

DEPARTMENT OF TAXATION

2016 Fiscal Impact Statement

1. **Patron** Scott A. Surovell

2. **Bill Number** SB 741

3. **Committee** Senate Finance

House of Origin:

X **Introduced**

 Substitute

 Engrossed

4. **Title** Tax Administration; Monetary Awards for
Information Regarding Tax Underpayments

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would authorize the Tax Commissioner to award monetary compensation to individuals who provide information that leads to the successful collection of delinquent taxes owed by other individual or business taxpayers. If the Tax Commissioner proceeds with any administrative or judicial action based on such information, the amount of the award would be 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 such action or from a settlement in response to such action. This bill would only apply to actions by the Department:

- Against any individual taxpayer, or married taxpayers, with gross income exceeding \$100,000 or any business taxpayer with gross income exceeding \$500,000; and
- If the tax penalties, interest, additions to tax, and additional amounts in dispute exceed \$50,000.

The effective date of this bill is not specified.

6. **Budget amendment necessary:** Yes.

Items(s): 275, Department of Taxation

Sum-sufficient to pay rewards out of collections.

7. **Fiscal Impact Estimates are:** Preliminary. (See Line 8.)

7a. **Expenditure Impact:**

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Positions</i>	<i>Fund</i>
2015-16	\$0	0	GF
2016-17	\$114,000	1	GF
2017-18	\$110,600	1	GF
2018-19	\$112,600	1	GF
2019-20	\$114,600	1	GF
2020-21	\$116,600	1	GF
2021-22	\$118,600	1	GF

8. Fiscal implications:

Administrative Costs

The Department of Taxation ("the Department") would require additional funding of \$114,000 in Fiscal Year 2017, \$110,600 in Fiscal Year 2018, \$112,600 in Fiscal Year 2019, \$114,600 in Fiscal Year 2020, \$116,600 in Fiscal Year 2021, and \$118,600 in Fiscal Year 2022 in order to implement the provisions of this bill. Such funding would be necessary to compensate one full-time auditor and one wage employee to perform audits. The Department would also need a sum sufficient appropriation to pay awards.

Revenue Impact

This bill would result in an unknown increase in General Fund revenue. The amount of this gain depends on the number of informants and the quality of the information they provide. Because of the delay between the receipt of information and collection of delinquent tax, it would likely be several years before revenue would be generated. Based on the Internal Revenue Service's ("IRS") "whistleblower" data, a similar Virginia program might generate a few hundred thousand dollars.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Federal Whistleblower Statute

The Internal Revenue Code has included a whistleblower statute since 1867. In 2006, the Tax Relief and Health Care Act of 2006 made fundamental changes to the IRS informant awards program by creating a non-discretionary awards provision; by adding whistleblower appeal rights; and by requiring the IRS to create a Whistleblower Office. Depending on the circumstances, an award paid to an informant may be mandatory or discretionary.

Federal tax law provides a mandatory award and a discretionary award for certain tax whistleblowers. In order for an individual to be eligible for the mandatory award, the relevant action must be against a taxpayer whose tax, penalties, interest, additions to tax, and additional amounts in dispute exceed \$2 million. The statute only applies to actions against individual taxpayers if the individual's gross income exceeds \$200,000 for any taxable year subject to such action. An individual that qualifies for the mandatory award shall receive an award of at least 15 percent but not more than 30 percent of the collected proceeds resulting from an administrative or judicial action that was based on information provided by that individual. The collected proceeds include penalties, interest, additions to tax, and additional amounts. The Whistleblower Office's determination of the amount of

the award depends upon the extent to which the individual substantially contributed to the action.

If the Whistleblower Office determines the administrative or judicial action is based principally on disclosures of specific allegations from a source other than the individual, the Whistleblower Office is required to reduce the amount of the mandatory award. Such mandatory award may not exceed 10 percent of the collected proceeds resulting from the action. This provision does not apply in cases where the individual is the original source of the information that results in an administrative or judicial action.

