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Three New Qui Tam Lawsuits Likely to Move Forward in New York

Whistle-blowers, emboldened by a recent New York high court decision, are considering at least three more qui tam tax cases in the state, according to a prominent tax attorney.

Peter L. Faber, a partner at McDermott, Will & Emery LLP, told Bloomberg BNA that he is currently handling three new qui tam cases, but said he couldn't disclose any details because they are in the ''investigative stage'' and not yet public.

The defendants are likely to be large companies, because New York's False Claims Act allows qui tam actions only in tax cases in which the defendant's net income or sales is $1 million or more and the alleged damages are more than $350,000.

The cases come amid a continuing public debate between corporate defense attorneys and the qui tam plaintiffs' bar about the appropriateness of applying the False Claims Act in tax cases.

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.*, 2015 BL 344427 (N.Y. 2015) (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. Two other cases involving large companies, Citigroup Inc. and Vanguard Group Inc., are winding their way through the courts (248 DTR K-4, 12/29/15).

Large Companies Vulnerable. ''Large corporations are particularly vulnerable to FCA attacks,'' Faber told Bloomberg BNA in an e-mail. ''They have complicated tax returns that involve judgements as to the meaning of ambiguous tax laws.''

''They will often be taking positions that are contrary to department of revenue positions,'' he said. ''They are also likely to have employees who know of their tax practices and who, if their employment terminates, voluntarily or involuntarily, are likely to blow the whistle.''

Faber, whose clients include Goldman Sachs Group Inc., Loews Corp., Metropolitan Life Insurance Co., Morgan Stanley, Pfizer Inc., Starbucks Corp. and the New York Times Co., said companies should be sure to document the legal basis for their positions when they take positions that could be challenged.

Faber also recommended that in-house state and local tax counsel should consult with their in-house colleagues in the federal tax area because state tax laws often piggyback on federal laws. ''This means that an aggressive position taken on a federal tax return can affect state taxable income and, hence, can give rise to a state FCA claim,'' he said.

Turning Over Tax Enforcement. Faber said he opposes applying the False Claims Act to tax cases, particularly the treble damages provision in New York law and the idea of having the attorney general and plaintiffs' bar responsible for tax enforcement, rather than the Department of Taxation and Finance.

''If advocates of FCA procedures feel that state revenue departments are not adequately enforcing the tax laws, the remedy is to give them adequate budgets, which state legislatures seem reluctant to do, not to turn their jobs over to others—plaintiffs' lawyers, attorneys general—who are not equipped to do it competently and who are using tax enforcement for political (attorneys general) or financial (plaintiffs' lawyers) reasons,'' he said.

Jack Trachtenberg, counsel with Reed Smith LLP who supports repealing the tax provisions of the state's False Claims Act, said there is already adequate provision in state Tax Law ''to deter knowingly fraudulent tax avoidance.''

''Specifically, there are fraud penalties typically equal to twice the tax owed and criminal sanctions ranging from violations to felonies,'' he told Bloomberg BNA in an e-mail. ''Supporters of the False Claims Act say these tools are not enough, but that's because they are really looking to punish behavior that is not actually fraudulent under a statute they market as an anti-fraud statute.''

Trachtenberg said Reed Smith isn't currently handling any new qui tam tax cases in New York, but represents about 30 taxpayers in whistle-blower cases in Illinois, Delaware and other states.

Treble Damages. Erika A. Kelton, a whistle-blower attorney with Phillips & Cohen LLP, said ''potential treble penalties are a powerful deterrent.''

''Whistle-blowers—who can provide the government with detailed information about tax fraud that the government would never uncover—are not likely to report

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significant tax frauds without the financial incentives and protections of the False Claims Act,'' she told Bloomberg BNA in an e-mail. ''Whistle-blower assistance is transformative for government enforcement.''

Randall M. Fox, a partner at Kirby McInerney LLP, said opponents of qui tam tax cases forget that attorneys general are regularly involved in tax disputes on behalf of their states.

''They don't mention that most tax rules and tax frauds are perfectly simple, nor do they recognize that some are too willing to argue that the most straightforward rules are really ambiguous,'' Fox told Bloomberg BNA in an e-mail.

Fox, who was the bureau chief in the New York attorney general's Taxpayer Protection Bureau when the Sprint case was brought, said ''those who argue against having tax whistle-blower suits should answer whether tax enforcement is benefitted by having persons with knowledge raise instances of tax cheating that would not otherwise be caught.''

''They should answer whether it is easier to catch tax cheating through a broad based audit or by having someone point directly to misconduct,'' Fox said. ''They should answer whether taxpayers who responsibly pay their taxes are benefitted by more effective tax enforcement. it is not political motivation for an attorney general to pursue claims against people where there is a good faith basis for believing they have violated the law and deprived the government and taxpayers of money. That's an attorney general's job.''

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