

Practice

IRS LB&I Revised IDR Enforcement Process

By Charles Rettig

The IRS Large Business & International (LB&I) Division recently issued three Directives relating to the issuance and enforcement procedures regarding Information Document Requests (IDRs). The Directives are commonly referred to as the LB&I Directive on Information Document Requests (IDR Directive); the LB&I Directive on Information Document Requests Enforcement Process (Enforcement Directive); and the LB&I Directive on Updated Guidance for Examiners on Information Document Requests Enforcement Process (Guidance Directive).¹ The Guidance Directive incorporates and supersedes the earlier IDR and Enforcement Directives and provides further clarification of the use of the new IDR processes by LB&I examiners.

LB&I is generally responsible for examinations of corporations, S-corporations, high wealth individuals and partnerships with assets greater than \$10 million. These individuals and entities typically have large numbers of employees, deal with complicated issues involving tax law and accounting principles, and conduct their operations in an expanding global environment.

During an examination, the examiner must review sufficient documents and information to determine the accuracy of the taxpayer's return. The IRS has the authority to request and receive books, records, *etc.*, necessary to properly examine an entity's tax return.² The amount of documents and information to be reviewed and the depth of the examination is a matter of professional judgment. The IDR (IRS Form 4564) is used by the examiner to request information and documents from the taxpayer under examination. Each IDR is to be specific, clear, and concise and should not request more information than is essential to resolve the issues identified.³ The IDR must sufficiently specify the books, papers, records or other data requested and the particular activity and time period involved. Often the IDR will include a statement indicating that the examiner will probably request additional information as the examination progresses.⁴

Each IDR will include a response date for submission of the requested information or documents.⁵ Historically, IRS examiners have been somewhat flexible with respect to their requests for information and the timeliness of any taxpayer responses. The Guidance Directive acknowledges that enforcement procedures should only be needed infrequently if both the IRS and taxpayers engage in robust, good faith communication in advance of an IDR being issued.



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All LB&I examiners and specialists have recently completed two mandatory IDR training sessions covering both the requirements for issuing IDRs and the new procedures for enforcing IDRs in order to hopefully make the IDR process as efficient and transparent as possible. These new procedures are designed to improve the ability of the IRS to gather information in a timely manner and potentially reduce the need to enforce IDRs through issuance of summonses.

IDR Directive

The IDR Directive announced the requirement that all IDRs,⁶ must comply with the principles set forth in the training—IDRs must be issue focused, they must be discussed with the taxpayer, and the taxpayer and the examining agent must discuss the appropriate timeframes for the request. Before implementation of the new IDR enforcement process in any particular LB&I examination, all IDRs issued during the course of the examination must satisfy the requirements of the Directives. Issue focused IDR requests must include a reasonable time frames for a response.

Enforcement Directive

The IDR Enforcement Directive provided guidance on the enforcement process that must be used when a taxpayer does not timely respond to an IDR that is issue focused, has been discussed with the taxpayer, and contains a response date that has been discussed with the taxpayer and, in most instances, has also been mutually agreed upon. All LB&I managers, examiners and specialists were directed to ensure that all outstanding and future IDRs comply with the new requirements for issuing IDRs.⁷ The IDR Enforcement Directive identified three graduated steps to the new *mandatory* IDR enforcement process: (1) a Delinquency Notice; (2) a Pre-Summons Letter; and (3) a Summons. It requires LB&I managers at all levels be actively involved early in the IDR process and ensure that IRS Counsel is prepared to enforce IDRs through the issuance of a summons, when necessary.⁸

Guidance Directive

This Directive supersedes the IDR Directive and the IDR Enforcement Directive clarifying the procedures governing IDR issuance and enforcement; to continue to emphasize the importance of both the IRS and taxpayers engaging in “robust discussions” that include the examination issue that is the subject matter of a particular

IDR; information that is necessary to evaluate that issue and why; what information the taxpayer has and how long it will take to provide it; and the timeframe within which the IRS will review the information for completeness and respond to the taxpayer.

