J. EDGAR MURDOCK INN OF COURT

Tuesday, April 14, 2015

International Statute of Limitations Issues

**SCENE 1: Gathering Evidence**

Participants: Senior Partner (SP), Junior Associate (JA), Taxpayer (T)

(Setting is conference room in law firm. The three enter into the room.)

**SP**: T, I don’t believe you’ve met my new associate, Junior Associate. He/she started last month – just joined us from IRS Chief Counsel. Junior Associate, this is Taxpayer (they say hello, shake hands).

Junior Associate has been doing some research on your tax case, and I thought we’d take this opportunity to bring you up to speed.

**T**: Thanks, Senior Partner. It has been a few months since we last spoke. I believe we all agreed at that time my offshore businesses and bank accounts are none of the IRS’s business. (JA shoots SP a worried look).

It is the Government’s own fault that I have to have such complicated financial structures. The United States needs to be more business-friendly if it wants American businesses to return to America. At this point, I don’t know anyone in business that doesn’t have some interest in an offshore bank account!

**SP**: Unfortunately for you, the IRS has made your offshore activity their business. Moreover, T, I believe what we discussed at the last meeting were your “business reasons” for forming the offshore insurance company: Why Bermuda was the best place to form it, and once you were in Bermuda, that you discovered a real business need for a convenient banking facility, and then how you discovered that that bank was not only convenient for you, but for other businessmen too, so that you began to “grow” that “business.”

I advised then and advise you now, we should do all that we can to keep the lines of communication with the Government open. There are negative consequences to not providing the IRS with the information it seeks.

**T**: Negative consequences from WITHHOLDING information from the Government? I would have thought there would be negative consequences by GIVING them the information *(T breaks out of character and looks to audience)*, because IRS cannot tax what it does not know.

**SP**: Let me turn it over to Junior Associate to give you an overview of the issues we’re here to discuss. They involve certain actions, and failures to act, that could put you at a disadvantage concerning future controversy with the IRS. Junior Associate?

**JA***: (Stands, squares shoulders, clears throat.)*

**T***: (Unnerved)* Gee! Should I stand too?

**SP:** Certainly not. Sit down, JA. We’re not in court.

**JA**: *(looks sheepish, and takes a seat.)* First, we want to be sensitive to the Government’s requests for information and documents relating to the offshore insurance company and bank. If we are not responsive to the requests, the Government may feel the need to take additional measures.

**T**: Define “sensitive.” And define “responsive.” The IRS is the one that should be sensitive! I must have answered 20 questions already.

**SP**: What JA is trying to say is that the Government does have other options. The Government does not agree that you have answered – at least not fully – all of the questions it has asked. Let’s discuss that formal document request you recently received that resembled the prior IDR concerning the offshore insurance company and your offshore bank account.

**T**: Again, I don’t see how that is any of the Government’s business. I have been doing business in Bermuda for years. Isn’t it too late for the IRS to start investigating this? And anyway, Bermuda had strict secrecy laws. I cannot give the IRS all of this information without violating the laws of my haven … I mean host country.

I want to challenge this formal document request for foreign documents. I’ve given them the documents that I want to give them, and I’m pretty confident that they won’t be able to get those other documents any other way.

**SP**: T, we understand your frustration, but nonetheless recommend

a more practical approach.

**JA**: Under section 982 of the Internal Revenue Code, the Government may make what they call a Formal Document Request, which seeks foreign-based records, requiring a complete response from a taxpayer within 90 days. If the taxpayer does not provide the response, the taxpayer will be prohibited from using ANY foreign-based documents that are part of that request. This means that if you don’t give the information to the Government now, you won’t be able to use it later. In other words, you can’t only give the Government the documents that you want them to see, because the consequence for not complying is that you cannot use the documents that you do want them to see.

And you said earlier that you want to hold the IRS’s feet to the fire when it comes to acting within the statute of limitations. If we challenge the Formal Document Request in court, that may have the effect of extending the statute of limitations.

**T**: What do you mean by “Formal Document Request”? It not like the first 20 requests were made casually. Do you remember how those requests included a three-page rider of instructions directing me to provide “any and all” documents from emails to post-its. If that was an *informal* request, I hate to think what a formal document request will look like.

**JA**: I get what you’re saying. But, unlike the previous “informal” requests, the formal request will be sent to you by certified or registered mail and will spell out why your prior responses were insufficient. It will also warn you of the consequences of failing to respond to the Formal Document Request.

**T**: Well, some of the stuff they are asking for has nothing to do with my tax position, they shouldn’t care about those documents.

**SP**: This is where the sensitivity comes in. The specifics of the insurance contracts may indeed affect your tax liability – for example, if the Government takes the position that some or all of the coverages are not “insurance” for federal tax purposes.

