden ed., Richard Hildreth trans., Routledge & Kegan Paul Ltd. 1931) (1802); Becker, supra note 150 (to deter crime generally, the threat of punishment must outweigh the benefit of the act); Rasknolnikov, supra note 15.

158 See supra note 28.
more effectively than traditional monetary tax penalties.

Salience. The salience bias causes many individuals to pay greater attention to information that is prominent rather than that which is hidden. In their seminal work on cognitive biases and heuristics, Amos Tversky and Daniel Kahneman, hypothesized that the salience of information affects the “retrievability of instances” for individuals. For example, an individual may be more affected by witnessing a violent car accident in person than by reading anonymous statistics regarding car accidents in the newspaper. In a number of studies, scholars have noted that the effect of a particular tax on an individual’s purchasing decisions may increase with the salience of the tax. Consistent with these studies, collateral tax sanctions may serve as an effective deterrent because their features cause them to be more salient than traditional monetary penalties.

When an individual owes monetary tax penalties as a result of failing to report tax liability properly or pay outstanding tax liabilities, she may consider the tax penalties as indistinguishable from the overall tax bill. Because both items consist of money, tax liability and tax penalties may be fungible in the taxpayer’s mind. The government may inadvertently promote conflation. For example, when describing the collection of delinquent taxes, many state and local governments inform their residents that the tax assessor collects “taxes, including penalties and interest.” Similarly, in its instructions to taxpayers regarding installment agreements and offers in compromise, the IRS refers to tax liabilities as “taxes, including penalties and interest.” As a result of these formulations,


160 Tversky & Kahneman, supra note 28.

161 Id.


163 See, e.g., Ind. Code § 6-1.1-23-1(d)(“Determine the amount of the delinquent taxes, including penalties and interest accrued”); Mont. Code § 39-51-1304 (1) (“Unpaid taxes, including penalties and interest assessed on unpaid taxes); Salt Lake County, General Information – 2012 Board of Equalization, available at http://www.taxadmin.slco.org/html/boardGeneralInfo.html (“The Assessor collects taxes, including penalties and interest”).

164 Int. Rev. Serv., Form 433-D, Installment Agreement (“This agreement will remain in effect until your liabilities (including penalties and interest) are paid in full”);
individuals may consider tax penalties to be a part of the tax liability itself rather than separate punitive payments. If an individual has ignored outstanding tax liability, consequently, the threat of additional monetary penalties may not be salient enough to encourage her to comply. Tax liens are also not effective collection mechanism for many taxpayers, particularly wealthy individuals. One might ask, for instance, why the proponents of the passport revocation legislation or California’s driver’s license initiative advocated for these measures when they apply only after the taxing authority has filed a tax lien against the taxpayer. A tax lien alerts future purchasers of the taxpayer’s property and the taxpayer’s creditors that the government holds a claim against the property. Imagine that a wealthy individual owns three houses and the IRS (only knowing about one of them) files a Notice of Federal Tax Lien only where one of the houses is located. The filing of the lien may have no effect on the other two houses. In addition, if the taxpayer has no plans to sell the house that is subject to the tax lien, he may allow the lien to remain without suffering a serious consequence. Tax liens adversely affect individuals’ credit scores, but wealthy individuals may not suffer from this effect because they may not rely on borrowing from third-party lenders. Finally, if the property is already encumbered with mortgages, the IRS may not seek to foreclose on a house subject to a tax lien because, after the other creditors are satisfied, the IRS would collect little from the foreclosure proceedings. The IRS files millions of tax liens each year without recovering the outstanding tax liabilities.

Collateral tax sanctions, by contrast, target conspicuous privileges and services and, as a result, may evoke stronger psychological reactions from individual taxpayers. Several collateral tax sanctions—such as those which cause an individual to lose a driver’s license, forfeit a passport or face deportation hearings—may threaten crucial benefits. In turn, they tend to

Int. Rev. Serv., Form 656 Booklet, Offer in Compromise (“If your offer is defaulted, all compromised tax debts, including penalties and interest, will be reinstated.”).

165 See supra notes 108 to 116 and accompanying text.


167 I.R.C. § 6323(f) (describing place for filing of lien).


169 See I.R.C. § 7403 (foreclosure proceedings). A pre-existing mortgage lien takes priority over a tax lien filed by the IRS. Int. Rev. Man. 5.17.2.6 (2012).

receive significant publicity. For example, since the Senate first considered proposals to rescind or deny passports to tax delinquent individuals in 2011, this particular proposal has been the focus of hundreds of media reports.\(^{171}\) As a result, individuals may have an easier time imagining the consequences of losing one of these privileges than owing additional monetary penalties.

In addition, the salience of collateral tax sanctions may cause individuals to place a high value on the benefits that they revoke. Many of these benefits serve a mix of personal and business purposes. For example, a driver’s license may enable an individual to drive to work where she can earn a paycheck, but it may also allow her to drive to her son’s little league baseball game or a friend’s birthday party. For this reason, many consider the driver’s license to be one of the most valuable benefits they receive from their state government.\(^{172}\) Some may even consider this benefit to be beyond valuation. As one court noted when considering driving-while-intoxicated charges, “the fact remains that today the very livelihood of a man and his family may depend upon his license.”\(^{173}\) As a result, individuals may assign greater weight to collateral tax sanctions than to monetary tax penalties.

Last, not only are collateral tax sanctions themselves more salient than monetary tax penalties, but they may also be administered by government agencies that are more salient than the taxing authority. According to the IRS, nearly 60% of taxpayers in the United States use tax preparers or software to file their annual tax returns and do not interact with the IRS other than to write a check.\(^ {174}\) Collateral tax sanctions, on the other hand, force individuals to answer for their tax noncompliance directly by facing another government agency. Some of these agencies, such as the department of motor vehicles, have a reputation for being bound by strict rules and procedures.\(^ {175}\) As one example, in New Jersey, to receive a driver’s license, an individual must submit multiple specific identification

\(^{171}\) A search on LexisNexis ALL News Database for “passport” and “tax” and “deny” and “delinquent” between January 1, 2011 and September 24, 2012 yielded 55 different articles. A similar Google search yielded 1,390 articles.

\(^{172}\) See, e.g., Bechler v. Parsekian, 36 N.J. 242, 257 (1961) (“in today’s society a license to operate an automobile may be of vital significance and value to the licensee”).


documents and even refrain from excessive smiling when being photographed. If individuals are aware that they will forfeit a government benefit, such as a driver’s license, as a result of tax delinquency or other tax offenses, they may fear that the non-tax agency that enforces the sanction will be even less flexible than the taxing authority in correcting errors or compromising.

**Loss Aversion and Endowment Effect.** Collateral tax sanctions may also deter individuals from failing to comply with the tax system because they arouse two significant, related cognitive biases of individual taxpayers, loss aversion and the endowment effect. When individuals are forced to choose between two options—one that will lead them to experience a gain of some item and another that will cause them to suffer a loss of an item they already possess—individuals find it difficult to choose to experience the loss. As a result of their strong distaste for losses, individuals often experience the endowment effect, which causes them to develop an attachment to items they own and a reluctance to part with them. These two biases lead individuals to resist attempts by others to take their property, whether or not in exchange for compensation.

Many experiments have demonstrated that individuals are averse to losing things. In one of the most famous studies by Daniel Kahneman, Jack Knetsch and Richard Thaler, subjects were told that they were buyers or sellers. The sellers were given Simon Fraser University coffee mugs and the sellers were not given anything. When the buyers were asked to state the price at which they would purchase the coffee mug from the sellers,

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179 See Daniel Kahneman, Jack L. Knetsch & Richard H. Thaler, Experimental Tests of the Endowment Effect and the Coase Theorem, 98 J. POL. ECON. 1325, 1342 (1990) (describing “instant endowment effect”, which causes subjects to increase their valuation of certain goods as soon as they receive them).

180 Kahneman, Knetsch & Thaler, supra note 178.

181 Id. at 196.

182 Id.
they reported an average price of $2.87. The sellers, on the other hand, reported that they would be willing to sell the very same mugs to the buyers for an average price of $7.12. In another similar study, subjects were told that they would receive coffee mugs and were asked to speculate on the price for which they would be willing to sell the mugs. The subjects then received the actual mugs and were asked the same question. Once they held the mugs in their hands and “owned” them, they reported an average minimum selling price that was significantly higher than their original reported price. These and several other similar experiments reveal that individuals consider the experience of parting with property to be roughly twice as painful as gaining property of the same value.

Traditional monetary tax penalties may not induce strong loss aversion or endowment effects, especially if they are not applied at very high rates. Individuals do not experience loss aversion in all transactions. As the founding researchers in this area have stated, “buyers do not value the money spent on normal purchases as a loss, so long as the price of the good is not thought to be unusually high.” Others have stated the same principal using different terms, such as that loss aversion does not occur in “routine transactions” and that when individuals do not experience loss aversion when they spend money “as intended.” If these findings hold

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183 Id.
184 Id.
186 Id. at 932.
187 Id.
188 Kahneman, Knetsch & Thaler, supra note 178, at 199. This result is consistent with prospect theory. Daniel Kahneman & Amos Tversky, Prospect Theory: An Analysis of Decision Under Risk, 47 ECONOMETRICA 263 (1979) (individuals are risk averse when facing gains and risk seeking when facing losses). Several experiments have demonstrated the applicability of prospect theory to individual tax compliance. See, e.g., Gideon Yaniv, Tax Compliance and Advance Tax Payments: A Prospect Theory Analysis, 52 NAT. TAX J. 753 (1999) (finding that sufficiently high advance tax payments may induce compliance because individuals are risk averse when approaching tax refunds); Henk Elffers & Dick J. Hessing, Influencing the Prospects of Tax Evasion, 18 J. OF ECON. PSYCH. 289 (1997); Kathleen DeLaney Thomas, Presumptive Collection: A Prospect Theory Approach to Increasing Small Business Tax Compliance, 66 TAX L. REV. __ (2013) (offering proposal to impose presumptive collection on small business owners to cause them to expect tax refunds).
189 Kahneman, Knetsch & Thaler, supra note 178, at 200. See also Nathan Novemsky & Daniel Kahneman, The Boundaries of Loss Aversion, 42 J. OF MAR. RES. 119, 119.
190 Novemsky & Kahneman, supra note 189 at 119.
191 Id. (“A key idea is that exchange goods that are given up ‘as intended’ do not exhibit loss aversion.”)
true when applied to taxation, some taxpayers, particularly those who are habitually delinquent or otherwise noncompliant, may not consider monetary tax penalties to result in significant losses. When an individual deliberately decides not to pay outstanding taxes on time or fails to pay the appropriate amount of federal estimated tax payments each quarter, he knows that he may incur additional monetary tax penalties and interest.\textsuperscript{192} Individuals may consider monetary tax penalties such as these to be like any other payments that they intend to make during the year and, as a result, may not change their behavior in response to the threat of their imposition.

On the other hand, individuals may experience greater loss aversion when faced with the threat of collateral tax sanctions that would cause them to forfeit salient government benefits and services. Collateral tax sanctions may serve as more effective deterrents than traditional monetary tax penalties because many individuals are highly averse to the thought of having to sacrifice a license or benefit, such as the right to travel freely, apply for a subsidized federal loan or engage in a recreational activity like hunting or fishing. Unlike money that an individual allocates to the payment of monetary tax penalties, these government benefits and services may be considered “entitlements” in the minds of individual taxpayers, items that are similar to any other property they hold. News reports regarding collateral tax sanctions often use the terms “lose” or “forfeit” when discussing these sanctions, further stimulating individuals’ loss aversion biases.\textsuperscript{193}

Finally, collateral tax sanctions threaten to revoke benefits and services that cannot be replaced. An individual can pursue a number of different options, such as borrowing or increasing work hours, to replace the dollars spent on monetary tax penalties. But there is no private market for items such as passports, driver’s licenses, liquor licenses or many of the other government benefits and services that are the subject of collateral tax sanctions.\textsuperscript{194} In the face of collateral tax sanctions, the easiest way for individuals to avoid revocation of these benefits and services is to comply with the tax law.


