# Note

## Fine-Tuning the Tax Whistleblower Statute: Why Qui-tam Is Not a Solution

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Bradley C. Birkenfeld, a Massachusetts native who studied banking at the American Graduate School of Business in Switzerland, began work in 2001 for UBS AG, a global bank headquartered in Switzerland.[1] UBS sent Birkenfeld to various U.S. wealth havens to lure American investors into transferring their assets to UBS bank accounts.[2] During the five years he spent recruiting American clients for UBS—which managed some $20 billion in assets for Americans—he persuaded billionaires like Igor Olenicoff[3] to move several hundred million dollars to UBS.[4] Birkenfeld would set up phony companies for such clients to conceal assets and give them credit cards to access their concealed cash.[5] Birkenfeld resigned from UBS in October 2005 after a fall-out and subsequently blew the whistle to

* J.D. Graduate 2014, University of Minnesota Law School. Associate, Gislason & Hunter LLP. Heartfelt thanks to Professor Kristin Hickman for helping me choose a relevant topic and Professor Stephen Cribari for his insight on the issue of attorney-client privilege. Equally owed thanks to Morgan Helme and Jeff Simard who edited this Note as their own. Last but not least, many thanks to my beloved wife who has been a faithful witness and supporter during those intense three years in law school. 

1. David Kocieniewsk, *Whistle-Blower Awarded $104 Million by I.R.S.*, N.Y. TIMES (Sept. 11, 2012), http://www.nytimes.com/2012/09/12/business/whistle-blower-awarded-104-million-by-irs.html.

2. Sheryl Phipps, *The UBS Birkenfeld Case and the IRS' Whistleblower Protection Program*, 2013 EMERGING ISSUES 6910 (Jan. 31, 2013) (arguing how laxly the IRS is interpreting the "planned and initiated" exception to the whistleblower award mandate by granting a hefty award to an informant criminally convicted for his participation in the tax evasion).

3. Olenicoff is an American real estate developer on the Forbes 400 list of America's most wealthy citizens. *Igor Olenicoff*, FORBES (Sept. 16, 2013, 7:51 AM), http://www.forbes.com/profile/igor-olenicoff.

4. *Id.*

5. Stuart Pfeifer, *Banking*, L.A. TIMES (Oct. 26, 2009), http://articles.latimes.com/2009/oct/26/business/fi-swiss26.

the U.S. tax authorities about his former employer's tax evasion scheme.[6] As a result of the investigation that followed, the IRS collected underpayments from approximately 15,000 U.S. taxpayers that had hidden money in UBS accounts.[7] Although Birkenfeld spent two and a half years in jail for his participation in the scheme, he received $104 million from the $400 million restitution paid by UBS.[8] Mr. Birkenfeld's whistleblower award was the largest ever paid to an individual by the IRS.[9]

Although many—including Senator Charles E. Grassley who authored the tax whistleblower statute[10]—praised the IRS's handling of Mr. Birkenfeld's case as a successful application of the reward program, most whistleblower claims, in fact, "fizzle."[11] Several commentators have criticized the whistleblower program as an incomplete enforcement mechanism.[12] Since 1867, the Secretary of Treasury has had legal authority to make discretionary payments for information that aids in detecting tax underpayments and fraud.[13] In 2006, Congress substantially reinforced the tax whistleblower program by enacting § 7623(b) of the Internal Revenue Code (Tax Code).[14] Under this provision, if the IRS decides to proceed with any administrative or judicial action based on information provided by a whistleblower, the whistleblower is entitled to an award of up to thirty percent of the collected proceeds unless the informant gets con-

6. Phipps, *supra* note 2.

7. *Id.*

8. *Id.*

9. Kocieniewsk, *supra* note 1.

10. *Id.* ("Senator Charles E. Grassley, an Iowa Republican who helped write the law, said Mr. Birkenfeld's award was an important step, but urged the I.R.S. to build on the momentum it had generated.").

11. Robert W. Wood, *Grassley Blows Whistle on IRS Whistleblower Program*, FORBES (Sept. 30, 2013), http://www.forbes.com/sites/robertwood/2013/09/30/grassley-blows-whistle-on-irs-whistleblower-program.

12. *See, e.g.*, Joshua D. Rosenberg, *Narrowing the Tax Gap: Behavioral Options*, 117 TAX NOTES 517, 527–30 (2007) (arguing that the current tax whistleblower provision is as ineffective as pre-1986 qui tam provisions by not guaranteeing a minimum award for whistleblowers, not allowing individuals to participate in tax collection activities, and not providing any reimbursement of cost and attorney fees or job protection for whistleblowers); Dennis J. Ventry, Jr., *Whistleblowers and Qui Tam for Tax*, 61 TAX LAW. 357, 359 (2008) (explaining the difference between the private enforcement mechanism of other federal statutes and that of the tax code, and arguing for the adoption of a qui tam action to the tax whistleblower program in order to overcome the program's shortcomings).

13. Whistleblower 14106-10W v. Comm'r, 137 T.C. 183, 186 (2011).

14. 26 U.S.C. § 7623(b) (2012). The pre-2006 version of the tax whistleblower law, former § 7623, survives with minor changes as Section 7623(a).

victed for having "planned and initiated" such underpayment.[15] Most courts have interpreted the statutory language to mean that the IRS's decision to pursue the informant's claim is a prerequisite for demanding an award.[16] However, some commentators criticize this interpretation for leaving too much discretion to the IRS, which may sleep on the whistleblower's report or ignore it entirely.[17]

Suggestions have been made to amend the tax whistleblower statute to allow informants to bring qui tam actions[18] of the type allowed under the False Claims Act (FCA) when the IRS is irresponsive.[19] A qui tam action allows a private individual to bring a civil action against someone who submitted fraudulent claims to the U.S. government.[20] The logic of this theory is that allowing a private right of action closes the resource gap between the IRS and tax evaders, and becomes an effective remedy to the perceived agency inaction.[21]

This Note argues that the adoption of qui tam action into the tax realm would be unconstitutional and detrimental to taxpayer privacy—one of the fundamental tenets portrayed in § 6103 of the Tax Code—as well as to the IRS's prosecutorial

15. *Id.* § 7623(b)(3); *see also* Cooper v. Comm'r, 135 T.C. 70, 73 (2010) (describing the Secretary's discretionary power regarding whistleblower awards).

16. See *infra* Parts I.B.2 and I.C.2 for a discussion of the interplay between the Tax Court and the IRS's decision to pursue an informant's claim.

17. Jeremiah Coder, *The Whistleblower Whipsaw Process*, 138 TAX NOTES 1168 (2013) (pointing out the often criticized problem of giving too much discretion to the IRS when it comes to deciding whether to act on an informant's claim, and the lack of redress for informants whose reports have been ignored).

18. "Qui tam" is an abbreviated version of "*qui tam pro domino rege quam pro se ipso in hac parte sequitur*" that can be translated as "he who sues in this matter for the king as well as for himself." Douglas K. Rosenblum & John A. Schwab, *FCA 101: A Practitioner's Guide to the False Claims Act*, 26 CRIM. JUST. 26, 28 (2011).

19. 31 U.S.C. § 3730(b) (2012) ("A person may bring a civil action for a violation of section 3729 for the person and for the United States Government. The action shall be brought in the name of the Government."); *see also* Rosenberg, *supra* note 12; Ventry, *supra* note 12, at 371–72 (discussing qui tam actions).

20. *See* Rosenblum & Schwab, *supra* note 18, at 28. However, Tax Code violations are expressly excluded from the cause of action under the FCA. 31 U.S.C. § 3729(d) ("This section does not apply to claims, records, or statements made under the Internal Revenue Code of 1986.").

21. *See* Rosenberg, *supra* note 12, at 527–31 (describing the value of qui tam actions); Ventry, *supra* note 12, at 370–77 (arguing for the adoption of qui tam actions).

discretion.[22] Part I provides an overview of the tax whistleblower program and its current problems, along with a primer on FCA qui tam procedures. Part II examines why the adoption of FCA-type qui tam provisions to the Tax Code is unlikely to be successful. Part III offers alternative solutions to the problem, delineating specific modifications that are needed to fix the language of the current statutory provisions. This Note concludes that Congress should avoid bringing qui tam provisions into the tax whistleblower statute; it instead proposes a modification of the Tax Court appeal right and the clarification of the permitted use of information protected by the professional duty of confidentiality.

## I. THE EVOLUTION OF THE TAX WHISTLEBLOWER STATUTE AND ITS CURRENT ISSUES

Before assessing the feasibility of adopting a qui tam provision in the tax code, this Note will examine the current state of the Code. Section A lays out the earlier version of the tax whistleblower statute. Section B explains the whistleblower-friendly changes adopted by the 2006 amendment to the Code. Finally, Section C introduces the problems of the current whistleblower program and Professors Joshua D. Rosenberg and Dennis J. Ventry, Jr.'s idea of adopting qui tam provisions in the tax code to solve those problems.

### A. PRE-2006 ERA OF TAX WHISTLEBLOWING

The IRS's whistleblower program dates back to 1867.[23] Back then, the Secretary of the Treasury had an unchecked discretion to pay "such sums as he deems necessary" for detecting violations of internal revenue laws.[24] Courts consistently held that § 7623 gave the IRS broad discretion to determine whether to pay an award in the first instance and how much to pay.[25] The implementing regulations also provided that the size

22. *See* 26 U.S.C. § 6103 (2012) (providing statutory protection for taxpayer information collected by the IRS).

23. Michelle M. Kwon, *Whistling Dixie About the IRS Whistleblower Program Thanks to the IRC Confidentiality Restrictions*, 29 VA. TAX REV. 447, 451 (2010).

24. 26 U.S.C. § 7623(a); Treas. Reg. § 301.7623-1(a), (c) (as amended 1998).

25. Merrick v. United States, 846 F.2d 725, 726 (Fed. Cir. 1988) ("[A]uthorities give the IRS broad discretion to decide whether to make an award or how much to grant."); Carelli v. IRS, 668 F.2d 902, 904 (6th Cir. 1982) (listing cases that have respected the Secretary of the Treasury's award

of the reward would represent what "the district or service center director deems to be adequate" in the particular case.[26]

The earliest versions of the statute authorized the IRS to pay awards to informants largely for information leading to criminal tax violations.[27] This was the status quo until 1996, when Congress added a clause to authorize payment of awards for information relating to civil violations, namely, "for detecting underpayments of tax."[28]

Minor changes with respect to the award cap ensued in the following years. In 1997, the IRS raised the award ceiling from $100,000 to $2 million,[29] and in 2004 it was increased to $10 million.[30] Below this cap, the IRS could award an amount within its self-imposed range of one percent to fifteen percent of the amounts recovered from the taxpayer, according to its own administrative discretion.[31] An award could exceed fifteen percent of the recovered amounts in a rare case where the IRS and the whistleblower entered into a special agreement.[32]

Before 2006, there was no express statutory provision for judicial review of tax whistleblower claims.[33] Nevertheless, one way to challenge the agency decision was to raise a breach of an implied-in-fact contract claim, alleging that the IRS had not

discretion); McGrath v. United States, 207 Ct. Cl. 978 (1975) ("We have no power to inquire into his use of discretion given to him exclusively by law."); Saracena v. United States, 508 F.2d 1333, 1334–36 (Ct. Cl. 1975) (stating that the Service had "complete discretion in the first instance to determine whether an award should be made and . . . to fix what, in [its] judgment, amounts to adequate compensation").

26. Treas. Reg. § 301.7623-1(c) (1999).

27. Charles P. Rettig, *The IRS Whistleblower Program: Making Money the Old Fashioned Way!*, J. TAX PRAC. & PROC., Apr.–May 2012, at 21.

