

Speakers Complain of Narrow Proceeds Definition for Whistleblower Awards

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Private practitioners at a May 11 IRS hearing uniformly encouraged the agency to adopt a broader definition of collected proceeds when calculating whistleblower awards.

The proposed regs, released in January 2011, set out a definition of collected proceeds that allowed refunds and some credit balances to be included in the base amount used to calculate an award amount. But practitioners widely criticized the IRS for not expanding the types of collection actions that would potentially qualify for whistleblower awards. (For REG-131151-10, see *Doc 2011-880* or *2011 TNT 11-11*. For prior coverage, see *Doc 2011-883* or *2011 TNT 11-3*. For a collection of submitted written comments on the proposed reg, see *Doc 2011-9899* or *2011 TNT 90-33*.)

Linda J. Stengle of Kenney & McCafferty PC said the IRS needs to tweak the proposed regs to give whistleblowers incentive to report corporate fraud. She called the regs "a good step forward" but said they are too narrow. Prior IRS practice has been to take a broad approach to calculating the base of an award amount, she said, so the proposed regs constitute an "impermissible narrowing" of the definition of proceeds. Because the IRS unilaterally changed the definition of collected proceeds in the Internal Revenue Manual without any opportunity for public input, she said, the agency should not adhere to those provisions in the manual until they are publicly scrutinized.

Stengle said section 7623 lays out a "broader vision of collected proceeds" than the IRS interpretation of the statute in both the IRM and the proposed regs. Requiring an overpayment in the credit balance area is confusing, she testified, because any credit balance should constitute proceeds for determining the award base. Overpayment is an "obfuscation" of the term "credit balance," she said. It is "absurd" for the government to require an actual cash payment to the fisc before the whistleblower is entitled to an award, she said.

Ultimately, the government should adopt a definition of collected proceeds that encompasses any "positive net effect" on the Treasury, Stengle said. That would include corporate refunds, future benefits, and net operating losses, as well as criminal fines, which used to be included in whistleblower award calculations. She said that her personal experience shows that unless the definition of collected proceeds expands to include government recoveries from large corporations, there are "too many disincentives to blowing the whistle."

Thomas Kane, special counsel, IRS Office of Chief Counsel (Procedure and Administration), a member of the government panel assembled at the reg hearing, said

that NOLs, as a deduction, are just one of many items that could cause the IRS to recalculate a taxpayer's tax liability, which in turn could lead to a whistleblower award. "Our reg is intended to focus on certain elements of collected proceeds, which is the money at the end; it is not intended to focus on certain aspects or tax attributes that went into that calculation," he said. NOLs would be dealt with directly in future guidance, he said; therefore, they shouldn't be a concern.

Stengle responded that because of potential NOL carryforwards, the IRS should allow an NOL to factor into the award calculation for determining a particular year's tax liability. But Kane replied that the IRS doesn't have the statutory authority to determine the present value of some speculative, future use of an NOL in order to pay a currently due award.

Kane also said comments critical of the IRS position on criminal fines were premature, noting that the government has not finished its work in that area. Instead, it has only addressed the applicability of the Crime Victims Fund as it relates to an award payment.

Scott A. Knott of the Ferraro Law Firm expressed concern that the proposed language may not pick up all situations in which a refund claim is denied, saying, "It's a breadth issue." He also pointed out that in the corporate context of credits, there are many more situations of credit balances than just overpayments. The proposed reg unduly ties the hands of the IRS Whistleblower Office when credits like the foreign tax credit or alternative minimum tax credit may be in play. The IRS needs to "make sure that the reg does no harm to the statute" in limiting what was intended, he said.

Knott said waiting to pay an award until the period of limitations for filing a refund claim has expired may be overkill in some circumstances. But Kane said the IRS is concerned that a taxpayer could successfully challenge a refund denial; therefore, paying out an award on a collected tax liability that might be eventually handed back to the taxpayer is problematic. He agreed that Form 906 closing agreements "clear the deck" because those determinations are final but said claims covered by Form 870-AD are not as clear. The IRS will issue awards "if we're not in the position of having to pay money back," he said.

Thomas C. Pilske of Tax Whistleblower Law Firm LLC began his remarks by saying that the public holds the negative view that the IRS is opposed to the tax whistleblower program. Echoing the sentiments of the other speakers, he said that the government should embrace an expanded definition of collected proceeds that also includes related parties, related years, and related taxpayers. The IRS should also consider "springing awards" that would become payable if more taxes are collected in the future as a result of the information provided by the whistleblower, he said.

Pilske said that despite the proposed exclusion from the award base of criminal fines imposed by district courts, to the extent the IRS is considered a victim, fines collected and deposited into the Crime Victims Fund should be made available to the whistleblower.

Richard Rubin of Finch McCranie LLP said the IRS's limited definition of collected proceeds affects not only the potential amount of an award but the very existence of a possible claim. The IRS really hasn't set out a proposed definition at all in the regs, he said, adding that proceeds "remain to be defined." The fundamental principle behind proceeds is a net benefit to the Treasury, which is why the prevention of future tax evasion should be addressed in regulations, he said.

Michael Sullivan, also of Finch McCranie, said the IRS whistleblower program should provide meaningful and predictable rewards to help encourage whistleblowers to come forward. It was the plain intent of Congress to "expand the number and types of whistleblower claims that the IRS would receive, and ultimately be able to pursue, otherwise huge tax schemes would go undetected," he said.