



MULTISTATE TAX COMMISSION

Maximizing the synergies of multi-state tax cooperation

To: MTC Class Action and False Claims Act Work Group

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Subject: Summary of Internal Revenue Service Tax Whistleblower Statute and Regulations

I. Payment of Awards to Whistleblowers

Section 7623 of the Internal Revenue Code establishes the federal tax whistleblower program and provides for the payment of awards to whistleblowers in the event the IRS collects proceeds (including penalties, interest, additions to tax and additional amounts) from any action – including a related action – or from any settlement in response to such action, if the whistleblower provided information that substantially contributed to such action.

Under Section 7623(a), the IRS is authorized to promulgate regulations to govern the payment of awards, in the amount the Secretary deems necessary, if the information provided substantially contributed to (1) detecting underpayment of tax, or (2) detecting and bringing to trial and punishment persons convicted of violating the internal revenue laws or conniving at the same. Section 7623 does not apply if the payment of such awards is otherwise provided by law. Any amounts awarded are to be paid from the proceeds of amounts collected by reason of the information provided.

Pursuant to Section 7623(b)(1), the Secretary may award at least 15 percent but not more than 30 percent of collected proceeds, depending on the extent to which the whistleblower substantially contributed to such action.

If the Whistleblower Office determines that the information provided by the whistleblower resulted from a judicial or administrative hearing, from a government report, hearing, audit, or investigation or from the news media, the amount of the award is limited to no more than 10 percent of the amount of collected proceeds. Section 7623(b)(2)(A). The ten percent limitation is inapplicable if the whistleblower is the original source of the information. Section 7623(b)(2) (B).

The Whistleblower Office may reduce the amount of the award if the claim for an award is brought by an individual who planned and initiated the actions that led to the underpayment of tax. There is no award allowed if the whistleblower is convicted of criminal conduct arising from planning and initiating the actions. Section 7623(b)(3). An appeal of the award determination is provided for in Section 7623(b)(4).

Section 7623(b) applies to actions against any taxpayer. However, if the taxpayer is an individual Section 7623(b) only applies if the individual's gross income exceeds \$200,000 for any taxable year subject to an action under Section 7623 and if the tax, penalties, interest, additions to tax and additional amounts in dispute exceed \$2,000,000. Section 7623(b)(5).

II. Ineligible Individuals

The Secretary has promulgated regulations to implement Section 7623. 26 CFR §301.7623-1(b) lists those individuals who are ineligible for an award. Those individuals include;

1. An employee of the Department of the Treasury or who was such an employee when the individual obtained the information on which the claim is based.
2. An individual who obtained the information through his official duties as an employee of the Federal Government, or who is acting within the scope of those official duties.
3. An individual who is or was required by Federal law or regulation to disclose the information or who is or was precluded from doing so by Federal law or regulation.
4. An individual who obtained or had access to the information based on a contract with the Federal Government; or
5. An individual who filed a claim for award based on information obtained from an ineligible whistleblower for the purpose of avoiding the rejection of the claim based on said ineligibility.

III. Claims to be Based on Specific and Credible Information

Claims must be based on specific and credible information. Submissions that provide speculative information or which lack specific and credible information do not provide the basis for an award. 26 CFR §301.7623-1(c)(1). Claims must be made under penalty of perjury. 26 CFR §301.7623-1(c)(3).

IV. Definitions

26 CFR §301.7623-2 provides definitions for the statutory terms. Proceeds are considered based on information provided when the information substantially contributes to an action against the person identified by the whistleblower if, as a result of the information, the IRS initiates a new action, expands the scope of an ongoing action, or continues to pursue an ongoing action, that would not have been initiated, expanded or continued but for the information provided. 26 CFR §301.7623-2(b).

A related action is defined to mean an action against a person other than the person identified in the information provided and subject to the general action, when

1. The facts relating to the underpayment of tax or violation of the internal revenue laws by the other person are substantially the same as the facts described and documented in the information provided.
2. The IRS proceeds with the action against the other person based on the specific facts described and documented in the information provided, and
3. The other, unidentified person is related to the person identified in the information provided and can be identified using the information originally provided. 26 CFR §301.7623-2(c).

The amount in dispute means the greater of the maximum total of tax, penalties, interest, additions to tax, and additional amounts that resulted from the action with which the IRS proceeded based on the

information provided, or the maximum total of such amounts that were stated in formal positions taken by the IRS in the action. The IRS is to determine the amount in dispute when there has been a final determination of tax as defined in §301.7623-4(d)(2). 26 CFR §301.7623-2(e)(2).

V. Whistleblower Administrative Proceedings and Appeals

Whistleblower administrative proceedings and appeals of award determinations are governed by 26 CFR §301.7623-3.

VI. Factors in Setting Award

26 CFR §301.7623-4 defines the factors used to determine the specific award percentage. Pursuant to 26 CFR §301.7623-4(b)(1), the following factors support a higher award percentage.