28. COMM. ON WAYS AND MEANS, TAXPAYER BILL OF RIGHTS 2, at 101 (1996).

29. Rettig, *supra* note 27, at 22.

30. *Id.*

31. I.R.S., PUBLICATION 733: REWARDS FOR INFORMATION PROVIDED BY INDIVIDUALS TO THE INTERNAL REVENUE SERVICE (Oct. 2004) [hereinafter PUBLICATION 733], *available at* http://www.unclefed.com/IRS-Forms/2005/p733.pdf.

32. TREASURY INSPECTOR GEN. FOR TAX ADMIN., THE INFORMANTS' REWARDS PROGRAM NEEDS MORE CENTRALIZED MANAGEMENT OVERSIGHT 2 (2006) *available at* http://www.treasury.gov/tigta/auditreports/2006reports/200630092fr.pdf ("The limits on the reward percentage and dollar amount can be waived by the use of a special agreement between the informant and the IRS, which must be approved by the IRS Commissioner or his or her delegate.").

33. Whistleblower 14106-10W v. Comm'r, 137 T.C. 183, 186 (2011) (citing Colman v. United States, 96 Fed. Cl. 633, 638 (2011)).

lived up to its promises portrayed in Tax Code § 7623 (whistleblower provisions),[34] read in conjunction with the IRS Publication 733 (which details the payment process of whistleblower awards).[35] However, federal courts often deferred to the judgment of the agency, holding that Tax Code § 7623 and Publication 733 were merely the government's *invitation* to the informants to make an offer, and not a legally binding offer by themselves.[36] Furthermore, courts emphasized that the IRS's "District Director has complete discretion . . . to determine whether an award should be made."[37]

### B. CHANGES OF THE 2006 AMENDMENT: MANDATORY AWARD AND APPEAL RIGHT

Because of these award ceilings and the unchallengeable discretion the IRS possessed over the award, the IRS whistleblower program was largely dormant and underutilized until a major amendment was passed in 2006.[38] The 2006 amendment to § 7623 "breathed life into the statute," by providing increased incentives and means to challenge the IRS's award determination in the Tax Court.[39] Additionally, the enabling legislation authorized the Service to create a centralized Whistleblower Office to process tips received from individuals who "spot tax problems."[40] The Office determines whether and how much to pay informants, a responsibility previously delegated to Service District Directors dispersed throughout the

34. 26 U.S.C § 7623 (2012).

35. Krug v. United States, 41 Fed. Cl. 96, 97 (1998), *aff'd*, 168 F.3d 1307 (Fed. Cir. 1999) (holding that the court must defer to the judgment of the Secretary because no implied contract ever existed between the informant and the IRS, and thus there was no abuse of discretion); PUBLICATION 733, *supra* note 31; *see* Kwon, *supra* note 23, at 453–54 (discussing § 7623 and Publication 733); *cf.* 28 U.S.C. § 1491(a)(1) (2012) (also known as the Tucker Act, giving the Court of Federal Claims jurisdiction to hear contract claims against the United States).

36. Krug v. United States, 168 F.3d 1307, 1309 (Fed. Cir. 1999) ("[I]n Publication 733 . . . § 7623 and the regulation, the Government *invites* offers for a reward; the informant *makes* an offer by his conduct; and the Government *accepts* the offer by agreeing to pay a specific sum."); *Krug*, 41 Fed. Cl. at 98 ("The United States cannot be contractually bound merely by invoking the cited statute and regulation.").

37. *Krug*, 168 F.3d at 1310.

38. Ventry, *supra* note 12, at 361 ("In 1954, the statute was recodified as section 7623, where it remained largely unchanged, underutilized, and unknown.").

39. Ventry, *supra* note 12, at 361.

40. I.R.S., NEWS RELEASE IR-2007-25 (Feb. 2, 2007).

country.[41] Part I.B.1 explains the increased bounties for informants, and Part I.B.2 explains the whistleblowers' right to appeal to the Tax Court under § 7623(b)(4).

1. Mandatory, Increased Bounties for Whistleblowers

The amendment requires the IRS to pay at least fifteen percent of the "collected proceeds"—including penalties, interest, additions to tax, and any other amounts resulting from the action—to the whistleblower if the Secretary "proceeds with any administrative or judicial action" based on the informant's tips.[42] This was a major change from the prior law where the payments were discretionary, entirely dependent on what the District Director "deem[ed] to be adequate."[43] The amendment raised the maximum potential award to thirty percent of the recovered amounts and removed the $10 million cap.[44] Thus, what used to be the maximum amount allowed in the pre-amendment era—fifteen percent—became a bare minimum under the new whistleblower regime.[45] The award can be reduced to an amount less than ten percent if the claim is based primarily on already publicly disclosed information, except if the whistleblower was the "original source" of that information.[46] The specific amount of an award within the statutorily mandated range depends on the extent to which the whistleblower's information "substantially contributed" to the IRS's investigation.[47] Even a person who "planned and initiated" the tax evasion scheme may be entitled to an award, albeit a reduced one, unless that person is convicted of a crime for his or her role in the scheme.[48]

2. The New Tax Court Appeal Right

Perhaps the most controversial feature of the amended whistleblower provision is the whistleblower's right to appeal to the Tax Court.[49] Unlike the prior law, which left the informants

41. *Id.*
42. 26 U.S.C. § 7623(b)(1) (2012).
43. Treas. Reg. § 301.7623-1(c) (1999).
44. 26 U.S.C. § 7623(b)(1).
45. *Id.*
46. *Id.* § 7623(b)(2)(A), (B).
47. *Id.* § 7623(b)(1).
48. *Id.* § 7623(b)(3).
49. *See* Coder, *supra* note 17 at 1169 (discussing tension regarding whistleblowers' ability to appeal IRS determinations of award eligibility).

powerless over the IRS's determination as to the size of the award,[50] the new statute provides that "[a]ny determination regarding an award . . . may, within 30 days of such determination, be appealed to the Tax Court."[51] The Tax Court has exclusive jurisdiction over such appeals.[52] For instance, a letter from the IRS Whistleblower Office denying a claim because no award could be made under § 7623(b) constitutes a determination conferring jurisdiction upon the Tax Court.[53] However, § 7623 is completely silent as to which standard of review the Tax Court should use.[54] Moreover, § 7623(b)(4) is generally understood to mean that the whistleblower's appeal right is triggered if, and only if, the IRS *actually proceeds* with an administrative or judicial action.[55] This interpretation emphasizes that the plain language of paragraph one,[56] which is referred to by paragraph four,[57] is operative only after an administrative or judicial action. Accordingly, a determination by the IRS declining to take any action based on a whistleblower's information would be non-appealable.

Overall, the amended tax whistleblower program has been a success. In fiscal year 2012 for instance, the IRS received

50. *See supra* Part I.A (describing pre-2006 tax whistleblower law).

51. 26 U.S.C. § 7623(b)(4).

52. *Id.*; *see* Dacosta v. United States, 82 Fed. Cl. 549, 555 (2008) (stating that the Tax Court has exclusive jurisdiction over § 7623(b) claims).

53. Cooper v. Comm'r (*Cooper I*), 135 T.C. 70, 73 (2010).

54. Jeremiah Coder, *Private Claimant Suits Might Inform Future Whistle-Blower Cases*, 122 TAX NOTES 332 (2009). In an October 2008 press release adopting the final whistleblower rules, the Tax Court stated that "[w]ithout specific statutory direction establishing whether whistleblower actions are to be decided on the administrative record, the Court contemplates that the appropriate scope of review will be developed in case law." Press Release, United States Tax Court (Oct. 3, 2008), *available at* http://www.ustaxcourt.gov/press/100308.pdf.

55. 26 U.S.C. § 7623(b)(1); Cohen v. Comm'r, 139 T.C. 299, 302 (2012), *aff'd*, 550 Fed. App'x 10 (D.C. Cir. 2014) ("Our jurisdiction under section 7623(b) does not contemplate that we review the Commissioner's determinations of the alleged tax liability to which the claim pertains. . . . Nor does section 7623 confer authority to direct the Commissioner to commence an administrative or judicial action."); *see* Kwon, *supra* note 23, at 465.

56. 26 U.S.C. § 7623(b)(1) ("*If* the Secretary proceeds with any *administrative or judicial action* described in subsection (a) based on information brought to the Secretary's attention by an individual, such individual shall . . . receive as an award at least 15 percent but not more than 30 percent of the collected proceeds . . . ." (emphasis added)).

57. *Id.* § 7623(b)(4) ("Any determination regarding an award under paragraph (1), (2), or (3) may, within 30 days of such determination, be appealed to the Tax Court.").

8,634 whistleblower submissions and paid awards in 128 of those cases.[58] The total amount of taxes collected based on the whistleblower information was $592,498,294 and from that amount, $125,355,799, i.e., 21.2% of the total collected proceeds, was awarded to the whistleblowers.[59] However, many have raised concerns that despite the appeal right, whistleblowers are left without any recourse when the IRS simply chooses not to act on the whistleblowers' information.[60]

### C. WHISTLEBLOWERS LEFT HELPLESS AGAINST IRS'S SLUGGISHNESS AND INACTION

Despite the reinforced incentives for informants, there has been a "flood of negative comments over the past six years" concerning how the IRS has treated whistleblowers.[61] Under the current regime, the IRS may forever delay in making the award determination and the informants would have no recourse for seeking relief while waiting for the IRS's decision.[62] Likewise, when the IRS denies an award claim, "the informant is left empty-handed both monetarily and remedywise."[63] Part I.C.1 explores the factors that affect the IRS's claim processing time, Part 1.C.2 briefly examines some of the most recent Tax Court appeal cases, and Section 3 introduces a tentative suggested solution to the problem, which will ultimately be refuted in Part II.

#### 1. Reasons for Delay and Agency Inaction

Whistleblower claims can take years to go through the IRS review and award determination process.[64] For example, in 2011, about 66 percent of claims submitted in the first two

58. I.R.S., FISCAL YEAR 2012 REPORT TO THE CONGRESS ON THE USE OF SECTION 7623, 17 (2012) [hereinafter FY2012 I.R.S. REPORT]. The number of claims surged 1000% from 2007. Stephen Ohlemacher, *Tips on Tax Cheats Skyrocket with Bigger Rewards*, ASSOCIATED PRESS (Oct. 1, 2009), http://www.whistleblowers.org/storage/whistleblowers/documents/aptipsontaxcheats.pdf.

59. FY2012 I.R.S. REPORT, *supra* note 58 at 17.

60. *See, e.g.*, Coder, *supra* note 17, at 1169 (describing the IRS's ability to thwart whistleblower relief).

61. *Id.* at 1168.

62. *Id.*

63. *Id.* at 1169.

