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## Summons Enforcement Under IRC §§ 7602, 7604, and 7609

## SUMMARY

Pursuant to Internal Revenue Code (IRC) § 7602, the IRS may examine any books, records, or other data relevant to an investigation of a civil or criminal tax liability.<sup>1</sup> To obtain this information, the IRS may serve a summons directly on the subject of the investigation or any third party who may possess relevant information.<sup>2</sup> If a person summoned under IRC § 7602 neglects or refuses to obey the summons; to produce books, papers, records, or other data; or to give testimony as required by the summons, the IRS may seek enforcement of the summons in a United States district court.<sup>3</sup>

A person who has a summons served on him or her may contest its legality if the government petitions to enforce it.<sup>4</sup> Thus, summons enforcement cases are different from many other cases described in other Most Litigated Issues because often the government, rather than the taxpayer, initiates the litigation. If the IRS serves a summons on a third party, any person entitled to notice of the summons may challenge its legality by filing a motion to quash or by intervening in any proceeding regarding the summons.<sup>5</sup> Generally, the burden on the taxpayer to establish the illegality of the summons is heavy.<sup>6</sup> When challenging the summons's validity, the taxpayer generally must provide "some credible evidence" supporting an allegation of bad faith or improper purpose.<sup>7</sup> The taxpayer is entitled to a hearing to examine an IRS agent about his or her purpose for issuing a summons only when the taxpayer can point to specific facts or circumstances that plausibly raise an inference of bad faith.<sup>8</sup> Naked allegations of improper purpose are not enough, but because direct evidence of IRS's bad faith "is rarely if ever available," circumstantial evidence can suffice to meet that burden.<sup>9</sup>

We identified 87 federal cases decided between June 1, 2015, and May 31, 2016 involving IRS summons enforcement issues. The government was the initiating party in 58 cases, while the taxpayer was the initiating party in 29 cases. Overall, taxpayers fully prevailed in three cases, while five cases were split. The IRS prevailed in the remaining 79 cases.

1 Internal Revenue Code (IRC) § 7602(a)(1); Treas. Reg. § 301.7602-1.

2 IRC § 7602(a).

3 IRC § 7604(b).

4 *U.S. v. Powell*, 379 U.S. 48, 58 (1964).

5 IRC § 7609(b).

6 *U.S. v. LaSalle Nat'l Bank*, 437 U.S. 298, 316 (1978).

7 *U.S. v. Clarke*, 134 S. Ct. 2361, 2367 (2014), *vacating* 517 F. App'x 689 (11th Cir. 2013), *rev'g* 2012-2 U.S. Tax Cas. (CCH) ¶ 50,732 (S.D. Fla. 2012).

8 *Id.* (stating that "[t]he taxpayer need only make a showing of facts that give rise to a plausible inference of improper motive").

9 *Id.* at 2367-68.

## TAXPAYER RIGHTS IMPACTED<sup>10</sup>

- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

## PRESENT LAW

The IRS has broad authority under IRC § 7602 to issue a summons to examine a taxpayer's books and records or demand testimony under oath.<sup>11</sup> Further, the IRS may obtain information related to an investigation from a third party if, subject to the exceptions of IRC § 7609(c), it provides notice to the taxpayer or other person identified in the summons.<sup>12</sup> In limited circumstances, the IRS can issue a summons even if the name of the taxpayer under investigation is unknown, *i.e.*, a “John Doe” summons.<sup>13</sup> However, the IRS cannot issue a summons after referring the matter to the Department of Justice (DOJ).<sup>14</sup>

If the recipient fails to comply with a summons, the United States may commence an action under IRC § 7604 in the appropriate U.S. District Court to compel document production or testimony.<sup>15</sup> If the United States files a petition to enforce the summons, the taxpayer may contest the validity of the summons in that proceeding.<sup>16</sup> Also, if the summons is served upon a third party, any person entitled to notice may petition to quash the summons in an appropriate district court, and may intervene in any proceeding regarding the enforceability of the summons.<sup>17</sup>

Generally, a taxpayer or other person named in a third-party summons is entitled to notice.<sup>18</sup> However, the IRS does not have to provide notice in certain situations. For example, the IRS is not required to give notice if the summons is issued to aid in the collection of “an assessment made or judgment rendered against the person with respect to whose liability the summons is issued.”<sup>19</sup> Congress created this exception because it recognized a difference between a summons issued in an attempt to compute the taxpayer's taxable income and a summons issued after the IRS has assessed tax or obtained a judgment.

10 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

11 IRC § 7602(a). See also *LaMura v. U.S.*, 765 F.2d 974, 979 (11th Cir. 1985) (citing *U.S. v. Bisceglia*, 420 U.S. 141, 145-46 (1975)).

