

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF RHODE ISLAND

CAROL SMITH, CAROL SMITH, LLC and :
CAROL SMITH NEVADA, LLC :
Petitioners, :
v. : MC No. 13-42 S
UNITED STATES OF AMERICA :
Respondent. :

MEMORANDUM AND ORDER

VACATING ORDER QUASHING SUMMONS AND

SETTING FURTHER BRIEFING REGARDING MOTION TO DISMISS

Petitioners Carol Smith, Carol Smith, LLC and Carol Smith Nevada, LLC (collectively “Petitioners”) initiated this federal proceeding by miscellaneous petition to quash a summons issued by the Internal Revenue Service (“IRS”) to the Bank of Newport (“Bank”). The IRS summons requested Petitioners’ account records from the Bank in connection with a collection action against another taxpayer; Petitioners claim that they have no relationship to the taxpayer. Petitioners served the miscellaneous petition on the Bank and the IRS Revenue Officer who issued the summons. After the Bank and the Respondent United States did not object to the petition, this Court granted the relief sought and quashed the summons.

Before the Court is the Motion of the United States to Vacate Order Quashing Summons and to Dismiss Petition to Quash Summons. ECF No. 3. Cognizant that “[e]ven the most dedicated trial judges are bound to overlook meritorious [arguments] without the benefit of an adversary presentation,” Bounds v. Smith, 430 U.S. 817, 826 (1977), the United States’ motion to vacate the order quashing the summons is GRANTED because the United States did not receive adequate notice of the miscellaneous petition.

The United States' motion to dismiss is a more complex matter. This Court's jurisdiction to consider the petition turns on whether Petitioners were entitled to notice of the summons from the IRS pursuant to 26 U.S.C. § 7609(c)(2)(D)(i). The briefing of the parties not only fails to address whether this Court should adopt the rule articulated by the Ninth Circuit in Ip v. United States, 205 F.3d 1168 (9th Cir. 2000), but also fails to provide the Court with factual information regarding the relationship between the Petitioners and the taxpayer sufficient to establish that notice was not required under any view of the correct interpretation of 26 U.S.C. § 7609(c)(2)(D)(i). Accordingly, the Court orders the parties to supplement the briefing to address one or both of these matters.

I. BACKGROUND

On March 4, 2013, the IRS issued the summons to the Bank for Petitioners' account records as part of a collection action against a taxpayer named Brendan Smith, who has been assessed for \$191,354.05 in back taxes for the years 2007 through 2011. The summons required the Bank to produce "records from all accounts" that Petitioners hold at the Bank from January 3, 2011, to April 8, 2013. The summons named the responsible IRS Revenue Officer and set April 8, 2013, as the date for compliance. Because it issued pursuant to § 7609(c)(2)(D)(i), which does not require notice of a summons in aid of collection of assessed taxes, the summons included the following statement: "UNDER IRC 7609(c)(2)(D), THIS SUMMONS IS EXEMPT FROM THE NOTICE REQUIREMENTS PERTAINING TO THIRD PARTY SUMMONSES." Consistent with this warning, the IRS did not provide notice of the summons either to the taxpayer or the Petitioners. However, on March 19, 2013, the Bank provided a copy of the summons to Petitioners and informed them that it planned to comply unless otherwise directed by court order.

On April 3, 2013, Petitioners filed this miscellaneous petition seeking to quash the summons, naming the United States as Respondent; as grounds, they alleged that Petitioner Carol Smith has no relationship to the taxpayer (Brendan Smith) and that the taxpayer has no ownership interest in the entity Petitioners. They provided notice of the petition by certified mail to the Bank and to the IRS Revenue Officer, but did not send the petition to the U.S. Attorney in Rhode Island or the Attorney General in Washington, D.C. Neither the United States nor the Bank filed a timely objection; as a result, on April 26, 2013, this Court granted the relief sought, quashing the summons. ECF No. 2.

On May 2, 2013, Respondent United States filed its motion to vacate the order quashing the summons and to dismiss the petition, arguing that it did not receive legally sufficient notice and that the doctrine of sovereign immunity bars Petitioners from seeking to quash the IRS's summons. The United States also contends that the IRS "has discovered that the Taxpayer has been using a corporate account to make payments to petitioners." Petitioners have objected because they do not owe any funds to the IRS and the individual Petitioner has no relationship with the taxpayer. They assert, "[t]here has been no evidence presented to the Petitioners as to why its records have been summoned."

