IN THE SUPERIOR COURT OF THE VIRGIN ISLANDS
DIVISION OF ST. THOMAS AND ST. JOHN
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DEBORAH J. CLOUTIER, individually and derivatively on behalf of JDM ASSOCIATES, LLC,	) **CASE NO. ST-17-MISC-73**
Plaintiff,	) **PENDING IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE C.A. No. 2017-0794-JTL**
v.	)
JOHN M. KLEIN,	)
Defendant.	)

MEMORANDUM OPINION AND ORDER

Before the Court is a Motion to Quash Subpoena Duces Tecum, which was filed by the Virgin Islands Bureau of Internal Revenue ("BIR") on December 28, 2017.[1] Deborah J. Cloutier served the BIR with a subpoena *duces tecum.* The BIR contends that the subpoena contradicts laws protecting the privacy of documents filed with the BIR. Finding the subpoena asks for documents protected from disclosure by Virgin Islands law, the Court will grant the Motion in part.

BACKGROUND

This matter stems from a pending case before the Court of Chancery of the State of Delaware with case number 2017-07794-JTL. Cloutier and John M. Klein are stakeholders in JDM Associates, LLC. Cloutier has a forty-nine percent (49%) membership stake and Klein has a fifty-one percent membership stake (51%).[2] In the underlying suit, Cloutier seeks in part the judicial removal of Klein as a manager of JDM Associates. JDM Associates has an office on St. Thomas and Klein is a resident of the Virgin Islands. The Delaware court issued a subpoena requiring the BIR to provide Cloutier with, among other things, "All documents, communications, and electronically stored information transmitted between VIBIR" and various entities and persons. On December 20, 2017, the Clerk of the Court issued an identical subpoena. The subpoena was issued in accordance with title 5, § 4924 of the Virgin Island Code, which permits the Clerk of the Court to enter a subpoena directed to person in the Virgin Islands by a foreign court.

Notably, the subpoena demands, in part, copies of communications between the BIR and

[1] The title of the Motion is "Defendants' Motion to Quash Subpoena Duces Tecum." However, the BIR is not a defendant in this matter.
[2] *JDM Assocs., LLC & John Klein v. Deborah Cloutier*, Case No. ST-17-CV-421, First Am. Compl. ¶¶ 2, 3 (Nov. 3, 2017).

JDM Associates from April 7, 2005 to the present.[3]

STANDARD

Virgin Islands Rule of Civil Procedure 45(d) provides protections for persons served with a subpoena. Rule 45(d) requires a court, upon a motion, to quash or modify a subpoena if the subpoena "(i) fails to allow a reasonable time to comply; (ii) requires a person to comply beyond the geographical limits specified in Rule 45(c); (iii) requires disclosure of privileged or other protected matter, if no exception or waiver applies; or (iv) subjects a person to undue burden."

APPLICATION

In *Gustav A. Danielson & Co., P.C. v. Witty*, the Territorial Court held that "sound public policy considerations militate against [tax returns'] unnecessary disclosure."[4] "This public policy arises from the Government's need to encourage taxpayers to file complete and accurate returns."[5] However, Virgin Islands courts have not addressed whether the V.I. Code prevents the BIR from disclosing tax information when served with a subpoena. The Court in *Gustav A. Danielson & Co., P.C.*, issued a protective order against a discovery demand calling for disclosure of a party's tax returns because it found that the tax returns were irrelevant to the lawsuit. However, the issue for consideration by the Court is not whether the subject subpoena demands relevant information but whether it contradicts Virgin Islands law, as argued in the BIR's Motion.

I. Public Policy Proscribes the Disclosure of Tax Returns by the BIR.

The Virgin Islands Code does not clearly reveal the BIR's obligation to disclose tax information when served with a subpoena. Title 33, § 822(a) of the Virgin Islands Code provides that tax returns reflecting certain taxes imposed by the Virgin Islands tax laws should be open to inspection only upon an order by the Governor or Director of the BIR.[6] While § 822(a) discusses "inspection" of tax returns, it does not address how the BIR should respond to subpoenas. Other statutes also touch upon disclosure of tax information by the BIR. For example, title 33, § 1532 imposes penalties upon public employees who disclose tax return information without proper authorization. However, no statute or regulation specifically addresses the BIR's obligation to respond to subpoenas.

