BAKER & McKENZIE

Baker & McKenzie LLP

300 East Randolph Street, Suite 5000
Chicago, IL 60601
United States
Tel: +1 312 861 8000
Fax: +1 312 861 2899
www.bakermckenzie.com

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Via Federal Express

Honorable Michael B. Thornton
Chief Judge
United States Tax Court
400 Second Street, N.W.
Washington, D.C. 20217

Dear Chief Judge Thornton:

On September 11, 2015, Internal Revenue Service Chief Counsel William Wilkins proposed several changes to the United States Tax Court's Rules of Practice and Procedure (the "Rules") on behalf of the Internal Revenue Service (the "Service"). On behalf of Baker & McKenzie LLP, we submit the following comments in response to the Chief Counsel's proposed changes to the Court's Rules. We appreciate the opportunity to comment on the Chief Counsel's proposals and hope that our comments prove to be helpful.

Subpoenas

The Chief Counsel has proposed amendments to the Court subpoena rules to allow subpoenas duces tecum directed to third-party custodians of records to be returned in advance of the trial calendar. To effect this change, the Chief Counsel has suggested that the Court either schedule hearings to allow for the return of subpoenas duces tecum at least 30 days prior to trial or amend Rule 74(c) to establish a legal presumption that depositions, an "extraordinary method of discovery," be available to a party that wishes to depose a third-party custodian of records. The Chief Counsel suggests that this change is necessary, because the current rule often results in production of records at the call of the calendar for the trial session and that this can hinder the parties' ability to adequately examine documents in preparation for trial.

In our experience, it is more of an exception, rather than a rule, that parties are faced with insufficient time to examine subpoenaed documents in advance of trial. In instances when third-party custodians are delayed in document production, it can be due to a number of reasonable factors, such as (1) the breadth of the request for documents, (2) the nature of the recipient's business, (3) the size of the recipient's business, (4) the estimated cost of compliance, and (5) the extent to which the recipient must compile information from his or her records and documents. As it currently exists, Rule 147 provides recognition of these factors, while still requiring timely return of subpoenas. To eliminate this flexibility would be unduly burdensome to third parties. Nevertheless, we agree that there may be some merit to allowing the return of a subpoena duces tecum prior to trial if it can be done in a way that minimizes any additional burden on the third party and on the taxpayer.

We do not think, however, that the Chief Counsel's alternative proposal to amend Rule 74(c) should be considered. The Chief Counsel's proposal disregards the Service's broad power to gather documents from the taxpayer and from third-party custodians during the audit and investigative stages. See I.R.C. § 7602. Further, the Chief Counsel's proposal would result in third parties and taxpayers potentially incurring significant costs to comply with a subpoena in cases where the Chief Counsel would not be able to satisfy the longstanding requirement that a deposition be used only as an extraordinary method of discovery, as discussed in detail below. For example, in the recent case, Medtronic, Inc., v. Commissioner, Dkt. No. 6944-11, the Commissioner sought such a deposition from a third-party document custodian who was not related or otherwise a party to the transactions at issue in the case. The Court denied the Commissioner's request. Under the Chief Counsel's proposal, however, the third-party document custodian, as well as the taxpayer, would have been obligated to incur significant costs to comply with the subpoena or to move to quash the subpoena. The Chief Counsel's proposal to amend Rule 74 would move discovery in this Court closer to that of federal district courts, without the limitations that exist in the Federal Rules of Civil Procedure.

Nonconsensual Depositions of Party Witnesses

The Chief Counsel also has proposed an amendment to Rule 74 to allow for nonconsensual depositions of party witnesses upon notice to the party without requiring leave of the Court by motion. We think that such an amendment would significantly change the way in which Tax Court practice is conducted and that to do so would be a grave mistake. The Commissioner's proposal would increase the costs of Tax Court litigation for taxpayers and would move the Tax Court to a more formal discovery process, as in federal district courts, which is contrary to the stipulation process, the bedrock of Tax Court practice. See Branerton Corp. v. Commissioner, 61 T.C. 691 (1974).

Under the current Rule 74(c), a nonconsensual deposition is considered an "extraordinary method of discovery" and may be authorized only when the information sought has not been or cannot be obtained otherwise. Specifically, Rule 74(c)(1)(B) provides that:

> The taking of a deposition of a party, a nonparty witness, or an expert witness under this paragraph is an extraordinary method of discovery and may be used only where a party, a nonparty witness, or an expert witness can give testimony or possess documents, electronically stored information, or things which are discoverable within the meaning of Rule 70(b) and where such testimony, documents, electronically stored information, or things practically cannot be obtained through informal consultation or communication (Rule 70(a)(1)), interrogatories (Rule 71), a request for production of documents, electronically stored information, or things (Rule 72), or by a deposition taken with consent of the parties (Rule 74(b)).