If an outstanding IDR does not meet the requirements set forth in the Guidance Directive, it must be reissued to conform to the new requirements including a new response date, at which time the new enforcement procedures will apply to that IDR. *The enforcement process is mandatory and has no exceptions.*

The Guidance Directive set forth an exception to a requirement of the Enforcement Directive that an IDR identify a particular issue. An IDR that is issued at the beginning of an examination that requests basic books and records and general information about a taxpayer’s business is not subject to this requirement. Further, if during the discussion of an IDR, a taxpayer indicates that the requested information will not be provided without a Summons, the IDR enforcement procedures do not apply and the IRS will move directly to the issuance of a Summons.

Requirements for Issuing IDRs

The Guidance Directive sets forth the following requirements for issuance of all IDRs by LB&I examiners:

1. Discuss the issue related to the IDR with the taxpayer.
2. Discuss how the information requested is related to the issue under consideration and why it is necessary.
3. After this consultation with the taxpayer, determine what information will ultimately be requested in the IDR.
4. Ensure the IDR clearly states the issue that is being considered and that the IDR only requests information relevant to the stated issue. An IDR issued at the beginning of an examination that requests basic books and records and general information about a taxpayer’s business is not subject to this requirement #4. Once this initial IDR has been issued, subsequent IDRs must state an issue in compliance with this requirement #4.
5. Prepare one IDR for each issue.
6. Utilize numbers or letters on the IDR for clarity.
7. Ensure that the IDR is written using clear and concise language.
8. Ensure that the IDR is customized to the taxpayer or industry.
9. Provide a draft of the IDR and discuss its contents with the taxpayer. Generally, this process should be completed within 10 business days.
10. After this discussion is complete, determine with the taxpayer a reasonable timeframe for a response to the IDR.

11. If agreement on a response date cannot be reached, the examiner or specialist will set a reasonable response date for the IDR.
12. When determining the response date, ensure that the examiner or specialist commits to a date by which the IDR will be reviewed and a response provided to the taxpayer on whether the information received satisfies the IDR. Note this date on the IDR.

IDR Enforcement Process

The IDR enforcement process is mandatory and there are no exceptions. If responses are not complete, for any reason, the enforcement process will be implemented.

Extension Authority

Before the enforcement process is triggered, an IRS examiner or specialist has the discretion to grant a taxpayer an extension of up to 15 business days before the enforcement process begins. However, an examiner or specialist may only grant one extension with respect to the same IDR which may be granted in the following two situations:

1. **Taxpayer Fails to Respond.** If a taxpayer fails to provide any response by the IDR due date, the examiner or specialist, should, within five business days of the IDR due date, discuss with the taxpayer the cause of the failure to respond and determine if an extension is warranted. If the examiner or specialist determines that the taxpayer's explanation warrants it, the examiner or specialist may grant the taxpayer an extension of up to 15 business days from the date the extension determination is made and communicated to the taxpayer.
2. **Taxpayer Provides Incomplete Response.** If a response is received but the examiner or specialist determines that it is not complete, the examiner or specialist should discuss with the taxpayer the reasons why the response is not complete and determine within five business days whether an extension is warranted. If the examiner or specialist determines that the taxpayer's explanation warrants it, the examiner or specialist may grant the taxpayer an extension of up to 15 business days from the time the extension determination is made and communicated to the taxpayers.

Timing of Application of IDR Enforcement Process

The timing of the application of the IDR enforcement process depends upon if and when a response is received.

No Response Received by Due Date

If no response is received by the IDR due date and no extension is granted, the IDR enforcement process begins on the date the extension determination is communicated to the taxpayer. If an extension is granted and no response is received by the extended due date, the IDR enforcement process begins as of the extended due date.

Response Received by Due Date

If a response is received by the due date, the IRS must determine whether the response is complete. This determination will be made on or before the date set forth in the IDR. If the IDR is considered complete upon review, the examiner or specialist must notify the taxpayer that the IDR is complete and closed.

Historically, IRS examiners have been somewhat flexible with respect to their requests for information and the timeliness of any taxpayer responses.

If the IDR response is not complete and no extension is granted, the IDR enforcement process begins on the date the extension determination is communicated to the taxpayer. If the IDR response is not complete and an extension is granted and no additional information is received at the end of the extension period (may be up to 15 business days), the IDR enforcement process begins at the end of the extension period. If additional information is received at the end of the extension period, this information must be reviewed for completeness. This review should be completed as soon as practical but in most cases not more than 15 business days from receipt of the response. If the IDR response is then determined to be incomplete, the IDR enforcement process begins on the date the examiner or specialist notifies the taxpayer that the response remains incomplete. If the IDR is complete, the examiner or specialist should notify the taxpayer and close the IDR.

