

# Does Tax Crime Pay (Whistleblowers)?

*By Erica L. Brady*

Erica L. Brady criticizes the exclusion of criminal fines from whistleblower awards.

The IRS has recently changed its position on the inclusion of criminal fines in the amount on which a whistleblower award can be paid. The change in position came after the enactment of amendments to Code Sec. 7623, which requires the IRS to pay awards to whistleblowers who meet certain criteria. Had the IRS not expressly excluded criminal fines from “collected proceeds,”<sup>1</sup> the monies the IRS collects from criminal prosecutions based on the information provided by the whistleblower likely would have been included in the “collected proceeds,” as they traditionally had been. The IRS’s change in policy appears to be based on an overly constrained interpretation of the 1984 Victims of Crime Act,<sup>2</sup> which requires criminal fines to be deposited into a specific fund. Contrary to the IRS’s interpretation is a Congressional mandate that whistleblowers be paid a designated percentage of collected proceeds as an award for providing information to the IRS.<sup>3</sup> Since the Congressional mandate occurred long after the enactment of the Victims of Crime Act, the more recent mandate should be read as Congress’s current expression of their intent and all collections from criminal prosecutions, including criminal fines, should be included in collected proceeds.

While the amount of criminal fines is generally small in comparison to the amount of the underpaid taxes in any given tax case, it is still unfair for the government to collect monies for violations

of tax laws based on the information provided to the IRS by a whistleblower and not pay a portion of the monies collected to the whistleblower. Considering that those convicted of a tax crime are the ones who committed the most flagrant violations of tax law, the IRS should be incentivizing potential whistleblowers with information regarding the most flagrant violations of internal revenue laws to come forward. Especially because the IRS has the tools to incentivize these potential whistleblowers as criminal prosecutions are expressly included as award eligible actions under Code Sec. 7623.

Congress revised the IRS whistleblower program in the Tax Relief and Health Care Act of 2006, significantly changing a previously existing, but ineffective, program.<sup>4</sup> Congress’s intent in enacting the enhanced whistleblower award provisions was to “provide focus on large-dollar cases with the potential of collecting billions of dollars for the Department of Treasury.”<sup>5</sup> The enhanced award provisions mandate that:

If the Secretary proceeds with any administrative or judicial action described in subsection (a) based on information brought to the Service’s attention by an individual, such individual shall, subject to paragraph (2), receive as an award at least 15 percent but not more than 30 percent of the collected proceeds (including penalties, interest, additions to tax, and additional amounts) resulting from the action (including related actions) or from

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any settlement in response to such action. The determination of the amount of such award by the Whistleblower Office shall depend upon the extent to which the individual substantially contributes to such action.<sup>6</sup>

Subsection (a) describes the administrative or judicial actions that are award eligible as “(1) detecting underpayments of tax, or (2) detecting and bringing to trial and punishment persons guilty of violating the internal revenue laws or conniving at the same.”<sup>7</sup> In order to ensure that the enhanced award provisions target large-dollar cases, the statute requires that the amount in dispute exceeds \$2 million and, if the information relates to an individual taxpayer, the individual’s gross income exceeds \$200,000 for any tax year subject to such action.<sup>8</sup>

At the time that Congress enacted the enhanced whistleblower provisions, criminal fines were regularly included in collected proceeds. For example, the technical explanation of the Tax Relief and Health Care Act of 2006 states that the law in effect at that time was that “[a]mounts are paid on a percentage of tax, fines, and penalties (but not interest) actually collected based on the information provided.”<sup>9</sup> In addition, obsolete Publication 733<sup>10</sup> and the standard contract the IRS entered into with whistleblowers<sup>11</sup> included taxes, fines and penalties (but not interest) in collected proceeds. The 2006 Treasury Inspector General for Tax Administration (TIGTA) Report, *The Informants’ Reward Program Needs More Centralized Management Oversight*, states that “[t]he dollar amount of the reward is computed by multiplying the reward percentage by the amount of taxes, fines, and penalties (but not interest) collected.”<sup>12</sup>

In fact, some guidance still identifies criminal fines as part of collected proceeds. The regulations under Code Sec. 7623, specifically Reg. §301.7623-1(c), which was enacted prior to the change in the statute, expressly includes fines in the types of monies collected that are used to pay an award several times. The Treasury Regulation even provides that “[p]artial reward payments, without waiver of the uncollected portion of taxes, penalties, or fines involved may be made when a criminal fine has been collected prior to the completion of the civil aspects of a case ... .”<sup>13</sup> Also, IRS Policy Statement 4-27 provides:

1. Rewards determined by value of information furnished and Computation and payment of rewards
2. The Internal Revenue Service will pay claims for reward applied for on Form 211 commensurately with the value of the information furnished voluntarily and upon the informant’s own initiative with respect to taxes, fines, and penalties (but not interest) the IRS collects.<sup>14</sup> ...

