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Information Reporting

In the second installment of a series of articles on U.S. persons' foreign accounts, Stephen Dunn of Dunn Counsel looks at how the IRS has used "John Doe" summonses to gain information regarding U.S. account holders, examining the evolution of cases involving UBS AG, the Stanford Group Cos. and Sovereign Management & Legal Ltd. The latest case "is troubling for what it portends—John Doe summonses issued to U.S. telecommunications companies, e-mail servers, etc. seeking the identity of their U.S. customers who have communicated with an organization like Sovereign Management, or with a foreign financial institution," he writes.

The Use of 'John Doe' Summonses in Identifying U.S. Persons' Accounts

By STEPHEN J. DUNN

The first article in this series examined the status of intergovernmental exchange agreements in identifying U.S. persons' foreign accounts.¹ This article addresses another, more expeditious, weapon available to the Internal Revenue Service in identifying U.S. persons' noncompliant foreign accounts—"John Doe" summonses.

'John Doe' Summonses

Internal Revenue Code Section 7602(a) empowers the IRS to summon persons to appear and produce

¹ Dunn, "Status of Intergovernmental Information Sharing Concerning U.S. Persons' Foreign Financial Accounts," (211 DTR J-1, 11/2/15).

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books and records and give testimony as may be relevant in determining a person's tax liability.

If the IRS issues a summons for the giving of testimony or the production of records with respect to a taxpayer other than the person to whom the summons is issued, i.e., a "third-party" summons, then, under I.R.C. Section 7609(a)(1), the IRS must provide notice of the summons to the taxpayer who is the target of the summons.

The notice must be given within three days after the summons is served, and not later than the 23rd day before the day fixed in the summons as the day upon which the summoned records are to be examined.² Within 20 days after the target is served with notice of the summons, the target may move in U.S. District Court to quash the summons. In any such proceeding, the IRS may seek to compel compliance with the summons.³

² The notice may be delivered to the taxpayer in person or mailed to him at his or her last known address or, if the Service is on I.R.C. Section 6903 notice of a fiduciary relationship concerning the taxpayer, mailed to the fiduciary's last known address. I.R.C. Section 7609(a)(2).

³ I.R.C. Section 7609(b)(2)(A). In *United States v. Powell*, 379 U.S. 48 (1964), the Supreme Court held that, in a summons enforcement proceeding, the IRS must prove the following: (1) that the investigation will be conducted pursuant to a legitimate purpose, (2) that the inquiry may be relevant to the purpose, (3) that the information sought isn't already within the

If the IRS issues a summons endeavoring to ascertain the identities of taxpayers, it isn't possible to give such taxpayers notice of the summons. Under I.R.C. Section 7609(f), the IRS may serve such a John Doe summons only after a court proceeding in which the Service establishes that:

- the summons relates to the investigation of a particular person or ascertainable group or class of persons,
- there is a reasonable basis for believing that such person or group or class of persons may fail or may have failed to comply with any provision of any internal revenue law, and
- the information sought to be obtained from the examination of the records or testimony (and the identity of the person or persons with respect to whose liability the summons is issued) isn't readily available from other sources.

The U.S. District Court for the district within which the person to be summoned resides or may be found has jurisdiction to hear and determine a proceeding for service of a John Doe summons under I.R.C. Section 7609(f).⁴ Such proceedings are necessarily *ex parte*, and made solely on petition and affidavit(s).⁵

If the IRS issues a summons endeavoring to ascertain the identities of taxpayers, it isn't possible to give such taxpayers notice of the summons.

If the court grants a petition for issuance of a John Doe summons under I.R.C. Section 7609(f), then the statute of limitations on assessment or collection of tax with respect to the taxpayer under I.R.C. Section 6501(a) and on prosecution of the taxpayer under I.R.C. Section 6531 is suspended:

- beginning on the date that is six months after service of such summons, and
- ending with final resolution of such response.⁶

UBS AG

UBS AG private bankers and managers had counseled U.S. taxpayers to create accounts in the names of offshore nominee companies, which the U.S. taxpayers

commissioner's possession, and (4) that the administrative steps required by the code have been followed.