Revised IDR Enforcement Process

The process has three graduated steps: (1) a Delinquency Notice; (2) a Pre-Summons Letter; and (3) a Summons. This process is mandatory and has no exceptions. It requires LB&I managers at all levels to be actively involved early in

the process and ensures that Counsel is prepared to enforce IDRs through the issuance of a Summons when necessary.

Delinquency Notice (Letter 5077)

Once the IDR Enforcement Process applies, the examiner or specialist along with their manager must complete the Delinquency Notice phase of the enforcement process by discussing issuance of the Delinquency Notice with the taxpayer. During this discussion, IRS representatives will attempt to ensure that the taxpayer understands the potential next steps in the enforcement process if the information requested in the IDR is not provided by the response date established in the Delinquency Notice. The Delinquency Notice, signed by the Team Manager, will be issued to the taxpayer within 10 days of the beginning of application of the Enforcement Process. The Delinquency Notice will include a response date that is generally no more than 10 business days from the date of the Delinquency Notice. Any extension beyond 10 business days must be approved by the Territory Manager. A copy of the Delinquency Notice and the IDR will be provided to IRS Counsel.

Pre-Summons Letter (Letter 5078)

If a taxpayer does not provide a complete response to an IDR by the Delinquency Notice response date, the examiner or specialist must complete the Pre-Summons Letter phase of the enforcement process by discussing the lack of a complete response to the Delinquency Notice with the IRS Team Manager, Specialist Manager, the respective Territory Managers and Counsel and prepare the Pre-Summons Letter. The appropriate Territory Manager must discuss the Pre-Summons Letter with the taxpayer. During this discussion, IRS representatives will attempt to ensure that the taxpayer understands the next steps in the enforcement process if the information requested in the IDR is not provided by the response date established in the Pre-Summons Letter.

The Pre-Summons Letter, signed by the appropriate Territory Manager, will be issued as quickly as possible but generally no later than 10 business days after the due date of the Delinquency Notice. The Pre-Summons Letter will be addressed to the taxpayer management official that is at a level equivalent to the LB&I Territory Manager—a level of management above the taxpayer management official that received the Delinquency Notice. The Pre-Summons Letter will include a response date that is generally 10 business days from date of Pre-Summons Letter. Any extension beyond 10 business days must be approved by the Director of Field Operations (DFO). A copy of the Pre-Summons Letter and the IDR must be discussed with IRS Counsel.

DFO(s) must be made aware of the Pre-Summons Letter prior to issuance.

Summons

If a taxpayer does not provide a complete response to an IDR by the Pre-Summons Letter response date, the examiner or specialist must complete the Summons phase of the enforcement process by discussing the lack of response to the Pre-Summons Letter with the IRS Team Manager, Specialist Manager, the respective Territory Managers and DFOs, and Counsel and coordinate preparation and issuance of the Summons with IRS Counsel.⁹ A Summons cannot be used to require a taxpayer to prepare or create document. It is not self-enforcing and requires that the Department of Justice file an enforcement action in District Court to compel compliance—a process likely to involve substantial delay that could result in the Court setting a new timeframe for a response, after assessing the reasonableness of any earlier delayed response.

IRS Training Materials Regarding the IDR Enforcement Process

The IRS will try to mutually agree on a reasonable time frame for a response to each IDR. However, the Directives set forth fairly rigid timeframes in the event an agreement on a response date cannot be agreed upon. In such event, the examiner or specialist will have the sole responsibility of setting a reasonable response date for the IDR. The Training Materials include several enlightening comments that should not be overlooked:

- **IDR Enforcement Training**—“As the LB&I Commissioner states in the Field Focus Guide, the principles for sound tax administration are accountability, professionalism, discipline, and transparency. It is critical that we demonstrate to the taxpaying public that we adhere to these principles so there is confidence in both the voluntary compliance system and the agency charged with administering the tax law. To this end, we continuously review and assess our examination practices to accomplish these objectives.”
- **Effective IDR Review**—“Let me recap some best practices that you heard in the IDR Process training. The issues should be stated on the IDR and discussed with the taxpayer. We saw that, limiting the IDR to a single issue, Identifying questions using numbers and/or letters make it easier for the taxpayer to track and respond to IDRs. Asking specific questions using clear and concise language with terminology used by the taxpayer will

help the taxpayer understand what you are asking for. And also writing an effective IDR is not only critical to effective information gathering, it is also important in the event that you need the enforcement process.”