**T**: You’ve got to be kidding. An IRS agent is going to tell me what I need insurance for? What am I supposed to do? You can’t get coverage for things like alien-invasion-business-interruption on the domestic commercial market!

**SP**: Again, the point is that we need to carefully review this request and get it answered so we can be sure we will be able to use the documentation that supports your position when we need it.

**T**: Fair enough. I’ll do some work on that response over the weekend. Frankly, I don’t see why they are asking me anyway. We know that the Government filed a bunch of John Doe summonses - one of my former clients tried to squash one!

**SP**: Yes, someone filed a petition to quash, and the proceeding is still ongoing. (Turns to JA.)

**JA**: That throws another monkey wrench into the IRS’s statute of limitations. Under section 7609(e), the petition to quash the John Doe summons tolls the statute of limitations for both civil and criminal actions during the time that the John Doe proceeding is pending, including any appeal.

**T**: Why do I care? That case was filed by my **former** client.

**JA**: You care because some of the information sought in the summons also affects your tax liability. If the summons is not quashed, and it appears that it will not be, the statute of limitations under section 6501 (which relates to civil assessment and collection) and 6531 (which relates to criminal prosecutions) are suspended vis a vis your potential liability and remain so until the final resolution. This is because more than six months have elapsed since the summons was served, and there has been no response.

**T**: I guess this is bad news for me, but good news for you folks. You can keep churning fees, while I keep looking over my shoulder. You have said the word “criminal” twice. I’m just a businessman, and that word makes me a little nervous. Is there anything else I should know?

**SP**: Well, to the extent that you are worried about the statute of limitations, you need to remember that not only does the Government have a longer time, in most circumstances, to begin a criminal case, there are sometimes situations where that longer limitations period may be extended without you even knowing about it.

**TP:** Like some sort of Star Chamber?

**SP:** More like a grand jury. It’s possible that the Government has attempted to obtain certain records concerning the offshore bank from the foreign government. Based on feedback we’ve gotten from other clients with offshore banks in Bermuda, it appears the Government has routinely been pursuing information through its criminal mutual legal assistance treaty with Bermuda, so the Government could wind up with this information anyway. In those cases, Section 3292 of Title 18, which is not the Internal Revenue Code but the general criminal title of the U.S. Code, allows the Government to file an uncontested motion, under seal, with the district or magistrate judge overseeing a grand jury to extend a criminal limitations period for as many as three years.

We suggest to you that it is to your advantage to provide the information, now, to the civil revenue agent who is requesting the information.

Possible questions:

1. **Has anyone in the audience had first-hand experience with a formal document request under section 982?** 
   1. There do not appear to be any [recent] reported cases. Has anyone encountered a Formal Document Request in an audit?
2. **What if the taxpayer to whom the formal document request is issued is prohibited under foreign law—for instance, under a “blocking” statute or EU-style data protection law—from producing the documents in the course of an IRS examination?**
   1. Subsection (b) of section 982 provides a reasonable cause exception for non-compliance; however, subsection (c) provides that the fact that a foreign non-disclosure law would impose civil or criminal liability on the taxpayer (or any other person) is *not* reasonable cause.
   2. Although foreign authorities in the past rarely enforced blocking statutes, there are indications that enforcement is being stepped up in some jurisdictions. This potentially puts Taxpayer between the proverbial “rock and a hard place,” as the blocking statutes carry potential civil and criminal liability, including imprisonment.
3. **In Europe, so-called “data protection” laws enable parties whose personal data is contained in documents to object to their disclosure to foreign authorities like the IRS or U.S. DoJ. As a result, documents are often produced in redacted form until the objections are litigated in the local jurisdiction. What if, in such a circumstance, the Taxpayer lost the data protection case and did not unredact the documents? Should section 982 apply? Does it matter whether the redacted information is relevant to the tax liability?**
4. **As Junior Associate alludes to, the limitations periods with respect to Taxpayer’s potential civil and criminal liability will be tolled under subsection (e)(2) of section 7609 in the absence of “resolution” of the summoned party’s response to the summons six months after the service of such summons. Under the language of statute, the periods are tolled until the “final resolution of such response.” Does anyone see any practical problems in determining whether or when there has been a “resolution” of the summoned party’s response to the summons?** 
   1. Rather defining the tolling period as ending upon the “resolution” or “final resolution,” the preceding subsection (i.e., (e)(1)) refers to the period during which the statute of limitations is tolled as consisting of “the period during which a proceeding, and appeals therein, with respect to the enforcement of such summons is pending.”
   2. Does the use of different language in subsection (e)(2) suggest that “resolution” or “final resolution” could occur earlier than a final, non-appealable judgment or order?