Under the mandatory award program, if the Whistleblower Office determines that the claim for an award is brought by an individual who planned and initiated the actions that led to the underpayment of tax or the violation of internal revenue laws, then the Whistleblower Office may appropriately reduce the award. If the individual is convicted of criminal conduct arising from this role, any award shall be denied.

Any mandatory award determination may be appealed to the Tax Court within 30 days of the determination.

In cases where the requirements for the mandatory award are not met, the individual that provided information which led to the collection of proceeds in an administrative or judicial action is eligible for the discretionary award. A taxpayer that qualifies for the discretionary award may receive an award up to 15 percent of the amounts collected by reason of the taxpayer's information. The amount of such award may not exceed \$10 million. Discretionary awards are not generally paid when the disclosures were based on public information, or when the informant participated in the tax non-compliance. Discretionary award determinations may not be appealed.

Individual informants do not need to enter into a contract to receive an award under the whistleblower statute. Any individual informant may be represented by counsel. No award may be made unless the information is submitted under penalty of perjury.

State Whistleblower Statutes

New York False Claims Act

New York provides monetary awards to tax whistleblowers under the New York False Claims Act. Under the False Claims Act, any person who commits an act within the statute which constitutes a claim, record or statement made under tax law is liable for penalties and damages. However, the False Claims Act only applies to claims, records or statements made under the tax law if the net income or sales of the person against whom the action is brought equals at least \$1 million for any taxable year subject to the action. Further, the total damages pleaded within the relevant action against that person must exceed \$350,000.

New York's False Claims Act allows for individuals to bring qui tam civil actions for violations of the act. If proceeds are recovered in such an action, the individual who initiated the action shall receive between 15 percent and 30 percent of the recovered proceeds depending on the circumstances. However, if the court determines that the

action is based primarily on the disclosure of specific information relating to the allegations or transactions in court, in a legislative or administrative report, hearing, audit or investigation, or from the news media, then the court may not make an award of over 10 percent of the proceeds. Further, if the court finds that the qui tam civil action is being brought by a person who planned or initiated the violation of the False Claims Act, then the court may reduce the award to the extent it deems appropriate. Finally, if the person bringing the qui tam civil action is convicted of criminal conduct arising from his role in a False Claims Act violation, then he will not receive any share of the proceeds recovered in such an action.

False Claims Acts in Other States

Twenty-eight states and the District of Columbia have False Claims Acts similar to New York's and provide monetary awards to qui tam plaintiffs. However, none of those states specifically allow claims, records or statements made under tax laws to fall within their False Claims Acts like New York. The False Claims Acts in five states (Delaware, Florida, Nevada, New Hampshire, and Washington) have been interpreted by courts to allow qui tam actions involving tax matters. In contrast, six states (California, Hawaii, Massachusetts, North Carolina, Tennessee, and Virginia) and the District of Columbia explicitly prohibit tax actions from being brought under their False Claims Acts. Three (Illinois, Indiana, and Rhode Island) prohibit income taxes from being brought under their False Claims Acts, but do not explicitly prohibit other types of taxes. The remaining fifteen states (Colorado, Connecticut, Georgia, Iowa, Louisiana, Maryland, Michigan, Minnesota, Montana, New Jersey, New Mexico, Oklahoma, Texas, and Vermont) limit their False Claims Acts to Medicaid-related claims and other types of fraud.

Texas Contracts for Information

Texas may enter into contracts with people who have information regarding potential claims that the state may pursue in order to recover revenue or other property. The total consideration to be paid to the person with the relevant information must be contingent upon a recovery by the state. Further, the total consideration may not exceed 5 percent of the total revenue or value that the state recovers as a result of the information provided. Finally, the total consideration may be contractually limited to a specific and absolute dollar amount.