In drafting the 2006 amendments to Code Sec. 7623, Congress expressly included criminal tax prosecutions in the actions that are award eligible under Code Sec. 7623(b) by referencing the actions in subsection (a). Criminal tax prosecutions result in two types of payments to the government, criminal fines and restitution payments. As criminal prosecutions are expressly included in the types of actions that are award eligible, the monies that are regularly collected from these actions should logically be included in collected proceeds.

Congress did not expressly define the limits of “collected proceeds” anywhere in Code Sec. 7623. The section only provides a nonexclusive list by stating “collected proceeds (including penalties, interest, additions to tax, and additional amounts).”<sup>15</sup> The language of Code Sec. 7623 specifying what is included in collected proceeds should be read as an exemplary, rather than an exhaustive list of the types of monies included in collected proceeds. The statute prefaces the list of the types of monies included in collected proceeds with the term “includes,” which “when used in a definition contained in [Title 26] shall not be deemed to exclude other things otherwise within the meaning of the term defined.”<sup>16</sup> Therefore, the list included in the statutory language should not be treated as an exhaustive list of the types of monies that fall into collected proceeds, but rather as examples of types of monies that are included in collected proceeds. Moreover, collections in criminal cases are reasonably included in the plain and ordinary meaning of additional amounts because the ordinary meaning of additional amounts is amounts not otherwise listed, which reasonably includes collections from criminal tax prosecutions.

***Collections from criminal prosecutions should be part of collected proceeds.*** As Code Sec. 7623 ex-

pressly refers to criminal prosecutions as one of the actions that can result in payment of an award, collections from criminal prosecutions, which include criminal fines and restitution payments, should be included in collected proceeds.

***Criminal fines should be included in collected proceeds because criminal prosecutions are one of the actions upon which the IRS must pay whistleblower awards.*** Criminal fines serve to punish those who have violated criminal laws. Criminal tax charges are brought under a number of sections found in Title 18 and Title 26, all of which provide for the possibility of criminal fines, as well as jail time, as punishment.<sup>17</sup> The purpose of criminal fines is strictly punitive. In fact, all criminal fines collected from persons convicted of offenses against the United States, with a handful of the exceptions related to certain environmental, railroad unemployment insurance and postal service violations, are deposited in to the Crime Victims Fund.<sup>18</sup> The IRS has taken the position, in PTMA 2010-60<sup>19</sup> and in the IRM 25.2.2, that criminal fines, which must be deposited into the Crime Victims Fund, are excluded from collected proceeds.

As no tax crimes generate criminal fines within a statutory exception to the Victims of Crime Act, all criminal fines from tax prosecutions are deposited in the Crime Victims Fund under the IRS's reading of the statute.

The IRS first publicly stated that criminal fines were not part of collected proceeds in the revised whistleblower provisions of the IRM. The IRM states, "[c]riminal fines, which must be deposited into the Victims of Crime Fund [sic], cannot be used for payment of whistleblower awards."<sup>20</sup> Later the IRS released PTMA 2010-60, in which the IRS simply dismisses criminal fines from being part of collected proceeds "because the IRS does not collect fines imposed by a court in connection with a criminal prosecution, [the IRS does] not think that these fines can be considered 'collected proceeds' [sic]"<sup>21</sup> The PTMA goes on to state that Code Sec. 7623(b) and the Victims of Crime Act can be read harmoniously, giving full effect to both statutes.

The topic of the inclusion of criminal fines in collected proceeds was a constant theme in the comments on Proposed Reg. §301.7623-1(a), which provides further clarification of what is included in collected proceeds.<sup>22</sup> During the public hearing, held May 11, 2011, on the Proposed Treasury Regulations the IRS claimed:

I think there is also a misconception out there about where we stand on criminal fines. I think the only thing that we have said so far with respect to criminal fines is with respect to a very narrow circumstance where criminal fines are deposited into and segregated into a fund specifically identified under Title XVIII or another title of the code.<sup>23</sup>

The IRS's statement improperly tries to narrow the issue. In other words, the IRS is saying that it cannot pay awards on just some criminal fines, but what it really means to say is it cannot pay awards on any criminal fines. The IRS's position is that Code Sec. 7623(b) does not create an exception to the Victims of Crime Act, thus any criminal fines that must be deposited in the Crime Victims Fund are unavailable to pay whistleblower awards. However, section 10601(b) of Title 42 requires that *all* fines that are collected from persons convicted of offenses against the United States, unless specifically excluded, be deposited into the Crime Victims Fund. None of the criminal fines specifically excluded by statute are tax crimes; therefore, according to the IRS's position, they are unable to pay awards on any criminal fines.