12 IRC § 7602(c). Those entitled to notice of a third-party summons (other than the person summoned) must be given notice of the summons within three days of the day on which the summons is served to the third party but no later than the 23rd day before the day fixed on the summons on which the records will be reviewed. IRC § 7609(a).

13 The court must approve a “John Doe” summons prior to issuance. In order for the court to approve the summons, the United States commences an *ex parte* proceeding. The United States must establish during the proceeding that its investigation relates to an ascertainable class of persons; it has a reasonable basis for the belief that these unknown taxpayers may have failed to comply with the tax laws; and it cannot obtain the information from another readily available source. IRC § 7609(f).

14 IRC § 7602(d). This restriction applies to “any summons, with respect to any person if a [DOJ] referral is in effect with respect to such person.” IRC § 7602(d)(1).

15 IRC § 7604.

16 *U.S. v. Powell*, 379 U.S. 48, 58 (1964).

17 IRC § 7609(b). The petition to quash must be filed not later than the 20th day after the date on which the notice was served. IRC § 7609(b)(2)(A).

18 IRC § 7609(a)(1); Treas. Reg. § 301.7609-1(a)(1). See, e.g., *Cephas v. U.S.*, 112 A.F.T.R.2d (RIA) 6483 (D. Md. 2013).

19 IRC § 7609(c)(2)(D)(i). The exception also applies to the collection of a liability of “any transferee or fiduciary of any person referred to in clause (i).” IRC § 7609(c)(2)(D)(ii).

For example, the IRS does not have to give notice to the taxpayer or person named in the summons if it is attempting to determine whether the taxpayer has an account in a certain bank with sufficient funds to pay an assessed tax because such notice might seriously impede the IRS's ability to collect the tax.<sup>20</sup> Courts have interpreted this "aid in collection" exception to apply only if the taxpayer owns a legally identifiable interest in the account or other property for which records are summoned.<sup>21</sup> Additionally, the IRS is not required to give notice when, in connection with a criminal investigation, an IRS criminal investigator serves a summons on any person who is not the third-party record-keeper.<sup>22</sup>

Whether the taxpayer contests the summons in a motion to quash or in response to the United States' petition to enforce, the legal standard is the same.<sup>23</sup> In *United States v. Powell*, the Supreme Court set forth four threshold requirements (referred to as the *Powell* requirements) that must be satisfied to enforce an IRS summons:

1. The investigation must be conducted for a legitimate purpose;
2. The information sought must be relevant to that purpose;
3. The IRS must not already possess the information; and
4. All required administrative steps must have been taken.<sup>24</sup>

The IRS bears the initial burden of establishing that these requirements have been satisfied.<sup>25</sup> The government meets its burden by providing a sworn affidavit of the agent who issued the summons declaring that each of the *Powell* requirements has been satisfied.<sup>26</sup> The burden then shifts to the person contesting the summons to demonstrate that the IRS did not meet the requirements or that enforcement of the summons would be an abuse of process.<sup>27</sup>

The taxpayer can show that enforcement of the summons would be an abuse of process if he or she can prove that the IRS issued the summons in bad faith.<sup>28</sup> In *United States v. Clarke*, the Supreme Court held that during a summons enforcement proceeding, a taxpayer has a right to conduct an examination of the responsible IRS officials about whether a summons was issued for an improper purpose only when the taxpayer "can point to specific facts or circumstances plausibly raising an inference of bad faith."<sup>29</sup> Blanket claims of improper purpose are not sufficient, but circumstantial evidence can be.<sup>30</sup>

20 H.R. REP. No. 94-658 at 310, *reprinted in* 1976 U.S.C.C.A.N. at 3206. *See also* S. REP. No. 94-938, pt. 1, at 371, *reprinted in* 1976 U.S.C.C.A.N. at 3800-01 (containing essentially the same language).

21 *Ip v. U.S.*, 205 F.3d 1168, 1172-76 (9th Cir. 2000).

22 IRC § 7609(c)(2)(E). A third-party record-keeper is broadly defined and includes banks, consumer reporting agencies, persons extending credit by credit cards, brokers, attorneys, accountants, enrolled agents, and owners or developers of computer source code but only when the summons "seeks the production of the source or the program or the data to which the source relates." IRC § 7603(b)(2).

23 *Kamp v. U.S.*, 112 A.F.T.R.2d (RIA) 6630 (E.D. Cal. 2013).

24 *U.S. v. Powell*, 379 U.S. 48, 57-58 (1964).

25 *Fortney v. U.S.*, 59 F.3d 117, 119-20 (9th Cir. 1995).

26 *U.S. v. Dynavac, Inc.*, 6 F.3d 1407, 1414 (9th Cir. 1993).

