

## CLIENT ALERT

### Ninth Circuit Holds IRS Failed to Provide "Reasonable Notice" in Third-Party Summons Case

Mar.18.2019

The Internal Revenue Code requires that the IRS notify taxpayers before contacting third parties. The IRS has interpreted this requirement to mean that a general notice to a taxpayer that it may contact third parties, without providing any specific information regarding the third parties in question, complies with the Code. While district courts are split as to whether more specific notice is required, the Ninth Circuit recently held that the IRS is required to give taxpayers specific notice of a third-party summons that identifies the third party. The Ninth Circuit reasoned that, by providing a taxpayer more specific notice, the taxpayer may have the opportunity to produce the documents or information to the IRS itself, thereby obviating the need for a third-party summons that could harm the taxpayer's "reputational interest."

In *J.B. v. United States*, No. 16-15999, 2019 WL 923717 (9th Cir. Feb. 26, 2019), an elderly California couple was selected for random audit by the IRS. At the beginning of the audit, the taxpayer received a letter from the IRS informing them of the audit and instructing them to contact the IRS regarding their tax return and the examination process. Enclosed with the mailing was IRS Publication 1, which states that, in the course of an examination, the IRS may need to obtain information from third parties that the taxpayer has not provided or verify information the IRS has received. Two years after the initial correspondence, the IRS issued a summons to the California Supreme Court requesting documents regarding payments to the taxpayer during the tax year under audit. The payments were related to the taxpayer's representation of indigent criminal defendants in cases where he was appointed as counsel by the California Supreme Court. The IRS did not inform the taxpayer that it was issuing the third-party summons. In fact, the taxpayer only learned of the summons when his daughter, who was also his personal representative, received a notice of service of the summons in the mail. The taxpayer then moved to quash the summons.

To evaluate the taxpayer's petition to quash, the U.S. District Court looked to *Powell v. United States*, 379 U.S. 48 (1964), which sets forth what the IRS must prove in order to enforce a summons: (1) the underlying investigation is for a legitimate purpose, (2) the inquiry requested is relevant to that purpose, (3) the information sought is not already in the government's possession, and (4) the IRS followed the administrative requirements of the Internal Revenue Code. If the IRS does not meet all four of the *Powell* requirements, the court may quash the summons.

In *J.B.*, the U.S. District Court found that, although the IRS was able to show that the first three *Powell* elements were met, the IRS could not show it had met the fourth element. At issue was the administrative requirement under Section 7602(c)(1), which provides:

An officer or employee of the Internal Revenue Service may not contact any person other than the taxpayer with respect to the determination or collection of the tax liability of such taxpayer **without providing reasonable notice in advance to the taxpayer** that contacts with persons other than the taxpayer may be made.

I.R.C. § 7602(c)(1)(emphasis added).

The Ninth Circuit held that, by enacting Section 7602(c)(1), Congress intended for the advance notice provision to provide the taxpayer with a meaningful opportunity to produce information to avoid third-party contacts. The court held that the IRS's mailing of the introductory letter and IRS Publication 1 did not provide such an opportunity because it did not specifically identify who the IRS planned to contact or the documents that it planned to request.

While "reasonable notice" may differ based on the specific facts of each case, in future cases (at least in the Ninth Circuit) the IRS will need to provide more than a generic notice to taxpayers prior to making third-party contacts. It is unclear whether the IRS will change its policy nationwide regarding the notice it provides taxpayers of third-party summonses, or will limit such a change to the states in the Ninth Circuit. To the extent the IRS attempts to limit compliance to the Ninth Circuit, it is likely that taxpayers in other states will file motions to quash citing the *J.B.* decision.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

**Robert L. Willmore**

Partner – Washington, D.C.  
Phone: +1 202.624.2915  
Email: [rwillmore@crowell.com](mailto:rwillmore@crowell.com)

**Carina C. Federico**

Associate – Washington, D.C.  
Phone: +1 202.654.6712  
Email: [cfederico@crowell.com](mailto:cfederico@crowell.com)