64. U.S. GOVERNMENT ACCOUNTABILITY OFFICE, TAX WHISTLEBLOWERS: INCOMPLETE DATA HINDERS IRS'S ABILITY TO MANAGE CLAIM PROCESSING TIME AND ENHANCE EXTERNAL COMMUNICATION 8 (2011) [hereinafter GAO, TAX WHISTLEBLOWERS] (reporting to Congress the reasons for the tax whistleblower program's lack of transparency and long claim processing time).

years of the program—fiscal years 2007 and 2008—were still in process.[65] Additionally, 447 claims submitted in fiscal year 2010 had been in the Whistleblower Office's initial claim review step for at least 200 days.[66] One of the reasons for the long processing time is that the IRS Subject Matter Experts (SMEs) and the staff at its Whistleblower Office are vastly outnumbered by the claims submitted each year.[67] After the initial screening by the Whistleblower Office, SMEs with in-depth knowledge in various industries review the claims and decide whether to pursue the issue raised by the whistleblower.[68] However, the IRS's three civil divisions (Large Business and International, Small Business/Self-Employed, and Tax Exempt and Government Entities) only have between seven and ten SMEs each, and the SMEs often have other work priorities that may delay their review of whistleblower claims.[69]

As identified by Stephen A. Whitlock, head of the Whistleblower Office, another important reason for the delay is that the IRS spends a tremendous amount of time filtering out information it is not supposed to use.[70] Many of the tips submitted by informants contain privileged information that may taint the integrity of the whistleblower program and be of limited use in a courtroom.[71] Parsing through the submitted materials that may include attorney-client privileged and other legally protected information and insulating them from the IRS audit team can be a time-consuming endeavor.[72] Finally, the taxpayer's appeal process and two-year refund period may substantially delay the whistleblower's receipt of the award.[73]

65. *Id.*

66. *Id.*

67. *See id.* at 9.

68. Taxpayers Against Fraud Educ. Fund, *An Interview with IRS Whistleblower Office Director Stephen A. Whitlock*, 52 FALSE CLAIMS ACT & QUI TAM Q. REV. 81, 87 (2009) [hereinafter *Whitlock Interview*].

69. *Id.*

70. *Id.* at 96.

71. *Id.* at 87.

72. *Id.* at 87–88. In addition, the IRS spends time investigating the relationship between the whistleblower and the taxpayer because certain individuals are not eligible at all for awards, including federal employees who learn of tax noncompliance in the course of their work activities or individuals who are current representatives, such as attorneys or accountants, of the targeted taxpayer. GAO, TAX WHISTLEBLOWERS, *supra* note 64, at 9.

73. GAO, TAX WHISTLEBLOWERS, *supra* note 64, at 10 (explaining that taxpayers can appeal the IRS's assessment of tax, so that the case can be reviewed by the U.S. Tax Court, U.S. Court of Federal Claims, or a U.S. district court).

2. Whistleblower's Right To Appeal and the Tax Court's Limited Power

What happens if the IRS declines to take any action based on the informant's tips and subsequently declines to give out any award to the informant? "Nothing" would be the correct answer under the current state of the law. In *Cooper v. Commissioner*, the Tax Court decided that it had jurisdiction in such cases where the IRS declined to pursue a claim and issued a letter notifying the informant that an award could not be made.[74] However, the Tax Court held in subsequent cases that it did not have any authority to *compel* the IRS to pursue an informant's claim.[75]

For instance, in *Cohen v. Commissioner*, a whistleblower challenged the IRS's decision not to pursue information he had provided on the ground that the IRS abused its discretion.[76] The whistleblower alleged that the IRS denied his claim for an award without instituting an administrative or judicial action or collecting any proceeds.[77] The Tax Court held that although it had jurisdiction with respect to the IRS's *award* determination, its jurisdiction under § 7623(b) did "not contemplate" that the court should review the IRS's determinations of the alleged tax *liability*.[78] Moreover, the court determined that § 7623 does not "confer authority to direct the Commissioner to commence an administrative or judicial action."[79] Hence, the court dismissed the whistleblower's petition for failure to state a claim.[80]

In other words, the new Tax Court appeal right under

74. Cooper v. Comm'r (*Cooper I*), 135 T.C. 70, 76 (2010) (holding that IRS's denial to pursue claims constituted an IRS determination that tees up a whistleblower's appeal rights).

75. *See* O'Donnell v. Comm'r, 489 Fed. App'x 469 (D.C. Cir. 2012) (per curiam) (holding that the IRS was correct in its denial of a whistleblower award); Cohen v. Comm'r, 139 T.C. 299, 304 (2012) (holding similarly to *Cooper II* but on the ground of failure to state a claim); Whistleblower 14106-10W v. Comm'r 137 T.C. 183 (2011) (ruling that, under § 7623(b)(1), a whistleblower award is dependent both upon the initiation of an administrative or judicial action and the collection of tax proceeds and that if the IRS does not proceed, there can be no whistleblower award); Cooper v. Comm'r (*Cooper II*), 136 T.C. 597, 601 (2011) (holding that the Tax Court lacked authority to direct the IRS to proceed with an administrative or judicial action in response to applicant's information regarding alleged underpayment of tax).

76. *Cohen*, 139 T.C. at 299.

77. *Id.* at 299–300.

78. *Id.* at 302.

79. *Id.*

80. *Id.* at 304.

§ 7623(b)(4) turned out to be a tiger with no teeth when the case law became settled that the Tax Court could do nothing about the IRS's inaction. Practically the only time the Tax Court can intervene and adjudicate on the IRS's determination is when the actual amount of the bounty is in dispute.[81]

3. Is Bringing Qui Tam into the Tax Code the Solution?

Two tax professors based in California have proposed a solution to the problem that would change the complete landscape of the tax enforcement system: adoption of qui tam action.[82] Subsection a provides a brief overview of the FCA's qui tam process and its relation to the tax code. Subsection b introduces Professor Rosenberg's idea—later elaborated on by Professor Ventry—of adopting a private enforcement mechanism in the Tax Code.

*a. Overview of the FCA's Qui Tam Provisions*

Many federal statutes, including antitrust laws and the Racketeer Influenced and Corrupt Organizations (RICO) Act, authorize private rights of action for statutory violations.[83] Private suits by the victims of statutory violations often serve an important public function, "in that the threat of private enforcement can deter potential violators."[84] One type of private enforcement action oriented toward public law enforcement is the so-called "qui tam" suit, in which "a private party, known as a 'relator,' brings suit against a private defendant on behalf of the government to redress some public wrong."[85] The qui tam

81. Kevan P. McLaughlin, *IRS Should Modify Whistleblower Program, California State Bar Member Says*, 2013 TAX NOTES TODAY 132-42, Part II.B (2013) ("Under the *Cooper II* logic then, the court appears left with only one role in overseeing whistleblower awards—adjudicating whether the IRS was correct in deciding to pay a 15% award, as opposed to an 18%, 22%, 26%, or some other amount."); Robert W. Wood, *What if IRS Doesn't Pursue Your Whistleblower Claim?*, FORBES (Oct. 15, 2012), http://www.forbes.com/sites/robertwood/2012/10/15/what-if-irs-doesnt-pursue-your-whistleblower-claim.

82. *See* Rosenberg, *supra* note 12, at 517; Ventry, *supra* note 12, at 406.

83. *See, e.g.*, 15 U.S.C. §§ 15, 26 (2012) (allowing a private right of action for antitrust violations); 18 U.S.C. §§ 1961–68 (2012) (allowing private civil remedies under RICO to compensate for limited governmental resources).

84. Matthew C. Stephenson, *Public Regulation of Private Enforcement: The Case for Expanding the Role of Administrative Agencies*, 91 VA. L. REV. 93, 98 (2005) (summarizing the pros and cons of different types of private enforcement arrangements and arguing that the executive branch rather than Congress should have more control over the existence and scope of private enforcement actions).

85. *Id.*

suit seeks to strengthen the enforcement of federal law by "deputizing" private individuals as "private attorney generals."[86]

Qui tam is an important private enforcement mechanism used by the FCA. Under the FCA, it is unlawful to knowingly present, or cause to be presented, "a false or fraudulent claim for payment or approval" to the government.[87] It is similarly unlawful to knowingly make "a false record or statement material to a false or fraudulent claim."[88]

Prior to filing a complaint under the FCA, a relator must serve a pre-filing disclosure of all allegations and material evidence on the government.[89] Thereafter, the complaint is filed under seal in the U.S. district court of the relator's choice.[90] A copy of the complaint must be served on the government, and the complaint remains under seal for a minimum of sixty days to provide the government time to investigate the matter without the defendant knowing of the allegations.[91] The sixty-day seal is routinely extended by order of the court upon motion of the government for good cause shown.[92]

Upon conclusion of its investigation, the government notifies the whistleblower whether or not it will intervene in the case.[93] If the government proceeds with the action, it takes over the primary responsibility for prosecuting the action and is not bound by an act of the relator.[94] If the government declines to intervene, whistleblowers have the right to prosecute the case themselves.[95] The FCA permits whistleblowers to share in the

86. *Id.* at 99–100.

87. 31 U.S.C. § 3729(a)(1)(A) (2012). The majority of recoveries by the federal government under the FCA have been in the health care and defense sectors—the two areas that account for a massive portion of the government's budget. Rosenblum & Schwab, *supra* note 18, at 27.

88. 31 U.S.C. § 3729(a)(1)(B).

89. *Id.* § 3730(b)(2) ("A copy of the complaint and written disclosure of substantially all material evidence and information the person possesses shall be served on the Government pursuant to Rule 4(d)(4) of the Federal Rules of Civil Procedure.").

90. *Id.*

91. *Id.* ("The complaint shall be filed in camera, shall remain under seal for at least 60 days, and shall not be served on the defendant until the court so orders. The Government may elect to intervene and proceed with the action within 60 days after it receives both the complaint and the material evidence and information.").

92. *Id.* § 3730(b)(3).

93. Rosenblum & Schwab, *supra* note 18, at 28.

94. 31 U.S.C. § 3730(c)(1).

95. Rosenblum & Schwab, *supra* note 18, at 28.

resulting recoveries if they win.[96] Qualifying whistleblowers can receive fifteen to thirty percent of recoveries, depending on whether the United States took over prosecution of a case.[97] There is no cap on the amount that can be recovered, and whistleblowers have the right to enforce their claims to rewards in federal district court.[98]

In addition to those who submit fraudulent claims, the FCA punishes someone who knowingly makes a false statement as to an obligation to pay money to the government or knowingly conceals and avoids an obligation to pay money to the government.[99] However, it is important to note that the FCA contains a major exclusion that makes the qui tam provisions inapplicable to "claims, records, or statements made under the Internal Revenue Code."[100]

#### *b. Importing Qui Tam: Privatizing Tax Enforcement*

Even though Congress explicitly prohibited the use of the FCA in the tax context, some academics have entertained the idea of adopting a qui tam option to the tax whistleblower statute. Professor Joshua Rosenberg was the first to make such an argument in 1996.[101] While noting the success of the qui tam provisions under the FCA, Rosenberg wrote:

> [S]ome large tax *qui tam* cases would likely attract significant media attention. Attorneys, accountants, and other tax planners and tax compliance personnel would realize that they could no longer rely on the silence and acquiescence of others, and that cheating on taxes had become a dangerous sport both for their employer and, because their participation would inevitably be exposed, for themselves.[102]

96. Paul D. Scott, *Tax Whistle-Blowers To Receive Increased Rewards*, 114 TAX NOTES 441, 441 (2007).

97. 31 U.S.C. § 3730(d)(1)–(2).

98. Scott, *supra* note 96, at 442.

99. 31 U.S.C. § 3729(a)(1)(G).

100. *Id.* § 3729(d); United States *ex rel*. Lissack v. Sakura Global Capital Mkts., Inc., 377 F.3d 145, 157 (2d Cir. 2004) (holding that the FCA's explicit tax bar precluded relator's claim of "yield burning," a federal income tax evasion scheme); Almeida v. United Steelworkers Int'l Union, 50 F. Supp. 2d 115, 127 (D.R.I. 1999) ("The Court is unable to imagine how Congress could have expressed its intent more clearly than it did in § 3729(e).").

101. Joshua D. Rosenberg, *The Psychology of Taxes: Why They Drive Us Crazy, and How We Can Make Them Sane*, 16 VA. TAX REV. 155, 210 (1996).

102. *Id.* at 211.