The logic of the IRS's position, as laid out in PTMA 2010-60, is flawed in that it ignores Congress's express mandate to include criminal proceedings as award eligible actions in a mandatory award program; thereby, not giving full effect to both statutes. Currently it is impossible to give both statutes full effect because Code Sec. 7623(b) requires award payments from proceeds collected from the "punishment of persons guilty of violating internal revenue laws."<sup>24</sup> In order to read both statutes in a manner that gives full effect to both, 15 to 30 cents of every dollar collected as a criminal fine must be distributed twice, once to the Crime Victims Fund and again to the whistleblower.

Where two statutes cannot be read in a manner that allows for both statutes to be given full effect, the more recent statute is given effect as the most recent expression of Congressional intent and the older is treated as impliedly amended to allow for the newer statute.<sup>25</sup> In the case of the conflict between the mandate that awards be paid from collected proceeds to whistleblowers in Code Sec. 7623(b) and that all criminal fines, unless specifically exempted, be deposited in the Crime Victims

Fund, would mean that Code Sec. 7623(b) should be given full effect. The conflict between the two statutes did not arise until 2006 when Congress mandated payments from monies collected to whistleblowers who provide information to the IRS that leads to the punishment of persons guilty of violating internal revenue laws. At the time the amendments that created the award mandate were drafted, Congress sought to strengthen an already existing program. The existing program included criminal fines as part of the collected proceeds upon which an award could be paid at the discretion of the IRS. Code Sec. 7623 was amended in 2006 to create the mandatory award program that pays awards from collected proceeds, long after the Victims of Crime Act was enacted. Therefore, Code Sec. 7623(b) should be given full effect as the more recent expression of Congressional intent. Thus, the whistleblower would receive between 15 and 30 percent of the criminal fines, and the remainder would be deposited into the Crime Victims Fund. Therefore, not only is the IRS's position that criminal fines are not part of collected proceeds damaging to the administration of the whistleblower program, but, for the reasons discussed above, the position lacks legal support.

***Restitution payments should be included in collected proceeds because restitution payments are payments of tax.*** The IRS has been silent on its position with regard to restitution payments. Restitution payments are clearly "collected proceeds" because restitution payments are "in fact and law a payment of unpaid taxes."<sup>26</sup> Restitution payments serve to compensate a victim for the loss caused by the defendant and often serve as a substitute for a civil judgment.<sup>27</sup>

In criminal tax cases, the IRS may be identified as a victim and the defendant may be ordered to pay restitution to the IRS for the tax related loss.<sup>28</sup> Restitution is ordered pursuant to 18 USC §3556, and enforcement of the restitution order is retained by the government under Title 18, including 18 USC §3664.<sup>29</sup> In 1982, Congress in an attempt to encourage courts to make broader use of restitution enacted the Victim and Witness Protection Act of 1982 (VWPA).<sup>30</sup> The VWPA provides for restitution in among other cases, Title 18 criminal cases and any criminal case (including Title 26 cases) when a defendant agrees to pay restitution as a part of a plea agreement. Fourteen years later, Congress enacted the Mandatory

Victim Restitution Act of 1996 (MVRA), which generally requires full restitution for all Title 18 criminal cases, including cases involving non-Title 26 tax-related charges, including charges under 18 USC §§286, 287, 371, 1001.<sup>31</sup>

In 2002, a joint task force between the IRS and the Department of Justice was formed to study the issue of restitution in criminal tax cases in response to a growing perception that many criminal defendants, despite being convicted of violating tax laws, are nevertheless escaping all responsibility for the payment of the taxes associated with the offenses for which they had been convicted.<sup>32</sup> In May 2005, the Attorney General issued new guidelines on victim and witness assistance, which require that prosecutors in all cases "must consider 'requesting that the defendant provide full restitution to all victims of all charges contained in the indictment or information, without regard to the counts to which the defendant actually plead[s].'"<sup>33</sup>