- **Process Review**—“For the IDR process to be effective we need to hold the taxpayer accountable for the agreed to response time and we need to be accountable to provide a response to the taxpayer whether the IDR is complete within an agreed upon and reasonable time frame. When the agreed upon IDR response time frames are not met, we will follow the IDR enforcement process. This process will be used for all LB&I cases. As with any process you should use your professional judgment considering the taxpayer’s history of cooperation and the issues you are working to determine the most efficient way to implement the process.”
- **Continuous Review and Assessment of the Examination Process**—“The information gathering process relies extensively on communication, collaboration and commitments with the taxpayers in planning and executing the Information exchange. There will be a renewed emphasis on securing complete responses within the timeframes to which the taxpayer has agreed.”
- **Information Availability**—“With our examinations being very current, with modern technology such as e-mail, e-fax, electronic media these are just some of the reasons why information is much more readily available. Therefore, if the taxpayer has taken a position on their return there should be documentation available which they relied upon. It follows then, that this information should be available and accessible when requested.”
- **Partial Response**—

“QUESTION: How would you handle a situation where you have a historically cooperative taxpayer that completes 90% of an IDR on time? Don’t you think it’s a little harsh to be issuing a Delinquency Notice for the missing items?”

RESPONSE: It doesn’t matter what percentage or portion of an IDR is completed, to ensure consistency throughout the process: the only two outcomes of an IDR response are either completed or delinquent. Any items on the IDR not completed by the due date will be considered delinquent.”

- **Elevating to Taxpayer Executives**—

“QUESTION: “What’s the significance of raising this to the next level of taxpayer management. Isn’t that like going over our contact’s head?”

RESPONSE: This is simply to ensure the executive level of the taxpayer is aware of the delay in responding to a request The Pre-Summons Letter ensures that the delay has risen to an appropriate level.”

- **Due Dates**—“Due dates need to be both reasonable and realistic taking into account the complexity of the IDR and your taxpayer’s history. In this example, the information requested already existed and should be readily available. . . It is important that we follow the process and engage management quickly to keep the process moving.”
- **Communication**—“Communication and persistence is key to successfully executing the enforcement process. There is an expectation to establish a response date for ‘each’ IDR. All actions and discussions with the taxpayer should be properly documented so there is a clear record of our attempts to secure the information requested.”
- **IDRs and Summonses**—“An IDR request may be broader than a summons. You IRS may appropriately ask for items in an IDR that you cannot legally obtain by summons.¹⁰ A simple example might be a request for items that the taxpayer may not presently possess and would have to create, such as an organizational chart. Counsel will advise you that you cannot summons an item that doesn’t exist. However, clearly you should still request chart informally if it would assist in the examination. If the taxpayer does not produce the chart, then Counsel may suggest that you summons testimony to ask for the names and positions of employees in order to create your own chart. In this regard, summonsed testimony can serve as the functional equivalent of the item you requested in the IDR, but cannot summons.”
- **Changing Behavior**—“Credibility is the key to changing behavior. We should never say we are considering using a summons, unless we mean it and unless we are prepared to actually issue a summons. Likewise, we should never issue a summons unless we are willing to seek enforcement. These IDR enforcement procedures are designed to assure that we will follow-through with the summons process if necessary to complete our examination.”
- **Set the Date Scenario**—“I’ve noticed that you consistently request 60 days or more for many response dates and in many cases you’ve been late on those responses as well. The information requested on this IDR wasn’t overly complicated and we just can’t have every request taking 60 days. Like you, we have limited resources and specific time frames to meet so we need to eliminate the long delays in securing the data.”
- **Scenario Highlights**—“Remember the exam team maintains control of the IDR process. Due dates need

to be both reasonable and realistic taking into account the complexity of the IDR taxpayer's history. In this example, the information requested already existed and should be readily available. You have some flexibility here based on your particular circumstances. Remember we want to be reasonable but at the same time we need to maintain control of the examination.”