California Informant Reward Program

California law allows the state's Franchise Tax Board to conduct an informant reward program. However, no funding has ever been appropriated to start such a program. In 2010, proposed legislation would have required California's Franchise Tax Board to establish an informant reward program. The requirements of the program would have largely tracked the federal mandatory whistleblower award program. However, the bill did not pass. Analysts estimated that the cost of the program would be approximately \$420,000 per year, while the revenue generated from the program would be \$200,000 for Fiscal Year 2011, \$350,000 for Fiscal Year 2012 and \$400,000 Fiscal Year 2013.

Proposed Legislation

This bill would authorize the Tax Commissioner to award monetary compensation to individuals who provide information that leads to the successful collection of delinquent taxes owed by other individual or business taxpayers. If the Tax Commissioner proceeds with any administrative or judicial action based on such information, the amount of the award would be 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 such action or from a settlement in response to such action. The determination of the amount of such award by the Tax Commissioner would depend on the extent to which the individual informant substantially contributed to such action. Award payments would be paid only from the proceeds collected by reason of the information provided.

If the Tax Commissioner determines that the administrative or judicial action is based principally on disclosures of specific allegations from some source or sources other than information provided by the individual, then the Tax Commissioner would be authorized to award an amount that he or she deems appropriate. The award payment would not be allowed to exceed 10 percent of the collected proceeds, including penalties, interest, additions to tax, and additional amounts, resulting from such action or from a settlement in response to such action. The Tax Commissioner would be required to take into account the significance of the individual's information and the role played by such individual or his or her legal representative in assisting in such action.

This bill would authorize the Tax Commissioner to deny an award if:

- The claim is brought by an individual who is a federal, state, or local tax official and the information provided was obtained in the course of the individual's official duties;
- If the information provided by an individual is information that the Department routinely receives from other sources, such as through an information exchange with the IRS, other state agencies, or local commissioners of the revenue;
- If the claim is brought by an individual who planned or initiated the actions that led to the underpayment of taxes; or
- If such individual is convicted of criminal conduct arising from a claim for an award, then the Tax Commissioner would be required to deny any award.

If two or more individuals claim an award with respect to the same action, then this bill would require the Tax Commissioner to divide the award in proportion to the significance of each individual's information and the role played by each individual or his legal representative in assisting in such action. The total of all awards would not be allowed to exceed 30 percent of the collected proceeds, including penalties, interest, additions to tax, and additional amounts, resulting from such action or from a settlement in response to such action.

If any portion of the amount collectible is to be collected over time under an installment plan or restitution order, then this bill would prohibit the payment of any awards until all such amounts have been collected. However, this bill would allow an award to be paid based on amounts collected to date if the Tax Commissioner and the individual agree that the collection of additional amounts is unlikely.

This bill would only apply to actions by the Department:

- Against any individual taxpayer, or married taxpayers, with gross income exceeding \$100,000 or any business taxpayer with gross income exceeding \$500,000; and
- If the tax penalties, interest, additions to tax, and additional amounts in dispute exceed \$50,000.

This bill would allow any individual informant that is not satisfied with a determination regarding an award made by the Tax Commissioner to bring an action in the circuit court within 30 days of such determination. The burden of proof would be on the individual to show, by a preponderance of the evidence, that the information he or she provided substantially contributed to the collection of the additional tax proceeds and that the Tax Commissioner abused his discretion in determining the amount of the award. Any information provided to the individual, his representative, or the court about the action would be considered tax information protected from further disclosure unless the person who was the subject of the action is a party to the action in the circuit court.

This bill would authorize the Tax Commissioner to require individuals to submit information in the form of an affidavit under oath in contemplation of eventual proceedings in a circuit court regarding an award determination.

This bill would require the Tax Commissioner to develop guidelines and forms implementing the provisions of this bill. Such guidelines would be exempt from the provisions of the Administrative Process Act.

The effective date of this bill is not specified.

cc : Secretary of Finance

Date: 2/1/2016 MTH
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