27 *Id.*

28 *U.S. v. Powell*, 379 U.S. 48, 58 (1964).

29 *U.S. v. Clarke*, 134 S. Ct. 2361, 2367 (2014), *vacating* 517 F. App'x 689 (11th Cir. 2013), *rev'g* 2012-2 U.S. Tax Cas. (CCH) ¶ 50,732 (S.D. Fla. 2012).

30 *Id.* at 2367-68.

A taxpayer may also allege that the information requested is protected by a constitutional, statutory, or common-law privilege, such as the:

- Fifth Amendment privilege against self-incrimination;
- Attorney-client privilege;<sup>31</sup>
- Tax practitioner privilege;<sup>32</sup> or
- Work product privilege.<sup>33</sup>

However, these privileges are limited. For example, courts reject blanket assertions of the Fifth Amendment,<sup>34</sup> but note that taxpayers may have valid Fifth Amendment claims regarding specific documents or testimony.<sup>35</sup> However, even if a taxpayer may assert the Fifth Amendment on behalf of him or herself, he or she cannot assert it on behalf of a business entity.<sup>36</sup>

Additionally, taxpayers cannot, on the basis of the Fifth Amendment privilege, withhold self-incriminatory evidence of a testimonial or communicative nature if the summoned documents fall within the “foregone conclusion” exception to the Fifth Amendment. The exception applies if the government establishes its independent knowledge of three elements:

1. The documents’ existence;
2. The documents’ authenticity; and
3. The possession or control of the documents by the person to whom the summons was issued.<sup>37</sup>

The attorney-client privilege protects “tax advice,” but not tax return preparation materials.<sup>38</sup> The “tax shelter” exception limits the tax practitioner privilege and permits discovery of communications between a practitioner and client that promote participation in any tax shelter.<sup>39</sup> Thus, the tax practitioner privilege does not apply to any written communication between a federally authorized tax practitioner and “any person, any director, officer, employee, agent, or representative of the person, or any other person holding a capital or profits interest in the person” which is “in connection with the promotion of the direct or indirect participation of the person in any tax shelter.”<sup>40</sup>

31 The attorney-client privilege provides protection from discovery of information where: (1) legal advice of any kind is sought, (2) from a professional legal advisor in his or her capacity as such, (3) the communication is related to this purpose, (4) made in confidence, (5) by the client, (6) and at the client’s insistence protected, (7) from disclosure by the client or the legal advisor, (8) except where the privilege is waived. *U.S. v. Evans*, 113 F.3d 1457, 1461 (7th Cir. 1997) (citing 8 JOHN HENRY WIGMORE, EVIDENCE IN TRIALS AT COMMON LAW § 2292 (John T. McNaughten rev. 1961)).

32 IRC § 7525 extends the protection of the common law attorney-client privilege to federally authorized tax practitioners in federal tax matters. Criminal tax matters and communications regarding tax shelters are exceptions to the privilege. IRC § 7525(a)(2), (b). The interpretation of the tax practitioner privilege is based on the common law rules of attorney-client privilege. *U.S. v. BDO Seidman, LLP*, 337 F.3d 802, 810-12 (7th Cir. 2003).

33 The work product privilege protects against the discovery of documents and other tangible materials prepared in anticipation of litigation. FED. R. CIV. P. 26(b)(3); see also *Hickman v. Taylor*, 329 U.S. 495 (1947).

34 See, e.g., *U.S. v. McClintic*, 113 A.F.T.R.2d (RIA) 330 (D. Or. 2013).

35 See, e.g., *U.S. v. Lawrence*, 113 A.F.T.R.2d (RIA) 1933 (S.D. Fla. 2014).

36 See, e.g., *U.S. v. Ali*, 113 A.F.T.R.2d (RIA) 1863 (D. Md. 2014) (citing *U.S. v. Wujkowski*, 929 F.2d 981, 983 (4th Cir. 1991)).

37 *U.S. v. Bright*, 596 F.3d 683, 692 (9th Cir. 2010).

38 *U.S. v. Frederick*, 182 F.3d 496, 500 (7th Cir. 1999).

