NEW YORK CITY BAR

REPORT ON LEGISLATION BY THE STATE AND LOCAL TAX COMMITTEE

A.9975 **M. of A. Weinstein**
S.8815 **Sen. Krueger**

AN ACT to amend the state finance law, in relation to the liability of a person who presents false claims for money or property to the state or local government

THIS BILL IS OPPOSED

The State and Local Tax Committee of the New York City Bar Association writes to express opposition to A.9975/S.8815 (the Bill), which would further expand the False Claims Act ("FCA"), found at N.Y.S. Finance Law §§ 187 to 194, into matters of tax administration which, for the reasons explained below, are more properly vested by the state's Department of Taxation and Finance ("Department") under its existing authority.[1]

I. THE FALSE CLAIMS ACT'S ORIGINS: NO APPLICABILITY TO TAX CLAIMS

The State's FCA did not originally apply to tax claims. In 2010, as part of amendments that sought to create a "false claims act on steroids"[2] and with the Department recommending approval, the FCA was expanded to include state tax claims. L. 2010, c. 379. That legislation included treble damages and mandatory civil penalties for tax fraud and created the "first-in-the-nation program to allow whistle-blowers to go after millionaire tax cheats that defraud the state of over $350,000."[3] Supporters of the legislation touted it as a fraud deterrence and revenue raising measure. However, detractors of the FCA tax expansion provisions pointed to its potential misuse and its long statute of limitations period (10 years), which substantially exceeds the statute of limitations periods provided under the State's tax laws (generally three years and extended to six

[1] The Report represents the views of the Committee members and not those of their firms, companies or clients. Certain members of the Committee, David Bunning, Jahlionais (Elisha) Gaston, and Malinda Sederquist recused themselves from the preparation of this report.

[2] Senator Eric T. Schneiderman Shepherds Historic Anti-Fraud Taxpayer Protection Measure Through Legislation (Jan. 1, 2010), https://www.nysenate.gov/newsroom/press-releases/eric-t-schneiderman/senator-eric-t-schneiderman-shepherds-historic-anti. (All websites last visited May 23, 2022.)

[3] *Id.*

years if there has been a substantial tax understatement). There is no statute of limitations in instances of fraud. Another criticism of using the FCA in tax matters is that such application may directly conflict with considered positions taken by the Department on audit, undermining the Department's ability to resolve disputed issues with finality.[4] The proposed Bill would expand the FCA's reach even further, by extending the FCA's tax law provision to N.Y.S. Finance Law § 189(1)(h) ("knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the state or a local government, or conspires to do the same"). Notably, paragraph (1)(h) was part of legislation addressing Medicare fraud and was expressly omitted from the contemporaneous changes made to N.Y.S. Finance Law § 189(4)(iii).[5] That provision should remain inapplicable to tax cases which, as discussed below, often involve unsettled legal positions that are best addressed by the Department of Taxation and Finance.

II. THE ATTORNEY GENERAL DEEMS NONFILERS WITHIN THE SCOPE OF THE FCA

The bill would extend the FCA[6] to instances where a taxpayer knowingly fails to file a return, which the sponsor's memo states is a "loophole" in the current FCA because the statute imposes a liability where a person made or used false statements or records that were material to an obligation to pay money to the government, such that nonfilers may be viewed as falling outside the FCA's scope. However, the Attorney General's office has long taken the position that nonfilers are within the scope of the FCA, settlements have been obtained on such basis, and the position has already been upheld by the courts.[7]

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[4] *See, e.g., Anonymous v. Anonymous (Moody's Corp.)*, 165 A.D.3d 19 (1st Dep't 2018) (rejecting argument that the FCA action was precluded since both the State and City had audited and settled the issue challenged under the FCA and had entered into closing agreements and consents and waivers); *cf. People ex rel. James v. Starbucks Corp.*, 60 Misc.3d 204 (N.Y. Sup. Ct. N.Y. Cnty. 2018) (in dismissing the complaint, court appeared swayed by the fact that the Department regularly audited the taxpayer and the issues involved in the relator's claim were reviewed during the audits and resulted in no additional sales tax being assessed).

[5] Laws of 2013, ch. 56.

[6] The bill would extend the FCA retroactively. Retroactive legislation that is punitive in nature is generally disfavored, and for good reason. The Court of Appeals long ago observed the injustice of retroactive laws, *Guillotel v. Mayor*, 10 Abb. N. Cas. 318 (1882), and the U.S. Supreme Court has identified due process concerns, *see United States v. Carlton*, 512 U.S. 26 (1994). Although *modest* retroactivity of tax statutes is generally permitted, the retroactivity period proposed in the bill is not modest. *See generally Caprio v. N.Y.S. Dep't of Taxation & Finance*, 25 N.Y.3d 744 (2015).