Virgin Islands courts have not yet addressed whether the V.I. Code prevents the BIR from disclosing tax information. Therefore, the Court looks to other jurisdictions for guidance. In *Kirk v. First National Bank*, a federal district court considered whether the Internal Revenue Service had to comply with a subpoena demanding tax information.[7] Considering 26 U.S.C. § 6103, which

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[3] Subpoena Duces Tecum, p. 13, ¶ 6 (Dec. 5, 2017).
[4] *Gustav A. Danielson & Co., P.C. v. Witty*, 17 V.I. 32, 34 (V.I. Super. Ct. 1980).
[5] *Id.*
[6] The BIR also cites 26 U.S.C. §§6103 and 7213 as authority. These federal statutes address disclosure of information by the Internal Revenue Service, a federal agency. They do not dictate the BIR's obligation to protect taxpayers' returns.
[7] 1976 U.S. Dist. LEXIS 13453 (N.D. Ga. Aug. 27, 1976).

mirrors 33 V.I.C. § 822(a), and reading it congruently with federal statutes that similarly impose penalties upon public employees for divulging tax information, the federal district court held that 26 U.S.C. § 6103 "reflects a valid public policy against disclosure of tax returns grounded in the interest of the government that this policy of confidentiality encourages the full disclosure of income by taxpayers who are assured that their neighbors or competitors will not be apprised of the intimate details of their financial lives."[8] In addition, the court stated that "[i]ncome tax returns are confidential communications between the government and a taxpayer . . . [and] confidentiality ensures full disclosure by the taxpayer and maximizes the revenue to the government."[9]

The Court finds the analysis in *Kirk v. First National Bank* convincing. Section 822(a), when read together with §1532, indicates a legislatively created public policy against the disclosure of tax returns by the BIR. Rules 45(d)(iii) requires the Court to quash or modify a subpoena if it "requires disclosure of privileged or other protected matter, if no exception or waiver applies." The Court determines that the subpoena requests protected matter. Therefore, finding no apparent way to modify the subject subpoena so that it comports with public policy, the Court will quash the subpoena's request for tax returns, except as provided in Section III of this Memorandum Opinion and Order.

II. The Public Policy Proscribes the Disclosure of Other Documents Discussing a Taxpayer's Tax Obligations and Financial Information.

The subpoena does not only request copies of tax returns but all communications between the BIR and various persons. The subpoena defines "communications" as "any transmission of information . . .." This ostensibly would include documents discussing a taxpayer's financial information besides tax returns, such as emails negotiating tax settlements, payment plans, discussions on tax liens, etc. Section 822 only mentions tax returns. However, logically, the same rationale against disclosure of tax returns by the BIR applies to other communications. The Government also needs taxpayers to communicate honestly and forthrightly with the BIR when discussing their tax obligations outside the confines of a tax return.

The Court again looks to *Kirk v. First National Bank* for guidance. The federal district court considered whether technical advice memoranda should also come within the scope of the non-disclosure provisions of 26 U.S.C. § 6103. The federal district court found that allowing the disclosure of other documents discussing information found in tax returns "would frustrate the purpose of maintaining the confidentiality of the taxpayer's returns and the information developed in connection therewith." This Court agrees and finds that forcing the BIR to disclose other documents discussing the same information found in tax returns would undermine the public policy against divulgence of said tax returns. In other words, such an exception would swallow the rule. Therefore, the Court finds there is also a public policy against the BIR disclosing other documents depicting communications between taxpayers and itself. Accordingly, the Court will quash the subpoena's demand for other documents besides tax returns, except as provided in Section III of this Memorandum Opinion and Order.