The Supreme Court added that the burden of showing abuse of the court's process in a summons enforcement proceeding is upon the taxpayer, and that such burden isn't met by merely showing, as Powell did, that the period for assessing a deficiency had run, or that the records in question had already been once examined. 379 U.S. at 57-58.

⁴ I.R.C. Section 7609(h)(1).

⁵ I.R.C. Section 7609(h)(2).

⁶ I.R.C. Section 7609(e)(2).

used to engage in securities trades and other financial transactions without reporting the income from such transactions on their U.S. income tax return.

The UBS private bankers and managers had accepted and included in UBS's account records IRS Forms W-8BEN, Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding, (or UBS substitute forms) provided by directors of the offshore companies that represented under penalty of perjury that the nominee companies were the beneficial owners of the assets in the UBS accounts. But in many cases U.S. taxpayers beneficially owned the accounts, controlling the accounts and distributions therefrom for their benefit. The U.S. taxpayers thus used the accounts to perpetrate a large-scale evasion of U.S. income tax.

UBS entered into a deferred prosecution agreement with the U.S. in which it agreed, among other things, to cease such banking practices, pay the U.S. \$780 million in penalties, and disclose certain U.S. account holders' identities and account information. The deferred prosecution agreement doesn't provide protection from prosecution for any crime other than those set forth in the agreement. Nor does it protect any person other than UBS from prosecution.

The U.S. on June 30, 2008, filed in the U.S. District Court for the Southern District of Florida, Miami, a petition to serve a "John Doe" summons upon UBS.⁷ The petition averred that UBS "is found" at an office in Miami.

The John Doe summons sought the identity and certain account documents of accounts of U.S. taxpayers, who at any time during the years ended Dec. 31, 2002, through Dec. 31, 2007, had signature or other authority (including authority to withdraw funds; to make investment decisions; to receive account statements, trade confirmations or other account information; or to receive advice or solicitations) with respect to any financial accounts maintained at, monitored by or managed through any office in Switzerland of UBS AG or its subsidiaries or affiliates and for whom UBS AG or its subsidiaries or affiliates:

- didn't have in its possession Forms W-9, Request for Taxpayer Identification Number and Certification, executed by such U.S. taxpayers; and
- hadn't filed timely and accurate Forms 1099 naming such U.S. taxpayers and reporting to U.S. taxing authorities all reportable payments made to such U.S. taxpayers.⁸

The petition was granted.

The Stanford Group Cos.

The Stanford Group Cos. perpetrated a massive Ponzi scheme. Stanford International Bank Ltd. attracted billions in deposits to its Latin American branches by offering exorbitant rates of return. The U.S. Securities and Exchange Commission prosecuted Stanford Group principals, and had a receiver with offices in Dallas appointed for Stanford Group Cos.' as-

⁷ *In re Tax Liabilities of John Does*, No. 08-21864-MC-Lenard/Garber (S.D. Fla. 2008).

⁸ *In re Tax Liabilities of John Does*, No. 08-21864-MC-Lenard/Garber, John Doe Summons at pg. 1 (S.D. Fla. 2008).

sets and records. The Stanford Group Cos.' assets were ordered frozen.

Believing that U.S. clients of the Stanford Group had failed to report the income from their Stanford accounts on their U.S. income tax returns, the IRS filed an ex parte petition with the U.S. District Court for the Northern District of Texas, Dallas, for leave to serve a John Doe summons on the receiver of the Stanford companies' assets and records.⁹

The summons sought the identities of the U.S. persons who, at any time during the years ended Dec. 31, 2002, through Dec. 31, 2008, had signature authority over an account at Stanford International Bank Ltd., or a beneficial ownership interest in an account at Stanford International Bank Ltd., directly or through a corporation, trust, foundation or other entity formed by or managed through Stanford Trust (Antigua).

The petition was granted.