\textsuperscript{193} \textit{See}, e.g., \textit{California to tax scofflaws: Pay up or lose your driver’s (or CPA) license}, ACCOUNTINGWEB.COM, Sept. 20, 2011, available at http://www.accountingweb.com/topic/tax/california-tax-scofflaws-pay-or-lose-your-drivers-license; \textit{State gets license to keep tax cheats off road}, BOSTON HER., Jul. 11, 2008, (“Don’t pay your taxes, and you will lose your driver’s license.”).

\textsuperscript{194} This statement refers to markets for legal, rather than counterfeit, licenses.
2. Reciprocity

While collateral tax sanctions may deter tax noncompliance by individuals who respond positively to the threat of penalties and punishment, they may also promote tax compliance by individuals who pay their taxes because they believe that other taxpayers are doing so as well. Reciprocity theory hypothesizes that many individuals are inclined to pay their taxes only if they believe that other individuals are reciprocating their compliant behavior. For “reciprocator” taxpayers, it is essential that the government appears to detect and punish free riders, individuals who fail to comply with the tax system. The federal government’s strategic publicity of its own tax enforcement actions reveals that its officials are well aware of the basic concept of reciprocity theory. As one former head of the U.S. Department of Justice Tax Division has commented, “[p]eople who pay what the law requires deserve the assurance that those who don’t, and those who promote or facilitate tax evasion, will not get away with it.” For several reasons, collateral tax sanctions may enable the government to provide this assurance more effectively than the threat of monetary penalties or strategic publicity of its tax enforcement efforts.

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195 The application of reciprocity theory to tax compliance is derived from several studies. In perhaps the most famous reciprocity study involving tax compliance, the Minnesota Department of Revenue provided different cover letters with individual tax returns to subjects. See Stephen Coleman, Minn. Dep’t of Revenue, THE MINNESOTA INCOME TAX COMPLIANCE EXPERIMENT: STATE TAX RESULTS (1996). Only one letter attempted to create the perception of widespread compliance by stating that “[m]ost taxpayers file their returns accurately and on time.” Id. at 48-51. The study found that this letter resulted in the most cost-effective increase in voluntary tax compliance. Id. at 25. In another study, Michael Wenzel found a positive relationship between an individual’s willingness to comply with the tax law and his perception that other taxpayers share norms of “taxpaying morality and responsibility.” Michael Wenzel, Misperceptions of Social Norms About Tax Compliance (2): A Field-Experiment 22 (Austl. Nat’l Univ. Ctr. for Tax Sys. Integrity, Working Paper No. 8, 2001). Whether one agrees that the findings of these studies and others like the are generalizable, taxing authorities, both in the United States and in other countries, have attempted to incorporate their predictions in their tax enforcement strategies. See, e.g., Behavioural Insights Team, United Kingdom, Annual Update 2011-2012 (reporting reciprocity experiments that encouraged individuals to pay outstanding tax liabilities).

196 See Fehr & Gächter, supra note 151; Kahan, supra note 151.

197 See id.

198 See HERBERT GINTIS, GAME THEORY Evolving 255 (2000). Several studies have demonstrated that individuals may reduce their compliance with the law if they perceive that others are cheating. See, e.g., James Andreoni, Cooperation in Public-Goods Experiments: Kindness or Confusion?, 85 AM. ECON. REV. 891 (1995); Joyce Berg et al., Trust, Reciprocity, and Social History, 10 GAMES & ECON. BEHAV. 122 (1995).

Publicity. Collateral tax sanctions generate significant amounts of media attention. California’s enactment of the driver’s license revocation provision in 2011, the U.S. Senate’s debate over the revocation of passports in 2012\(^{200}\) and the passage of legislation in Louisiana that empowered the state to rescind hunting licenses from tax delinquent individuals,\(^{201}\) just to name a few examples, were featured in dozens of stories in newspapers, radio and television reports and blog posts. This media attention is attributable to the high salience of the government benefits and services that collateral tax sanctions confiscate and the controversy that often surrounds the enactment of these measures. Further, because the federal and state legislatures rarely implement new dramatic changes in the monetary tax penalty structure,\(^{202}\) the introduction of collateral tax sanctions presents an opportunity for journalists to write entertaining and digestible news stories about tax developments. This heightened media coverage, thus, may cause reciprocator taxpayers to develop a perception that the government is focused on preventing tax noncompliance.

Observability. Collateral tax sanctions may also strengthen feelings of reciprocity by causing the public to observe specific examples of the government’s success in detecting and punishing tax noncompliant individuals. Under federal and state law, tax return information is protected by broad taxpayer privacy rules.\(^{203}\) As a result of these protections, the general public cannot determine whether a particular taxpayer has been audited or required to pay a monetary tax penalty. Even tax liens are not easily observable, as individuals must search court records to discover them and, with the exception of celebrities, the news media does not report on most tax liens.\(^{204}\) Scholars have argued that the “non-observability” of the compliance or non-compliance of other taxpayers poses a “serious problem” to attempts to apply reciprocity theory to taxpayer behavior.\(^{205}\)

Collateral tax sanctions, however, may force some noncompliant taxpayers who have been caught and punished to appear in front of the curtain of taxpayer privacy. For example, the owner of a restaurant may feel confidence in the government’s tax enforcement capabilities when he observes a forfeiture of liquor license sign in the window of one of his competitors who has failed to pay outstanding tax liability.\(^{206}\) Likewise, when a physician learns that a fellow doctor has forfeited his medical

\(^{200}\) See supra notes 86-89 and accompanying text.
\(^{201}\) See supra notes 125-129 and accompanying text.
\(^{202}\) For discussion, see Leigh Osofsky, The Case Against Strategic Tax Law Uncertainty, 64 TAX L. REV. __ (2012).
\(^{203}\) I.R.C. § 6103(a).
\(^{204}\) See, e.g., Lifsher & Wilson, supra note 168 (describing celebrity tax liens).
\(^{205}\) See, e.g., Doran, supra note 15 at n. 133.
\(^{206}\) See supra notes 122-124 and accompanying text.
license as a result of engaging in tax evasion, he may feel that few of his colleagues are likely willing to engage in similar acts, given the significance of the resulting penalty.® Collateral tax sanctions thus may provide reciprocator taxpayers with specific examples of the government’s tax enforcement success, where the use of monetary tax penalties results in much less memorable anonymous tax enforcement statistics.

Peer Group Examples. In addition to generating specific examples, collateral tax sanctions may also apply to members of a reciprocator taxpayer’s peer group. As tax compliance scholars have noted, the cooperative behavior posited by reciprocity theory most likely occurs when an individual believes that “other members of one’s in-group” are cooperating as well.

The media often publicizes instances where an individual taxpayer receives a criminal sanction for failing to comply with the tax law. As the federal government wins nearly all criminal tax cases, it attempts to maximize this publicity by prosecuting high-profile individuals, where possible, and by timing these prosecutions and guilty pleas to coincide with time periods when individuals are focused on preparing their individual tax returns. During the 2006 criminal trial of Wesley Snipes, for instance, the public learned that the movie star had filed millions of dollars in fraudulent refund claims, adopted the “861 position” (a tax protester argument) and even signed fabricated tax return forms. While Snipes was ultimately convicted for willfully failing to file tax returns, it is possible that some reciprocator taxpayers viewed this conviction as an indication that only extreme acts of tax evasion committed by tax protestors are the types of offenses that result in detection and prosecution by the

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207 See supra note 117 and accompanying text.
208 For further discussion of the power of specific examples, see Blank, supra note 28 at 288-290.
210 See, e.g., Jeffrey A. Dubin, Criminal Investigation Enforcement Activities and Taxpayer Noncompliance, 35 PUB. FIN. REV. 500, 502 (2007) (finding that the media play a large role in the dissemination of stories on tax enforcement, which increases tax compliance); Robert M. Melia, Is the Pen Mightier than the Audit?, 34 TAX NOTES 1309, 1310–11, 1311 n.3 (1987) (observing that the media play a large role in the dissemination of tax-enforcement stories).
211 See Blank, supra note 28 at 316-317 (discussing role of media).
taxing authorities.

Because collateral tax sanctions result in specific examples of enforcement and may affect a diverse group of taxpayers, however, they may further increase reciprocator taxpayers’ confidence in the government’s ability to ensure that their peers are paying their fair share of taxes. For example, when a prominent attorney at a New York City law firm forfeited his law license in 2012 as a result of his failure to file tax returns or pay taxes for several years, he appeared in a public court and the press covered his story extensively.\textsuperscript{214} Upon hearing this news, another New York City law firm partner who dutifully files her tax returns in dozens of jurisdictions in which her firm conducts business may have felt satisfied that she has not engaged in burdensome tax return preparation and made sizeable tax payments while her colleagues at other firms, or even the same firm, simply ignored their tax obligations.\textsuperscript{215}

For reciprocator taxpayers, observable punishments for tax delinquency are especially important. If reciprocator taxpayers perceive that the taxing authority is not capable of detecting blatant acts of tax delinquency, they may become skeptical that it possesses the ability to attack far more sophisticated forms of tax avoidance and evasion. By generating media attention due to their salience and, in some cases, exposing specific tax offenders who have been detected and punished, collateral tax sanctions may preserve or enhance reciprocator taxpayers’ beliefs that the government is capable of controlling the growth of tax noncompliance.

3. Signaling

Certain collateral tax sanctions may also influence the behavior of individuals who fear the negative signals that the sanctions may convey to others. In order to avoid the collateral tax sanctions and their accompanying signals, some individuals may feel compelled to report and pay their tax liabilities properly.

Signals are costly actions that individuals undertake in order to provide information to other individuals.\textsuperscript{216} When a professor wears a suit and tie to class, he may do so, in part, to signal to his students that he possesses knowledge, professionalism, discipline or other characteristics. This signal provides two types of information: direct information (he is wearing a suit


\textsuperscript{216} \textit{See} Posner, \textit{supra} note 33 at 1787.
and tie) and indirect information (he is professional). According to the signaling model, individuals engage in cooperative relationships with other individuals, which take the form of a repeated prisoner’s dilemma.217 Because people want to engage in as many of these cooperative relationships as possible, they must find ways to signal to others they are “good types” who will not try to take advantage of them.218

In the tax context, proponents of the signaling theory, most notably Eric Posner, have argued that tax compliance serves as a signal that an individual is a good type who can be trusted.219 Conversely, tax noncompliance may act as a signal that an individual will cheat others just as he cheated the government.220 According to this theory, a possible explanation for high rates of voluntary compliance in a self-assessment tax system is that most individuals do not want to signal to others that they are bad types.221

The signaling model as an explanation for why people pay taxes has been subject to harsh criticism by both social norms and tax law scholars.222 Their primary objection is that unlike other types of signals, such as wearing suits and ties, acts of tax compliance and tax non-compliance usually cannot be observed by other individuals.223 Again, tax return information is protected by taxpayer privacy rules that prevent individuals from seeing others’ tax returns, including whether they were audited by the taxing authority or required to pay monetary tax penalties.224 Few individuals reveal their tax returns information voluntarily to others.225 In defending his theory of signaling in general, even Eric Posner himself appears to have ultimately agreed that his theory may have limited application to tax compliance.226

In contrast to traditional monetary tax penalties, which taxpayers pay

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217 Id. at 1786-1788.
218 Id. at 1786-1790.
219 Id.
220 Id.
221 Id. at 1818-1819.
223 See Kahan, supra note 222 at 378.
224 I.R.C. § 6103 (a).
225 See Kahan, supra note 222 at 379 (“There is in fact no such norm of spontaneous tax disclosure in our society”).
during settlement with the taxing authority behind the curtain of taxpayer privacy, certain collateral tax sanctions may indeed produce observable negative signals. As I describe below, these signals may result in significant adverse professional and personal consequences, which may effectively deter acts of tax noncompliance.