His main argument was that a whistleblower system that incorporates a qui tam provision can establish a "norm of tax honesty," rather than tax evasion."[103]

Additionally, Professor Rosenberg argued that adopting a qui tam provision would close the resource gap between the IRS and large institutional private taxpayers.[104] His assumption was that "[m]ost if not all of the transactions reported by whistleblowers . . . are likely to be large, and potentially complex, transactions, and most of the taxpayers reported are likely to be able to afford large teams of high-priced [defense] lawyers."[105] Even if it is assumed that the IRS has equally brilliant and dedicated attorneys, he states, taxpayers involved in disputes with the IRS may be able to outman the IRS simply because they can throw more money at the case.[106] He argues that this imbalance "would be quickly undone if attorneys . . . seeking to *collect* taxes were compensated at rates and in amounts similar to those seeking to *avoid* them.[107] In his view, qui tam provisions that provide for attorney's fees could "go far towards leveling the playing field."[108]

Professor Ventry further elaborated on Professor Rosenberg's argument in a 2008 article, advocating qui tam as an effective way to increase transparency by incentivizing insiders to come forward with the "concealed" information.[109] He argues, as Rosenberg did, that the qui tam action could significantly reinforce compliant behavior by publicizing the conviction of tax code violations, and that it could narrow the resource gap between the taxpayers and the IRS.[110]

Although Professor Ventry discusses the concerns about taxpayer privacy and abusive law suits that are inextricably related to the qui tam procedure, he dismisses the concerns as "eminently surmountable."[111] He argues that the public's need for increased tax compliance easily trumps the need for the protection of taxpayer information.[112] Further, he argues that frivo-

103. Rosenberg, *supra* note 12, at 525.
104. *Id.* at 526.
105. *Id.*
106. *Id.* at 526–27.
107. *Id.* at 527.
108. *Id.*
109. *See* Ventry, *supra* note 12, at 371.
110. *Id.* at 376–78.
111. *Id.* at 372–76.
112. *See id.* at 373–74.

lous, meritless claims can be controlled by imposing restrictions on such claims, setting a high-dollar threshold for a qui tam action, or by giving an exclusive power to the IRS to dismiss abusive claims.[113] Part II of this Note refutes Professor Ventry's assertions on four distinct grounds.

## II. WHY QUI TAM IS NOT A SOLUTION

This Note refutes some of the primary assumptions underlying the argument that qui tam actions should be imported into the tax whistleblower program. Section A discusses how a tax qui tam relator would lack standing under Article III of the U.S. Constitution. Section B explains the importance of safeguarding taxpayer information and how qui tam actions may destroy the confidentiality of taxpayer information. Section C explains the importance of preserving the IRS's administrative discretion. Finally, Section D discusses the challenges of choosing an appropriate forum for a tax qui tam action.

### A. TAX RELATOR'S LACK OF ARTICLE III STANDING

Even if Congress adds qui tam provisions to the Tax Code, the U.S. Supreme Court would likely nullify the amendment as unconstitutional. A plaintiff "must meet three requirements in order to establish Article III standing."[114] First, a plaintiff must show that "it has suffered an 'injury in fact' that is (a) concrete and particularized and (b) actual or imminent, not conjectural or hypothetical."[115] Second, the plaintiff must establish causation by showing that the injury was "fairly traceable to the challenged action of the defendant."[116] Finally, the plaintiff must demonstrate redressability—a substantial likelihood "that the injury will be redressed by a favorable decision."[117] These three requirements together constitute the "irreducible constitutional minimum" of standing under Article III's case-or-controversy requirement.[118]

113. *Id.* at 375.

114. Vt. Agency of Natural Res. v. United States *ex rel.* Stevens, 529 U.S. 765, 771 (2000) (citing Friends of the Earth, Inc. v. Laidlaw Envtl. Servs., Inc., 528 U.S. 167, 180–81 (2000)).

115. *Friends of the Earth, Inc.*, 528 U.S. at 180.

116. *Id.*

117. *Id.* at 181.

118. Lujan v. Defenders of Wildlife, 504 U.S. 555, 560 (1992) (holding that a citizen environmental group challenging a rule promulgated by the Secretary of the Interior interpreting § 7 of the Endangered Species Act of 1973

Irrespective of these minimum requirements, in *Vermont Agency of Natural Resources v. United States ex rel. Stevens*, the Supreme Court held that the FCA's grant of qui tam standing to private individuals did not violate Article III's standing requirement.[119] The Court relied mainly on two rationales: the Assignment of Claim doctrine and the history and tradition of qui tam litigation.[120] Justice Scalia first found the "adequate basis for the relator's suit . . . in the doctrine that the assignee of a claim has standing to assert the injury in fact suffered by the assignor."[121] He ruled that the FCA effected "a partial assignment of the Government's damages claim" to a private individual.[122] Second, the Court went on to analyze "the long tradition of *qui tam* actions in England and the American Colonies."[123] According to Justice Scalia, "[t]hat history is particularly relevant to the constitutional standing inquiry since . . . Article III's restriction of the judicial power to 'Cases' and 'Controversies' is properly understood to mean 'cases and controversies of the sort traditionally amenable to, and resolved by, the judicial process.'"[124] The Court observed that qui tam actions originated around the thirteenth century and "have been as prevalent in America as in England, at least in the period immediately before and after the framing of the Constitution."[125] Thus, it was "nigh conclusive" that qui tam actions were "cases and controversies . . . traditionally amenable to . . . the judicial process."[126]

However, the *Vermont Agency* rationales are not readily applicable to the federal tax context. First, the IRS is the only government agency in the United States that does not need to

lacked standing because the plaintiff did not suffer any concrete injury and only claimed a generalized grievance).

119. Vt. Agency of Natural Res. v. United States *ex rel.* Stevens, 529 U.S. 765, 777–78 (2000).

120. *Id.* at 773–76.

121. *Id.* at 773.

122. *Id.*

123. *Id.* at 774.

124. *Id.* ("[J]udicial power could come into play only in matters that were the traditional concern of the courts at Westminster and only if they arose in ways that to the expert feel of lawyers constituted 'Cases' or 'Controversies.'" (quoting Coleman v. Miller, 307 U.S. 433, 460 (1939) (opinion of Frankfurter, J.).

125. *Id.* at 774, 776.

126. *Id.* at 777 (quoting Steel Co. v. Citizens for a Better Env't, 523 U.S. 83, 102 (1998)).

bring a lawsuit to collect money due from a citizen.[127] The IRS can take direct actions to collect the liability by: 1) imposing a federal tax lien; 2) serving a notice of levy; or 3) offsetting a refund to which the taxpayer is entitled.[128] Further, the IRS can impose monetary penalties when taxpayers underpay their federal income taxes.[129] In this sense, *Vermont Agency*'s assignor-assignee doctrine would have questionable applicability in the tax context where the IRS typically does not raise a "legal claim" against the taxpayer in a judicial forum, but enforces the tax code through its own collection mechanism. If Congress can readily "assign" this unique type of agency prerogative to a private individual in the form of a private right of action, then the separation of powers principle may suffer. As Justice Scalia himself pointed out in *Lujan*, "[t]o permit Congress to convert the undifferentiated public interest in [tax compliance] into an 'individual right' vindicable in the courts is to permit Congress to transfer from the President to the courts the Chief Executive's most important constitutional duty, to 'take Care that the Laws be faithfully executed.'"[130] Adoption of qui tam action in the Tax Code would thus "enable the courts, with the permission of Congress, 'to assume a position of authority over the governmental acts of another and co-equal department,'" and to become "virtually continuing monitors of the wisdom and soundness of Executive action."[131]

Furthermore, unlike the conventional type of qui tam under the FCA, there has been no such history or tradition of private enforcement when it comes to collecting federal taxes. Section 3729(d) of the FCA explicitly bars the application of the qui tam provisions to "claims, records, or statements made under

127. *See generally Topic 201–The Collection Process*, IRS.GOV, http://www.irs.gov/taxtopics/tc201.html (last updated Aug. 7, 2014) (explaining how the IRS collects money from citizens).

128. *Id.*; I.R.S., PUBLICATION 594, at 4–7, *available at* http://www.irs.gov/pub/irs-pdf/p594.pdf.

129. *Topic 306–Penalty for Underpayment of Estimated Tax*, IRS.GOV, http://www.irs.gov/taxtopics/tc306.html (last updated June 18, 2014); *see also*, Jim Blankenship, *Understanding the Underpayment Penalty and How To Avoid It*, FORBES (June 25, 2012), http://www.forbes.com/sites/advisor/2012/06/25/understanding-the-underpayment-penalty-and-how-to-avoid-it (explaining that the IRS will assess an underpayment penalty when individuals fail to pay enough taxes during the year).

130. Lujan v. Defenders of Wildlife, 504 U.S. 555, 577 (1992) (quoting U.S. CONST. art. II, § 3).

131. *Id.* (citations omitted) (quoting Massachusetts v. Mellon, 262 U.S. 447, 489 (1923); Allen v. Wright, 468 U.S. 737, 760 (1984)).

the Internal Revenue Code of 1986."[132] This "Tax Bar" was added to the FCA in 1986, along with the "reverse false claims" provision— section 3729(a)(1)(G)—which created FCA liability for false statements designed to conceal, reduce, or avoid "an obligation to pay . . . money or property to the Government."[133] The Senate Report states that "the False Claims Act does not apply to income taxes cases, and the Committee does not intend that it should be so used."[134] Additionally, "courts that have considered the Tax Bar have concluded that it was intended to codify case law existing before the 1986 amendment, which reserved discretion to prosecute tax violations to the IRS and barred FCA actions based on tax violations."[135]

Although some states have enacted their own versions of false claims acts without the explicit Tax Bar, New York is the only state that has explicitly allowed a private right of action based on state tax law violations.[136] Nevertheless, New York's tax qui tam provision has only been in place since August 2010.[137] In light of these underlying facts, it is highly unlikely that the Supreme Court would find a long-standing history of private enforcement in the federal income tax context.

### B. SECTION 6103 AND THE SANCTITY OF TAXPAYER INFORMATION

Adopting qui tam provisions in the Tax Code runs the risk of unduly exposing taxpayer information protected under § 6103 to the general public.[138] Before the Tax Reform Act of 1976, § 6103 gave the IRS broad discretion to disclose tax in-

132. 31 U.S.C. § 3729(d) (2012).

133. *See* False Claims Amendments Act of 1986, Pub. L. No. 99-562, § 2, 100 Stat. 3153, 3153–54 (codified as amended at 31 U.S.C. § 3729(a)(1)(G), (d)).

134. S. REP. NO. 99-345, at 18 (1986), *reprinted in* 1986 U.S.C.C.A.N. 5266, 5283.

135. United States *ex rel.* Lissack v. Sakura Global Capital Mkts., Inc., 377 F.3d 145, 152–53 (2d Cir. 2004); *see also* United States *ex rel.* U.S.-Namibia Trade & Cultural Council v. Africa Fund, 588 F. Supp. 1350, 1351 (S.D.N.Y. 1984) ("In essence, plaintiff is attempting to enforce the tax laws through an improper vehicle—the False Claims Act.").

136. *See* N.Y. STATE FIN. LAW § 190(2)(a) (McKinney 2013); Franziska Hertel, Note, *Qui Tam for Tax?: Lessons from the States*, 113 COLUM. L. REV. 1897, 1915–16 (2013).

137. GAO, TAX WHISTLEBLOWERS, *supra* note 64, at 7 ("New York's [whistleblower] program has a tax qui tam provision that was enacted in August 2010.").