39 IRC § 7525(b). See also *Valero Energy Corp. v. U.S.*, 569 F.3d 626 (7th Cir. 2009).

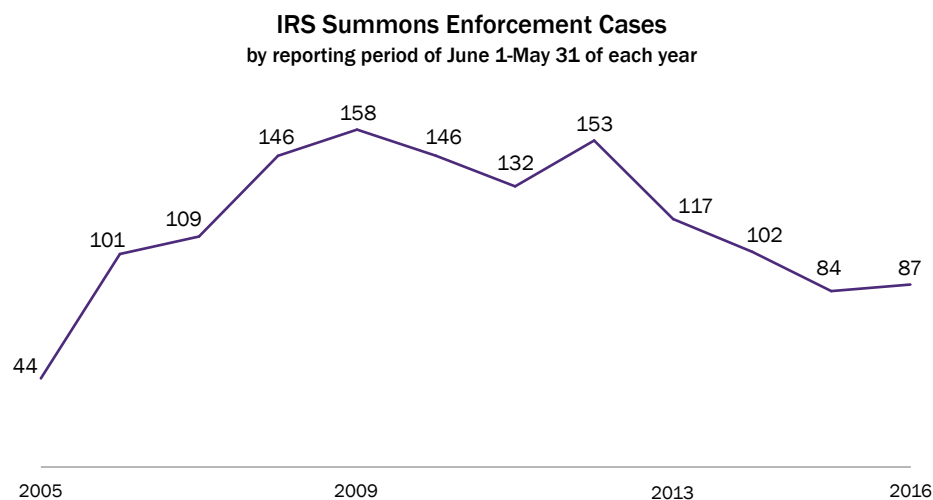
40 *Id.* A tax shelter is defined as “a partnership or other entity, any investment plan or arrangement, or any other plan or arrangement, if a significant purpose of such partnership, entity, plan, or arrangement is the avoidance or evasion of Federal income tax.” IRC § 6662(d)(2)(C)(ii).

In July 2016, the IRS issued final regulations providing that outside parties with whom the IRS or the Office of Chief Counsel contracts for services — such as economists, engineers, consultants, or attorneys — may receive books papers, records, or other data summoned by the IRS and, in the presence of an IRS officer or employee, participate fully in the interview of a person who the IRS has summoned as a witness to provide testimony under oath.<sup>41</sup>

## ANALYSIS OF LITIGATED CASES

Summons enforcement has been a Most Litigated Issue in the National Taxpayer Advocate's Annual Report to Congress every year since 2005, when TAS identified only 44 cases but predicted the number would rise as the IRS became more aggressive in its enforcement initiatives. The number of cases peaked at 158 for the reporting period ending on May 31, 2009, but had steadily declined, except for a one-year increase for the year ending May 31, 2012, as shown in Figure 3.3.1. This year, the number of summons enforcement cases picked up slightly, as we identified 87 cases for the reporting period ending on May 31, 2016, an increase from the 84 cases we identified during last year's reporting period. A detailed list of these cases appears in Table 3 of Appendix 3.

**FIGURE 3.3.1**



Of the 87 cases TAS reviewed this year, the IRS prevailed in full in 79, a 91 percent success rate, which is a slight decline from the IRS's 96 percent success rate during the 2015 reporting period.<sup>42</sup> Taxpayers had representation in 38 cases (44 percent) and appeared *pro se* (*i.e.*, on their own behalf) in the remaining 49. This is a notable climb in the number of represented taxpayers as only 27 percent of taxpayers were represented during last year's reporting period.<sup>43</sup> Seventy-two cases involved individual taxpayers, while

41 See Treas. Reg. § 301.7602-1(b)(3). As we noted in last year's Annual Report, the IRS issued temporary regulations on this topic in June 2014. See Temp. Treas. Reg. § 301.7602-1T(b)(3); National Taxpayer Advocate 2015 Annual Report to Congress 470-71. These temporary regulations were the subject of summons enforcement litigation involving the IRS's use of an outside law firm in an audit of Microsoft Corporation's transfer pricing arrangements, a case that will be discussed below.

42 See National Taxpayer Advocate 2015 Annual Report to Congress 471.

43 *Id.*

the remaining 15 involved business taxpayers, including sole proprietorships.<sup>44</sup> Cases generally involved one of the following themes.

### Petitions to Enforce and *Powell* Requirements

The United States petitioned to enforce a summons in 58 cases and successfully met its burden under *Powell* in 57 cases.<sup>45</sup> In only one case, *United States v. Lamotte*, did the IRS fail to satisfy the *Powell* requirements.<sup>46</sup> In *Lamotte*, the IRS issued two summonses to Mr. Lamotte, who was the treasurer of Northern Tree Service, Inc. (Northern) and director of two captive insurance companies that provided insurance to Northern. One of the summons sought documents and the other testimony relating to Northern's utilization of a captive insurance tax structure.<sup>47</sup>

With respect to the summons requesting documents, Mr. Lamotte argued that the IRS was already in possession of the documents.<sup>48</sup> The district court agreed, finding that the IRS already had the documents it sought and was therefore not entitled to a summons enforcement order under *Powell*.<sup>49</sup>