**Professional Signals.** Individuals who hold positions of trust, such as lawyers and physicians, may not only fear the potential suspensions of their licenses that may result from failing to comply with tax law, but may also fear reputational damage of the suspensions. For example, if a physician’s medical license is temporarily suspended for failing to file tax returns for several years, a potential patient may learn of the suspension and the underlying offense and may feel that he will not be able to trust the physician to reach accurate and timely medical treatment decisions. Not only will the physician owe tax penalties and interest on her delinquent tax liability and will suffer financial losses during the period when she cannot practice medicine, but future patients may learn of her medical license suspension. If the physician were subject solely to monetary tax penalties, however, it is unlikely that the potential patient would ever learn about the tax offenses as a result of tax privacy protections. Especially in the online era, once the physician’s license is suspended, potential patients can easily learn this information through their own research.

In addition, collateral tax sanctions may lead some potential clients and business associates to assume incorrectly that the individual subject to the sanctions committed an act even more harmful than tax noncompliance. For example, if a lawyer receives a collateral tax sanction for failing to file tax returns and loses his law license, a potential client may learn of this suspension but not its cause. The client may assume that it was due to any number of offenses beyond tax noncompliance, such as commingling a client’s funds with the lawyer’s own personal account or even engaging in the use of illegal narcotics. Similarly, a notice of suspension of liquor license sign in the window of the restaurant whose owners have failed to pay state taxes may cause potential customers to wonder whether the restaurant had engaged in any number of offenses, ranging from the serving of minors to the sale of altered alcohol. The far-reaching and uncertain

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227 See supra note 117 and accompanying text.

228 See, e.g., [www.healthgrades.com](http://www.healthgrades.com) (physician research website).

229 For example, a lawyer can be disbarred for commingling accounts. See, e.g., North Carolina State Bar, Disciplinary Actions from the Most Recent Journal, available at [http://www.ncbar.com/discipline/](http://www.ncbar.com/discipline/).

nature of the negative signals of collateral tax sanctions, thus, may further deter some individuals from failing to report and pay their taxes properly.

**Personal Signals.** Certain collateral tax sanctions may also cause individuals to reveal tax noncompliance to their personal associates. While an individual may not normally disclose to his friends that he has paid monetary tax penalties, if an individual’s tax delinquency causes him to lose the use of his driver’s license for a period of time, he may be forced to reveal his failure to pay his taxes to others. As a result of the driver’s license suspension, for instance, an individual may need to ask for assistance from friends and family members in order to travel to work, complete household errands and transport his children to and from after-school activities. This individual may feel compelled to admit his tax noncompliance to his friends and family members because he may not want his personal associates to assume that he committed a more dangerous act, such as driving while intoxicated. Even with this explanation, friends and personal associates of the individual may view him as someone who fails to follow rules or authority. As long as an individual fears adverse reactions from personal associates, or at least is embarrassed that he will have to reveal his tax noncompliance to them, the potential negative signals of certain collateral tax sanctions may, in the individual’s mind, overshadow the benefits of tax noncompliance.

4. **Duty of Citizenship**

A final oft-discussed motivation of individual tax compliance is that some individuals feel that paying taxes is an important duty of citizenship. As Justice Oliver Wendell Holmes, Jr. famously proclaimed, “I like paying taxes. With them I buy civilization.” In addition to the effects discussed above, the growing use of collateral tax sanctions may have positive impacts on tax compliance by individuals who feel a similar patriotic obligation to pay their taxes.

Scholars have long argued that the government may preserve, and

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231 See supra notes 172-173 and accompanying text.


233 Felix Frankfurter, Mr. Justice Holmes and the Supreme Court 42-43 (1938) (quoting Oliver Wendell Holmes, Jr.).
perhaps even improve, tax compliance among patriotic taxpayers by convincing them that their tax dollars provide valuable government benefits and services. As economist Richard Bird has phrased this objective, an “essential institutional feature” of tax administration is the government’s demonstration of clear “expenditure-revenue links” between tax payments and the services and benefits they fund.\(^{234}\) Numerous studies have confirmed that as the perception that among taxpayers that the government is using their tax dollars to provide public goods increases, the willingness of taxpayers to cooperate with the state and pay their taxes out of a duty of citizenship, often described as “tax morale,” rises as well.\(^{235}\)

The challenge, of course, is that the link between tax revenues and government expenditures is not always apparent to taxpayers. As a result, several scholars have offered proposals that would increase positive publicity of the government benefits and services that tax dollars provide. For example, Yair Listokin and David Schizer have argued that the government should “trumpet” its accomplishments using taxpayer dollars in “signs about ‘your tax dollars at work,’” in press releases from politicians about benefits secured for constituents, and the like,” just as charitable organizations rely heavily on the use of print and electronic media to inform their donors and potential donors of the specific initiatives that their contributions support.\(^{236}\) Similarly, Joshua Rosenberg has argued that the government should produce advertisements featuring projects and services such as “brief shots of hospitals, schools, roads, jetfighters, people eating wholesome food, taking safe drugs, etc.” to enhance positive associations toward tax payments.\(^{237}\) Outside the United States, several national governments have deployed television and radio advertisements similar to these proposals.\(^{238}\)


\(^{238}\) The Canada Revenue Agency has used television advertising as a way to discourage people from paying contractors under the table. See, e.g., http://www.cra-arc.gc.ca/ndgrnd/wtchvd-eng.html. South Africa has also tried to use television
Collateral tax sanctions offer another approach for enhancing tax morale. By rescinding benefits and services from individuals who have failed to pay their outstanding tax liabilities, the government may maintain and strengthen a public perception that tax dollars indeed fund critical benefits and services. As a result of the high salience of collateral tax sanctions and their likely implication of the loss aversion bias, individuals may pay greater attention to the possibility of losing these benefits than to the government’s positive publicity regarding benefits and services that they already enjoy and are not in immediate danger of losing.

Collateral tax sanctions establish explicit links between tax payments and concrete government benefits and services, and may do so even more effectively than positive publicity campaigns. Even if the federal government publicizes its improvements to the interstate highway system or its assistance to home mortgage borrowers, for example, some individuals may be skeptical that their tax dollars actually contributed to these efforts. By revoking an individual’s driver’s or recreational hunting license, on the other hand, a state government may cause its residents to perceive taxes as payments that fund structurally sound roads and safe and maintained hunting grounds. Likewise, if the federal government enacts legislation that would revoke passports from tax delinquents, it may remind individuals that their tax dollars pay for protections that the U.S. government and its embassies provide when Americans travel abroad. Collateral tax sanctions, thus, essentially encourage individuals to view their taxes as “user fees” that they pay for commonly used benefits and services.

Another advantage of collateral tax sanctions is that they may enhance expenditure-revenue links in the minds of individual taxpayers without provoking contradictory messages that often surround positive publicity campaigns. As advocates of the positive publicity approach, such as Listokin and Schizer, acknowledge, when the government publicizes its programs, political opponents of the incumbent party may criticize the effort as an act of credit claiming. For example, when the U.S. Department of Labor advertised its new “green jobs” training programs in 2009, opponents of the Obama Administration publicly dismissed the publicity effort as a political use of taxpayer dollars that did not “pass the basic sniff test.”

239 Collateral tax sanctions, thus, essentially encourage individuals to view their taxes as “user fees” that they pay for commonly used benefits and services.

240 See Listokin & Schizer, supra note 236 at 15.

value of the new program for many taxpayers. Collateral tax sanctions do not create similar opportunities for politicians to accuse each other of attempting to publicize specific government benefits or programs. Instead of requiring government officials to “trumpet”\(^\text{242}\) specific government benefits and services, collateral tax sanctions simply take these benefits and services away from individuals who do not pay for them.

A significant benefit of collateral tax sanctions is that they may serve as an accessible reminder of the connection between tax payments and valuable government benefits and services. For taxpayers who are motivated by the belief that their taxes are payments for “civilization,”\(^\text{243}\) collateral tax sanctions may preserve, and even improve, their continued willingness to comply with the tax law.

C. Drawbacks

Collateral tax sanctions may encourage the proper reporting and payment of tax liability by individuals who are influenced by different, often overlapping, motivations of compliance, yet they also present several potential drawbacks. These are discussed below.

1. Spillover Effects

A significant drawback of certain collateral tax sanctions is that by revoking government privileges and benefits, they may impose external costs, or spillover effects, on parties other than noncompliant taxpayers.\(^\text{244}\)

Consider a few illustrations of the people and activities that are affected by several of the collateral tax sanctions described above. When an individual forfeits her driver’s license as a result of failing to pay her established tax liability, she loses the ability to drive herself to professional and personal activities. But, the driver’s license revocation may also adversely affect this individual’s children and other family members who rely on the individual for transportation. Further, depending on the individual’s occupation, her employer may incur costs, such as hiring a more expensive temporary employee. Monetary tax penalties, on the other hand, are borne more directly by the individual who committed the initial tax offense because they do not affect government benefits upon which

\(^{242}\) Listokin & Schizer, supra note 236 at 15.
\(^{243}\) Frankfurter, supra note 233 at 42.
\(^{244}\) For general discussion of negative externalities, see Daniel B. Kelly, Strategic Spillovers, 111 COLUM. L. REV. 1641, 1642-44 (2011).
individuals other than the noncompliant taxpayer rely.

The potential spillover effects of collateral tax sanctions increase as the scope and application of these sanctions grows. If collateral tax sanctions such as revocation of professional licenses, for instance, apply to common tax reporting errors or mistakes, they may result in substantial social costs. In light of the spillover effects, governments should be cautious when considering applying collateral tax sanctions to tax offenses that may be committed by many individuals.

2. Brute Deterrence

Another possible harmful effect of collateral tax sanctions is that taxpayers may view some of these measures as illegitimate acts of brute deterrence by the government. This reaction may especially occur in instances in which individuals do not feel that the government enforces collateral tax sanctions with the same due process that it metes out when applying other penalties. A consequence of this perception is that some individuals may reduce, rather than increase, their tax compliance.

If people do not consider the law or legal institutions to be legitimate, they may choose not to obey the law. Based on findings in several social psychology studies, Tom Tyler has argued that individuals comply with the law because they feel that “legal authorities are legitimate and their actions are generally fair.” For example, one study of individuals’ reactions to the behavior of the police found that if individuals perceive that the police are applying the law fairly, they will yield to the authority of the police and will cooperate with the police when necessary. Another study found that a belief by individuals that the government acts in a procedurally fair manner corresponds with a sizeable increase in individuals’ likelihood to cooperate with various agencies of the government, including the taxing authority. While few studies of this theory have been conducted

245 Steven M. Sheffrin & Robert K. Triest, Can Brute Deterrence Backfire?, in Why People Pay Taxes 211-14 (Joel Slemrod ed., 1992) (taxpayers who read reports regarding the “tax gap” were less likely to comply).


specifically in the tax context. If individuals feel that the government’s tax enforcement efforts are not fair, they may react in a manner that is consistent with these studies.

Certain collateral tax sanctions may appear to be illegitimate to some individuals. A perception of illegitimacy may develop if individuals believe that a particular collateral tax sanction is directly at odds with a related tax administration objective of the government. For example, individuals who have failed to pay their taxes may object to a rule that forces them to forfeit their driver’s license because they may argue that the effect of this policy will be to deprive them of the ability to earn income necessary to repay the tax liability. Individuals may also view a collateral tax sanction as illegitimate if it imposes an excessive personal hardship, including its spillover effects. Finally, some individuals may feel that certain collateral tax sanctions are illegitimate if they apply without due process of law.

How might individuals who harbor such feelings of illegitimacy respond to collateral tax sanctions? One possibility is that, consistent with Tyler’s legitimacy research, some individuals may respond to hefty collateral tax sanctions by making greater efforts to escape detection by the taxing authorities rather than by cooperating at all. For example, if taxpayers view the threat of collateral tax sanctions that revoke professional licenses that enable individuals to earn income, such as liquor or professional licenses, as unfair, it is possible that some may respond by shifting business operations in the black market, where the government lacks the ability to monitor whether they even owe tax liability, let alone have paid it in a timely manner.

3. Tax Privacy

Collateral tax sanctions also raise tax privacy concerns that traditional monetary tax penalties do not. A potential drawback of collateral tax sanctions is that they may cause individuals to fear that government agencies and officials other than the taxing authority will gain access to


250 See Bill Analysis, Assembly Bill 1424, California, The Delinquent Taxpayer Accountability Act (May 2, 2011) (stating that revocation of driver’s license will reduce individual’s ability to earn income).

