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Quit Tam Plaintiffs' Bar Expects Increase in New York Whistle-Blower Cases

Now that New York's highest court has allowed a high-profile whistle-blower tax case to proceed, members of the qui tam plaintiffs' bar tell Bloomberg BNA that more of these types of cases will be filed.

They said qui tam cases will help the state close its tax gap, while also leveraging resources that may not be available to the state. In addition, they said qui tam cases will help the state identify specific areas of potential noncompliance and fraud that would otherwise be difficult to uncover through audits and other means.

In a case of first impression, the New York Court of Appeals ruled Oct. 20 that the state may proceed with its False Claims Act case against Sprint Nextel Corp. for the company's alleged failure to collect and pay sales taxes on flat-rate calling plans (*People v. Sprint Nextel Corp.*) (203 DTR K-1, 10/21/15).

The closely watched *Sprint* case was remitted to the New York Supreme Court in Manhattan, where a trial date has been set for April 5 (*People ex rel v. Sprint Commc'ns, Inc.*, N.Y. Sup. Ct., No. 103917/2011).

''The New York AG (attorney general's) office has already been viewed as incredibly welcoming and open to tax whistle-blowers with good cases that are well-drafted,'' Dean Zerbe, a partner at Zerbe, Fingeret, Frank & Jadav P.C., told Bloomberg BNA in a Dec. 22 e-mail.

Welcome Mat for Cases. ''The Sprint case will make the New York AG's welcome mat to tax whistle-blowers even bigger,'' said Zerbe, who helped draft the IRS whistle-blower statute in 2006 when he was tax counsel to the chairman of the Senate Finance Committee.

''It is clear that the cases that are going to be well-received are those that are: well-documented; involve open/current tax years; have significant dollars at issue; a credible whistle-blower; provide a thorough understanding of the applicable law; and are well-briefed,'' he said.

The *Sprint* case was the first one in which Attorney General Eric Schneiderman (D) agreed to pursue claims on behalf of a whistle-blower plaintiff. Schneiderman, who sponsored the FCA statute when he was a state senator, declined to take on two other prominent qui tam cases.

One of the other cases was dismissed Nov. 13 by the New York Supreme Court, which ruled that the whistle-blower, a former in-house tax attorney for the Vanguard Group Inc., couldn't proceed with the case because he violated confidentiality provisions in the state's ethics rules for attorneys.

The court said the plaintiff, David Danon, improperly relied on confidential documents obtained while he was employed by Vanguard to bring the action under the FCA (*State of New York ex rel. David Danon v. Vanguard Grp., Inc.*, N.Y. Sup. Ct., No. 100711-13, 11/13/15).

Texas Vanguard Case Settled. Danon settled a similar case in Texas and is expected to appeal the New York decision (225 DTR H-3, 11/23/15).

Another case is before the U.S. District Court for the Southern District of New York and alleges that Citigroup improperly deducted net operating losses from its taxable income in relation to the sale of stock to the Treasury Department under the Troubled Asset Relief Program (TARP). The qui tam plaintiff in the case is Eric Rasmusen, a professor of economics and public policy at the Indiana University Kelley School of Business (*New York ex rel. Rasmusen v. Citigroup, Inc.*, S.D.N.Y., No. 1:15-cv-07826).

Randall M. Fox, a partner at Kirby McInerney LLP, was the bureau chief in the attorney general's Taxpayer Protection Bureau when the *Sprint* case was taken on by Schneiderman and the Vanguard and Citigroup cases weren't. He declined to discuss why Schneiderman chose not to intervene in the two other cases, referring the question to the AG's office.

Fox said qui tam cases ''change the mind-set'' of taxpayers from one of ''catch me if you can.'' He said the cases allow tax authorities to zero in on the specific area of dispute, as opposed to trying to find a needle in a haystack.

''Some people have gotten awfully good at hiding needles in haystacks,'' he told Bloomberg BNA Dec. 18.

Aggressive Tax Positions. Fox said companies that take aggressive or questionable tax positions should ''carefully consider the legality of what they're doing'' and be in a position to explain why it was a valid position.

Erika A. Kelton, an attorney with Phillips & Cohen LLP, said ''whistle-blowers bring significant frauds to light.''

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''These are improper business practices that likely would never have been discovered but for an individual stepping forward and blowing the whistle,'' she told Bloomberg BNA in a Dec. 28 e-mail.

Corporate tax attorneys and others have criticized the use of the FCA in tax cases, arguing that complex tax cases should be handled by the state Department of Taxation and Finance and don't rise to the level of fraud under the Act.

Jack Trachtenberg, an attorney with Reed Smith LLP, has been an outspoken critic of the FCA in tax cases. He told Bloomberg BNA that outright repeal of the statute is on his ''wish list'' for next year, although its highly unlikely.

Bad Tax Policy? ''This (law) was a mistake and represents bad policy,'' Trachtenberg, who was New York's first Taxpayer Rights Advocate in 2009, said in a Dec. 17 e-mail. ''The law is billed as an anti-fraud measure, but it is not. It is a tool to leverage compliance with the state's view of the Tax Code, even when the taxpayer has a good-faith disagreement with the state's interpretation of the law.''

He said that ''tax enforcement should be left to the Department of Taxation and Finance, and the adjudication of tax disputes should be left to the well-established administrative appeal procedures.''

Zerbe disagrees, saying the qui tam cases are causing ''a sea change when it comes to tax enforcement'' and use of False Claim Acts in the area of taxes is ''arguably the smartest and most effective change that has happened in tax enforcement in a generation.''

''The tax cheats used to getting away with not paying their fair share are now waking up to a new world and naturally they don't like it,'' he said. ''None of the unsubstantiated and speculative 'sky-is-falling' hysteria put forward by the tax-cheat enablers has come to pass in the long history and experience of the False Claims Act at the federal and state level.''

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