II. DISCUSSION

A. Motion to Vacate

This Court's prior order quashing the summons must be vacated because the United States did not receive legally sufficient notice of the miscellaneous petition. Petitioners' attempt to achieve service by sending notice by certified mail to the Bank and the IRS Revenue Officer got them only halfway there.

When challenging an IRS summons, 26 U.S.C. § 7609(b)(2)(B) requires a petitioner to provide notice by registered or certified mail to the person summoned and to “such office as the Secretary may direct in the notice [of the summons].” Since the Revenue Officer’s contact information appeared on the face of the summons, Petitioners met this requirement by serving him and the Bank. See Dorsey v. United States, 618 F. Supp. 471, 474 (D. Md. 1985) (service to agent’s address on the summons satisfies § 7609(b)(2)(B)); see also MacAlpine v. United States, Civil No. 1:12mc15, 2012 WL 1313202, at *1 (W.D.N.C. Apr. 17, 2012) (same). However, pursuant to Rule 4(i), Petitioners should also have served the U.S. Attorney in Rhode Island and the Attorney General in Washington, D.C., by registered or certified mail. Fed. R. Civ. P. 4(i). Petitioners’ failure to comply with Rule 4(i) means that the United States did not receive adequate notice of the miscellaneous petition. Bank of Newport Summons v. IRS, C.A. No. 08-64S, 2008 WL 4376865, at *3 (D.R.I. Sept. 25, 2008) (United States must be served pursuant to Rule 4(i)); Wahler v. IRS, No. MISC 1:02MC54, 2002 WL 32081856, at *5 (W.D.N.C. Nov. 22, 2002) (petitioner must serve notice pursuant to § 7609(b)(2)(B) and Rule 4(i)); Vaughan v. United States, No. 5:01-CV-990-F(3), 2002 WL 1058118, at *1-2 (E.D.N.C. Apr. 11, 2002) (same). Since the United States was not properly served, this Court’s order quashing the summons must be vacated.

B. Motion to Dismiss

The motion of the United States to dismiss requires focus on the doctrine of sovereign immunity. An action to quash an IRS summons is a suit against the United States. Barnes v. United States, 199 F.3d 386, 388 (7th Cir. 1999) (per curiam). Unless the United States consents to be sued, this Court lacks subject matter jurisdiction over claims against the federal government. See United States v. Sherwood, 312 U.S. 584, 586 (1941); Thames Shipyard &

Repair Co. v. United States, 350 F.3d 247, 253 (1st Cir. 2003). In the context of an IRS summons, waiver of sovereign immunity turns on whether Petitioners were entitled to notice when the IRS issued the summons. The United States has waived sovereign immunity for persons who are statutorily entitled to notice of the summons issued by the IRS, but not for those who are not entitled to notice of the summons. See Bank of Newport Summons, 2008 WL 4376865, at *2; see also Barmes, 199 F.3d at 388. As a corollary, if notice is not mandated, a party cannot file a petition to quash a summons. Id.

Here, the IRS served a third-party summons on the Bank pursuant to 26 U.S.C. § 7609. Consistent with constitutional principles, § 7609 normally requires the IRS to serve anyone whose financial records are sought in a third-party summons with notice. Barmes, 199 F.3d at 388. However, § 7609(c) carves out exceptions to the notice requirement; the exception relevant here provides that the IRS need not give notice when it issues a third-party record-keeper summons “in aid of the collection of . . . an assessment made or judgment rendered against the person with respect to whose liability the summons is issued.” 26 U.S.C. § 7609(c)(2)(D)(i); Davidson v. United States, 149 F.3d 1190, 1998 WL 339541, at *2 (10th Cir. June 9, 1998) (unpublished table decision). The elimination of the notice requirement is justified in such circumstances because notice to the taxpayer is unnecessary once the tax has been assessed, as well as to protect against fraud that might occur when the target of the summons, having a relationship to the taxpayer, tips off the scofflaw taxpayer. See Ip v. United States, 205 F.3d 1168, 1173 (9th Cir. 2000).

These justifications work well in circumstances where the owner of the records sought by the summons is the assessed taxpayer or has a legal or other relationship to the taxpayer (such as husband and wife or entity and the owner of the entity). See Bank of Newport Summons, 2008

WL 4376865, at *2 (no-notice exception applies, so no jurisdiction over challenge, where summons sought taxpayer's records from third-party bank). However, when the owner of the records targeted by the summons has no legal or other relationship to the taxpayer, the lack of notice eliminates the right of persons whose financial records are summonsed to argue that the summons seeks privileged materials or that the IRS is using its powers to issue third-party summonses for an improper purpose. United States v. Powell, 379 U.S. 48, 58 (1964) (laying out factors to evaluate motion to quash IRS summons). This issue is squarely presented here because Petitioners assert that they have no relationship to the taxpayer and the IRS has failed to allege any legal or other relationship to justify the lack of notice, arguing only that the taxpayer used a corporate account to make payments to Petitioners.