251 See Tyler, supra note 246.
their personal tax return information.\textsuperscript{252} Even though taxing authorities regularly share tax return information with other government agencies as a result of a large number of statutory exceptions to taxpayer confidentiality,\textsuperscript{253} providing other agencies with access to individuals’ tax return information could result in abuses.\textsuperscript{254} These abuses could potentially involve the inappropriate use of personal tax return information by officials other than taxing authority employees or the improper revocation of government benefits and services by non-tax agencies that attempt to apply collateral tax sanctions.\textsuperscript{255}

Whether or not the perception is accurate, if individuals believe that collateral tax sanctions reduce their tax privacy protections, they may respond in ways that negatively affect the taxing authority’s ability to administer and enforce the tax law. If individuals perceive that collateral tax sanctions will allow non-tax government agencies to gain access to their tax returns, they may limit the information that they reveal to the taxing authority.\textsuperscript{256} Further, individuals may feel that the sharing of tax return information with other agencies is illegitimate or unfair, especially if the other agency applies harsh collateral tax sanctions in an inconsistent and unpredictable manner, and they may reduce their own individual tax compliance in response.\textsuperscript{257}

Although these reactions may occur if individuals believe that collateral tax sanctions enable non-tax agencies to gain broad access to their individual tax returns, it is unlikely that they are justified in the case of many existing collateral tax sanctions, such as those aimed at tax delinquency. In these cases, non-tax agencies receive narrowly tailored,

\textsuperscript{252} Commentators have long argued that taxpayers will not cooperate with the taxing authority unless, as former Treasury Secretary Andrew Mellon famously stated, they trust that their personal tax information “stops with the government.” \textsc{1 Office of Tax Policy, Dep’t of the Treasury, Report to the Congress on Scope and Use of Taxpayer Confidentiality and Disclosure Provisions} 19 (2000) (attributing the quote to Andrew Mellon). \textit{See also} Blank, \textsc{supra} note 28 at 280-282.

\textsuperscript{253} I.R.C. § 6103(c)-(o).

\textsuperscript{254} \textit{See}, e.g., Bill Analysis, Assembly Bill 1424, California, \textsc{The Delinquent Taxpayer Accountability Act} (May 2, 2011) (describing abuse concerns regarding driver’s license revocation); Jacoba Urist, \textit{No Taxes, No Travel: Why the IRS Wants the Right to Seize Your Passport}, TheAtlantic.com, Apr. 17, 2012 (quoting Daniel Shaviro as stating that passport revocation from tax delinquents could “be misused, say, to harass specific individuals whom government officials dislike”). \textit{See id.}

\textsuperscript{255} \textit{See id.}

\textsuperscript{256} The IRS itself has articulated this view. \textsc{Irs, Dep’t of the Treasury, Pub. No. 4638, Disclosure & Privacy Law Reference Guide}, 1-7 (“By the single act of filing a tax return, a record is created and also a trust.”) \textit{See} Blank, \textsc{supra} note 28 at 280-282, for further discussion.

\textsuperscript{257} \textit{See} Tyler, \textsc{supra} note 246; \textit{see also} Levi, Sacks & Tyler, \textsc{supra} note 248 at 359.
limited personal tax information of individuals directly from the taxing authority, such as a list of individuals who owe outstanding tax liabilities exceeding a certain threshold. Nonetheless, because individuals place significant trust in the government when they submit detailed personal information on their tax returns, government officials should not ignore the potential tax privacy concerns that certain types of collateral tax sanctions may raise.

4. Observability

Last, the observability of some collateral tax sanctions is a feature that may cause them to strengthen tax compliance among certain individuals. However, if these sanctions are applied too broadly, observability could instead reduce tax compliance. If the government applies collateral tax sanctions that result in observable effects, such as individuals’ loss of professional licenses, to common tax offenses or to tax offenses that meet a low dollar threshold, many individuals may incur these sanctions. For individuals who are motivated by feelings of reciprocity, the frequent imposition of observable collateral tax sanctions may lead them to perceive that many individuals have engaged in tax noncompliance. A possible reaction from these reciprocator taxpayers may be to reduce their own compliance. Additionally, if the government applies collateral tax sanctions too frequently, the negative signal of tax noncompliance may become muted. If most individuals lose their professional licenses temporarily as a result of a common tax offense, individuals’ fear of emitting this particular signal may decrease. Government officials, consequently, should consider the potential adverse effects of observability, along with each of the other drawbacks discussed above, when deciding whether to deploy collateral tax sanctions as a means of enforcement.

IV. WHEN SHOULD COLLATERAL TAX SANCTIONS APPLY?

When should governments apply collateral tax sanctions? While the previous discussion illustrated that collateral tax sanctions may encourage tax compliance more effectively than the threat of additional monetary tax penalties, it also demonstrated that collateral tax sanctions present several

258 For example, in California, the Department of Motor Vehicles revokes driver’s licenses of individuals who appear on lists that it receives directly from the taxing authority. Cal. Veh. Code § 35623.1. See supra note 108 and accompanying text.
259 See supra notes 195-199 and accompanying text.
260 See Posner, supra note 33, at 1790 (“Stigma arises only when a behavior or its detection is rare”).
significant drawbacks.\textsuperscript{261} If governments do not address these drawbacks, their use of collateral tax sanctions may be detrimental to their tax enforcement efforts.

In light of the foregoing analysis of the competing benefits and detriments, governments are in need of guidance regarding how they should apply collateral tax sanctions to maximize their positive impact on compliance. This Part proposes guiding principles for the design and implementation of collateral tax sanctions, applies these principles to specific examples, and, finally, outlines publicity strategies for taxing authorities.

A. \textit{Proposed Principles}

Below are three guiding principles that I propose governments should consider when crafting collateral tax sanctions.

1. \textit{Tax Offense Is Violation of Tax Rule, Not Tax Standard}

Collateral tax sanctions should apply when the underlying tax offense represents a violation of a tax rule, not a tax standard. A tax rule is clear, specific guidance that dictates \textit{ex ante} whether a taxpayer is required to engage, or prohibited from engaging, in a particular action.\textsuperscript{262} For example, the requirement that individual taxpayers file their annual personal income tax returns on April 15\textsuperscript{th} is a tax rule.\textsuperscript{263} A tax standard, by contrast, consists of general guidelines or factors regarding particular conduct.\textsuperscript{264} The only way to determine with absolute certainty whether a taxpayer has violated a tax standard is by receiving an \textit{ex post} judgment from an adjudicator such as a court.\textsuperscript{265} For instance, the requirement that a taxpayer’s transaction possess “economic substance”\textsuperscript{266} is a tax standard, because it is not possible to know with absolute certainty whether the

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\textsuperscript{261} See supra notes 244-260 and accompanying text.
\textsuperscript{263} IRC § 6072(a).
\textsuperscript{264} See Kaplow, supra note 262, at 560; Blank, supra note 262, at 543.
\textsuperscript{265} See id.
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transaction satisfies this requirement until a judge reviews it. For several reasons, collateral tax sanctions will promote tax compliance more effectively, and avoid many of the potential drawbacks described above, if they apply to situations where taxpayers violate tax rules rather than tax standards.

First, the taxing authority may best provide advance notice of collateral tax sanctions that result from violations tax rules. Many criminal scholars have criticized the collateral consequences that stem from criminal convictions as unfair because defendants often have no knowledge of these consequences when they agree to enter guilty pleas. But this concern is also relevant to the design of collateral tax sanctions. Without clear advance notice, the threat of collateral tax sanctions is unlikely to serve as an effective deterrent for taxpayers who are influenced by their fear of sanctions. A collateral tax sanction that results from violation of an explicit tax rule, like the requirement that taxpayers pay established tax liability by a specific date, is easier for the government to publicize with clear communication than one that results from a violation of a more ambiguous tax standard, such as a requirement that taxpayers not claim tax positions that reflect “negligence” or a “disregard of rules and regulations.”

Further, a collateral tax sanction may affect fewer taxpayers if it applies to violations of a tax rule rather than violations of a tax standard. Compared to tax rules, tax standards are inherently ambiguous. A state government, for instance, could create a rule that provides that any physician who engages in a transaction that is an abusive tax shelter must forfeit his medical license. The dilemma created by this provision is that taxpayers may not be able to predict with certainty whether a particular transaction indeed lacks economic substance until an audit and possibly a trial occurs. If the loss of a medical license in this example were to apply to situations where taxpayers had engaged in abusive tax shelters, the result could be the appearance of many observable instances of tax noncompliance. And without a definition of “tax shelter,” it is unclear whether collateral tax sanctions would even be capable of reducing their occurrence. Increased observability of tax noncompliance poses risks

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268 See supra note 71 and accompanying text.
269 IRC § 6662(b)(1).
270 See, e.g., Calvin H. Johnson, What’s a Tax Shelter?, 68 TAX NOTES 879, 879 (Aug. 14, 1995) (commenting that there is “no consensus definition of a ‘tax shelter’ in the law”): The Code contains a general definition of tax shelter as a transaction that possesses a “significant purpose of . . . avoidance of Federal income tax.” IRC § 6662(d)(2)(C).
under both the reciprocity and signaling models of tax compliance.\(^{271}\)

A final reason to restrict the use of collateral tax sanctions to violations of tax rules is that individuals may be less willing to enter settlements with the taxing authority in tax controversies if their admission of committing a tax offense will result in the revocation of a significant government benefit or service.\(^{272}\) If a state government, for instance, required individuals who underpaid their taxes negligently to forfeit their driver’s license for a specified period of time, individuals facing this sanction may be unwilling to settle the tax controversy with the taxing authority. As a result of the magnitude of the potential collateral tax sanction, they may desire to argue their cases in front of judges, who would decide whether they violated the negligence tax standard, rather than accept the taxing authority’s charge. If the driver’s license suspension in this example instead resulted from a violation of a clear tax rule, such the requirement to pay established outstanding tax liability on time, the individual may settle the matter and face the collateral tax sanction because he may consider his chances of succeeding in court to be low.

2. Tax Offense Defined by Tax Law and Identified by Taxing Authority

Collateral tax sanctions that result from a tax offense that the tax law defines and that a taxing authority identifies will likely enhance tax compliance objectives more effectively than those that stem from definitions contained in non-tax statutes, which are applied by non-tax agencies. It is possible that non-tax agencies may have authority to revoke government benefits as a result of tax offenses, which are defined in their own governing statutory or administrative law, rather than the tax law.\(^{273}\) These agencies may apply different, possibly broader, definitions of tax offenses than the taxing authority as a result of special qualifications relating to the specific benefits that these agencies provide. Further, it is possible that one might offer proposals that affirmatively allow non-tax agencies to describe and detect abusive tax activities, rather than merely

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\(^{271}\) See supra notes 259-260 and accompanying text.

\(^{272}\) The IRS Appeals Division settles approximately 85% of all tax controversies. See B. John Williams, Jr., Chief Counsel, Internal Revenue Serv., Resolving Tax Shelters: By Settlement or Litigation, Address Before the Chicago Bar Association Federal Taxation Committee (Feb. 25, 2003).

revoke government benefits due to tax non-compliance.\textsuperscript{274} For example, if current tax privacy rules were altered,\textsuperscript{275} Congress could empower the Department of State to issue regulations that could enable it to define tax offenses that result in the suspension of a U.S. passport and to identify instances where these offenses occur. For several reasons, however, such measures may not maximize the compliance benefits of collateral tax sanctions.\textsuperscript{276}

The taxing authority may lack the ability to deter tax noncompliance through advance publicity of collateral tax sanctions that result from law other than the tax law and that are identified by other agencies. Extending the hypothetical from above, if the Department of State were authorized to apply its own definition of tax noncompliance when determining to revoke individuals’ passports, officials in this agency may develop their own internal standards for determining when certain acts of tax noncompliance merit revocation. Without coordination between agencies, IRS officials may not be aware of these standards, at least not in such depth that they would be capable of warning taxpayers \textit{ex ante} of the potential collateral tax sanction of passport removal in response to uncertain tax offenses.