When a defendant makes restitution payments, the IRS must adjust the unpaid civil tax liability because restitution in tax cases is a payment of unpaid taxes.<sup>34</sup> Prior to August 16, 2010, the IRS was unable to administratively collect on a restitution order because restitution is not an assessable tax.<sup>35</sup> However, that is no longer the case since The Firearms Excise Tax Improvement Act of 2010 added Code Sec. 6201(a)(4).<sup>36</sup> Code Sec. 6201(a)(4) now requires the IRS to "assess and collect the amount of restitution under an order pursuant to section 3556 of title 18, United States Code, for failure to pay any tax imposed under this title in the same manner as if such amount were such tax." As restitution payments represent unpaid taxes and are assessed and collected as a tax per statute, restitution payments should be included as part of collected proceeds for purposes of making a whistleblower award determination just as any other tax assessed and collected by the IRS would be included as part of collected proceeds.

## **Conclusion**

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Although "collected proceeds" is not defined in Code Sec. 7623, it is clear that Congress intended the definition of collected proceeds to be broad. Specifically, collected proceeds should include criminal fines and restitution payments resulting from the prosecution of tax crimes. Congress intended to strengthen the whistleblower program by

increasing incentives for whistleblowers to come forward. To that end, Congress mandated that an award be paid from the proceeds collected based on the information the whistleblower provided.

By excluding criminal penalties from collected proceeds, the IRS is discouraging potential whistleblowers with knowledge of the most egregious tax law violations from providing information.