- **Role of the Taxpayer**—“The taxpayers have a responsibility to validate transactions reflected on the return, it would be key for the taxpayer to be proactive and participate in a robust discussion with the IRS Team on the issue identified and the records available to validate the position taken on the return. It is expected that the taxpayer work with the team to determine a “firm” yet reasonable response date on IDRs. In summary, if the parties have worked to identify the appropriate information needed to evaluate the issue identified and have agreed to a firm response time for each IDR, there should be no exception to a timely response. However if the response is not received, the team will initiate the enforcement process.”
- **Closing**—“This IDR Enforcement process has been created to give LB & I examiners the ability to more consistently manage the flow of information received from taxpayers and conduct their examinations comprehensively with as little delay as possible.”

Summary

The new LB&I procedures were designed to impose consistency and discipline in the overall IDR enforcement process but may result in a cultural change increasing examination tensions. Most taxpayers and practitioners maintain a courteous, professional relationship with the IRS during an examination. Information requests are made, discussed, whatever can be readily obtained is provided and a cooperative path forward is discussed for whatever information is not yet provided.

All discussions regarding IDR responses must be open and clear since the examiner is basically unable to modify the due dates once the IDR has been issued. Although there may be a great working relationship with the exam team, the examiner and the taxpayer will feel the pressure inherent in the new IDR mandatory procedures.

Good working relationships are important. However, all discussions regarding IDR responses should be well documented and include the location (foreign or domestic) of the requested documents, availability of key employees, and time frame necessary for a review of potential privileges. If the taxpayer is unable to agree with a response date set by the examiner, it is imperative that this disagreement be documented and elevated

to a Territory Manager. Although some taxpayers fear that doing so might harm their working relationship with their exam teams, such issue elevations are generally expected in a business environment. IRS managers need to understand all relevant concerns as soon as possible to be able to ensure that the IDR process is working. For large taxpayers, management should be apprised of the status of IDR requests during the examination.

The LB&I examiner is generally required to issue the IDR within 10 days following issuance of the draft IDR. As such, it is imperative that any perceived difficulties in responding timely should be thoroughly discussed with the examiner. A request for a lengthy response date should not occur with respect to each IDR—agreeing to shorter timeframes with respect to information that might be readily available will lend credibility to requests for longer timeframes for other information. Any concerns regarding the requested response date should be elevated, in writing, to the exam team manager and possibly beyond. Once the IDR becomes delinquent on either the original due date or any extended date, the mandatory three-step enforcement process must be implemented.

There is not a technical definition of an “issue” but it is likely to be dependent upon positions set forth in the return and could be a transaction or books and records for a particular deduction. The examiner might divide an issue to into several sub-issues, each with a separate IDR. Since each issue will have a separate IDR, partial responses are mostly irrelevant.

Many, but not all, high wealth individuals maintain a family office providing assistance with investments and coordination with outside professional advisors regarding investments, financial reports, tax return preparation, business operations and the like. However, upon receipt of a notice of examination, such individuals and/or their family office may not be able to readily ascertain the foreign or domestic location of requested information, may have to seek outside representation to coordinate the examination and make determinations regarding potential privileges, *etc.* In such event, it would seem overly optimistic that information requested near the commencement of an examination being conducted under the new IDR enforcement procedures would be provided in a timely manner. Further, much of the requested information is likely possessed by others who may not feel the pressure to immediately search their files.

As the LB&I IDR enforcement process is currently structured, large entities with ongoing tax representation may be better suited to timely respond than high wealth or closely held entities. Large and public entities generally prefer to not be publically perceived as aggressive, noncooperative taxpayers. As such, they typically do not like the public aspects associated with the summons enforcement process. Further, even though the exam team representing

the entity is exercising its best efforts and working closely with the IRS exam team, the relatively strict IDR timeframe under the enforcement process might lead to an IRS notification to the CFO or the equivalent indicating potential problems in the examination process.