1. The whistleblower acted promptly to inform the IRS or the taxpayer of the noncompliance.
2. The information provided identified an issue or transaction of a type previously unknown to the IRS.
3. The information provided identified taxpayer behavior that the IRS was unlikely to identify or that was particularly difficult to detect through the IRS's exercise of reasonable diligence.
4. The information provided thoroughly presented the factual details of tax noncompliance in a clear and organized manner, particularly if doing so saved the IRS work and resources.
5. The whistleblower or its legal representative provided exceptional cooperation and assistance during the pendency of the action.
6. The information provided identified assets of the taxpayer that could be used to pay liabilities, particularly if the assets were not otherwise known by the IRS.
7. The information provided identified connections between transactions, or parties to transactions, that enabled the IRS to understand tax implications that might not otherwise have been understood by the IRS.
8. The information provided had an impact on the behavior of the taxpayer, such as causing the taxpayer to correct a previously-reported improper position.

The following factors support a lower award percentage.

1. The whistleblower delayed informing the IRS after learning the relevant facts, particularly if the delay adversely affected the IRS's ability to pursue an action or issue.
2. The whistleblower contributed to the underpayment of tax or tax noncompliance identified.
3. The whistleblower directly or indirectly profited from the underpayment of tax or tax noncompliance, but did not plan and initiate the actions that led to the underpayment of tax or actions described in section 7623(a)(2).
4. The whistleblower or its legal representative negatively affected the IRS's ability to pursue the action.
5. The whistleblower or its legal representative violated instructions provided by the IRS, particularly if the violation caused the IRS to expend additional resources.
6. The whistleblower or its legal representative violated the confidentiality agreement described in §301.7623-3(c)(2)(iv).
7. The whistleblower or its legal representative violated the terms of a contract entered into with the IRS pursuant to §301.6103(n)-2.

8. The whistleblower provided false or misleading information or otherwise violated the requirements of section 7623(b)(6)(C) or §301.7623-1(c)(3).

26 CFR §301.7623-4(b)(2).

26 CFR §301.7623-4(c)(1) provides for a computational framework for increasing the award for substantial contributions from a base level of 15 percent to either 22 or 30 percent or decreasing it to 15, 18, 22 or 26 percent. 26 CFR 26 CFR §301.7623-4(c)(2) provides a computational framework for determining an award for a less than substantial contribution.

26 CFR §301.7623-4(c)(3) provides that awards are to be reduced or denied if the whistleblower planned and initiated the actions, transactions, or events that led to the underpayment of tax or actions described in section 7623(a)(2). A whistleblower planned and initiated the underlying acts if the whistleblower;

1. Designed, structured, drafted, arranged, formed the plan leading to, or otherwise planned, an underlying act.
2. Took steps to start, introduce, originate, set into motion, promote or otherwise initiate an underlying act, and
3. Knew or had reason to know that an underpayment of tax or actions described in section 7623(a)(2) could result from planning and initiating the underlying act.

In order to determine the appropriate award reduction, the Whistleblower Office must first determine if the whistleblower's role as a planner and initiator was primary, significant, or moderate. 26 CFR §301.7623-4(c)(3)(iii)(A). The award paid to a primary planner and initiator is to be reduced from 67 percent to 100 percent, by 34 percent to 66 percent in the case of a significant planner and initiator, or by 0 percent to 33 percent in the case of a moderate planner and initiator. Awards are to be denied to any whistleblower convicted of criminal conduct arising from his or her role in planning and initiating the underlying acts. 26 CFR §301.7623-4(c)(3)(iii)(B).

Factors demonstrating the extent of a whistleblower's planning and initiating include (but are not limited to) the following.

1. The whistleblower's role as a planner and initiator. Was the whistleblower the sole decision-maker or one of several contributing planners and initiators? To what extent was the whistleblower acting under the direction and control of a supervisor?
2. The nature of the whistleblower's planning and initiating activities. Was the whistleblower involved in legitimate tax planning activities? Did the whistleblower take steps to hide the actions at the planning stage? Did the whistleblower commit any identifiable misconduct (legal, ethical, etc.)?
3. The extent to which the whistleblower knew or should have known that tax noncompliance could result from the course of conduct.
4. The extent to which the whistleblower acted in furtherance of the noncompliance, including, for example, efforts to conceal or disguise the transaction.
5. The whistleblower's role in identifying and soliciting others to participate in the actions reported.

VII. Disclosure of Returns and Return Information

26 CFR 26 CFR §§301.6103(h)(4) – 1 and (n) -2 set forth procedures for disclosure of returns and return information to whistleblowers in whistleblower administrative proceedings. Section 301.6103(h)(4) – 1 governs limited disclosure to whistleblowers regarding preliminary award recommendations or denial, the award report package, meetings with the whistleblower to review documents supporting the preliminary award recommendation and the award decision letter, and the award determination or denial letter. Section 301.6103(n) -2 more broadly provides for disclosure of taxpayer return information to whistleblowers pursuant to written contract subject to the civil and criminal penalties applicable to disclosure of such information.