In addition, if a collateral tax sanction results from a non-tax agency’s definition and identification of a tax offense, taxpayers may feel that the non-tax agency lacks the expertise necessary to make this determination. While officials in non-tax agencies are certainly capable of reading the existing tax law when reviewing an individual’s tax returns, they may have little understanding of the case law, administrative rulings or policy rationale that are necessary for an informed application of the tax law to particular facts. If individuals perceive that non-tax agencies receive authority not only to revoke significant government benefits as a result of violations of the tax law, but also to determine whether these violations have in fact occurred, they may consider the collateral tax sanctions to lack legitimacy and may reduce their cooperation with the government.\textsuperscript{277}

Last, if individuals perceive that non-tax agencies have authority to review their private tax return information to determine whether tax offenses have occurred, they may fear that these agencies will use the power to harass particular individuals. As an example of this concern, in

\textsuperscript{274} Such an argument might be made in the interest of efficiency and reduction of bureaucratic waste. See, e.g., Mark Landler, \textit{Obama seeks power to merge agencies for efficiency’s sake}, N.Y. TIMES, Jan. 13, 2012 (quoting President Obama as calling on Congress to grant him authority to merge government agencies, with its approval).

\textsuperscript{275} I.R.C. § 6103. Federal law currently allows for limited sharing of individual tax return information between the IRS and other agencies, including state taxing authorities. I.R.C. § 6103(c)–(o).

\textsuperscript{276} See supra notes 157-243 and accompanying text.

\textsuperscript{277} See supra notes 246-249 and accompanying text.
2012, the New York State Department of Taxation and Finance entered into an agreement with the state’s Office of the Inspector General, a non-tax agency, that would allow dozens of employees of the Inspector General’s office to review the tax returns of state employees and investigate whether violations of the law, including tax offenses, had occurred. Critics characterized this arrangement as “very, very dangerous,” arguing that it could allow officials in the non-tax agency to pursue “witch hunts” against state employees. If the use of collateral tax sanctions results in similar perceptions of the authority of non-tax agencies, individuals may limit the information they share with the taxing authority.

3. Collateral Tax Sanction Is Proportionate to Tax Offense

Finally, when the government applies a collateral tax sanction, the benefit or service that it revokes from an individual should have a proportionate relationship to the magnitude of the tax offense that triggers the sanction. Proportionality is frequently raised as a goal of punishment design for equity or constitutional reasons. One could argue, for instance, that simply as a matter of fundamental fairness, the government should not suspend a benefit as a result of tax noncompliance if this act would be disproportionate to the underlying tax offense. An overarching objective of designing any collateral tax sanction thus could be to ensure that the resulting sanction represent just desert for the offender. Yet in addition to the general normative objective that tax penalties should be fair, governments should also consider the potential relationship of proportionality and compliance. As this final principle illustrates, disproportionate collateral tax sanctions may have detrimental effects on

279 Id.
280 See supra note 252.
281 Criminal law scholars often criticize the collateral consequences of drug convictions, which can cause offenders to forfeit participation in federal educational programs and the opportunity to secure various forms of employment, as unfair because they are disproportionate to the gravity of the drug offense. See, e.g., Pinard & Thompson, supra note 16 at 588 (noting severity of collateral consequences of drug convictions).
individuals’ tax compliance decisions and the government’s ability to administer the tax law efficiently.

Collateral tax sanctions should satisfy a proportionality principle in order to maintain individuals’ willingness to cooperate with the taxing authority. Many people intuitively support the biblical mandate of *lex talionis*, commonly referred to as “eye for eye, tooth for tooth.”²⁸³ Criminal law theorists, such as Paul Robinson and John Darley, have argued that if the government deviates from this principle by applying disproportionate sanctions, it will weaken the law’s “moral credibility,” which in turn may “undercut its ability to help in the creation and internalization of norms and its power to gain compliance by its moral authority.”²⁸⁴ Although this theory of penalty design has been subject to criticism,²⁸⁵ it has also been supported by several empirical studies that report that individuals may reduce their compliance with the law in response to the government’s application of disproportionate sanctions for offenses ranging from tax noncompliance²⁸⁶ to possession and use of marijuana.²⁸⁷ While predictions of taxpayers’ responses to the government’s use of disproportionate collateral tax sanctions may not hold true for all individuals, in light of the existing empirical and theoretical support, governments should consider proportionality when determining which benefits and privileges to revoke.

and for what length of time, in response to specific tax offenses.

If the financial and utility costs of a collateral tax sanction outweigh the harm to the government resulting from the underlying act of tax noncompliance, individuals may again perceive the sanction to be unfair. For example, if the government attempted to revoke the driver’s license of any individual who owed any outstanding tax liability until it is repaid, it is possible that an individual who owes a very small amount, such as an amount less than $100, could suffer the loss of driving privileges for a period of time, until her payment of her small tax liability is processed, which could take a number of days, or a longer period of time if the individual is not able to make the payment immediately. As a result of their increased potential spillover effects, disproportionate collateral tax sanctions may further weaken the moral credibility and legitimacy of the government’s tax enforcement authority.

The difficult question, of course, is when would individuals perceive a collateral tax sanction to be disproportionate to the underlying tax offense? The U.S. Supreme Court has decided several cases that address the constitutionality of disproportionate criminal sanctions and civil forfeitures. In United States v. Bajakajian, an individual attempted to board a plane from Los Angeles to Cyprus, carrying $357,144 in cash, but was stopped by United States customs officials. Bajakajian was charged with failing to declare his removal of more than $10,000 cash from the United States. Even though the maximum criminal fine was $5,000, the government sought to force Bajakajian to forfeit the entire $357,144 because Bajakajian provided misleading answers regarding the reasons for his transport of the cash. The Supreme Court held that this sanction represented a violation of the Excessive Fines Clause of the Eighth Amendment because it was “grossly disproportional” to the gravity of the defendant’s offense.

See supra note 244 and accompanying text.

See, e.g., Scholz & Lubell, supra note 286.


Id. at 325.

Id.

Id. at 326. In response to this decision, Congress amended the forfeiture statute. See 18 U.S.C. 983(g) (introducing proportionality standard).
While our analysis is not focused on the potential constitutionality of collateral tax sanctions, taxpayers may consider some of the same factors as judges when forming a view of whether a particular penalty is disproportionate to the offense. They may weigh the magnitude of the harm caused by the tax offense against the severity of the collateral tax sanction. To conduct this analysis, we can ask several questions. Is the tax offense similar to other offenses that result in the same sanction? What is the harm that results from the tax offense? What is the maximum formal tax sanction, whether civil or criminal, that an individual could face as a result of committing this particular tax offense? While the application of this analysis will not offer precise measurements, these factors provide a roadmap for determining whether individuals would likely perceive a collateral tax sanction to lack proportionality.

B. Beyond Tax Delinquency?

Many of the collateral tax sanctions that apply to tax delinquency satisfy the three principles that I have proposed. As a result, the compliance benefits of these sanctions likely outweigh their potential detriments to individuals’ willingness to obey the tax law and cooperate with the taxing authority.

Consider, for example, California’s policy of suspending driver’s licenses from the top 500 taxpayers who owe income taxes and the top 500 taxpayers who owe sales taxes. As I argued previously, this sanction possesses characteristics that would have a positive impact on individuals affected by different, often overlapping, tax compliance motivations. But would it satisfy the three principles outlined above or result in some of the drawbacks of collateral tax sanctions? First, California revokes driver’s licenses as a result of a violation of an explicit tax rule, the requirement to

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297 See supra note 281. While an examination of the constitutionality of each collateral tax sanction is beyond the scope of this Article, it is possible that some sanctions would likely be deemed to be remedial, even though they also serve a deterrent purpose. Suspension of professional licenses due to tax noncompliance, for example, prevents individuals who lack moral character from engaging in positions of trust. See, e.g., Kvitka v. Board of Registration In Medicine, 551 N.E.2d 915, 918 n.4 (Mass. 1990) (revocation of physician’s professional license for unlawfully dispensing controlled substances considered remedial rather than punitive). See also State v. Young, 530 N.W.2d 269, 278 (Neb. App. 1995) (holding purpose of driver’s license revocation is to protect public).

298 See supra notes 262-297 and accompanying text.

299 Cal. Veh. Code § 35623.1 (“Suspension of Motor Carrier Permit: Franchise Tax Board or Board of Equalization Deficiencies”).

300 See supra note 171 and accompanying text.
pay established tax liability by a specified date. Second, this offense results from a violation of California’s tax laws and the California taxing authority provides a list of the names of the top tax delinquents to the department of motor vehicles. Third, it is unlikely that taxpayers consider this sanction to be disproportionate to the underlying tax offense. The individuals who are subject to this collateral tax sanction are not significantly different from other individuals who lose their driving privileges for other reasons, such as failing to attend driver’s education program or simply renewing their outstanding license. The harm to the state imposed by the particular individuals on this list (the worst offenders) may consist of millions of dollars of unpaid tax liability and, until each offender pays the outstanding tax liability or enters into an installment payment plan, the harm is ongoing. Finally, the sanction is not excessively severe compared to other sanctions that could apply to this offense, such as levies on property. This sanction will likely produce its intended compliance benefits without generating significant adverse effects.

Could governments apply collateral tax sanctions to address offenses other than tax delinquency? To consider this question, this Subpart applies the three guiding principles described above to several hypothetical collateral tax sanctions. The objective of this Subpart is not to provide an exhaustive list of new collateral tax sanctions. Rather, it is to illustrate how policymakers should apply the principles that I have proposed above when deciding whether to adopt a particular sanction.

1. Non-Filing and Professional Licenses

The failure to file tax returns, as opposed to the failure to pay outstanding taxes, causes taxing authorities to face significant difficulty in calculating and collecting taxes. In California, for example, in 2009, over 900,000 residents who were required to file state tax returns ignored their obligation, resulting in an estimated $650 million of unpaid tax liability, or 10% of California’s state tax gap. At the federal level, at least $28 billion

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301 See supra note 299.
302 Id.
304 See Miranda, supra note 108 (describing multi-millionaire tax delinquents).
305 See California State Board of Equalization, Tax Collection Procedures, October 2009 (describing levy process).
of tax revenue is not collected each year due to non-filing.\textsuperscript{307} While many states have enacted collateral tax sanctions that revoke benefits and services from individuals who have failed to pay established tax liability, they have not developed similar sanctions that specifically apply to individuals who have failed to file tax returns.

To address the problem of tax return non-filing, a state government could suspend or deny any professional license issued by a state agency in that state if the individual who holds or seeks the license has failed to file personal state tax returns for the past two consecutive years, where the individual had a legal obligation to do so, until the individual files the outstanding tax returns. This sanction would apply in addition to any monetary tax penalties and interest due to the taxing authority as a result of the failure to file. This proposal expands the scope of existing collateral tax sanctions by targeting non-filing of tax returns, rather than just non-payment of taxes, and could apply to many professionals other than lawyers and physicians, such as pharmacists, electricians, psychologists, and building contractors, just to name a few.\textsuperscript{308}

Considering the motivations of compliance that affect many individuals, this proposal could reduce instances of non-filing among individuals who hold professional licenses. The threat of revocation of a professional license, which could result in significant loss of future income, should serve as an effective deterrent against the failure to file. This sanction should also have a positive influence on individuals who work in professions where the negative signal of tax noncompliance could cause them to lose the trust of their patients, customers or clients.\textsuperscript{309} The sanction would encourage these individuals to file their tax returns, so that they would not have to explain the reasons for their temporary license suspension. And for aspiring professionals who do not yet hold a license, this policy could instill in them an understanding of their legal obligation to comply.

In addition to its potential compliance benefits, this policy likely avoids potential drawbacks of collateral tax sanctions because it satisfies each of the three proposed principles.