In such circumstances, courts have struggled with the correct interpretation of 26 U.S.C. § 7609(c)(2)(D)(i). On one end of the spectrum, the Ninth Circuit's thoughtful decision in Ip expressed discomfort with an interpretation that permits the IRS to access financial information from individuals or entities with no relationship to the taxpayer without notice simply because the totally unrelated taxpayer is the subject of an assessment or judgment. 205 F.3d at 1173-74. Ip rejects a literal read of the language of clause (i) in favor of a construction of the statute based on context and legislative purpose. Id. at 1174-75. Ip's holding that the no-notice exception is limited to circumstances where the taxpayer has some legal interest or title in the object of the summons was recently reaffirmed in Viewtech, Inc. v. United States, 653 F.3d 1102, 1105 (9th Cir. 2011) (no notice proper where summons to bank sought records of entity significantly intertwined with taxpayer).

While the brief of the United States seeking dismissal of the petition mentions cases from other Circuits (but not Ip), on close review almost all involve factual circumstances where the

summons sought records of the husband or wife of, or some other person or entity related to, the assessed taxpayer. See, e.g., Barmes, 199 F.3d at 389-90 (no notice to wife of taxpayer and her business); Davidson, 149 F.3d 1190, at *2 (no notice to wife of taxpayer). While some of these cases articulate reliance on the literal interpretation of the statute, permitting no notice without regard to the relationship, virtually all of these courts approve the use of the no-notice exception only after reciting that there has been a showing by the IRS of a relationship between the target of the summons and the taxpayer. See, e.g., Health Plus Chiropractic, Inc. v. United States, No. 6:11-cv-560-Orl-31DAB, 2011 WL 1791289, at *4 (M.D. Fla. Apr. 18, 2011) (where undisputed facts establish taxpayer is employed by, and his spouse is sole shareholder of, entity from which records sought, no notice required); Armijo v. United States, No. 09-81588-MC, 2010 WL 2342444, at *4 (S.D. Fla. May 3, 2010) (taxpayer is employed by bank account owner who also paid her home mortgage payments; no notice approved); Sanders v. United States, No. MC 09-0125-PHX-JAT, 2010 WL 1640982, at *2 (D. Ariz. Apr. 22, 2010) (where assessed taxpayer has legally cognizable interest in the records summonsed from Wells Fargo, no notice approved); Grant v. IRS, Civil Action No. 06-CV-402-JMH, 2007 WL 2174731, at *3 (E.D. Ky. July 27, 2007) (where taxpayer has a recognizable legal interest in the records subpoenaed, notice to the record owner not required); Ginsburg v. United States, No. 3:02CV176 (WWE), 2002 WL 31367262, at *2 & n.1 (D. Conn. Sept. 25, 2002) (facts establish that summons issued for financial records of wife of taxpayer; no notice needed).

As far as the Court has been able to discover, the only case in this Circuit that has addressed the meaning of § 7609(c)(2)(D)(i) considered a summons for records owned by the taxpayer herself, not records of an owner unrelated to the taxpayer; accordingly, it does not discuss how to interpret the statute in a case where the record establishes that the owner of the

records is totally unrelated to the taxpayer. See Bank of Newport Summons, 2008 WL 4376865, at *1-2. Specifically, neither Bank of Newport Summons nor any other court in this Circuit has addressed the issues analyzed in Ip.

To assist the Court in addressing these important issues of first impression in this Circuit, the United States is hereby ordered (i) to submit supplemental briefing on how the First Circuit would likely interpret 26 U.S.C. § 7609(c)(2)(D)(i) as applied in a circumstance where there is no relationship between the owners of the records and the taxpayer, in light of the cases referred to above, and/or (ii) to provide the Court with factual information regarding a relationship between Petitioners and the taxpayer comparable to the relationships established in cases holding that no notice was required, due by June 14, 2013. Petitioners may file responsive briefing or factual information by June 21, 2013.

III. CONCLUSION

For the foregoing reasons, the motion of the United States to vacate the order quashing the summons (ECF No. 3) is GRANTED. The motion of the United States to dismiss will be decided after the time set for supplemental briefing and/or factual submissions by both parties. So ordered.

ENTER:

/s/ Patricia A. Sullivan
PATRICIA A. SULLIVAN
United States Magistrate Judge
June 4, 2013