Sidney B. and Vera L. Stern, Petitioners v. Commissioner of Internal Revenue, Respondent, 74 T. C. 1075 (1980)

The Tax Court will not automatically order reimbursement for subpoena compliance costs unless the subpoena is deemed unreasonable or oppressive.

Summary

In Stern v. Commissioner, the IRS subpoenaed records from Bank of America related to trusts established by the Sterns, which had not been disclosed on their tax returns. The bank requested reimbursement for the costs of compliance, arguing that the IRS should have subpoenaed all relevant documents concurrently. The Tax Court denied the bank's motion, holding that reimbursement is not automatic and is only warranted if the subpoena is oppressive or unreasonable. The court found no such conditions existed, emphasizing that the IRS had no prior knowledge of the undisclosed trust, which justified the timing of the subpoenas.

Facts

Sidney and Vera Stern transferred Teledyne, Inc. , shares to the Hylton trust in 1971 and the Florcken trust in 1972 in exchange for annuities. The Hylton trust transaction was disclosed on their 1971 tax return, but the Florcken trust transaction was not disclosed on their 1972 return. The IRS issued a statutory notice of deficiency for the years 1971-1973, leading to a subpoena for documents related to the Hylton trust from Bank of America. After obtaining these documents, the IRS discovered references to the Florcken trust and subsequently subpoenaed related documents. Bank of America sought reimbursement for compliance costs, citing the need for foreign legal consultations and the timing of the subpoenas.

Procedural History

The IRS issued a statutory notice of deficiency to the Sterns in 1978. After the Sterns filed a petition, the IRS moved for document production related to the Hylton trust. Bank of America initially resisted due to foreign secrecy laws but complied after the Sterns consented to disclosure. The IRS then discovered the Florcken trust and subpoenaed related documents. Bank of America moved for a protective order to be reimbursed for compliance costs, which the Tax Court denied.

Issue(s)

1. Whether the Tax Court should condition the production of subpoenaed documents on the IRS reimbursing Bank of America for reasonable compliance costs.

Holding

1. No, because the subpoena was not deemed oppressive or unreasonable, and the IRS's timing of the subpoenas was justified by the late discovery of the undisclosed

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Florcken trust.

Court’s Reasoning

The Tax Court applied Rule 147(b) of its Rules of Practice and Procedure, which allows for the quashing or modification of a subpoena if it is unreasonable and oppressive, or conditioning denial of such a motion on the advancement of reasonable costs. The court looked to Federal Rule of Civil Procedure 45(b) for guidance, noting that reimbursement is not automatic but a means to ameliorate oppressive or unreasonable subpoenas. The court considered factors such as the nature and size of the recipient’s business, estimated compliance costs, and the need to compile information. The court found that Bank of America, as a large financial institution, should reasonably bear the costs of compliance. Furthermore, the court rejected the bank’s argument that the IRS was at fault for the timing of the subpoenas, as the IRS only learned of the Florcken trust after obtaining Hylton trust documents. The court quoted from *Securities & Exchange Commission v. Arthur Young & Co.* , emphasizing that “subpoenaed parties can legitimately be required to absorb reasonable expenses of compliance,” and that reimbursement is only warranted when the financial burden exceeds what the party should reasonably bear.

Practical Implications

This decision clarifies that non-party recipients of subpoenas, particularly large financial institutions, should not expect automatic reimbursement for compliance costs. It underscores the importance of disclosing all relevant financial transactions on tax returns, as failure to do so may lead to later discovery by the IRS and subsequent subpoenas. The ruling may influence how banks and other institutions budget for compliance with government subpoenas, recognizing such costs as part of doing business. Future cases involving similar requests for reimbursement will likely be analyzed under the same factors, with emphasis on whether the subpoena is oppressive or unreasonable. This case also demonstrates the IRS’s diligence in uncovering undisclosed financial arrangements, which may encourage taxpayers to fully disclose all relevant information.

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