### Petitions to Quash and Lack of Subject Matter Jurisdiction

Taxpayers petitioned to quash an IRS summons to a third party in 29 instances;<sup>50</sup> however, in most of these cases, courts dismissed the petitions for lack of jurisdiction on procedural or notice grounds. For example, two United States Courts of Appeals affirmed district court dismissals of a taxpayer's petition to quash a summons issued to the taxpayer's bank because the summons was to aid in the collection of a tax liability, and the taxpayer was therefore not entitled to notice.<sup>51</sup>

In *Haber v. United States*, the taxpayer filed a petition to quash an IRS summons served on a bank that sought documents and testimony relating to assets held by the taxpayer's wife, which the district court dismissed for lack of subject matter jurisdiction because the United States has not waived sovereign immunity to allow suits to quash summonses that are issued to aid in the collection of an assessed tax.<sup>52</sup> On appeal to the Second Circuit, the taxpayer argued that, because he had brought various legal challenges to the assessment which prevented the IRS from beginning actual collection, the summons

44 There were cases in which the IRS issued summonses for investigations into both the individual taxpayer and his or her business. For the purposes of this MLI, TAS placed these cases into the business taxpayer category.

45 See, e.g., *Davis & Campbell, LLC v. U.S.*, 116 A.F.T.R.2d (RIA) 7124 (S.D.N.Y. 2015); *Neuberger v. U.S.*, 2016 U.S. Dist. LEXIS 59371 (W.D. Pa. 2016); *Wood v. U.S.*, 117 A.F.T.R.2d (RIA) 1919 (D. Md. 2016).

46 *U.S. v. Lamotte*, 117 A.F.T.R.2d (RIA) 1725 (D. Mass. 2016), *adopting* 117 A.F.T.R.2d (RIA) 1718 (D. Mass. 2016), *appeal dismissed*, No. 16-1940 (1st Cir. August 2, 2016).

47 *Id.*, *adopting* 117 A.F.T.R.2d (RIA) 1718 (D. Mass. 2016), *appeal dismissed*, No. 16-1940 (1st Cir. August 2, 2016). A captive insurance structure is where a business sets up an insurance company to protect against certain risks. While this may be structured with legitimate tax benefits, there are situations where it can be abused. See IRS, *Abusive Tax Shelters Again on the IRS "Dirty Dozen" List of Tax Scams for the 2016 Filing Season* (Feb. 16, 2016), [https://www.irs.gov/uac/newsroom/abusive-tax-shelters-again-on-the-irs-dirty-dozen-list-of-tax-scams-for-the-2016-filing-season?\\_ga=1.49174374.1518734088.1474380960](https://www.irs.gov/uac/newsroom/abusive-tax-shelters-again-on-the-irs-dirty-dozen-list-of-tax-scams-for-the-2016-filing-season?_ga=1.49174374.1518734088.1474380960).

48 With respect to the summons seeking testimony, the court declined to enforce that summons because, as will be discussed below, Mr. Lamotte had properly invoked the Fifth Amendment privilege.

49 *U.S. v. Lamotte*, 117 A.F.T.R.2d (RIA) 1725 (D. Mass. 2016), *adopting* 117 A.F.T.R.2d (RIA) 1718 (D. Mass. 2016), *appeal dismissed*, No. 16-1940 (1st Cir. August 2, 2016).

50 In some instances, the taxpayer made the motion to quash in its answer to the government's petition to enforce.

51 *Haber v. U.S.*, 823 F.3d 746 (2d Cir. 2016), *aff'g* 115 A.F.T.R.2d (RIA) 2221 (S.D.N.Y. 2015); *Maehr v. Comm'r*, 641 F. App'x 813 (10th Cir. 2016), *aff'g* 116 A.F.T.R.2d (RIA) 5398 (D. Colo. 2015). Under IRC § 7609(c)(2)(D)(i), the IRS is not required to provide notice to the taxpayer and the taxpayer therefore has no right to quash the summons if the summons is issued to aid in the collection of the taxpayer's liability.

52 *Haber v. U.S.*, 115 A.F.T.R.2d (RIA) 2221 (S.D.N.Y. 2015), *aff'd* 823 F.3d 746 (2d Cir. 2016).

was not issued to aid in collection, and thus, he should be able to quash the summons.<sup>53</sup> The court disagreed, analyzing the language of the statute under IRC § 7609(c)(2)(D), and finding that there was no requirement that IRS have “present authority to collect on the assessment or the actual collection is ‘imminent.’”<sup>54</sup> The court therefore affirmed the lower court’s dismissal of the taxpayer’s petition to quash.<sup>55</sup>