\textit{Tax Rule.} The requirement to file a tax return is an explicit tax rule, not a tax standard. As long as a taxpayer meets the threshold income requirement, there is no ambiguity regarding whether the taxpayer must take a specific action. In almost all cases, the taxpayer can make a determination \textit{ex ante} that he is required to file a return and does not need to

\textsuperscript{308} See, e.g., Washington State Dep’t of Licensing, Types of Licenses, \textit{available at} http://www.dol.wa.gov/business/professionals.html.
\textsuperscript{309} See \textit{supra} notes 217-230 and accompanying text.
receive a formal judicial opinion or administrative ruling. The taxing authority and license-granting agencies can clearly communicate the policy that individuals who fail to meet the explicit tax rule that requires them to file tax returns will forfeit their ability to practice their profession legally.

**Tax Law and Taxing Authority.** The revocation of a professional license under this policy occurs as a result of a violation of a tax rule contained in the tax law, the requirement to file returns. To ensure that the taxing authority makes the determination that an individual has failed to file tax returns for two years, the taxing authority could provide a list to each license-granting agency in the state a list of all taxpayers who have, according to the taxing authority’s records, failed to file tax returns for two years. This arrangement would avoid creating the perception that license-granting agencies are launching their own investigations of individuals’ tax returns. It is also consistent with the approach that many states currently use when empowering non-tax agencies to revoke licenses from individuals who have failed to pay outstanding taxes in excess of threshold amounts.

**Proportionality.** Individuals would likely consider the revocation and denial of professional licenses as a proportionate sanction for the offense of failing to file tax returns for two years. The tax offense of failing to file a tax return is certainly comparable, if not significantly greater than, other offenses that may also result in revocation of a professional license. Under this proposal, for example, lawyers who fail to file tax returns for two years would forfeit their law license until they file their outstanding tax returns, just as lawyers who fail to pay established outstanding tax liability may also lose the same privilege. The potential harm to the government from an individual’s failure to file a tax return could be significant, as the government may expend resources to attempt to determine the individual’s income or, alternatively, may have little ability to detect the individual’s failure to pay taxes on significant amounts of income. Individuals may not consider the sanction to be excessively severe, given that if the criminal tax law were applied, individuals who deliberately fail to file tax returns could be subject to far greater tax penalties, including prison sentences.

An objection to this proposal may be that it may result in the suspension of professional licenses from individuals who fail to file tax returns even though they are not legally required to file them because they have low or no taxable income. This objection, however, should not

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310 See Kaplow, supra note 262, at 560.
311 See, e.g., California Franchise Tax Board, Do I need to file?, available at https://www.ftb.ca.gov/individuals/fileRtn/index.shtml.
312 See, e.g., supra note 108.
313 See supra notes 118-121 and accompanying text.
dissuade state governments from adopting the license revocation proposal. States can develop procedures for license-granting agencies to provide advance notice to individuals before revoking their professional licenses for failing to file tax returns, which would allow individuals an opportunity to rebut the assertion that they failed to meet their tax return filing obligations. Several of the existing collateral tax sanctions that apply to individuals who have failed to pay outstanding tax liability contain such notice and appeal provisions.  

2. Household Employment Taxes and FDIC Insurance

Most individuals who pay household employees do not comply with the household employment tax rules. Under federal law, individuals who pay at least $1,800 per year to a household employee, such as nanny, health aide or housekeeper, are required to withhold Social Security and Medicare taxes from the employee’s wages and to pay an employer’s share of these taxes, plus federal unemployment insurance taxes as well. The household employer is required to complete a form with her annual personal tax return, and remit these taxes to the IRS, along with additional information regarding the wages paid to the employee. Compliance with these rules is notoriously low. According to one recent study, the household employment tax noncompliance rate may be as high as 70%, resulting in a tax revenue loss of at least $15 billion annually.

One possible approach to this problem is that the federal government could enact legislation that provides that if the IRS determines that an individual has paid a household employee at least $30,000 in wages during the year and has not paid all required household employment taxes, the individual will forfeit Federal Deposit Insurance Corporation (FDIC) coverage on all personal bank accounts until the end of the calendar year following the year of detection by the IRS, in addition to paying civil tax

315 See, e.g., Cal. Veh. Code § 35623.1 (“Suspension of Motor Carrier Permit: Franchise Tax Board or Board of Equalization Deficiencies”).
316 I.R.C. § 3101. Employers are required to withhold 4.2% from the employee’s wages for Social Security and 1.45% for Medicare. In addition, the employer is required to pay 6.2% of the paid wages for Social Security and 1.45% for Medicare.
317 I.R.C. § 3301 (.8% rate on the first $7,000 of employee’s wages).
318 Int. Rev. Serv., Schedule H.
320 See CATHERINE B. HASKINS, HOUSEHOLD EMPLOYER PAYROLL TAX EVASION: AN EXPLORATION BASED ON IRS DATA AND ON INTERVIEWS WITH EMPLOYERS AND DOMESTIC WORKERS (2010).
penalties on the underpayment of the taxes. The FDIC provides free insurance to individuals of up to $250,000 for deposits in a qualifying bank, which may be expanded significantly if the individual is married or other conditions are present. This proposal could be modified to increase the threshold amount of wages or the length of the suspension depending upon the number of years of noncompliance.

The theory behind this particular collateral tax sanction is that it may raise awareness of household employment tax obligations and induce cooperation in an area where noncompliance is high. FDIC coverage is a salient government benefit for individuals who hold liquid savings in bank accounts, especially in times of uncertainty regarding the financial viability of banking institutions. Many of the individuals who would be subject to this proposal, which again keys off payment of at least $30,000 in wages per year, likely hold funds in bank accounts in addition to their other investments. For some of these individuals, the thought of forfeiting FDIC coverage, even for one year, may provide significant motivation to comply with the household employment tax rules. Under the example above, if an individual loses FDIC coverage and one of the banks holding his personal funds were to fail by the end of 2013, the individual would receive no protection from the federal government.

The next inquiry is whether, despite the theoretical compliance benefits, this proposal would implicate some of the potential negative effects of collateral tax sanctions. As the analysis below demonstrates, the FDIC collateral tax sanctions may satisfy only some of the proposed guiding principles.

**Tax Rule.** At first blush, the failure to pay household employment taxes is a violation of an explicit tax rule. The Internal Revenue Code clearly states that individuals who pay wages to household employees in excess of a specified amount, $1,800, must pay the required taxes. Upon closer inspection, however, an individual may not know with certainty whether the IRS would characterize a particular service provider, such as a gardener or driver, as an “employee” for tax purposes until the IRS, or possibly a court, reviews the relevant facts.

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323 See supra notes 178-194 and accompanying text.

324 I.R.C. § 3102(a); IRS Notice 2011-102, 2011-52 IRB 932 (setting forth threshold wage amounts).

325 See, e.g., I.R.C. § 3121(b); Int. Rev. Serv., Independent Contractor (Self-Employed) or Employee?.

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them. Whether the requisite “control” element is present, however, is not necessarily apparent \textit{ex ante}. A possible consequence of imposing such a salient collateral tax sanction is that when individuals face household employment challenges from the IRS, they may be less willing to settle the controversy and pay the resulting monetary tax penalties than if the collateral tax sanction were not in effect.

\textit{Tax Law and Tax Agency.} The proposed FDIC collateral tax sanction would result from the application of federal tax law and a determination by the IRS. If the proposed sanction were adopted, federal tax privacy rules would need to be amended to allow the IRS to provide to the FDIC the list of individuals who have paid a tax penalty for failing to report household employment taxes and the length of their insurance coverage suspension periods. As the IRS would be permitted by statute to share only this discrete information with the FDIC, individuals’ concerns that the introduction of this collateral tax sanction could lead to abuse of discretion by a non-tax agency should be allayed.

\textit{Proportionality.} Individuals would likely view the proposed FDIC collateral tax sanction as proportionate for several reasons. First, as this sanction would be the only instance in which individuals would forfeit FDIC insurance, a fact which should make the sanction all the more salient, individuals would not compare the offense of home employment tax nonpayment to other offenses that result in the same sanction. Second, the government could argue that the nonpayment of this tax results in significant harm. When household employers disregard these rules, not only do they contribute to federal tax gap, but they also prevent the IRS from detecting and taxing household employees. In addition, the widespread nature of the problem drives up the price that a compliant individual must pay to a household employee if she is one of the few taxpayers who withhold and remit the required taxes. Last, assuming that the IRS publicizes the collateral tax sanction effectively, individuals may not view it as excessively severe. This sanction is certainly not greater in value than the potential criminal tax sanctions that could apply in the case of intentional nonpayment of the taxes.

This proposal provides an example of collateral tax sanction that may represent a violation of a tax standard rather than a tax rule, but satisfies the other two principles. How should governments decide whether to pursue such collateral tax sanctions as means of tax enforcement? To answer this

\begin{enumerate}
\item See supra note 272 and accompanying text.
\item See, e.g., Int. Rev. Serv., Examples of Employment Tax Fraud Investigations - Fiscal Year 2012 (describing federal employment tax evasion criminal cases).
\end{enumerate}
question, we can consider specific elements of the proposed sanction that relate to the justifications for the tax rule principle. If the FDIC collateral tax sanction implicates a tax standard, rather than a tax rule, because the definition of “employee” is not clear, it is possible that some individuals may not settle disputes involving this issue with the IRS. However, this concern is likely alleviated by the fact that some individuals who would be subject to this sanction might be unwilling to reveal publicly that they have failed to report wages and pay required taxes for their household employees. As many presidential nominees have demonstrated, others may perceive the failure to pay household employment taxes to be a negative signal of lack of integrity or competence, or both. These individuals, consequently, may still choose to settle the dispute and forfeit their FDIC coverage privately rather than reveal the in litigation publicly.

3. “Fraud and Deceit” Tax Offenses and Deportation

Would the federal government increase tax compliance by deporting lawful permanent residents who willfully mislead a taxing authority? As has been discussed, in Kawashima v. Holder, the U.S. Supreme Court upheld the deportation of two lawful permanent residents who had previously pled guilty to willfully filing false tax returns. While the Immigration and Nationality Act specifically designates an offense under Section 7201 of the Internal Revenue Code, tax evasion, as an “aggravated felony” which can result in automatic deportation, Akio and Fusako Kawashima argued that this provision did not apply to them because they pled guilty to a lesser offense. The Court rejected this argument by finding that the Act’s reference in a separate provision to an offense that constitutes “fraud or deceit” and results in a loss of more than $10,000 to the victim implicitly includes tax offenses. Specifically, the Court held that for purposes of federal immigration law, the words “fraud and deceit” encompass tax offenses that involve willfulness and false statements, even

331 See supra notes 227-230 and accompanying text.
333 Id.
335 Brief for the Petitioners, 5, Kawashima v. Holder, 565 U.S. ___ (2012), appealing 615 F.3d 1043 (9th Cir. 2010).
though the federal tax law may not specify that fraud is an element of these offenses.\footnote{337}

The federal government could attempt to incorporate the \textit{Kawashima} holding into its existing deportation policies. A potential collateral tax sanction could be an affirmative policy by the U.S. Immigration and Customs Enforcement to treat as an aggravated felony any criminal conviction of a lawful permanent resident for any tax offense that involves willfulness and false statements and tax liability of more than $10,000. These tax offenses may involve the willful delivery of false information to the taxing authority, as was the case in \textit{Kawashima}, but they may also include other tax offenses at the federal, state and local levels. Last, the immigration authorities could apply this sanction to any past criminal convictions as well, as current law does not include a statute of limitations on the identification of aggravated felonies.\footnote{338}

Proponents of this policy might argue that it would not only help ensure that only citizens with good moral character retain lawful permanent resident status,\footnote{339} but that it would also increase tax compliance. For a lawful permanent resident, there is no government benefit more salient than a green card.\footnote{340} This benefit enables individuals to live in the United States, attain employment and, possibly, receive naturalized citizenship.\footnote{341} A primary objective of the active application of \textit{Kawashima}, supporters would likely argue, is to encourage individuals who are motivated by the fear of sanctions to report and pay their tax liability properly. In theory, if federal immigration authorities threaten to strip this treasured benefit from lawful permanent residents who engage, or have engaged, in criminal tax offenses involving willfulness and false statements, some lawful permanent residents may respond by refraining from engaging in any acts of tax noncompliance.