138. Section 6103 states that "[r]eturns and return information shall be confidential." 26 U.S.C. § 6103(a) (2012).

formation by providing that "returns . . . shall constitute public records."[139] The Service treated tax returns and other return information as a "generalized government asset" that was widely disseminated to federal, state, and local government officials.[140] However, Congress amended § 6103 in 1976 in the aftermath of the Watergate scandal in which the Nixon White House obtained some of its political opponents' tax returns from the IRS for improper political purposes.[141] The 1976 amendments thus marked a philosophical shift from treating tax information as a "governmental asset" that the executive branch was able to distribute at will, to a confidential, protected asset that only Congress could disseminate.[142]

Leaks of taxpayer information and misuse of that information in political fights is not an antiquated fear. The American Center for Law & Justice recently filed a complaint against

139. *See* CHARLES DAVENPORT ET AL., REPORT ON ADMINISTRATIVE PROCEDURES OF THE INTERNAL REVENUE SERVICE TO THE ADMINISTRATIVE CONFERENCE OF THE UNITED STATES, S. DOC. NO. 94-266, at 835–53 (1975) (summarizing the history of the disclosure of federal tax information).

140. PRIVACY PROT. STUDY COMM'N, FEDERAL TAX RETURN CONFIDENTIALITY 13–14 (1976) [hereinafter PRIVACY COMMISSION REPORT]; *see also* STAFF OF J. COMM. ON TAXATION, 94TH CONG., GENERAL EXPLANATION OF THE TAX REFORM ACT OF 1976, 313–15, 324 (1976), *reprinted in* 1976-3 C.B. 2, at 325–27, 335 (stating that "the Justice Department and other Federal agencies, as a practical matter, [were] able to obtain that information for nontax purposes almost at their sole discretion"); OFFICE OF TAX POLICY, DEP'T OF TREASURY, REPORT TO THE CONGRESS ON SCOPE AND USE OF TAXPAYER CONFIDENTIALITY AND DISCLOSURE PROVISIONS, VOLUME 1: STUDY OF GENERAL PROVISIONS 21 (2000) [hereinafter 2000 TREASURY REPORT] ("Congress recognized that the IRS had more information about citizens than any other Federal agency, and that other agencies routinely sought access to that information.").

141. One of the articles of impeachment alleged that President Nixon had "endeavored to obtain from the Internal Revenue Service, in violation of the constitutional rights of citizens, confidential information contained in income tax returns for purposes not authorized by law." COMM. ON THE JUDICIARY, IMPEACHMENT OF RICHARD M. NIXON, PRESIDENT OF THE UNITED STATES, H.R. REP. NO. 93-1305, at 3 (1974); *see also* James N. Benedict & Leslie A. Lupert, *Federal Income Tax Returns–The Tension Between Government Access and Confidentiality*, 64 CORNELL L. REV. 940, 941–42 (1979) (stating that "Watergate-related events in the 1970's where evidence was uncovered that President Nixon may have had income tax audits and investigations initiated and conducted in a discriminatory manner for purposes unrelated to the collection of taxes" partly motivated the amendment of § 6103).

142. PRIVACY COMMISSION REPORT, *supra* note 140, at 28 (concluding that Congress, rather than the executive branch, should have the authority to permit the IRS to make disclosures of tax information); *see also* DAVENPORT ET AL., *supra* note 139, at 1023 ("[A]dministrative practice should largely be reversed, and the veil of confidentiality drawn around returns once again. If it is to be lifted, Congress should do so.").

the IRS, alleging that IRS employees divulged the Tea-Party plaintiffs' confidential information in violation of § 6103.[143] In May 2013, the IRS indeed revealed that it inappropriately selected Tea Party political groups for stricter scrutiny in the 2012 presidential campaign.[144] Although there is no evidence that directly links the IRS misconduct to the White House,[145] this incident is another example that shows the importance of safeguarding the broad array of taxpayer information that lies in the IRS's hands.

1. Sanctity of Taxpayer Privacy Under § 6103

Section 6103 renders tax returns and return information strictly confidential. The section prohibits the IRS from disclosing taxpayers' tax information absent an explicit statutory exception.[146] Items protected from disclosure include tax returns; the taxpayer's identity; the nature, source, and amount of income, gain, deductions, credits, and other tax return items; as well as whether the taxpayer "was, is being, or will be examined or subject to other investigation or processing."[147] Virtually any information received, prepared, or collected by the IRS regarding a person's tax liability is protected from disclosure.[148] For instance, in *Krug v. United States*, the Court of Federal Claims asked the IRS to provide reasons for its denial of a whistleblower award, and the IRS rejected the request asserting that "it was unable to give specific reasons for denial of Krug's reward claims because of the restrictions imposed on

143. Complaint at 76–78, Linchpins of Liberty v. United States, No. 1:13-cv-000777-RBW (D.D.C. May, 29, 2013), *available at* http://media.aclj.org/pdf/second-amended-complaint-filed-redacted.pdf.

144. Zachary A. Goldfarb & Karen Tumulty, *IRS Admits Targeting Conservatives for Tax Scrutiny in 2012 Election*, WASH. POST (May 10, 2013), http://www.washingtonpost.com/business/economy/irs-admits-targeting-conservatives-for-tax-scrutiny-in-2012-election/2013/05/10/3b6a0ada-b987-11e2-92f3-f291801936b8_story.html (stating that the IRS acknowledged that groups with the words "tea party" or "patriot" in their applications for tax-exempt status faced additional screening).

145. *IRS Scandal Investigation Continues*, THE PATRIOT POST (Nov. 11, 2013), http://patriotpost.us/articles/21558 ("Rep. Sandy Levin (D-MI) says, 'There is zero evidence that the White House was involved in this.'").

146. 26 U.S.C. § 6103(a) (2012).

147. *Id.* § 6103(b)(1) (defining "return"); *id.* § 6103(b)(2) (defining "return information").

148. *See, e.g.*, Snider v. United States, 468 F.3d 500, 506 (8th Cir. 2006) (noting that the term "return information" is defined broadly); Payne v. United States, 289 F.3d 377, 381 (5th Cir. 2002) (noting the same point).

disclosing confidential tax information."[149] The court eventually conducted *in camera* review of the taxpayer documents "to determine whether the Secretary had a rational basis for denying plaintiff's reward claims."[150] Although taxpayer privacy was not the main issue in the case, the court's cautious handling of taxpayer information shows its willingness to preserve confidentiality even when a whistleblower challenges the "integrity of the IRS procedure."[151]

Section 6103 contains thirteen exceptions to the general rule.[152] Major exceptions include disclosures to Congress, Department of Justice and Treasury employees, and state tax officials for tax administration purposes.[153] Additional exceptions include disclosures for nontax criminal investigations and terrorist activities investigations.[154] These exceptions are often very narrowly prescribed.[155] To date, no exception permits the IRS to disclose a taxpayer's information to a whistleblower.[156]

### 2. How Qui Tam Litigation May Invade Upon Taxpayer Privacy

Adoption of qui tam litigation will undermine two important policy objectives nested within § 6103: preservation of the taxpayer's reasonable expectation of privacy and the voluntary compliance scheme of the American federal income tax system.

#### *a. Disrupting the Taxpayer's Reasonable Expectation of Privacy*

Safeguarding federal tax information is an important aspect of protecting privacy.[157] The IRS proclaims on its website:

149. Krug v. United States, 41 Fed. Cl. 96, 98 (1998), *aff'd*, 168 F.3d 1307 (Fed. Cir. 1999).

150. *Id.* (whistleblower alleged that the IRS decision was an abuse of administrative discretion).

151. *Id.* at 98–99.

152. 26 U.S.C. § 6103(c)–(o).

153. *Id.* § 6103(d) (state tax officials); *id.* § 6103(f) (congressional committees); *id.* § 6103(h)(1) (Department of Treasury employees); *id.* § 6103(h)(2) (Department of Justice employees).

154. 26 U.S.C. § 6103(i)(l), (3).

155. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-231SP, TAXPAYER PRIVACY: A GUIDE FOR SCREENING AND ASSESSING PROPOSALS TO DISCLOSE CONFIDENTIAL TAX INFORMATION TO SPECIFIC PARTIES FOR SPECIFIC PURPOSES 4 (2011) [hereinafter GAO, TAXPAYER PRIVACY].

156. Kwon, *supra* note 23, at 472.

157. GAO, TAXPAYER PRIVACY, *supra* note 155, at 17.

"Protecting sensitive data entrusted to us by taxpayers is a top priority of ours. We believe it is vital to maintaining public trust in the tax administration system."[158] This policy is in line with' Fair Information Practice Principles, which state "it is important to ensure that information collected for one government function is not used indiscriminately for other, unrelated functions."[159]

When it comes to collecting individually identifiable data, it is often said that the IRS compiles more information about more people than any other agency.[160] Much of the information the IRS collects is considered highly sensitive. The individual income tax return, for example, requires the taxpayer to reveal his place of residence, marital status, dependents, the source of his income, and is an annual measure of the taxpayer's financial well-being.[161] To obtain itemized deductions, the taxpayer may need to reveal even more intimate details, including the taxpayer's religious affiliation and whether the taxpayer is under the care of a doctor or psychiatrist.[162]

Furthermore, Congress granted a powerful investigatory authority to the IRS by promulgating § 7602.[163] This provision gives the IRS the power to "examine any books, papers, records, or other data which may be relevant" to determining the cor-

158. *What Are We Doing To Protect Taxpayer Privacy?*, IRS.GOV, http://www.irs.gov/uac/What-are-we-doing-to-protect-taxpayer-privacy%3F (last updated Apr. 8, 2014).

159. GAO, TAXPAYER PRIVACY, *supra* note 155, at 18; *see also* U.S. FED. TRADE COMM'N, PRIVACY ONLINE: A REPORT TO CONGRESS 8–9 (1998), *available at* http://www.ftc.gov/sites/default/files/documents/public_events/exploring-privacy-roundtable-series/priv-23a.pdf (explaining the importance of the privacy holder's "choice" related to secondary uses of his or her information); THE WHITE HOUSE, NATIONAL STRATEGY FOR TRUSTED IDENTITIES IN CYBERSPACE 45 (2011), *available at* http://www.whitehouse.gov/sites/default/files/rss_viewer/NSTICstrategy_041511.pdf (listing the Fair Information Practice Principles).

160. S. REP. NO. 94-938, at 316 (1976), *reprinted in* 1976 U.S.C.C.A.N. 3438, 3746; *see* Meade Whitaker, *Taxpayer Privacy vs. Freedom of Information: Proposals To Amend Sec. 6103*, 6 TAX ADVISER 198, 199 (1975) (referring to the IRS as a "gold mine" of information).

161. U.S. INTERNAL REVENUE SERV., FORM 1040—UNITED STATES INDIVIDUAL INCOME TAX RETURN (2013), *available at* http://www.irs.gov/pub/irs-pdf/f1040.pdf.

162. 26 U.S.C. § 170 (2012) (charitable contribution deduction); *id.* § 213 (medical expense deduction); U.S. INTERNAL REVENUE SERV., SCHEDULE A (FORM 1040)—ITEMIZED DEDUCTIONS (2013), *available at* http://www.irs.gov/pub/irs-pdf/f1040sa.pdf (allowing deductions for medical and dental expenses and gifts to charity).