Similarly, in *Maehr v. Commissioner*, the Tenth Circuit affirmed a district court dismissal of a taxpayer’s petition to quash a summons served on his bank.<sup>56</sup> The appellate court found that, because the summons was issued to aid in the collection of an assessment under IRC § 7609(c)(2)(D), the IRS was not required to give notice to the taxpayer and he was therefore not permitted to quash the summons.<sup>57</sup>

### Privileges

As in past years, taxpayers attempted to invoke various privileges, including Fifth Amendment, attorney-client, or other privileges in response to an IRS summons. For example, two United States Courts of Appeals, in cases of first impression before each circuit, agreed with the unanimous view of the other Courts of Appeals that had considered the issue and held that records required to be kept under the Bank Secrecy Act fell within the required records exception to the Fifth Amendment privilege.<sup>58</sup>

In *United States v. Chabot*, the IRS issued summonses to the taxpayers to give testimony and produce documents relating to their foreign bank accounts for the 2006 through 2009 tax years, which it then amended and narrowed to foreign bank account documents required to be kept under 31 C.F.R. § 1010.420.<sup>59</sup> The taxpayers did not comply with the summons, claiming that doing so might subject them to prosecution for failing to provide this information in annual Report of Foreign Bank and Financial Account filings. They also claimed that the required records exception to the Fifth Amendment privilege should not apply to their case.<sup>60</sup> The district court found that the required records exception applied and granted the government’s petition to enforce the summons. On appeal, the court found that the required records exception trumped the taxpayers’ Fifth Amendment privilege claim and affirmed the district court’s granting of the Government’s petition to enforce the summons.<sup>61</sup>

In a similar case, *United States v. Chen*, the First Circuit held that foreign banking records required to be kept under the Bank Secrecy Act fell within the required records exception to the Fifth Amendment privilege and thus were subject to the summonses.<sup>62</sup> However, with respect to other documents for which

53 *Haber v. U.S.*, 823 F.3d 746 (2d Cir. 2016), *aff’g* 115 A.F.T.R.2d (RIA) 2221 (S.D.N.Y. 2015).

54 *Id.*

55 *Id.* The court also dismissed the taxpayer’s contention that the IRS’s issuance of the summons was improper because a Department of Justice referral was in effect under IRC § 7602(d) and that the taxpayer was entitled to jurisdictional discovery.

56 *Maehr v. Comm’r*, 641 F. App’x 813 (10th Cir. 2016), *aff’g* 116 A.F.T.R.2d (RIA) 5398 (D. Colo. 2015).

57 *Id.* The appellate court noted that it was affirming the decision of the district court but for a different reason. The court stated that the district court had found that it lacked subject matter jurisdiction because the taxpayer’s motion to quash was not brought timely under IRC § 7609(b)(2), which requires a taxpayer to bring suit within 20 days after the IRS gives notice. However, the appellate court emphasized that the taxpayer was not entitled to notice in the first place but reached the same result as the district court.

58 *U.S. v. Chabot*, 793 F.3d 338 (3d Cir. 2015), *aff’g* 114 A.F.T.R.2d (RIA) 6235 (D.N.J.), *cert. denied*, 136 S. Ct. 559 (2015); *U.S. v. Chen*, 815 F.3d 72 (1st Cir. 2016), *aff’g in part, vacating in part, and remanding* 952 F.Supp.2d 321 (D.Mass. 2013).

59 *U.S. v. Chabot*, 793 F.3d 338 (3d Cir. 2015), *aff’g* 114 A.F.T.R.2d (RIA) 6235 (D.N.J.), *cert. denied*, 136 S. Ct. 559 (2015).

60 The required records exception to the Fifth Amendment privilege against self-incrimination excludes from the protection of the privilege certain records that an individual is required by law to keep.

61 *Id.*

62 *U.S. v. Chen*, 815 F.3d 72 (1st Cir. 2016), *aff’g in part, vacating in part, and remanding* 952 F.Supp.2d 321 (D.Mass. 2013).



the taxpayer had claimed Fifth Amendment privilege, the court vacated the decision of the district court and remanded the case because the district court had not provided an explanation of why it had denied the taxpayer's privilege claims.<sup>63</sup>

However, taxpayers were in some cases successful in asserting privileges. For example, as discussed above, in *United States v. Lamotte*, the IRS issued two summonses to Mr. Lamotte, one seeking documents and the other testimony relating to the taxpayer's utilization of a captive insurance tax structure.<sup>64</sup> As noted earlier, the court found that the IRS already had possession of the documents it sought and was therefore not entitled to a summons enforcement order with respect to the summons seeking documents.<sup>65</sup> Moreover, with respect to the IRS summons for Mr. Lamotte's testimony, the court found that he had properly invoked his Fifth Amendment privilege against self incrimination, as "the incriminating nature of the testimony sought by the government is evident on its face."<sup>66</sup>