The new IDR enforcement process places a premium on cooperation with the IRS exam team. However, the new procedures create an enforcement process that seems to have little patience for unanticipated situations, vacations and real life personal issues that often arise during the course of every examination. The potential IDR enforcement timeline begins with the issuance of a draft IDR followed by issuance of the actual IDR within 10 days thereafter, issuance of a Delinquency Notice within 15 days of determining a response to the IDR was less than complete, up to 15 days to respond to the Delinquency Notice, issuance of a Pre-Summons Letter within 14 days of determining a response to the Pre-Summons Letter was less than complete, up to 10 days to respond to the Pre-Summons Letter, and an unspecified timeframe regarding the summons and potential federal court summons enforcement proceeding. There would seem

to be sufficient overall time built in to the process to avoid an actual federal court summons enforcement proceeding since, along the way, taxpayers will presumably be continuing their efforts to locate and provide missing information requested in the IDR.

The Directives are intended to reflect the “best practices” applicable to IDRs that are being utilized by all LB&I examiners. It is uncertain to ascertain the extent, if any, to which these new enforcement procedures may spread throughout the remaining IRS operating divisions. However, whether dealing with LB&I or any other division of the IRS, meaningful, regular communications and cooperation between the IRS and taxpayers at each stage of an examination is essential. Ensure that every member of the exam team clearly understands exactly what is being requested in the IDRs, who has responsibility for obtaining the requested information, that the IDR is issue-focused and includes a response date is realistic and achievable.

When appropriate ... elevate, elevate, elevate each concern to upper IRS management.

ENDNOTES

¹ LB&I Directive on Information Document Requests (IDRs) [LB&I-04-0613-004 issued on June 18, 2013]; LB&I Directive on Information Document Requests Enforcement Process [LB&I-04-1113-009 issued on Nov. 4, 2013]; and LB&I Directive on Updated Guidance for Examiners on Information Document Requests Enforcement Process [Directive LB&I-04-0214-004 issued on Feb. 28, 2014]. The IDR Enforcement Process became effective on March 3, 2014 although Delinquency Notices could not be issued prior to April 3, 2014. The IDR Directive, the Enforcement Directive and the Guidance Directive are collectively referred to as the “Directives.”

² Internal Revenue Code (IRC) 7602, Examination of Books and Witnesses, Treas. Reg. 301.7602-1(a), Examination of Books and Witnesses. Under Code Sec. 7602, the IRS has the authority to examine any books, papers, records or other data that are relevant to the matters required to be included in any return and to summons any person having this information. Rather than seek information by issuing

summonses, the IRS usually requests information by issuing an IDR to the taxpayer. If the taxpayer fails to remit the requested information by the IDR's due date, the IRS may seek to compel production of the requested documents by issuing a summons and pursuing enforcement of the summons in court. The IRS must file a petition in a U.S. district court to enforce a summons and to order the summonsed party to comply, see, e.g., *R.T. Gilleran*, CA-9, 93-1 ustrc ¶150,536, 992 F2d 232, and *Samuels, Kramer & Co.*, CA-9, 83-2 ustrc ¶19525, 712 F2d 1342.

³ Internal Revenue Manual (IRM) §4.10.2.9.2 (Jan. 17, 2012) and 4.46.4.

⁴ IRM §4.10.2.9.2 (Jan. 17, 2012).

⁵ *Id.*

⁶ Issued after June 30, 2013.

⁷ Attachment 1 to the Enforcement Directive summarizing these requirements was revised and attached to the Guidance Directive as Attachment 1.

⁸ Attachment 2 to the Enforcement Directive summarizing the IDR enforcement process was revised and attached to the Guidance Directive as Attachment 2.

⁹ Summons procedures can be found in IRM §25.5; The IRS has considerable latitude in seeking records from taxpayers during the examination process, see *Arthur Young & Co.*, S Ct, 84-1 ustrc ¶19305, 465 US 805, 816, 104 S Ct 1495 (stating that, “In order to encourage effective tax investigations, Congress has endowed the IRS with expansive information gathering authority.”).

¹⁰ In *M. Powell*, S Ct, 64-2 ustrc ¶19858, 379 US 48, 85 S Ct 248, the Supreme Court enunciated a four-part test by which the IRS can establish a *prima facie* case for summons enforcement. Often demonstrated by an affidavit from the IRS examiner who issued the summons, the government can meet its burden by demonstrating: (1) the investigation has a legitimate purpose, (2) the information summoned is relevant to that purpose, (3) the documents sought are not already in the possession of the government, and (4) the procedural steps required by the Internal Revenue Code for issuing the summons were followed. Most successful defenses to the summons enforcement relate to claims of privilege.

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