## ENDNOTES

- <sup>1</sup> IRM 25.2.2.12 (9) (6-18-2010).
- <sup>2</sup> Victims of Crime Act of 1984 (P.L. 98-473).
- <sup>3</sup> Act Sec. 406 of the Tax Relief & Health Care Act of 2006 (P.L. 109-432).
- <sup>4</sup> Act Sec. 406 of the Tax Relief & Health Care Act of 2006 (P.L. 109-432), 120 Stat. 2958. See Michelle M. Kwon, *Whistling Dixie About the IRS Whistleblower Program Thanks to the IRC Confidentiality Restrictions*, 29 VA. TAX REV. 447, 451–55 (2010) for a discussion of the history of the Internal Revenue Service's whistleblower program.
- <sup>5</sup> Treasury Inspector General for Tax Administration, *Deficiencies Exist in the Control and Timely Resolution of Whistleblower Claims* (Aug. 20, 2009), available at [www.ustreas.gov/tigta/auditreports/2009reports/200930114fr.pdf](http://www.ustreas.gov/tigta/auditreports/2009reports/200930114fr.pdf), at 1.
- <sup>6</sup> Code Sec. 7623.
- <sup>7</sup> Code Sec. 7623(a).
- <sup>8</sup> Code Sec. 7623(b)(5). Where statutory thresholds in Code Sec. 7623(b)(5) are not met, an award may be paid at the IRS's discretion under Code Sec. 7623(a). Code Sec. 7623(b)(2) provides for awards in cases of less than substantial contributions, and Code Sec. 7623(b)(3) provides rules for determining when there can be a reduction in, or a denial of, an award.
- <sup>9</sup> The Joint Committee on Taxation staff's technical explanation of H.R. 6408, The Tax Relief and Health Care Act of 2006, as introduced in the House on December 7, 2006 (JCX-50-06, Dec. 7, 2006).
- <sup>10</sup> Publication 733, *Rewards for Information Provided by Individuals to the Internal Revenue Service* (Obsoleted).
- <sup>11</sup> *Confidential Informant 92-95-932X*, FedCl, 2000-2 USTC ¶ 50,785, 45 FedCl 556 (2000); *B.W. Jarvis*, FedCl, 99-1 USTC ¶ 50,559, 43 FedCl 529 (1999).
- <sup>12</sup> Treasury Inspector General for Tax Administration Report 2006-30-092, *The Informants' Rewards Program Needs More Centralized Management Oversight* (June 2006).
- <sup>13</sup> Reg. §301.7623-1(c): "Payment of a reward will be made as promptly as the circumstances of the case permit, but not until the taxes, penalties, or fines involved have been collected."
- <sup>14</sup> IRM §1.2.13.1.12 (emphasis added).
- <sup>15</sup> Code Sec. 7623(b)(1).
- <sup>16</sup> Code Sec. 7701(c).
- <sup>17</sup> 18 USC §§286, 287, 371, 1001, and Code Sec. 7201 *et sec.* Charging a defendant in a tax case with a Title 18 offense is often preferred because restitution is more readily available for Title 18 offenses than Title 26 offenses. 2008 Department of Justice Criminal Tax Manual 22.02[1].
- <sup>18</sup> 42 USC §10601 (2006). The Crime Victims Fund was established by the Victims of Crime Act of 1984 (P.L. 98-478), title II, §1402, Oct. 12, 1984, 98 Stat. 2170, to fund victim services throughout the nation.
- <sup>19</sup> PMTA 2010-60, Criminal Fines and Whistleblower Awards (February 22, 2010), released April 20, 2011.
- <sup>20</sup> IRM §25.2.2.12.9.
- <sup>21</sup> *Supra* note 16.
- <sup>22</sup> 26 CFR Part 301 [REG-131151-10] (Jan. 18, 2011).
- <sup>23</sup> Transcript of Public Hearing on Proposed Regulations 26 CFR Part 301 "Rewards and Awards for Information Relating to Violations of Internal Revenue Laws" [REG-131151-10] (May 11, 2011).
- <sup>24</sup> Code Sec. 7623(a)(2).
- <sup>25</sup> *Blue Cross and Blue Shield of Alabama, Inc. v. Nielsen*, CA-11, 116 F3d 1406, 1410 (1997); see also 73 Am. Jur. 2d Statutes §169.
- <sup>26</sup> *L.M. Helmsley*, CA-2, 91-2 USTC ¶ 50,455, 941 F2d 71, 102 (1991).
- <sup>27</sup> "There is a split in the circuits concerning whether restitution inflicts a criminal punishment and is therefore punitive." CRIMINAL TAX MANUAL §44.01, note 1. Referencing, *compare Perez*, CA-3, 514 F3d 296, 298 (2007) (restitution is criminal penalty), and *Cohen*, CA-4, 459 F3d 490, 496 (2006) (although restitution allows victims to recover losses that might be available in civil litigation, restitution is part of criminal defendant's sentence), with *Serawop*, CA-10, 505 F3d 1112, 1122–23 and note 4 (2007) (Mandatory Victim Restitution Act of 1996 does not inflict criminal punishment and is not punitive; collecting cases discussing circuit split).
- <sup>28</sup> The United States and its agencies, including the IRS, may qualify as victims under VWPA and MVRA. See, e.g., *Leahy*, CA-7, 464 F3d, 793 (2006); *Senty-Haugen*, CA-8, 449 F3d 862, 865 (2006) (MVRA definition of victim same as VWPA, IRS is eligible victim under MVRA); *Ekanem*, CA-2, 383 F3d 40, 42–44 (2004); *Butler*, CA-6, 297 F3d 505, 518 (2002) (approving order to pay restitution to the IRS); *Lincoln*, CA-9, 277 F3d 1112, 1114 (2002); *Tucker*, CA-8, 217 F3d 960, 962 (2000); *Min-neman*, 143 F3d, at 284; *Vaknin*, 112 F3d, at 591; *Martin*, 128 F3d, at 1190–92; see also *Kirkland*, CA-5, 853 F.2d 1243, 1246 (1988) (upholding restitution order to the Farmers Home Administration); *Sunrhodes*, CA-10, 831 F2d 1537, 1545–46 (1987) (quoting *Ruffen*, CA-9, 780 F2d 1493, 1496 (1986)) (upholding restitution order to Indian Health Service).
- <sup>29</sup> CC-2011-018, *The Assessment and Collection of Criminal Restitution*.
- <sup>30</sup> Victims and Witness Protection Act of 1982 (P.L. 97-291), 96 Stat. 1248 (codified as amended in scattered sections of 18 USC, with restitution provisions at 18 USC §3663).
- <sup>31</sup> Act Sec. 204(a) of the Antiterrorism and Effective Death Penalty Act of 1996 (P.L. 104-132), 110 Stat. 1227 (codified as amended at 18 USC §3663A).
- <sup>32</sup> Memorandum re Standard Language for Pleas and Orders in Criminal Tax Cases Involving Restitution (updated November 2010).
- <sup>33</sup> Memorandum re Standard Language for Pleas and Orders in Criminal Tax Cases Involving Restitution (updated November 2010) citing Guidelines at 39, citing Act Sec. 209 of P.L. 104-132; 18 USC §3551 note.
- <sup>34</sup> *Helmsley*, *supra* note 23, 941 F2d, at 102.
- <sup>35</sup> CC-2011-018, *The Assessment and Collection of Criminal Restitution* (Aug. 26, 2011).
- <sup>36</sup> Act Sec. 3 of the Firearms Excise Tax Improvement Act of 2010 (P.L. 111-237), 124 Stat. 2497.

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