163. 26 U.S.C. § 7602.

rectness of the taxpayer's return, as well as the authority to issue an administrative summons requiring the taxpayer to produce those records.[164] The IRS's expansive authority to obtain taxpayer information also extends to facts and records held by third parties, including the taxpayer's employer, bank, customers, and business associates.[165]

Allowing qui tam action would pose a serious threat to the confidentiality of taxpayer information because a qui tam plaintiff would naturally request the production of relevant documents—in this case, tax returns and additional tax-related information—from the defendant, which, under normal circumstances, only the IRS has the authority to examine.[166] In *Lampert v. United States*,[167] the Ninth Circuit noted that "once [tax] return information is lawfully disclosed in a judicial forum, its subsequent disclosure by press release does not violate [§ 6103]."[168] In reaching this conclusion, the court considered the taxpayer's privacy interests in the return information: "We believe that Congress sought to prohibit only the disclosure of confidential tax return information. Once tax return information is made a part of the public domain, the taxpayer may no longer claim a right of privacy in that information."[169]

Similar reasoning can be found in *United States v. Posner*.[170] In *Posner*, the District Court refused the defendant's re-

164. *Id.* § 7602(a); *see* United States v. Norwest Corp., 116 F.3d 1227, 1231 (8th Cir. 1997) ("Given the agency's 'broad mandate to investigate and audit persons who *may be* liable for taxes,' courts should be wary of 'restricting that authority so as to undermine the efficacy of the federal tax system.'" (quoting United States v. Bisceglia, 420 U.S. 141, 145–46 (1975))).

165. 26 U.S.C. §§ 7602, 7609.

166. *See* FED. R. CIV. P. 34 ("A party may serve on any other party a request . . . to produce and permit the requesting party . . . to inspect, copy, test, or sample . . . any designated documents or electronically stored information—including writings, drawings, graphs, charts, photographs, sound recordings, images, and other data or data compilations—stored in any medium . . . .").

167. Lampert v. United States, 854 F.2d 335 (9th Cir. 1988), *cert. denied*, 490 U.S. 1034 (1989).

168. *Id.* at 338.

169. *Id.*; *see also* Nixon v. Warner Commc'ns, Inc., 435 U.S. 589, 597 (1978) (stating that judicial proceedings are public records). The Ninth Circuit reiterated its position that disclosure of return information already in the public domain does not violate § 6103 in Schrambling Accountancy Corp. v. United States, 937 F.2d 1485, 1488 (9th Cir. 1991). *Contra* Mallas v. United States, 993 F.2d 1111, 1121–24 (4th Cir. 1993) (holding that due to the absence of an explicit exception to § 6103 addressing the issue, information that has been made public nonetheless remains confidential in the hands of the IRS).

170. 594 F. Supp. 930 (S.D. Fla. 1984), *aff'd*, 764 F.2d 1535 (11th Cir. 1985).

quest for a protective order that would have prevented a local newspaper from inspecting his tax returns that were admitted into evidence during the criminal trial of his codefendant.[171] Rejecting the defendant's argument, which was couched on § 6103, the court ruled that even when the information is part of a federal tax return, once that information is in the public domain, entitlement to its privacy is lost.[172] Thus, once a suspected taxpayer's information is revealed in a courtroom during qui tam litigation, there will be no going back no matter how unfounded the relator's allegations turn out to be. A qui tam plaintiff would ultimately possess a dangerous weapon to pull all kinds of sensitive taxpayer information into the public domain regardless of the merit of its claims.

*b. Disrupting Taxpayer's Voluntary Compliance*

Another important public policy argument that buttresses the protection of taxpayer information in favor of adopting qui tam action is the continuation of America's "very successful voluntary assessment system."[173] Voluntary compliance is "the mainstay of the Federal tax system."[174] Breaching the confidentiality of returns and return information can affect compliance in several ways. People may hesitate to file a tax return or honestly report all income if the information may be used by someone besides the IRS in a way that may disadvantage them.[175] For instance, "the IRS determined that as a result of the institution of the refund offset program, some taxpayers changed their withholding (so that there would be no refund to offset) and a greater number of taxpayers stopped filing returns altogether."[176]

171. *Id.* at 931–32.

172. This line of decisions has its theoretical underpinning in the Supreme Court's ruling in *Cox Broadcasting Corp. v. Cohn*, which noted that "[w]hat transpires in the court room is public property. . . . *Those who see and hear what transpired can report it with impunity*." 420 U.S. 469, 492 (1975) (quoting Craig v. Harney, 331 U.S. 367, 374 (1947)); *see also Warner Commc'ns*, 435 U.S. at 609 (holding that the press has the right to publicize information in public court records, but not the right to obtain physical access to the information).

173. S. REP. NO. 94-938, at 317 (1976), *reprinted in* 1976 U.S.C.C.A.N. 3438, 3746

174. *Id.*

175. GAO, TAXPAYER PRIVACY, *supra* note 155, at 22.

176. 2000 TREASURY REPORT, *supra* note 140, at 33–34 (explaining that Congress recognized that taxpayers had a reasonable expectation of privacy which was an important component of voluntary compliance).

The taxpayer's willingness to submit information truthfully, without the threat of criminal investigation or summons, depends upon guarantees that the data collected by the IRS will be used for a proper purpose.[177] Allowing qui tam action would thus seriously undermine taxpayers' trust in the discreetness and confidentiality of the tax collection process and expose them to fears of meritless accusations. If taxpayers knew that their tax returns and the related personal information collected by the IRS may be used against them in a courtroom—especially by someone without expertise in tax law, or by someone who means to carry out a personal vendetta—they would be less inclined to comply with the various reporting requirements.[178]

### C. THE IRS'S ENFORCEMENT DISCRETION MATTERS

While noting the IRS's exceptional span of prosecutorial discretion, Justice Stevens wrote in *Allen v. Wright*: "The Executive requires latitude to decide how best to enforce the law, and in general the Court may well be correct that the exercise of that discretion, especially in the tax context, is unchallengeable."[179] Qui tam would open the gate for private individuals to act like private IRS commissioners and bring claims against taxpayers.[180] This Section analyzes various negative effects that

177. Stephen W. Mazza, *Taxpayer Privacy and Tax Compliance*, 51 U. KAN. L. REV. 1065, 1101 (2003) (analyzing the clash between the protection of taxpayer privacy and a strategy to enhance tax compliance by publicizing high-profile tax prosecution cases).

178. For a contrary opinion on the relationship between tax compliance and the protection of taxpayer confidentiality, see David E. Joyce, Note, *Raiding the Confessional—The Use of Income Tax Returns in Nontax Criminal Investigations*, 48 FORDHAM L. REV. 1251, 1267, 1279 (1980) (noting that any correlation between voluntary compliance and confidentiality is merely speculative).

179. Allen v. Wright, 468 U.S. 737, 792–93 (1984) (Stevens, J., dissenting). In *Allen v. Wright*, the Court held that: (1) the parents did not have standing to prevent the government from violating the law in granting tax exemptions; (2) absent allegation of direct injury, standing could not be predicated on a claim of stigmatization caused by racial discrimination; and (3) a claim of injury to their children's diminished ability to receive an education in a racially integrated school, although a judicially cognizable injury, failed because the alleged injury was not fairly traceable to the government's conduct that was challenged as unlawful. *See id.* at 740, 754, 756–57, *abrogated by* Lexmark Int'l, Inc. v. Static Control Components, Inc., 134 S. Ct. 1377 (2014).

180. In fact, the IRS does not need to bring a lawsuit to collect tax due from taxpayers. Thus, in a theoretical sense, it is unclear what kind of "claim" or authority the tax qui tam relator would get from the IRS by being given a pri-

the privatization of tax enforcement would bring to the overall tax enforcement system.

1. Proliferation of Weak Claims

First, the availability of qui tam suit would likely open a gate for excessive private enforcements.[181] The so-called "privatization" of tax enforcement would impact the quality of cases pursued, the number of cases pursued, and the strength of legal theories advanced when cases are pursued.[182] Due to the potential of a windfall, some qui tam relators may start a lawsuit with poor factual support or flimsy legal theories that tend to "establish bad precedent and waste public resources."[183] Unlike the IRS, the qui tam relator does not have the ethical obligation to protect the interests of the public at large.[184] Moreover, the private relator has no interest in considering the impact of frivolously imposing defense costs on target taxpayers.[185] The IRS, on the other hand, may carefully weigh the costs and benefits of exercising its prosecutorial power, taking into account the whole picture of the taxpayer's liability in light of its past returns and other mitigating circumstances.[186] Due to the vast amount of data that the IRS collects from a taxpayer, the agency would likely have a more balanced, vantage-point perspective on a defendant's overall tax liability, compared to an overly zealous qui tam plaintiff who might have fallen upon a single piece of evidence of tax deficiency in a single fiscal year.[187]

2. Interference with the Agency's Enforcement Scheme

A whistleblower's qui tam action may disturb the IRS's secret investigation or long-term enforcement plans. First, private relators' suits may disrupt the cooperative relationship between the IRS and taxpayers that is essential for long-term

vate right of action. The constitutional dimension of the assignability of the IRS's prerogative is further explained in this Part.

181. Stephenson, *supra* note 84, at 114–17 .

182. Dayna Bowen Matthew, *The Moral Hazard Problem with Privatization of Public Enforcement: The Case of Pharmaceutical Fraud*, 40 U. MICH. J.L. REFORM 281, 297 (2007) (summarizing the False Claims Act and critiquing how qui tam litigants have distorted prosecutorial decision making).

183. *Id.*

184. *Id.*

185. *Id.*

186. *See* GAO, TAX WHISTLEBLOWERS, *supra* note 64, at 24–25.

187. *See id.* For examples of data that the IRS collects from a taxpayer, see *supra* Part II.B.2.a.

compliance with the Tax Code.[188] Private enforcement actions may interfere with an agency's ability "to negotiate with regulated firms and other affected interests in order to establish a workable and consistent regulatory system."[189] Consequently, private enforcement suits may "engender an overemphasis on coercion and deterrence at the expense of negotiation and cooperation," regardless of the wishes of the IRS on a particular matter.[190]

Second, private enforcement actions can disrupt the IRS's enforcement efforts by allowing qui tam relators, rather than IRS officials, to set the enforcement agenda.[191] Under the FCA for instance, if a relator files a lawsuit, the government is often forced either to allow the suit to go forward, which may be undesirable from the government's perspective, or to pursue its own preemptive enforcement action.[192] Thus, private citizens would have the ability to skew the IRS enforcement priorities, perhaps even without intending to.[193] Furthermore, judicial decisions rendered in qui tam suits, brought piecemeal before potentially non-expert courts[194] by plaintiffs with their own private interests, may establish "inconsistent precedents that complicate or disrupt government enforcement efforts."[195]

### 3. Lack of Accountability

Another downside of allowing qui tam actions in the federal tax context is private plaintiffs' lack of accountability for the

188. *See, e.g.*, Frank B. Cross, *Rethinking Environmental Citizen Suits*, 8 TEMP. ENVTL. L. & TECH. J. 55, 67 (1989).

189. Richard B. Stewart & Cass R. Sunstein, *Public Programs and Private Rights*, 95 HARV. L. REV. 1193, 1292–93 (1982); *see also* Jeannette L. Austin, *The Rise of Citizen-Suit Enforcement in Environmental Law: Reconciling Private and Public Attorneys General*, 81 NW. U. L. REV. 220, 223 (1987) ("[Citizen] suits may impair the EPA's ability to develop longstanding, cooperative relationships with regulated firms. These relationships, when used in conjunction with aggressive enforcement, are vital to attaining environmental enforcement objectives."); Matthew D. Zinn, *Policing Environmental Regulatory Enforcement: Cooperation, Capture, and Citizen Suits*, 21 STAN. ENVTL. L.J. 81, 84 (2002) (stating that "[o]fficious citizen enforcers" might undermine cooperative enforcement efforts because "the informal bargains struck by regulators and regulatees cannot protect the latter from citizen litigation").

190. *See* Stephenson, *supra* note 84, at 118.