While this collateral tax sanction may cause some lawful permanent residents to respond positively, it may also result in adverse effects which could, in turn, weaken compliance. This policy fails all three of the guiding principles that I have argued governments should consider when designing collateral tax sanctions.

\textit{Tax Rule.} By considering the presence of willfulness and false statements in a criminal tax offense to be sufficient to qualify as an act of fraud or deceit under the immigration laws, the \textit{Kawashima} Court created

\begin{footnotesize}
\footnote{337} Id.
\footnote{338} See 8 U.S.C. § 1227(a)(2)(A)(iii) (“Any alien who is convicted of an aggravated felony at any time after admission is deportable.”).
\footnote{339} See 8 U.S.C. § 1427(a) (describing importance of “good moral character”).
\footnote{340} For description, see U.S. Citizenship and Immigration Services, Green Card (Permanent Residence), \textit{available at} http://www.uscis.gov.
\footnote{341} See id.
\end{footnotesize}
an extremely broad tax standard, not a narrowly tailored tax rule. As Justice Ginsburg commented in her dissent, many tax crimes of varying magnitude involve false statements or misleading conduct. 342 Such offenses could include delivery of a false Form W-2 to an employee, 343 the failure to truthfully collect and pay over taxes 344 or the submission of false documents to the taxing authority providing false documents, 345 among many others. It could also apply to misdemeanor offenses, such as the willful failure to file a tax return. 346 This rule could also, theoretically, apply to any state or local criminal tax offense that involves willfulness and false statements. In California, for instance, it is a misdemeanor to provide false information when requesting a property assessment reduction. 347 In light of Kawashima, it is not apparent which offenses may result in deportation.

An immediate consequence of the breadth of the Kawashima standard is that the IRS may lack the ability to publicize the specific types of tax offenses that may result in deportation. As it is not clear which tax offenses may lead to deportation after Kawashima, the IRS may have little ability to warn lawful permanent residents that particular types of tax offenses may lead not only to formal tax penalties, but also to deportation as well. Alternatively, if lawful permanent residents perceive that this collateral tax sanction may apply to any type of tax offense, some may overreact by adopting only the most conservative tax positions possible (such as by claiming the standard deduction rather than itemized deductions). 348 The adverse effect of such caution is that the IRS may not accurately assess individuals’ income and individuals may not take advantage of social programs that are enacted as tax expenditures.

Another implication is that lawful permanent residents who face criminal tax charges, whether felonies or misdemeanors, may refuse to enter guilty pleas if they fear that the immigration authorities may one day characterize these convictions as aggravated felonies. This reaction by lawful permanent residents may certainly occur in the case of charges of willfully filing false tax returns as a result of the holding in Kawashima. But, due to the ambiguous meaning of the standard and the immigration

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343 I.R.C. § 7204.
344 I.R.C. § 7202.
345 I.R.C. § 7207.
346 I.R.C. § 7203.
348 I.R.C. § 63(c).
authority’s ability to detect aggravated felonies without a statute of limitations, lawful permanent residents may display a similar response in any criminal tax case. Increased litigation may not only result in diversion of tax enforcement resources away from other important tax enforcement functions, but, given its public nature, may also cause taxpayers to view the government as prosecuting lawful permanent residents for tax offenses disproportionately compared to other types of offenders and offenses.

Tax Law and Tax Agency. In applying this collateral tax sanction, immigration officials may search public records for instances in which lawful permanent residents violated federal or state criminal tax laws. But the determination as to whether these offenses involve “fraud or deceit” sufficient to result in deportation is dependent upon immigration officials’ own interpretation of the Immigration and Nationality Act. Unlike the other collateral tax sanctions discussed thus far, such as those where the taxing authority provided a list of individuals who have committed specific tax offenses to the non-tax agency, this particular collateral tax sanction results from an offense that a non-tax agency identifies on its own.

This feature could muddle the government’s publicity of the collateral tax sanction of deportation in an attempt to increase compliance. Taxpayers, including lawful permanent residents, often learn about potential tax penalties from the IRS at the time when they are tax decisions ranging from whether to report particular types of income to whether to file tax returns. If IRS officials cannot accurately describe the tax offenses that lead to deportation under the aggravated felony statute because they do not know how the U.S. Immigration and Customs Enforcement will determine whether a particular tax offense merits this offense, they will have little ability to influence individuals’ tax reporting decisions at the time when they are making them.

The immigration authority’s separate interpretation of whether a particular offense constitutes fraud may also conflict with the IRS’s own public statements regarding what it views as fraud under the tax law. For example, in describing tax fraud to the public using its annual “Dirty Dozen Tax Scams” press release, the IRS describes extreme examples such as situations where an individual claims to be a “bishop” of a one-person, phony religious organization in order to receive non-profit status as a religious organization. They do not, on the other hand, describe offenses

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such as the delivery of a Form W-2 containing false information to an employee because the tax law does not treat this offense as an act of tax fraud.\textsuperscript{353} As a former IRS Commissioner has commented, “the criminal tax laws do not treat crimes involving the ‘willful’ provision of ‘false’ information as interchangeable and synonymous with those involving ‘fraud or deceit’ under the immigration laws.”\textsuperscript{354} An active application of Kawashima by immigration authorities, however, would conflate these two offenses for purposes of determining whether to seek deportation of a lawful permanent resident. The taxing authority’s ability to publicize the potential collateral tax sanction of deportation in advance of individuals’ tax reporting may be confused by such conflicting interpretations.

\textit{Proportionality.} If immigration officials actively apply Kawashima, some individuals may perceive the collateral tax sanction of deportation to be disproportionate to the underlying tax offense. This reaction may be especially prevalent if officials apply this policy retroactively, to lawful permanent residents who pled guilty to tax offenses involving false statements and willfulness, but that were lesser than tax evasion, prior to the Supreme Court’s decision in Kawashima.

An initial reason why individuals may view the sanction of deportation as disproportionate to a criminal tax offense involving willfulness and false statements is that this particular sanction is often levied upon far more harmful offenses. For example, under the Immigration and Nationality Act, aggravated felonies include murder,\textsuperscript{355} rape,\textsuperscript{356} sexual abuse of a minor\textsuperscript{357} and illicit trafficking of controlled,\textsuperscript{358} among other violent offenses. Individuals may not view the types of tax offenses potentially implicated by Kawashima, which could include misdemeanor tax offenses, such as willful failure to file a tax return, as crimes that are as grave as the non-tax related aggravated felonies. Further, offenses that involve physical violence or reckless disregard for the safety of others, such as driving while intoxicated,\textsuperscript{359} are not considered to be aggravated felonies, while potentially minor criminal tax offenses could result in deportation.

\textsuperscript{353} Id.
\textsuperscript{356} Id.
\textsuperscript{357} Id.
\textsuperscript{358} 8 U.S.C. §§ 1101(a)(43)(B).
While some tax offenses involving willfulness and false statements may prevent the taxing authority from collecting substantial tax liabilities, others could potentially result in significantly less harm, especially when compared to the harm that results from some of the violent aggravated felonies described above. The monetary threshold for a fraud and deceit tax offense that may result in deportation if crossed is $10,000.\footnote{8 U.S.C. §§ 1101(a)(43)(M)(ii).} If a lawful permanent resident is convicted of filing a series of Form W-2’s that contain false information and result in $3000 of lost tax revenue each year for a period of four years, for example, this individual could face deportation for committing an aggravated felony.\footnote{In this example, the total loss to the “victim”, the federal government, would be $12,000. For further discussion, see Brief for Amicus Curiae Johnnie M. Walters in Support of Petitioners, Kawashima v. Holder, 565 U.S. ___, 132 S. Ct. 1166 (2012).}

Individuals may also view the sanction of deportation for tax offenses involving willfulness and false statements as excessively severe, when compared to the maximum civil and criminal penalties for many of these tax offenses. As I described above, some criminal tax offenses that involve willfulness and false statements may result in a monetary fine. For example, in Ohio, the criminal offense of knowingly filing a false municipal tax return results in a $250.00 fine.\footnote{Columbus, Oh., City Code § 361.31(a)(4), (b), (d), discussed in Brief for Amicus Curiae Johnnie M. Walters in Support of Petitioners, Kawashima v. Holder, 565 U.S. ___, 132 S. Ct. 1166 (2012).} The additional sanction of deportation for this offense would likely appear to be vastly disproportionate to many individuals. But even for tax offenses that result in prison sentences, such as willfully filing a false tax return, the sanction of deportation may appear to be disproportionate. Some may argue that deportation for an aggravated felony—a sanction that may cause an individual to separate from children, forfeit a business and face a permanent ban against ever re-entering the United States—is a punishment that is even more severe than prison, irrespective of the length of the sentence.\footnote{See, e.g., Ng Fung Ho v. White, 259 U.S. 276, 284 (1922) (describing deportation as depriving an individual of “all that makes life worth living”).}

How might individuals respond if the government actively enforces Kawashima in a manner that they view as lacking proportionality? As scholars have predicted in other contexts, some lawful permanent residents may perceive the government’s use of a disproportionate sanction for a vaguely defined tax offense as lacking legitimacy.\footnote{See Tyler, supra note 246; Robinson & Darley, supra note 284; Robinson, Goodwin & Resig, supra note 284.} One recent study has found that the perception that the law lacks legitimacy may increase as individuals perceive that police target particular racial or religious groups
disproportionately compared to others. If individuals perceive the deportation of individuals who have committed tax offenses involving willfulness and false statements, some of which may have occurred prior to Kawashima, as illegitimate, they may reduce their cooperation with the taxing authority. Some lawful permanent residents may fail to report income or items that they believe the taxing authority may not detect, such as cash income or, for wealthy individuals, off-shore bank accounts in their home countries. Rather than risk facing a collateral tax sanction that they perceive as illegitimate, these individuals may take the minimum actions necessary, such as simply filing a personal tax return, to satisfy an immigration court that they have attempted to comply with the tax law.

As this discussion demonstrates, the government’s active application of Kawashima to individuals who have committed criminal tax offenses involving willfulness and false statements may produce mixed results. Some lawful permanent residents may believe they are required by law to abide by heightened standards of moral conduct and, as a result, they may adhere to the letter of the law, including the tax law. These individuals may respond to the immigration authority’s active application of Kawashima by continuing to report and pay their tax liability correctly, and, as described above, may even forego tax credits and deductions to which they are entitled. Others, however, may refuse to enter into plea agreements in criminal tax cases and may even limit the information they reveal to the taxing authorities in their tax returns. As a result, whether the use of the collateral tax sanction of deportation for fraud and deceit tax offenses will result in net tax compliance benefits is far from certain.

C. Publicity by Taxing Authorities

Many of the positive effects of collateral tax sanctions discussed in this Article will only occur if taxpayers are aware of these measures. Existing collateral tax sanctions currently receive publicity, but not as a result of direct communication from taxing authorities. Taxpayers may learn about the existence of collateral tax sanctions from other sources, and often after they have already engaged in tax noncompliance. In its publications and on its website, for example, the IRS does not discuss the potential for lawyers and doctors to forfeit their professional licenses in their respective states if


they engage in abusive tax activities.\textsuperscript{367} Taxing authorities should play a more active role in publicizing these sanctions, specifically when they satisfy the guiding principles described above. Rather than relying solely on non-tax agencies to spread the word, taxing authorities should deliver a coordinated message that describes formal civil and criminal tax penalties \textit{and} collateral tax sanctions. This Subpart outlines approaches that taxing authorities could adopt to publicize collateral tax sanctions effectively.

\textit{Strategic Publicity.} In contrast to their current passive stances, taxing authorities should publicize the threat of collateral tax sanctions strategically, during encounters and at times when this information is likely to have its maximum impact on taxpayers\’ perceptions and beliefs. Taxing authorities should pursue this approach in their direct and indirect communications with taxpayers.