### Civil Contempt

A taxpayer who "neglects or refuses to obey" an IRS summons may be held in civil contempt.<sup>67</sup> This year, six taxpayers were held in civil contempt for failing to comply with a court order enforcing an IRS summons.<sup>68</sup> Overall, contempt proceedings accounted for approximately seven percent of all summons-related cases. Unless the taxpayers complied with the court order, they were subject to arrest,<sup>69</sup> fines,<sup>70</sup> or both.<sup>71</sup>

### The Clarke Case Revisited

The *Clarke* litigation continues as the taxpayers maintained their litigation push for an evidentiary hearing after the Supreme Court's 2014 decision that set the standard for obtaining such a hearing.<sup>72</sup> After that decision, the case was remanded to the District Court for the Southern District of Florida, which denied the taxpayers' request for an evidentiary hearing and enforced the summons. On appeal, the Eleventh Circuit affirmed, holding that the fact that the summoned information might assist the IRS in preparing

63 *U.S. v. Chen*, 815 F.3d 72 (1st Cir. 2016), *aff'g in part, vacating in part, and remanding* 952 F.Supp.2d 321 (D.Mass. 2013).

64 *U.S. v. Lamotte*, 117 A.F.T.R.2d (RIA) 1725 (D. Mass. 2016), *adopting* 117 A.F.T.R.2d (RIA) 1718 (D. Mass. 2016), *appeal dismissed*, No. 16-1940 (1st Cir. August 2, 2016).

65 *Id.*

66 *Id.*, *adopting* 117 A.F.T.R.2d (RIA) 1718 (D. Mass. 2016), *appeal dismissed*, No. 16-1940 (1st Cir. August 2, 2016). In another case involving privilege, *Schaeffler v. U.S.*, 806 F.3d 34 (2d Cir. 2015), *vacating and remanding* 22 F. Supp. 3d 319 (S.D.N.Y. 2014), *dismissed as moot*, 117 A.F.T.R.2d (RIA) 2139 (S.D.N.Y. 2016), the Second Circuit found that the taxpayer had not waived the attorney-client privilege by sharing documents with a consortium of banks that had common legal interest with the taxpayer. The court also found that the work-product doctrine protected documents prepared at a time when the taxpayer believed that litigation was highly probable. However, the IRS subsequently withdrew the summons and the district court dismissed the case as moot.

67 IRC § 7604(b).

68 See *U.S. v. Anderson*, 117 A.F.T.R.2d (RIA) 1174 (N.D. Cal. 2016); *U.S. v. Belcik*, 117 A.F.T.R.2d (RIA) 926 (M.D. Fla. 2016), *adopting in part* 117 A.F.T.R.2d (RIA) 922 (M.D. Fla. 2016); *U.S. v. Butler*, 2016 U.S. Dist. LEXIS 59179 (W.D. Ky. 2016); *U.S. v. Singh*, 117 A.F.T.R.2d (RIA) 1069 (E.D. Cal. 2016), *enforcing* 116 A.F.T.R.2d (RIA) 5313 (E.D. Cal. 2015); *U.S. v. Soong*, 116 A.F.T.R.2d 5792 (N.D. Cal. 2015), *granting motion for civil contempt sanctions*, 113 A.F.T.R.2d (RIA) 1589 (N.D. Cal. 2014), *aff'd by* 117 A.F.T.R.2d (RIA) 1801 (9th Cir. 2016); *U.S. v. Thornton*, 621 F. App'x. 360 (8th Cir. 2015), *aff'g* 115 A.F.T.R.2d (RIA) 1258 (D. Minn. 2015), *cert. denied*, 136 S. Ct. 2424 (2016).

69 *U.S. v. Belcik*, 117 A.F.T.R.2d (RIA) 926 (M.D. Fla. 2016), *adopting in part* 117 A.F.T.R.2d (RIA) 922 (M.D. Fla. 2016).

70 *U.S. v. Soong*, 116 A.F.T.R.2d 5792 (N.D. Cal. 2015), *granting motion for civil contempt sanctions*, 113 A.F.T.R.2d (RIA) 1589 (N.D. Cal. 2014), *aff'd by* 117 A.F.T.R.2d (RIA) 1801 (9th Cir. 2016).

71 *U.S. v. Butler*, 2016 U.S. Dist. LEXIS 59179 (W.D. Ky. 2016).