[7] *See, e.g.,* Press Release, *A.G. Schneiderman Announces $6.2 Million Settlement with Lantheus Medical Imaging and Bristol-Myers Squibb for Failing to Pay New York Corporate Income Taxes* (Mar. 14, 2014), https://ag.ny.gov/press-release/2014/ag-schneiderman-announces-62-million-settlementwith-lantheus-medical-imaging; Press Release, *A.G. Schneiderman Announces $1.56 Million Settlement With New Jersey Appliance Retailer for Failing to Pay New York Taxes*, https://ag.ny.gov/press-release/2014/ag-schneiderman-announces-156-million-settlement-new-jersey-appliance-retailer. *See, e.g., State of N.Y., City of N.Y., ex rel. Campagna v. Post Integrations, Inc.*, 162 A.D.3d 592 (1st Dep't 2018) (rejecting taxpayer's argument that FCA claims "could be brought only against those who filed a tax-related document with New York State, and not against non-filers who otherwise made claims, records, or statements under the tax law.")

III. THE FACTORS UNDERLYING A DECISION WHETHER TO FILE A TAX RETURN ARE OFTEN MURKY

Further, many nonfiler situations involve nexus (tax jurisdiction) situations, determinations of domicile, and applications of Public Law § 86-272,[8] which often require subjective fact-specific determinations and the application of developing law. One need only review tax decisions on nexus, domicile and P.L. 86-272 to conclude that the delineation between taxable and nontaxable is often unclear and such determinations are best addressed by the Department as part of the normal tax administration function, rather than through the FCA.

IV. FURTHER DEFINING "KNOWLEDGE" IS CONFUSING AND UNNECESSARY

A.9975/S.8815 would explicitly recognize that for purposes of N.Y.S. Finance Law § 189(1)(h) "knowledge shall not be established because of an act occurring by mistake or as a result of mere negligence." However, N.Y.S. Finance Law § 188(3)(b) *already* provides that "[k]nowing and knowingly" does not include "acts occurring by mistake or as a result of mere negligence." The inclusion of language particular to section 189(1)(h) is unnecessary and could lead to the implication that the exception of instances of "mistake" or "mere negligence" are inapplicable or different from the exceptions applicable to sections 189(1)(a) through 189(1)(g).

Furthermore, attempting to use "mistake" or "mere negligence" as a safeguard in this context is troublesome given that nonfiling positions are often fact-driven and subjective and the law murky and/or inconsistent. The bill should include protections where (1) good faith legal positions exist for not filing returns, and (2) the purported taxpayer relied in good faith on the advice of a competent advisor. Purported taxpayers can be the target of *qui tam* litigation and be forced to expend significant resources to establish that they had such good faith legal positions, even in instances where they relied on the advice of competent advisors in determining that they did not have a filing requirement.

V. THE ATTORNEY'S FEES PROVISION IS NOT A DETERRENT AS WRITTEN

Under the Bill's proposed language, the possibility of a defendant recovering attorney's fees is highly unlikely. As currently written, the Bill allows for an award of reasonable attorney's fees and expenses if the claim was "clearly frivolous, clearly vexations, or brought primarily for purposes of harassment." Given the ease for a relator to put forth a "reasonable" basis for commencing an FCA suit, as written, the Bill will not act as an effective deterrent against those who would bring litigation for improper purposes.

The attorney's fee provision should also (1) not be limited to suits under section 189(1)(h) but should apply to *all* tax-related false claims; and (2) be expanded to grant such fees to defendants in instances where (a) the defendant ultimately prevails in the action; (b) the law and tax subjectivity is unclear; and (c) the defendant relied on advice from a competent advisor.

[8] Public Law § 86-272 (15 U.S.C. § 381, *et seq.*), is a federal law that preempts states from imposing a net income tax on persons that otherwise would have nexus if the person's activities meet certain restrictions. The activities must be limited to: (i) the solicitation of orders of tangible personal property; (ii) which orders are sent outside the state for approval or rejection; and (iii) if approved, are filled by shipment or delivery from a point outside the state.

VI. CONCLUSION

In sum, tax law is replete with nuances and ambiguities that are best resolved by the tax authority.[9] For this and other reasons stated above, the Committee recommends that this proposed legislation be rejected.

State and Local Tax Committee
Amy F. Nogid, Chair

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[9] *See, e.g.*, *People v. B&H Foto & Electronics Corp.*, Index No. 252106/2019 (NY Sup. Ct. NY County, Sept. 21, 2021) (concluding that "Instant Savings" program was not the equivalent of manufacturers' coupons and such amounts were not deemed to be receipts subject to sales tax; Court acknowledged that the mere recognition of a potential tax issue is not evidence of fraud, it must be coupled with a statutory violation: "the absence of a statutory violation means that persistent fraud or illegality was not committed even if B&H believed it was acting unlawfully").