

# IRS whistleblower provision

by Thomas J. Poulin, Esq. and Richard R. Zabel, CPA

**In 1954, the IRS instituted an informant rewards program. However, the program may not have been as successful as initially contemplated, due to the complete discretion of the IRS in determining reward amounts, a cap of 15 percent on the recovery amount and the lack of any appeals process to dispute a reward determination. With the tax gap estimate reaching \$300 billion per year, Congress passed the IRS Whistleblower Provision, 26 U.S.C. §7623, in the Tax Relief and Health Care Act of 2006, in hopes of reducing tax fraud and increasing tax recovery for the U.S. government.**

The IRS Whistleblower Provision is similar to provisions found in the False Claims Act, 31 U.S.C. §3279, which was originally passed in response to fraud involving federal contractors in the American Civil War. The False Claims Act is the primary mechanism used by the government to pursue individuals and corporations that defraud the government. A significant provision of the act allows citizens to sue on behalf of the government, in what is known as a “qui tam” action (“He who sues on behalf of the king as well as for himself”). Typical claimants include individuals with firsthand knowledge of fraudulent conduct, often referred to as “insiders.” These insiders are eligible to receive 15 to 30 percent of the recovery by the United States in successful actions.

Because the False Claims Act specifically excludes tax fraud under §3729(e), the Whistleblower Provision in the Tax Relief and Health Care Act of 2006 was passed to reform the current informant rewards program and to create an office for processing claims.

To fall within the Whistleblower Provision, a violation including taxes, penalties and interest, must exceed \$2 million. If the case involves an individual, there is an added requirement that gross income exceed \$200,000. Since there is no statute of limitations for tax fraud, a claim can be brought at any time. However, to submit a claim and receive a reward under the new IRS whistleblower law, attention to proper procedure is critical. Because of the severity of accusations involving tax violations, claims are submitted under penalty of perjury, with false claims subject to prosecution.

Unlike under the False Claims Act, only the IRS can file suit under the Whistleblower Provision in the Tax Relief and Health Care Act of 2006. The IRS makes reward determinations based on the quality of information and the level of contribution to the action. Individuals who substantially contribute to successful claims can receive a reward ranging between 15 and 30 percent of the amount collected by the government. The provision does, however, allow a lesser percentage not exceeding 10 percent, for whistleblowers who are not the original source, but contribute to the additional collection of information or for those who contribute to a lesser than substantial degree. As a further enticement to disclose tax violations, rewards less than an individual’s gross income are not considered income for tax purposes.

In general, rewards for claims based on similar allegations are typically awarded to the first to file. However, if a later filed claim contains greater detail or different underlying information, the reward would go to the individual who had the better information and contributed more to the case. Rewards are reduced for persons who either helped plan or initiate the actions that led to the tax violation. Further, rewards are denied to those convicted of criminal conduct arising from the action or employees of the government who discovered the information while performing official duties.

If an individual is not satisfied with the amount of a reward, he or she has 30 days from the IRS award determination to appeal to the United States Tax Court. Rewards are distributed when the IRS collects the amount owed.

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Congress estimates that the new Whistleblower Provision will raise at least \$32 million over five years and \$182 million over 10 years. Accordingly, at least \$27 million to \$54 million could be awarded to individuals over the next 10 years. Thus far, the IRS has received approximately 20 reward claims, with one claim alone involving \$350 million in underpaid taxes.

Despite the fact that the act was passed in December 2006, the Senate already passed modifications in February 2007 in an attempt to increase the number of tax violations reported and enable more whistleblowers to qualify for rewards. The first modification would decrease the minimum violation requirement from \$2 million to \$20,000. Such an action could significantly increase the number of claims submitted

and thus provide rewards for a greater number of whistleblowers. The second modification would preserve a whistleblower's identity. Currently, under the False Claims Act, a case is filed "under seal" during the investigation process, and thus a whistleblower's identity is preserved. Because most cases that meet the current Whistleblower Provision requirements tend to be more complex, consultation with knowledgeable legal counsel is recommended.

Finally, the entire process could take years to conclude. Whistleblowers interested in filing a claim must understand that the investigation of a tax fraud claim is time-consuming. The results of this newly enacted IRS law have yet to materialize, however, given the success of the False Claims Act, the new law is likely to involve substantial recoveries for the U.S. Treasury.



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