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December 20, 2004

**BY OVERNIGHT MAIL**

Hon. Chester J. Straub
United States Court of Appeals for the Second Circuit
1702 United States Courthouse
40 Foley Square
New York, New York 10007

RE: Schulz v. IRS
Docket No. 04-0196-cv

Dear Judge Straub:

As directed by the Court, the government submits this letter memorandum in response to three questions raised at the conclusion of oral argument on December 13, 2004. I have consulted regarding the content of this letter memorandum with the regional office of the Internal Revenue Service, Office of District Counsel, in New York City, and it remains the government's position that the district court correctly determined that it lacked jurisdiction over petitioner-appellant Schulz' action seeking to quash the administrative summonses on various bases prior to the initiation of enforcement action by the IRS.

The specific questions raised by the Court, and the government's responses, are as follows:

1. Is the taxpayer under compunction to comply with an IRS administrative summons?

While the IRS certainly maintains that a taxpayer is required to comply with a properly served administrative summons, this obligation is not self-enforcing. *See, e.g., Hudson Valley Black Press v. IRS*, 307 F. Supp. 2d 543, 546 n.5 (S.D.N.Y. 2004) ("A summons issued pursuant to § 7602 is not self-enforcing; if a taxpayer refuses to comply with a summons, the IRS must bring an adversary proceeding in a district court pursuant to § 7604 to enforce it.") (citing *United States v. Powell*, 379 U.S. 48, 58 (1964)). Thus, as indicated in oral argument, the IRS does not have the power to compel the taxpayer to obey an administrative summons without obtaining an order from the proper district court.

2. <u>What does the IRS do when a taxpayer fails to comply with a summons?</u>

When any person refuses or neglects to comply with an administrative summons, the IRS must seek judicial enforcement of the summons by bringing what it refers to as "a summons enforcement action" in district court. In such an action, the IRS can request an order from the court compelling testimony and/or production of relevant or material documents. 26 U.S.C. § 7604(b); *see Powell*, 379 U.S. at 58 ("It is the court's process which is invoked to enforce the administrative summons . . . ."): *Reisman v. Caplin*, 375 U.S. 440, 445-46 (1964) (enforcement action in the district court "would be an adversary proceeding affording a judicial determination of the challenges to the summons and giving complete protection to the witness."). The Internal Revenue Code grants the district court in the district where the person resides or is found jurisdiction to hear a summons enforcement suit initiated by the IRS. 26 U.S.C. §§ 7604(a), 7402(b). In such an action, the government would have the burden of establishing a *prima facie* case for enforcement of the summons, by showing that "(i) a legitimate purpose exists for the investigation, (ii) the summons may be relevant to that purpose, (iii) the information sought is not already in the possession of the government, and (iv) the procedural and administrative steps required by the Code for serving a summons have been followed." *PAA Management, Ltd. v. United States*, 962 F.2d 212, 215 (2d Cir. 1993) (citing *Powell*, 379 U.S. at 57-58). Once that showing has been made, the burden shifts to the party challenging the summons to show that it was issued for an improper purpose, issued in bad faith, or was otherwise deficient. *PAA Management*, 962 F.2d at 215 (citing *Reisman*, 375 U.S. at 449); *see generally United States v. LaSalle National Bank*, 437 U.S. 298, 316 (1977).

Thus, the taxpayer is afforded an opportunity to present challenges to the IRS summons prior to being found in contempt by the district court.[1] Moreover, the IRS indicates that, in the usual case, it seeks to have the information sought in the summons turned over to it. When the court orders the taxpayer to provide this information, but the taxpayer fails to comply with the order, it is the district court, not the IRS, that has the authority to then issue an order of contempt against the non-complying individual. 26 U.S.C. § 7604(b); *Resiman*, 375 U.S. at 450 (concluding that equitable relief is inappropriate because of "the comprehensive procedure of the Code, which provides full opportunity for judicial review before any coercive sanctions may be imposed").

3. <u>What is the impact of Judge Friendly's opinion in *Application of Colton* on the government's position?</u>

*Application of Colton*, 291 F.2d 487 (2d Cir. 1961), was a case with which the undersigned was unfamiliar when it was cited by the Court at oral argument. After reviewing the decision, it does appear to provide that the statutory framework described by the government and in § 7604 of the Code is not the exclusive remedy for challenging an administrative summons. 291 F.2d at 489-90. However, the Court's belief that the district court had jurisdiction over the motion to quash in *Colton* was based on its concern that a taxpayer could be assessed criminal penalties or possibly be found in contempt prior to a judge ordering enforcement of a subpoena. *Id.* This aspect of *Colton* does not survive the Supreme Court's 1964 decision in *Reisman*, which expressly prohibits such

[1] The summons issued to Schulz included IRS Form 2039, which sets forth relevant provisions of the Code, including the jurisdictional provisions of § 7604. A.162.

consequences without prior judicial review where a taxpayer wishes to interpose good faith challenges to an IRS summons. *See Resiman*, 375 U.S. at 447-48. It was on this basis that Judge Friendly himself subsequently recognized that *Reisman* "seems to destroy the basis underlying decisions of this court which authorized applications to vacate such a summons . . . in advance of any judicial proceeding by the Government for their enforcement." *United States v. Kulukundis*, 329 F.2d 197, 199 (1964) (citing, *inter alia*, *Colton* as being "destroy[ed]" by *Reisman*). The IRS District Counsel has confirmed that they believe *Resiman* overturned the jurisdictional holding of *Colton*, and that the district court does not have subject matter jurisdiction over a motion to quash that is filed by a taxpayer prior to the IRS seeking judicial enforcement of a summons.

In this regard, the government notes that, at oral argument, Schulz repeatedly emphasized that he believes this case is controlled by *Reisman*. We agree. The government respectfully submits that, at least since that decision, it has been absolutely clear that district courts do not have jurisdiction to consider a motion to quash such as that at issue herein, unless and until the IRS moves for enforcement in the district court.[2] There is nothing inequitable about this as, if and when that occurs, Schulz will have a full opportunity to raise all of his claims about the alleged impropriety of the summonses. Therefore, the order of the district court should be affirmed.

Respectfully submitted,

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cc: Robert L. Schulz, *pro se*

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[2] In his Reply Brief and at oral argument, Schulz relies upon language from *Reisman* and other cases involving the ability of parties in interest to challenge summonses issued to third-party record keepers, for which an exception to the general rule was created in § 7609(b). The summonses in question here were issued to Schulz himself, so this exception does not apply. *See* 26 U.S.C. § 7609(c)(2)(A).