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[8] *Id.* at *4 (quotations and brackets omitted)

[9] *Id.* (citing *Heathman v. U.S. Dist. Court for the Cent. Dist. of Cal.*, 503 F. 2d 1032 (9th Cir. 1974)).

III. As an LLC Member, Cloutier Has a Right to Inspect JDM's Tax Returns and Other Documents Transmitted to and from the BIR.

Section 822(b) provides shareholders of a corporation with the right to examine the annual income returns of such corporation and of its subsidiaries. Therefore, the statutorily expressed public policy against the BIR divulging tax information as discussed in Sections I and II does not apply to shareholders. While not specifically mentioned in § 822(b), the Court finds that the exception sensibly extends to LLC members.

Cloutier is a member of JDM Associates and, on page 13, paragraph 6, the subpoena demands copies of communications between the BIR and JDM Associates. Finding Cloutier has a right to such communications under § 822(b), the Court will order the BIR to respond to this demand.

IV. The Court Determines that Responding to the Subpoena Would Not Be Burdensome for the BIR.

The BIR contends that the subpoena subjects it to an undue burden because the time frame for compliance is too short, considering the purportedly vast number of documents Cloutier demands. The subpoena indicates a response deadline of December 27, 2017, and the BIR states Cloutier agreed to extend the deadline to January 19, 2018. BIR does not ask the Court to modify the subpoena by further extending the deadline. Instead, it only argues the Court should enter an order quashing the subpoena.

The Court finds that quashing page 13, paragraph 6 of the subpoena would be excessively severe. The Court will quash almost all of the subpoena's demands, which should significantly lessen the work needed to comply with the subpoena. In addition, if the BIR considers the time constraints posed by subpoena burdensome, the logical solution would be to extend the response deadline, instead of quashing the subpoena. However, the BIR did not suggest a new deadline. The Court finds that a one week extension is reasonable.

Accordingly, it is hereby

ORDERED that the Virgin Islands Bureau of Internal Revenue's Motion to Quash Subpoena Duces Tecum is **GRANTED in part** and **DENIED in part**; and it is further

ORDERED that all discovery demands made in the subpoena *duces tecum* served upon the Virgin Islands Bureau of Internal Revenue by Deborah Cloutier and entered on December 5, 2017 are **QUASHED**, except for the following:

> All documents, communications, and electronically stored information transmitted between VIBIR and JDM Associates, LLC or anyone acting on its behalf between April 7, 2005 to present;" and it is further

ORDERED that the Virgin Islands Bureau of Internal Revenue shall provide Deborah Cloutier's counsel with the documents, communications, and electronically stored information specified in the previous paragraph **on or before Friday, January 26, 2018**; and it is further

ORDERED that a copy of this Memorandum Opinion and Order shall be directed to the following:

A. Counsel for John M. Klein
- Kellerhals Ferguson Kroblin PLLC (Attorneys Christopher A. Kroblin and Aysha R. Gregory) and
- Berger Harris LLP (Attorneys Brian M. Gottesman, David B. Anthony, and Sean A. Meluney) at 1105 N. Market Street, Suite 1100, Wilmington, DE 19801

B. Counsel for Debra J. Cloutier
- Dudley, Topper, and Feuerzeig, LLP (Attorneys Gregory H. Hodges and Chad C. Messier),
- Richards, Layton & Finger, P.A. (Attorneys Raymond J. DeCamillo and Ryan P. Durkin) at 920 N. King Street, Wilmington, DE 19801, and
- Rees Broom, PC at 1900 Gallows Road, Suite 700, Tysons Corner, VA 22182

C. Counsel for the Virgin Islands Bureau of Internal Revenue

- Assistant Attorney General Hugh A. Greentree

DATED: January 11, 2018

Denise M. Francois

DENISE M. FRANCOIS
Judge of the Superior Court
of the Virgin Islands

ATTEST:
Estrella H. George
Clerk of the Court
By: Donna D. Donovan
Donna D. Donovan
Court Clerk Supervisor 1/12/2018