(Emphasis added.)

Underlying the "extraordinary" nature of nonconsensual depositions is the Court's well-established policy that parties resort primarily to voluntary and informal consultation. Rule 70(a)(1) specifically requires that parties "attempt to attain the objectives of discovery through informal consultation or communication before utilizing the discovery procedures provided in these Rules." The Court's explanation accompanying the 2009 promulgation of Rule 74 confirms the importance of considering the voluntary and informal consultation process before granting a party deposition request:

> The deposition of a party without consent is an extraordinary method of discovery and may be taken only pursuant to an order of the Court. . . . A judge or Special Trial Judge should only order such a deposition where the testimony or information sought practicably cannot be obtained through informal communications or the Court's normal discovery procedures and to the extent consistent with Rule 70(b)(2).

Note to Rule 74 (Sept. 18, 2009). By suggesting that nonconsensual depositions of party witnesses become more readily available, the Chief Counsel's proposal undermines the Court's long-standing expectation of a voluntary and informal consultation process.

The Chief Counsel's proposal to ease its ability to take depositions of party witnesses without any limitation once again disregards the broad ability of the Service to gather information during the audit and shifts the burden to the taxpayer to object to the requested depositions. The Chief Counsel cites large, complex cases, such as transfer pricing cases, as grounds for why he believes the rule needs to change, but disregards that in these very same cases, the Service is conducting a significant number of interviews of the taxpayer prior to issuing a Notice of Deficiency. Often, these interviews are taken under oath and recorded by a court reporter. For example, in the recent Medtronic case, the Service interviewed more than 40 individuals prior to issuing the Notice of Deficiency with a court reporter present at each interview. The Service, nonetheless, requested more than fifteen depositions during discovery, of which the requested topics had been covered by the prior interviews, in addition to a multitude of discovery questions. What happened in Medtronic is not unique to Medtronic. Indeed, in nearly every "complex" transfer pricing matter of which we are aware, the Service is conducting dozens of interviews of party witnesses, under oath, as it conducts its examinations. As this Court has found in Medtronic and in other cases where the Service has sought non-consensual depositions of party witnesses despite having conducted extensive factual investigation, there must be something "extraordinary" about the Service's need for the depositions. The Court's current rule ensures that both the Service's need for information that it could not otherwise gather during the examination and the taxpayers' need to manage its limited time and financial resources are respected.

Because the burden in each of these cases remains on the taxpayer, therefore, there is no compelling reason to change the rule to ease the Chief Counsel's ability to take

depositions. In fact, doing so, as the Chief Counsel has proposed, would limit judicial oversight and unreasonably place the cost and burden of objecting to the deposition on the taxpayer. The Court's explanation accompanying the promulgation of Rule 74 confirms the intentional inclusion of judicial oversight:

> The deposition of a party without consent is an extraordinary method of discovery and may be taken only pursuant to an order of the Court. Whether to issue such an order is a matter solely within the discretion of the Judge or Special Trial Judge who is responsible for the case.

Note to Rule 74 (Sept. 18, 2009) (emphasis added). The Rule places responsibility on the Court to grant such a deposition only in "extraordinary" instances. Judicial oversight is necessary to ensure the deposing party abides by this burden. The Chief Counsel's recommendation would drastically change this procedure by permitting Chief Counsel to take as many depositions as he desires, while shifting the onus to the taxpayer to object in instances when the "extraordinary" burden is not met. Altering this procedural step would be unduly burdensome to taxpayers, create the potential for abuse, and reduce the incentive to rely on the informal consultation and discovery rules and the stipulation procedures that are key to the Tax Court's long-standing practice.

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Again, we commend the Court for the time and thought that has been put into considering proposals to change its Rules. We also appreciate the opportunity to comment on the Chief Counsel's proposals and hope that our comments prove to be helpful. Please do not hesitate to contact us if you desire any additional information or wish to discuss our comments and recommendations in further detail.

Sincerely,

Jenny Austin
Partner
+1 312 861 8284
Jenny.Austin@bakermckenzie.com

Daniel Rosen
Partner
+1 212 626-4272
Daniel.Rosen@bakermckenzie.com