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Tax Collection
Whistleblower Tips Keep Coming; Program
Future Unclear; Awards Remain Mystery

SAN FRANCISCO--Tips about tax evaders continue to pour into the Internal Revenue Service's new Whistleblower Office, but until some cases become final and whistleblowers receive awards that they believe are fair, it is unclear whether the pace of tips will continue, panelists speaking at the American Bar Association Section of Taxation said Sept. 12.

It is also unclear whether client privilege laws are having a chilling effect on practitioners, especially lawyers, who are concerned they could face civil liability and professional sanctions for acting as whistleblowers in tax cases, panelists said.

Stephen Whitlock director of the IRS Whistleblower Office, said tips involving 900 taxpayers have come into his office since Jan. 1. In December 2007, when IRS released guidance on how to file a whistleblower action with the service, his office received 59 tips. By comparison, in the 12 months between enactment of the new whistleblower law in December 2006 and issuance of the guidance, his office received 80 tips.

"In the last year this has exploded," Whitlock said.

The office screens the tips to determine if they fall under the whistleblower law, which means they must indicate avoidance of \$2 million or more for corporations or high net worth individuals. The whistleblower office refers appropriate cases to the service's operating divisions, which decide whether to proceed with an audit or other investigation. It is unclear how many of the 900 tips reported this year will result in investigations, and it will be several years before any of those investigations result in a collection of tax that entitles the whistleblower to an award, Whitlock said.

Tipsters Disgruntled

Gregory Lynam an attorney with the Ferraro Law Firm in Washington, D.C., which represents whistleblowers, told attendees that, like IRS, his firm has a backlog of cases it is reviewing from potential whistleblowers. He and Whitlock agreed that most cases come from disgruntled tipsters, usually former spouses, business associates, executives, business competitors, or others. Many of the tipsters have direct knowledge of tax noncompliance, and are extremely skilled tax professionals.

Whistleblowers are entitled to between 15 percent and 30 percent of the final tax, with no cap. IRS can reduce or eliminate an award if the whistleblower participated in the tax noncompliance activity, and whistleblowers get no award if they are convicted of a tax evasion violation. Whistleblowers who believe their awards are not fair may appeal them to the U.S. Tax Court.

Whitlock said the service is still ironing out how awards will be determined. For example, if IRS adds an issue to a planned audit because of a whistleblower tip, or if IRS is already planning on auditing for a specific issue and a whistleblower provides information to help make the case, the whistleblower may receive less than if his or her information was more instrumental to the case.

But taxpayer confidentiality issues limit the amount of information about a case and its resolution the service can provide to a whistleblower, Whitlock said. IRS cannot give whistleblowers updates on a case's status such as whether the taxpayer has been audited or tax has been assessed, or explain the basis for an eventual award. Without

that information, it will be difficult for a whistleblower to decide if an award is fair. Whistleblowers who disagree with the amount of an award must then weigh whether to challenge it by appealing to tax court, in exchange for losing much of their own confidentiality protections.

"We have to find a way to explain ourselves," Whitlock said.

Waiting for Evidence of Awards

Until awards are made and publicized, or until the whistleblower office issues a few annual reports showing the results of the program and including awards to whistleblowers, the number of new tips coming in may level off or decline, Whitlock said. If just a few large awards are announced, the program could explode even further. "Once the process moves to an award or a substantial award, we'll see a new wave," Lynam agreed.

Little information is available yet on the progress of cases or awards, although the Ferraro Law Firm has announced several filings with the Whistleblower Office including a June announcement of a filing involving a Fortune 500 company that has allegedly underpaid its U.S. tax liability by more than \$4.4 billion (115 DTR G-4, 6/16/08).

Dennis J. Ventry, an acting professor of law at the University of California, Davis School of Law, told attendees that, although tax professionals are the logical people to blow the whistle, the competing obligations they face make it difficult. Practitioners, especially attorneys, often believe that their obligation to the attorney/client privilege of information is absolute and requires them to protect tax noncompliance.

Attorneys Have Authority to Blow Whistle

However, the growing federal regulation of tax attorneys give them much more authority than they often believe they have, Ventry said. For example, IRS Circular 230 creates a strict discipline regime under which tax practitioners must disclose information they were not previously required to disclose, or face possible fines or disciplinary action for failure to disclose.

Also, the Sarbanes-Oxley Act, in Section 307, essentially created a whistleblower statute for tax attorneys by requiring them to report violators of federal securities law up the chain of command at an organization, and then to board members if necessary.

Also, IRS Chief Counsel Notice 2008-011, which prohibits a practitioner who represents a taxpayer at audit from also blowing the whistle (59 DTR G-1, 3/27/08), does not apply to practitioners involved in planning a transaction, Ventry said.

A potential snag is the conflict between federal rules and state law obligations regarding client privilege, Ventry said. A practitioner may have the authority at the federal level to blow the whistle, but could face sanctions at the state level, for example from a state bar association, or could face civil liability such as a tort claim from the taxpayer.

No cases have emerged yet to test whether the federal rules trump client privilege obligations under state law, Ventry said. Meanwhile, it appears that few of the tipsters who have contacted the Whistleblower Office are attorneys.

By Laura Mahoney