"Final resolution" of a response to a John Doe summons under I.R.C. Section 7609(e)(2) is a vague term. Immediately following this article is a letter from IRS counsel declaring the response to the John Doe summons issued to the receiver of the Stanford Group Cos. to have been "finally resolved under I.R.C. Section 7609(e)(2)" as of the date of issuance of the letter, Nov. 7, 2012.

The John Doe summons had been served on the receiver on Dec. 9, 2009. Taking the letter at face value, under I.R.C. Section 7609(e)(2), the statute of limitations on assessment or collection of tax with respect to the taxpayer under I.R.C. Section 6501(a) and on prosecution of the taxpayer under I.R.C. Section 6531 was suspended from June 6, 2010, until Nov. 7, 2012.¹⁰

Sovereign Management & Legal Ltd.

Sovereign Management & Legal Ltd. facilitated the use of foreign accounts to evade U.S. income tax. It formed anonymous offshore corporations and foundations for U.S. taxpayers in Panama, and arranged for

⁹ See *In re Tax Liabilities of John Does*, No. 3:09-CV-2290-N (N.D. Tex. 2009).

¹⁰ A taxpayer could examine the factual basis for and challenge the assertion made in such a letter as to the "final resolution" date of the government's response to a John Doe summons.

foreign directors of them. It provided professional managers who appointed themselves as directors of its clients' offshore corporations. It arranged for transfer of funds from U.S. clients to foreign accounts by courier deliveries and wire transfers. It arranged for anonymous debit cards for repatriation of funds from foreign accounts.

In the most ingenious use of John Doe summons authority yet, the U.S. petitioned the U.S. District Court for leave to serve John Doe summonses on Federal Express Corp., FedEx Ground Package System Inc., DHL Express, United Parcel Service Inc., Western Union Financial Services Inc., the Federal Reserve Bank of New York, Clearing House Payments Co. LLC and HSBC Bank USA National Association for the identities of U.S. persons for whom such entities had processed transactions with Sovereign Management & Legal Ltd.

The petition for leave to serve John Doe summonses in the Sovereign Management case didn't make any jurisdictional allegations. But surely FedEx Corp., FedEx Ground, DHL Express, UPS, Western Union, the Federal Reserve Bank, Clearing House Payments and HSBC Bank each has a place of business in the Southern District of New York.

The petition was granted.¹¹

The Sovereign Management case is troubling for what it portends—John Doe summonses issued to U.S. telecommunications companies, e-mail servers, etc. seeking the identity of their U.S. customers who have communicated with an organization like Sovereign Management, or with a foreign financial institution.

John Doe summonses are an important weapon available to the IRS in identifying U.S. persons' noncompliant foreign accounts. Given the weapons available to the IRS in identifying U.S. persons' foreign accounts—intergovernmental information exchange agreements and John Doe summonses are prominent among them—it is perilous for U.S. persons who have or had foreign financial accounts to fail to comply with U.S. law concerning them.

The next article in this series will consider beneficial ownership of a foreign account, an elusive yet pivotal concept.

¹¹ *In re Tax Liabilities of John Does*, No. 1-14-mc-00417 (S.D.N.Y. 2014).

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Subject: In the Matter of the Tax Liability of: John Does,
Case No. 3-09-cv-00290-N
United States District Court for the Northern District of Texas,
Dallas Division

Dear Mr. Sadler:

I am writing to acknowledge that Ralph S. Janvey, as Receiver of the assets and records of Stanford Group Company and related entities, has fully complied with the Internal Revenue Summons served on him on December 9, 2009. As of the date of this letter, we consider the response to the summons finally resolved under I.R.C. §7609(e)(2). We greatly appreciate the cooperation of Mr. Janvey and your firm as counsel in arranging the production of records responsive to the summons.

Sincerely,

A handwritten signature in black ink that reads "John C. McDougal".

John C. McDougal
Special Trial Attorney

Cc: Revenue Agent Cheryl Kiger
Manuel J. Lena, U.S. Department of Justice Tax Division