Taxpayer Privacy: A Look at the Limitations Period for Wrongful Disclosure Claims.

Tax returns include a variety of sensitive information. Under Section 6103 of the Code, the federal government is required to treat this information as confidential and is only permitted to share it with designated entities, such as state taxing authorities. Confidentiality is reinforced by Section 7431 of the Code, which authorizes a civil action for improper inspection or disclosure of return information and provides for statutory damages or actual damages, along with attorneys' fees. Section 7431 of the Code is subject to a two year limitation period: an action must be brought "within 2 years after the date of discovery by the plaintiff of the unauthorized inspection or disclosure." I.R.C. § 7431(d).

In *Aloe Vera of America, Inc. v. United States,* 2012 U.S. App. LEXIS 23439 (9th Cir. Nov. 15, 2012)("*Aloe Vera II*"), the Ninth Circuit recently focused upon when the two year period begins to run. The taxpayers, who had been the subject of a combined audit between Japanese tax officials and the IRS, asserted that IRS employees had disseminated false tax return information to Japanese tax authorities. In an earlier appeal, the Ninth Circuit ruled that the limitations period begins to run "on the date when the plaintiff discovers that the unauthorized inspection or disclosure has taken place, regardless of whether the plaintiff believed at that time that the inspection or disclosure was authorized." *Aloe Vera of Am., Inc. v. United States,* 580 F.3d 867, 872 (9th Cir. 2009). *Aloe Vera II* focused on the proper application of this principle.

The Ninth Circuit initially focused on the knowledge requirement, concluding that the general federal inquiry notice standard was applicable. As a consequence, it ruled that the limitations period starts to run "when a plaintiff knows or reasonably should know" of a particular inspection or disclosure. *Aloe Vera II,* 2012 U.S. App. LEXIS 23439 at *10. While the court adopted an inquiry notice standard, it made clear that the statute of limitations is to be assessed on each separate disclosure or inspection: "inquiry notice is not triggered by a single generalized event, but rather by the plaintiff's actual or constructive knowledge of each particular disclosure." *Id.* at *12. As a consequence, it rejected that government's argument that knowledge of the joint audit was sufficient to put the taxpayer on notice for purposes of the statute of limitations, reasoning that "it does not make sense for the statute of limitations to start to run on a single date for all disclosures if some of the disclosures have not yet been made." *Id.* at *13-*14. The Ninth Circuit also noted that adopting the government's position would undercut the utility of Section 7431, since audits can take many years.

Another important aspect of the case is the Court's treatment of the taxpayers' claim that the government revealed false return information to Japanese tax authorities, specifically that the subject company had not reported $32 million in income. The government did not endeavor to demonstrate that the information was provided was correct; instead it tried to argue that this was an estimate. *Id.* at *25. The Court of Appeals gave this short shrift, noting that an estimate can be false if it is made by someone who knows that it cannot be true. As the government could not supply any basis for its "estimate," and since the record included evidence tending to show that the IRS knew that the income had been properly reported, the Ninth Circuit held that the plaintiff's claim was sufficient to survive summary judgment. *Id.* at *25-*26.

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