191. *See id.*

192. *See id.*

193. *See* Austin, *supra* note 189, at 236; Cross, *supra* note 188, at 68.

194. *See infra* Part II.D for the discussion of jurisdictional issues when it comes to a tax qui tam suit.

195. *See* Stephenson, *supra* note 84, at 119.

social impact of their enforcement decisions.[196] As Professor Matthew Stephenson has aptly pointed out in his discussion of the effective use of the private enforcement mechanism, "Prosecutorial discretion is an integral part of the American system of government, and executive agencies are accountable to the electorate for their exercise of this discretion through the President and, more indirectly, through congressional oversight."[197] Thus, when the IRS considers whether to increase or decrease the level of enforcement of particular Tax Code provisions, it will most likely become sensitive to the political repercussions that may follow such enforcement decisions.[198] As neither the citizens bringing tax qui tam suits nor the judges who decide them are subject to electoral reckoning, allowing this additional private enforcement scheme in the federal system may undermine the important democratic self-check function of American governance.[199]

The problem of allowing too much private enforcement in too many areas of the federal administrative law is sometimes thought to have a quasi-constitutional dimension, inasmuch as congressionally authorized citizen suits can interfere with the executive branch's efforts to "take Care that the Laws be faithfully executed."[200] Though private enforcement suits have been upheld as constitutional as long as the private plaintiffs satisfy the standing requirements of Article III,[201] many commentators perceive a constitutional problem with allowing qui

196. *See id.*

197. *Id.* (citing Harold J. Krent & Ethan G. Shenkman, *Of Citizen Suits and Citizen Sunstein*, 91 MICH. L. REV. 1793, 1801–04 (1993); Jerry L. Mashaw, *Prodelegation: Why Administrators Should Make Political Decisions*, 1 J.L. ECON. & ORG. 81, 91–99 (1985)).

198. *See* Krent & Shenkman, *supra* note 197, at 1803–04.

199. *See* Stewart & Sunstein, *supra* note 189, at 1292 (noting that private rights of action can "undermin[e] the advantages of political accountability, specialization, and centralization that administrative regulation was designed to provide"); *see also* Antonin Scalia, *The Doctrine of Standing As an Essential Element of the Separation of Powers*, 17 SUFFOLK U. L. REV. 881, 896 (1983) (arguing that, when judges insist on a level of enforcement that the political process would not demand of the executive, the judges are likely to be enforcing, perhaps unintentionally, the political prejudices of the elite class from which they come).

200. U.S. CONST. art. II, § 3; *see supra* Part II.A.

201. Vt. Agency of Natural Res. v. United States *ex rel.* Stevens, 529 U.S. 765, 777–78 (2000) (holding that the FCA's grant of qui tam standing to private individuals does not violate Article III's standing requirement, relying on the history of qui tam litigation which goes back to the thirteenth century and the assignment of claim doctrine).

tam relators to determine the stringency with which the law will be enforced.[202] This problem is particularly acute "when the private citizen's injury, even if sufficient to satisfy Article III, does not seem to be the kind of personal injury for which the law usually provides compensation."[203]

### D. PROBLEM OF JURISDICTION—TAX COURT OR DISTRICT COURT?

In addition to the often-predicted problems of breach of confidentiality, frivolous claims, and interference with the IRS's enforcement activities, a set of very practical problems remains against the adoption of the qui tam action. For instance, which court would have jurisdiction over a qui tam case involving a whistleblower plaintiff and a taxpayer defendant? Should the U.S. Tax Court have jurisdiction or should a federal district court have such jurisdiction? Should a tax relator be entitled to the forum of his choice between the two?

There is an important distinction between the two potential federal forums. If the Tax Court were to have jurisdiction over a qui tam case, the taxpayer defendant would be deprived of the presence of a jury during the trial because "[t]here is no right to trial by jury in the Tax Court."[204] Normally, the fact that there is no jury trial available in Tax Court is neither a violation of the Due Process Clause of the Constitution[205] nor a violation of the Seventh Amendment.[206] However, these hold-

202. *See, e.g.*, Krent & Shenkman, *supra* note 197, at 1794–95 (arguing forcefully that Article III precludes general citizen suits, but conceding that Congress may allow suits by individuals who are "injured distinctively" by failure to enforce the law); *cf.* Cross, *supra* note 188, at 72 (discussing environmental citizen suits).

203. Stephenson, *supra* note 84, at 120. In the tax context, it is unclear whether the IRS has suffered an "injury" in a legal sense that might be "assigned" to a third party private plaintiff. *Vt. Agency,* 529 U.S. at 773.

204. Fed. Tax Coordinator Second Series (RIA) ¶ U-2005 (July 3, 2013). Nor can a case be removed from the Tax Court to a district court merely in order to have a jury trial. *Id.*

205. Euzent v. Comm'r, No. 77-2023, 1978 WL 4593, at *2 (D. Md. Oct. 11, 1978) (refuting the plaintiffs' assertion that § 7422 violates the Due Process Clause of the Fifth Amendment by ruling that due process only requires the taxpayer be afforded a hearing at some stage before the tax is irrevocably fixed).

206. Beard v. Comm'r, No. 98-1823, 1999 WL 455324, at *1 (6th Cir. June 23, 1999) ("The Seventh Amendment protects the right to a jury trial as it existed in suits at common law. No right of action at common law existed against a sovereign. Thus, a right to jury trial in an action against the United States exists only as provided by statute and no statute provides for a jury trial in the

ings are based upon the fact that the *government* was being sued by a taxpayer who disputed the IRS's collection decision.[207] Here, a private qui tam plaintiff would be suing a private taxpayer. If the tax relator's claim involves a criminal violation of the Tax Code, the Sixth Amendment would require that the accused "enjoy the right to a . . . trial, by an impartial jury."[208]

Even if the case involves a simple tax underpayment, however, the Seventh Amendment of the U.S. Constitution would likely require a trial by jury.[209] The Seventh Amendment provides: "*In Suits at common law*, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved . . . ."[210] According to Justice Scalia, the author of the majority opinion in *Vermont Agency*,[211] qui tam action is deeply embedded in the common law tradition.[212] He traces the tradition of qui tam actions back to the 13th century when private individuals "began bringing actions in the royal courts on both their own and the Crown's behalf."[213] His logic seems to indicate that a qui tam action may fall within the ambit of the Seventh Amendment guarantee of civil jury trial because of its root in the common law.[214] Thus, if a tax qui tam action ends up being litigated in the Tax Court, the defendant taxpayer would likely challenge the constitutionality of the Tax Court's jurisdiction because of the deprivation of a jury trial.

On the other hand, if a U.S. district court were to adjudicate a qui tam claim against a taxpayer, both parties of the lawsuit would lose the benefit of the expertise that the Tax Court possesses. Trying a case before a judge with no federal tax expertise may turn out to be a risky venture for the targeted taxpayer who would be trying to defend its position in front of a jury. Seventy years ago, in *Dobson v. Commissioner*, the

Tax Court." (citations omitted)); Gillis v. I.R.S., 578 F. Supp. 69, 69 (D.N.H. 1983) (holding that since there is no common law right of action against the sovereign, the Seventh Amendment does not apply to suits against the United States and thus the United States was not required to furnish a taxpayer with a jury trial before seeking to assess a tax deficiency).

207. *Beard*, 1999 WL 455324, at *1; *Gillis*, 578 F. Supp. at 70; *Euzent*, 1978 WL 4593, at *1.

208. U.S. CONST. amend. VI.

209. U.S. CONST. amend. VII.

210. *Id.* (emphasis added).

211. Vt. Agency of Natural Res. v. United States *ex rel.* Stevens, 529 U.S. 765, 774–75 (2000).

212. *Id.*

213. *Id.* at 774.

214. *See* U.S. CONST. amend. VII.

Supreme Court characterized federal tax law as a body of law "so complex as to be the despair of judges."[215] The Court stated that "[i]t can never be made simple" because it "touches human activities at so many points."[216] Since this unavoidable complexity in the tax laws—"complexity which is built into the statutes and regulations, and which the courts are powerless to change"[217]—has increased even more since the time of *Dobson*, adjudicating tax qui tam cases in a non-expert court may prove to be an unwise policy as well. As the difficulties of adopting qui tam provisions to the Tax Code have been explored in depth, Part III of this Note will proceed to offer two alternative solutions to the problem.

## III. REMODELING TAX COURT APPEAL RIGHT & PROHIBITING SUBMISSION OF PRIVILEGED INFORMATION

In early 2013, the Treasury Department proposed a set of new regulations pertaining to the administration of the IRS whistleblower program.[218] Some of these new regulations were designed to correct the lack of transparency that critics have often complained about. For instance, the Proposed Treasury Regulation § 301.7623–3 permits claimants "to participate in the whistleblower administrative proceeding through a structured process involving correspondence and other communications with the Whistleblower Office."[219] According to the regulations, informants will be "afforded opportunities to review the Whistleblower Office's preliminary award recommendation, to provide additional information regarding their claims that is relevant to an award determination, and to submit comments challenging all aspects of the preliminary findings at the administrative level."[220]

These new regulations exemplify the IRS's recent efforts to improve the efficiency and transparency of the current whistleblower program. Nevertheless, this Part proposes two addition-

215. Dobson v. Comm'r, 320 U.S. 489, 498 (1943).

216. *Id.* at 494–95.

217. David F. Shores, *Deferential Review of Tax Court Decisions:* Dobson *Revisited*, 49 TAX LAW. 629, 629 (1996).

218. *IRS Issues Comprehensive Proposed Regs on Whistleblower Program*, 58 Fed. Taxes Weekly Alert (RIA) No. 51 Article 6 (Dec. 20, 2012).

219. Awards for Information Relating To Detecting Underpayments of Tax or Violations of the Internal Revenue Laws, 77 Fed. Reg. 74,798, 74,802 (proposed Dec. 18, 2012) (to be codified at 26 C.F.R. § 301.7623–1(b)(2)(iii)).

220. *Id.*

al changes to the program that would help increase the IRS's accountability towards informants and reduce the IRS's claim processing time. Part III.A proposes a statutory amendment of the existing tax court appeal right and Part III.B proposes granting a limited immunity to whistleblowers for providing their clients' confidential information to the IRS.

### A. CONGRESS SHOULD AMEND § 7623(B)(4) TO BREATHE LIFE BACK INTO THE TAX COURT APPEAL RIGHT.

One way to reinvigorate the IRS whistleblower program is to reinforce the tax court appeal right under § 7623(b)(4) by modifying its statutory language. As further explained in Part I.C.2, the Tax Court appeal right under § 7623(b)(4) lost its sting under a series of recent Tax Court decisions holding that the IRS's denial of award cannot be judicially revisited as long as the IRS did not take any action based on the informant's tips.[221] Furthermore, the United States Supreme Court effectively affirmed this reasoning on October 15, 2013, when it issued an order denying certiorari of *O'Donnell v. Commissioner*, a case where the Tax Court granted summary judgment in favor of the IRS because the information provided did not cause the IRS to initiate any action.[222]

A simple amendment to the language of § 7623(b)(4) will be sufficient to fix this problem.[223] Section 7623(b)(4) states that "[a]ny determination regarding an award under paragraph (1), (2), or (3) may . . . be appealed to the Tax Court . . . ."[224] Paragraph (1) of the same Section provides: "*If* the Secretary proceeds with any administrative or judicial action . . . based on

221. *See supra* Part I.C.2 and the related tax court decisions.