Taxing authorities often directly communicate with noncompliant taxpayers when they send them notices to request that they pay their outstanding tax liabilities. In the notices that taxing authorities send today, they do not inform taxpayers of the collateral tax sanctions that may await them if they continue to ignore their obligations to pay their outstanding taxes. For instance, under current law, when the IRS sends a Notice of Federal Tax Lien to taxpayers, it states the amount of their outstanding tax liabilities, informs them that the IRS may seek to attach a lien against their property and that they will continue to accrue monetary tax penalties and interest.\textsuperscript{368} However, the IRS does not describe the collateral tax sanctions that may occur in addition to these effects of their noncompliance.\textsuperscript{369} A more effective form of direct communication would be for the IRS to describe in this notice not only the additional monetary tax penalties and interest that taxpayers may accrue if they continue to ignore their obligation to pay the outstanding taxes, but also the government benefits that these individuals may sacrifice, such as a U.S. passport,\textsuperscript{370} qualification for an FHA Loan\textsuperscript{371} or the right to work for or enter into contracts with the federal government.\textsuperscript{372}

Taxing authorities should also publicize strategically the potential application of collateral tax sanctions during periods of the year when taxpayers are most focused on their tax reporting and payment obligations. The federal government appears to deliberately increase its publicity of its

\textsuperscript{369} See id.
\textsuperscript{370} See supra notes 83 - 89 and accompanying text.
\textsuperscript{371} See supra notes 99 - 101 and accompanying text.
\textsuperscript{372} See supra notes 102 - 103 and accompanying text.
tax enforcement actions, including criminal tax cases, during this period by issuing a disproportionate of tax enforcement press releases and announcements during this period compared to the rest of the year. Strategic publicity may have positive effects on individuals’ perceptions of the taxing authority’s enforcement capabilities and, ultimately, on compliance. Similarly, taxing authorities should issue public announcements regarding potential collateral tax sanctions during this period. Such strategic publicity is especially important if the collateral tax sanction stems from individuals’ tax reporting decisions, such as the proposed FDIC collateral tax sanction for household employment tax evasion. Individuals who learn of the collateral tax sanctions during the weeks leading up to Tax Day may, for example, revise the decision to omit their household employee and ignore their related tax obligations. But even if collateral tax sanctions would relate only nonpayment, rather than underreporting, of taxes, taxing authorities should nonetheless attempt to publicize these sanctions during this period. For individuals who are motivated to comply with the tax law as a result of feelings of reciprocity, this publicity may assure them that the most blatant form of tax avoidance, the simple refusal to pay, does not go undetected or unpunished.

Specificity. When taxing authorities publicize collateral tax sanctions, they should describe the tax offenses and the resulting denial or revocation of benefits with specificity. Due to the salient nature of the benefits at stake, if taxing authorities fail to describe the potential collateral tax sanctions clearly, confusion among taxpayers and resentment toward the taxing authorities by taxpayers may result.

Taxing authorities should actively publicize collateral tax sanctions, in part, because officials of non-tax agencies may not possess sufficient expertise in the tax law to describe these sanctions accurately to the general public. For instance, the Louisiana license statutes provide that an individual’s hunting or fishing license will be revoked only if the individual owes a final assessment “in excess of five hundred dollars of income tax…” Yet, the Louisiana Department of Wildlife and Fisheries website, a source that is much more likely to be accessed by individuals than statutes, states that an individual may not receive a hunting or fishing license unless the individual can demonstrate that, during the previous

373 See Blank & Levin, supra note 351 at 17 (finding that from April 1 to Tax Day, the government issued 128% more tax enforcement press releases per week than during the rest of the year).
374 For discussion, see Blank, supra note 28.
375 See supra notes 316 - 331 and accompanying text.
376 See supra notes 195 - 215 and accompanying text.
377 See supra notes 159 - 177 and accompanying text.
378 Louisiana Revised Statutes § 47:296.3.
twelve months, “he has filed a Louisiana state income tax return and has complied with state income tax laws and regulations.”\textsuperscript{379} Even though the law in Louisiana clearly applies only to the offense of tax delinquency, the plain English description of the law appears to expand its scope significantly. Under the interpretation of the statute of the Department of Wildlife and Fisheries, individuals may perceive that if they have failed to pay a small amount of tax or filed their return late, they may be forced to forfeit their hunting licenses. A consequence of such a broad description of the law is that individuals may perceive that it is disproportionate to the offense and may, in response, reduce their cooperation with the taxing authority (since this is agency that identifies the offenses that ultimately lead to the license revocation). By actively explaining the specific tax offenses that may result in collateral tax sanctions, the taxing authority may prevent mischaracterizations of the law and the perception that the taxing authority enlists other agencies to enforce unfair measures.

In addition, taxing authorities should explicitly publicize the limits of the application of collateral tax sanctions. For instance, in California, a state with a population of nearly 38 million individuals, the collateral tax sanctions that suspend driver’s licenses or deny their renewal affects only 1,000 tax delinquents,\textsuperscript{380} some of whom owe as much as $10.5 million in outstanding state taxes.\textsuperscript{381} Likewise, at the federal level, the proposed passport legislation would only apply to individuals who have failed to pay more than $50,000 in federal taxes.\textsuperscript{382} By publicizing such limits, the taxing authority would further protect itself from accusations that it is contributing to the enforcement of a disproportionate sanction. Such charges have been levied in the past. In March 2011, when the Senate passed the passport provision, commentators expressed sentiments similar to those of one talk radio host, who exclaimed that the law would empower the IRS to “arbitrarily” direct the Department of State to revoke an individual’s passport by asserting “any figure they wish to impose on a citizen without much recourse for the accused.”\textsuperscript{383} With a more active public role, taxing authorities could preempt such inaccurate reports.

Even if the taxing authority publicizes these limits, it is likely that, due to the high salience of these sanctions, some individuals may assume that

\textsuperscript{380} See supra notes 108-112 and accompanying text.
\textsuperscript{381} See Lifsher & Wilson, supra note 168 (describing $10.5 million tax debt of Halsey M. Minor, founder of CNET.com).
\textsuperscript{382} See supra notes 83-89 and accompanying text
\textsuperscript{383} CBS Radio, Owe the IRS? Bill Would Suspend Passport Rights for Delinquent Taxpayers, CBSLocal.com, April 4, 2012 (“[the IRS] can arbitrarily determine any figure they wish to impose on a citizen without much recourse for the accused”).
collateral tax sanctions have greater application than they actually do under the law. For example, while the individual audit rate is approximately 1%, several studies of individual taxpayers’ beliefs have shown that individuals estimate that audit rates are as high as 48% and over 60% of individuals report that their fear of being audited has an influence on their decision to pay taxes. But as long as the taxing authority clearly states the specific limits of collateral tax sanctions (just as the IRS explicitly describes the true 1% audit rate on its website), it may resist accusations that it has attempted to achieve tax compliance through misleading communications.

**Results.** When publicizing a particular collateral tax sanction that has been in effect for some time, taxing authorities should provide data regarding the effectiveness of the measure. As was discussed earlier, nearly every collateral tax sanction will result in spillover effects upon other individuals, such as children of tax delinquent individuals who must forfeit their driver’s licenses or patients of tax delinquent physicians who must seek alternative care during their physicians’ medical license suspensions. A consequence of such spillover effects is that taxpayers may perceive the collateral tax sanction is not justified in light of the underlying tax offense. The taxing authority can partially quell this concern by including in its public statements regarding the collateral tax sanctions statistics that reinforce the message that these sanctions are effective. For example, as California’s driver’s license suspension program only applies to the top 500 income tax delinquents and the top 500 sales tax delinquents, state officials could emphasize to the public that many individuals are removed from these lists each year as they make arrangements to satisfy their outstanding tax liabilities.

In addition to mitigating perceptions that the government has enacted overly harsh sanctions, this type of message would also have a positive effect on taxpayers affected by two specific motivations of compliance. For

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386 See Int. Rev. Serv., Fiscal Year 2009 Enforcement Results.

387 See supra note 117 and accompanying text.

388 See supra note 244 and accompanying text.


390 States that have attempted to publicly shame tax delinquents using online websites have also released public statements regarding the efficacy of these measures. See, e.g., Steven Walters, *Taxpayer List Scares Up Cash*, MIL. J. SENTINEL, May 30, 2006, at B3 (reporting on decreases of number names on Wisconsin’s delinquent taxpayer list). See also Blank, supra note 262 at 552.
reciprocator taxpayers, statements from the taxing authority that individuals change their behavior in response to collateral tax sanctions would confirm their belief that the government effectively deters tax noncompliance. For taxpayers who fear sanctions that would make their failure to obey the tax law observable by others, such as suspension of a professional license for failure to file tax returns, an announcement that such collateral tax sanctions are effective in forcing others to file their returns could lead these taxpayers to perceive that the negative signal of tax noncompliance is rare and, thus, strong.

When Drawbacks Outweigh Benefits. On occasion, legislatures will enact collateral tax sanctions that fail all of the principles I have proposed above, creating significant drawbacks that may outweigh many of the potential compliance benefits of the sanctions. The deportation of lawful permanent residents who have committed a criminal tax offense involving willfulness and false statements is an illustration of such a collateral tax sanction. In cases like these, the taxing authority should not actively publicize the collateral tax sanction. As I have argued, the taxing authority will be ill-equipped to describe accurately a collateral tax sanction that stems for a standard that is subject to the interpretation of another agency. Further, if the taxing authority publicizes this collateral tax sanction, such as deportation for tax offenses involving willfulness and false statements, individuals who perceive it to be disproportionate or unfair may direct their backlash at the taxing authority. Some may even suspect that the taxing authority works in concert with the non-tax agency by identifying tax offenses that would allow the non-tax agency to subject the taxpayer to a harsh collateral tax sanction, such as deportation. In these cases, it is best for the taxing authorities to refrain from attempting to enhance compliance by publicizing the collateral tax sanction.

V. CONCLUSION

This Article has offered a comprehensive analysis of an alternative approach to reducing tax noncompliance that can be deployed by federal, state and local governments – collateral tax sanctions. In contrast to the focus in the criminal law literature on the detrimental effects of the collateral consequences of criminal convictions, this Article has shown that collateral tax sanctions can promote voluntary compliance with the tax law more effectively than the threat of additional monetary tax penalties.

391 See supra notes 195-199 and accompanying text.
392 See supra notes 306-315 and accompanying text.
393 See supra notes 332-366 and accompanying text.
394 See supra notes 276-277 and accompanying text.
Collateral tax sanctions may encourage individuals who are influenced by different motivations of compliance to report and pay their tax liability properly more effectively than the threat of additional monetary tax penalties. Collateral tax sanctions may be effective deterrents as a result of the high salience of the government benefits that individuals may forfeit and individuals’ inherent loss aversion and endowment effect biases. They may also promote tax compliance by reciprocator taxpayers by reassuring these individuals that, given the hefty consequences that could result, few of their fellow taxpayers engage in tax noncompliance. In addition, collateral tax sanctions may induce compliance among individuals who fear the negative signals that certain sanctions, such as those that suspend or revoke professional licenses, could emit to others. Finally, by reminding taxpayers of specific, valued benefits that the government provides, publicity of collateral tax sanctions may have a positive impact on individuals who pay their taxes out of patriotism or civic duty.

After considering the potential drawbacks that may result from existing or potential collateral tax sanctions, this Article has proposed a set of guiding principles that governments should consider when designing a collateral tax sanction that would promote tax compliance. Under these principles, collateral tax sanctions are most effective as a means of encouraging compliance where (1) the tax offense results from a violation of a tax rule, not a tax standard, (2) the sanction results from a tax offense that the tax law defines and that a taxing authority identifies, and (3) the collateral tax sanction is proportionate to the underlying tax offense. Where these principles are satisfied, taxing authorities should actively publicize collateral tax sanctions in coordination with their existing efforts to inform taxpayers of potential civil and criminal tax penalties.

As tax scholars, policymakers and tax lawyers are well aware, the tax law serves multiple purposes, often bearing the burden of implementing social programs and policies that are unrelated to its core functions. Collateral tax sanctions, by contrast, require non-tax agencies to share with taxing authorities the responsibility for encouraging individuals to satisfy their obligations under the tax law. Governments in search of tax revenue should embrace this opportunity.

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395 See supra notes 178-194 and accompanying text. See also GEORGE GERSHWIN & IRA GERSHWIN, THEY CAN’T TAKE THAT AWAY FROM ME (RKO Radio, 1937) (“No, no, they can’t take that away from me.”).