72 *U.S. v. Clarke*, 816 F. 3d 1310 (11th Cir. 2016), *aff'g* 115 A.F.T.R.2d (RIA) 836 (S.D. Fla. 2015), *on remand from* 573 F. App'x 826 (11th Cir. 2014), *on remand from* 134 S. Ct. 2361 (2014), *vacating and remanding* 517 F. App'x 689 (11th Cir. 2013), *petition for cert. filed*, No. 16-358 (Sept. 19, 2016).



for tax court litigation did not make its motive improper, that the district court did not abuse its discretion by opting not to hold a status conference or permit additional evidence before determining if the IRS's motive was improper, and that the taxpayers' allegations failed to point to the IRS's bad faith or improper motive.<sup>73</sup> The taxpayers have once again petitioned for *certiorari*.<sup>74</sup>

### The Continued Impact of *United States v. Clarke* and *Microsoft* Litigation

The Supreme Court's decision in *Clarke* continued to have an impact on summons litigation, as taxpayers sought evidentiary hearings to challenge a summons. Most of these efforts were unsuccessful.<sup>75</sup> However, as discussed in this section last year, in *United States v. Microsoft*, Microsoft Corporation was successful in obtaining an evidentiary hearing in a summons enforcement case where the IRS used an outside law firm to assist in an audit of the company.<sup>76</sup> In that case, the court found that, by asserting that the IRS was improperly delegating an inherently governmental function to a third party, Microsoft had met its burden under *Clarke* and was entitled to an evidentiary hearing.<sup>77</sup>

While Microsoft was successful in obtaining an evidentiary hearing, the IRS was ultimately successful in having the summons enforced.<sup>78</sup> In an opinion subsequent to the one granting the evidentiary hearing, although the court was "troubled" by the level of the outside law firm's involvement in the audit of the taxpayer, it concluded that this delegation of authority was not legally prohibited by IRC § 7602 and therefore granted the IRS's petition to enforce the summons.<sup>79</sup>

Finally, as noted earlier, the IRS issued final regulations in July 2016 providing that outside parties with whom the IRS or the Office of Chief Counsel contracts for services — such as economists, engineers, consultants, or attorneys — may receive books papers, records, or other data summoned by the IRS and, in the presence of an IRS officer or employee, participate fully in the interview of a person who the IRS has summoned as a witness to provide testimony under oath.<sup>80</sup> Also of note is that members of both the House and Senate have introduced legislation that would prohibit individuals who are not IRS employees from receiving summoned records or taking summoned testimony.<sup>81</sup>

73 *U.S. v. Clarke*, 816 F.3d 1310 (11th Cir. 2016), *aff'g* 115 A.F.T.R.2d (RIA) 836 (S.D. Fla. 2015), *on remand from* 573 F. App'x 826 (11th Cir. 2014), *on remand from* 134 S. Ct. 2361 (2014), *vacating and remanding* 517 F. App'x 689 (11th Cir. 2013), *petition for cert. filed*, No. 16-358 (Sept. 19, 2016).

74 *Id.*

75 See, e.g., *Highland Capital Mgmt., L.P. v. U.S.*, 626 F. App'x 324 (2d Cir. 2015), *aff'g in part, vacating in part, and remanding in part* 51 F. Supp. 3d 544 (S.D.N.Y. 2014); *Gangi v. U.S.*, 638 F. App'x 16 (1st Cir. 2016), *aff'g* 2 F.Supp.3d 12 (D.Mass. 2014).

76 See National Taxpayer Advocate 2015 Annual Report to Congress 471; *U.S. v. Microsoft Corp.*, 115 A.F.T.R.2d (RIA) 2186 (W.D. Wash. 2015).

77 *U.S. v. Microsoft Corp.*, 115 A.F.T.R.2d (RIA) 2186 (W.D. Wash. 2015).

78 *U.S. v. Microsoft Corp.*, 154 F.Supp.3d 1134 (W.D. Wash. 2015).

79 *Id.* However, it appears that this litigation may not be over as Microsoft has withheld documents due to privilege claims. See *Microsoft Withholding Documents in IRS Summons Enforcement Case*, TAX NOTES TODAY (Sep. 14, 2016).

80 See Treas. Reg. § 301.7602-1(b)(3).

81 See Tax Administration Integrity Act, H.R. 3167, § 2, 114th Cong. (2015); Taxpayer Protection Act of 2016, S. 3156, § 135, 114th Cong. (2016).

## CONCLUSION

The IRS may issue a summons to obtain information to determine whether a tax return is correct or if a return should have been filed to ascertain a taxpayer's tax liability or to collect a liability.<sup>82</sup> Accordingly, the IRS may request documents and testimony from taxpayers who have failed to provide that information voluntarily.

Summons enforcement continues to be a significant source of litigation and the number of litigated cases rose slightly from last year. The IRS also continues to be successful in the vast majority of summons enforcement litigation. Taxpayers and third parties rarely succeed in contesting IRS summonses due to the significant burden of proof and strict procedural requirements.

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<sup>82</sup> IRC § 7602(a).