222. O'Donnell v. Comm'r, 489 F. App'x 469, 469 (D.C. Cir. 2012) (per curiam), *cert. denied*, 134 S. Ct. 446 (2013). The Treasury Department's proposed regulations promulgated in early 2013 also clarify that the IRS cannot pay an award under § 7623 without taking some action beyond simply analyzing or investigating information submitted to it. The IRS would have to initiate a new action that it wouldn't have initiated, expand the scope of an ongoing action that it wouldn't have expanded, or continue to pursue an ongoing action that it wouldn't have continued but for the information provided. Awards for Information Relating to Detecting Underpayments of Tax or Violations of the Internal Revenue Laws, 77 Fed. Reg. at 74,806.

223. *See* Kneave Riggall, *Should Tax Informants Be Paid? The Law and Economics of a Government Monopsony*, 28 VA. TAX. REV. 237, 267–68 (2008) ("[A]n informant's right to an independent judicial review of the Service's refusal to pay a reward would do more to increase the informant's expected value of that reward than would an unreviewable Service 'guarantee.'").

224. 26 U.S.C. § 7623(b)(4) (2012).

information brought . . . by an individual, such individual shall . . . receive as an award at least 15 percent . . . of the collected proceeds . . . ."[225] Read in conjunction, the Tax Court interprets these two provisions to mean "whistleblower awards are *preconditioned* on the Secretary's proceeding with an administrative or judicial action."[226] According to the court, "[i]f the Secretary does not proceed, there can be no whistleblower award."[227]

The Tax Court's holding would likely change if the language of § 7623(b)(4) were modified to include the IRS's denial to take any action. For example, "[a]ny determination regarding an award under paragraph (1), (2), or (3)"[228] could be changed into: "Any determination regarding the amount of an award under paragraph (1), (2), or (3), or failure to pursue an administrative or judicial action described in subsection (a)." This change clarifies that the IRS's denial to take any action may be judicially reviewed. Another way to improve the statutory language is to insert "with or without regard to the existence of any administrative or judicial action described in subsection (a)" within paragraph (4), so that the paragraph would read: "Any determination regarding an award under paragraph (1), (2), or (3), with or without regard to the existence of any administrative or judicial action described in subsection (a), may, within 30 days of such determination, be appealed to the Tax Court."[229]

Modifications of this sort will allow Congress to eliminate the current ambiguity in § 7623(b), which has been a fertile ground for lawsuits since the 2006 amendment.[230] Although skeptics might still argue that the reinforced appeal right may equally disturb the IRS's enforcement agenda by increased tax court intervention, at least the problems of constitutional standing, taxpayer privacy leak, and the forum selection paradox that are inherent under a qui tam regime will be eliminated. In addition, the lamented absence of any appeal right for informants whose information has been completely ignored by the IRS may thus be rectified.

225. *Id.* § 7623(b)(1) (emphasis added).

226. Cooper v. Comm'r (*Cooper II*), 136 T.C. 597, 601 (2011) (emphasis added).

227. *Id.*

228. 26 U.S.C. § 7623(b)(4).

229. *See id.*

230. *See* Coder, *supra* note 17, at 1168–69.

### B. CONGRESS SHOULD AMEND § 7623 IN ORDER TO CLARIFY THE PERMITTED USE OF CONFIDENTIAL INFORMATION

In order to reduce the whistleblower claim processing time and eliminate uncertainty, Congress should add a subsection under § 7623(b) to clarify the rules regarding the use of confidential information provided by a tax whistleblower. More specifically, the law should allow tax professionals to report their clients' tax code violation to the IRS even if it means that the clients' confidential information may be revealed in the process. On the other hand, matters that are protected by the attorney-client privilege should always be kept sacred.[231]

Navigating through the multi-layered structure of state laws concerning a tax professional's duty of confidentiality,[232] federal statutory exemptions to the duty of confidentiality that preempt the state laws,[233] and federal common law rules concerning the evidentiary use of privileged materials[234] is like exploring a labyrinth. It is no wonder the IRS claims its legal risk analysis team needs so much time to filter out privileged materials from the bulk of information provided by a whistleblower.[235]

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231. Although sometimes used interchangeably, "confidential" information and "privileged" communication are not synonymous. SUE MICHMERHUIZEN, ABA CENTER FOR PROFESSIONAL RESPONSIBILITY, CONFIDENTIALITY, PRIVILEGE: A BASIC VALUE IN TWO DIFFERENT APPLICATIONS 1 (2007), *available at* http://www.americanbar.org/content/dam/aba/administrative/professional_ responsibility/confidentiality_or_attorney.authcheckdam.pdf ("The attorney-client privilege only protects the essence of the communications actually had by the client and lawyer and only extends to information given for the purpose of obtaining legal representation. The underlying information is not protected if it is available from another source. . . . By contrast, the ethical duty of client-lawyer confidentiality is quite extensive in terms of what information is protected. It applies not only to matters communicated in confidence by the client but also to all information relating to the representation regardless of whether it came from the client herself, or from another source.").

232. Different categories of tax professionals are governed by different professional rules and state statutes. *See generally* Riggall, *supra* note 223, at 257–65 (analyzing the different rules applying to tax return preparers, IRS enrolled agents, CPAs, and attorneys).

233. *See, e.g.*, Sarbanes-Oxley Act § 307, 15 U.S.C. § 7245 (2012).

234. *See* FED. R. EVID. 501 ("The common law—as interpreted by United States courts in the light of reason and experience—governs a claim of privilege unless any of the following provides otherwise: the United States Constitution; a federal statute; or rules prescribed by the Supreme Court. But in a civil case, state law governs privilege regarding a claim or defense for which state law supplies the rule of decision.").

235. *See supra* Part I.C.1.

Perhaps due to this daunting complexity or the fear of disincentivizing the informants, the current Tax Code and treasury regulations are silent as to the use of confidential information provided by whistleblowers.[236] However, the IRS has set up an internal policy to filter out privileged information that may be of limited use in a courtroom in case the audited taxpayer challenges the validity of the information on evidentiary grounds.[237] This filtering process conducted by the agency's legal specialists consumes a tremendous amount of time, preventing the IRS from quickly moving on with the informant's claims.[238] Although the IRS boasts that such practice preserves the "integrity" of its audit procedure,[239] tax professionals who blew the whistle using their clients' confidential information suffer from delay in processing time and uncertainty in the ultimate outcome.

Presumably cognizant of the problem, the IRS proposed a new set of regulations on December 18, 2012, which expressly rejects any claim for an award filed by "an individual who is or was required by Federal law or regulation to disclose the information or who is or was *precluded* by Federal law or regulation from disclosing the information."[240] However, the proposed regulations have not yet been codified.[241]

Lamenting the absence of a provision in the Tax Code regarding the IRS's use of privileged information, a member of the Young Tax Lawyers Committee of the State Bar of California suggested that the IRS revise its proposed regulations to completely ban the holders of privileged information from becoming informants.[242] The Committee member views the proposed regulations' language as too weak and ambiguous to completely exclude an individual who holds privileged information from being "eligible" for awards.[243]

236. *See* McLaughlin, *supra* note 81, at 4 n.17.

237. *See Whitlock Interview*, *supra* note 68, at 86.

238. *See id.* at 87–88.

239. *Id.* at 86.

240. Awards for Information Relating To Detecting Underpayments of Tax or Violations of the Internal Revenue Laws, 77 Fed. Reg. 74,798, 74,805 (proposed Dec. 18, 2012) (to be codified at 26 C.F.R. § 301.7623–1(b)(2)(iii)) (emphasis added).

241. Although public comments were due February 19, 2013, no further developments have occurred as of the publishing of this note.

242. McLaughlin, *supra* note 81, at 6.

243. *Id.* at 4–5.

At the opposite side of the spectrum is Professor Ventry, who opined that Congress should amend the Tax Code, following the example of the Sarbanes-Oxley Act, by explicitly permitting attorney-informants to disclose confidential information when the taxpayer client is involved in a material violation of law.[244] A "material violation of law" under Sarbanes-Oxley does not have to rise to the level of a "crime or fraud," which would constitute a separate exception of its own to the confidentiality and attorney-client privilege rule.[245] According to Professor Ventry, the public benefits generated by aggressive tax enforcement outweigh this sacrifice of the professional duty of confidentiality.[246]

Neither Professor Ventry's nor the Committee' member's approach is sufficient to solve the problem. The Committee's position is too extreme, most likely to have a chilling effect on the potential whistleblowers that often hold the most accurate and direct information on tax cheats. Professor Ventry's idea, on the other hand, runs the risk of being misinterpreted by the public, who may lack the knowledge to distinguish between privileged communications and confidential information. Potential whistleblowers may thus bring in more and more unusable privileged information to the IRS, further clogging the operation of the Whistleblower Office.[247]

This Note proposes a combination of the two ideas with a slight adjustment: Congress should amend § 7623 by expressly

244. *See* Ventry, *supra* note 12, at 390, 401.

245. ABA Model Rule of Professional Conduct 1.6(b)(3) patently permits a lawyer to become a federal tax informant if she discovers that a client has used her services to intentionally violate a federal tax law. The rule states:

> A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary: . . . to prevent, mitigate or rectify substantial injury to the financial interest or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services.

MODEL RULES OF PROF'L CONDUCT R. 1.6(b)(3) (1983).

246. *See* Ventry, *supra* note 12, at 404–06.

247. According to § 7525 of the Tax Code, the common law protection of privileged information between a tax attorney and her client is equally applicable to other types of "federally authorized tax practitioner[s]" with respect to "tax advice." 26 U.S.C. § 7525(a) (2012) ("With respect to tax advice, the same common law protections of confidentiality which apply to a communication between a taxpayer and an attorney shall also apply to a communication between a taxpayer and any federally authorized tax practitioner to the extent the communication would be considered a privileged communication if it were between a taxpayer and an attorney.").

permitting tax professionals to blow the whistle based on their clients' confidential information when the tax professional is reasonably certain of a material Tax Code violation. However, the Code or the treasury regulations thereunder should be modified to make sure that any testimonial evidence protected by the privileges recognized under federal common law must be filtered out by the whistleblower before making a report to the IRS. This way, the holders of privileged information will not be barred completely from becoming whistleblowers and will be able to provide their taxpayer client's confidential information without fear of exposing themselves to malpractice lawsuits or disciplinary sanctions from their professional associations.[248] Additionally, the IRS would likely hasten its claim review process because it will be relieved of its burden to sort through the privileged information that may be disallowed in a federal courtroom.

## CONCLUSION

The IRS's tax whistleblower program provides handsome rewards for those who report incidents of Tax Code violations, reaching up to thirty percent of the total amount of collected proceeds. However, the program is also notorious for its excessively slow processing time which usually consumes several years and the IRS's nonappealable enforcement discretion in administering it. Although some commentators propose importing qui tam action to the Tax Code to remedy these problems, that approach would invoke challenges on constitutional grounds and give birth to dangerous consequences that would offset the purported benefits of increased private enforcement.

Instead of arguing for a drastic change in the tax enforcement scheme, this Note proposes amending the language under § 7623(b)(4) to correct the effects of the recent decisions that took the sting out of the Tax Court appeal right. In addition, this Note suggests adding a clause under § 7623 allowing for the use of confidential information provided by the tax professional-whistleblowers, but disallowing submission of materials protected by the privileges recognized under the federal com-

248. Most state laws on professional duty of confidentiality contain exceptions that allow disclosure that is authorized by law. *See* MICHMERHUIZEN, *supra* note 231, at 2. However, the tax professional informants may still be subject to civil liability based on a breach of contract theory, in case they signed a nondisclosure agreement with the taxpayer. *See* Riggall, *supra* note 223, at 256–57.

mon law. The latter solution will help alleviate the IRS's burden of filtering out illegitimate, unusable evidence as well as protect tax professional-whistleblowers from tort claims or professional sanctions.