How Schneiderman Changed Tax Fraud Enforcement in New York

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Eric Schneiderman’s tenure as a New York state senator and the state's attorney general changed the face of New York's False Claims Act (FCA), but practitioners say his sudden resignation is not expected to change the way the attorney general's office enforces the act.

Schneiderman's announcement that he was stepping down May 8, only hours after allegations that he physically assaulted women were published in a *New Yorker* article, came as a shock to many. Although he vehemently denied the allegations, he made sure his statement distinguished his private life from his time in office, saying “these allegations are unrelated to my professional conduct or operations of the office.”

Schneiderman made his mark as a Wall Street watchdog, and for many tax professionals, his tenure will be marked by his enforcement of the FCA, which he helped expand while serving in the state Senate. Under his leadership and guidance, New York has recovered millions of dollars for the state and its taxpayers.

Lori Pines, head of the FCA/qui tam group at Weil, Gotshal & Manges LLP, told Tax Analysts May 14 that the allegations against Schneiderman’s personal life shouldn’t detract from his legislative and legal accomplishments “including his leadership in New York on false claims issues.”

“The New York False Claims Act is a unique statute that is now embedded in New York jurisprudence,” Pines added.

New York Solicitor General Barbara Underwood is serving as interim attorney general while the Legislature interviews potential successors to carry out the remainder of Schneiderman's term. Underwood has said she has no plans to run for the office in November.

William Comiskey of Hodgson Russ LLP, who served as deputy commissioner for tax enforcement at the New York State Department of Taxation and Finance, praised Underwood and the staff at the attorney general's office. “The folks at the attorney general’s office are professionals and will stay the course, certainly under Barbara Underwood,” he told Tax Analysts.

David Koenigsberg of Menz Bonner Komar & Koenigsberg LLP told Tax Analysts that he doesn't think "the change in leadership will have any impact on how the cases are handled or pursued," adding that he expects the office "to proceed without any interruption.”

Numerous tax practitioners heavily involved in *qui tam* cases expect no serious changes in the way the state handles FCA cases, but they also don’t dispute Schneiderman's legacy of expanding and enforcing the FCA.

From Lawmaker to Enforcer

Before being elected attorney general in 2010, Schneiderman's 12-year tenure in the state Senate culminated with the passage of the Fraud, Enforcement & Recovery Act (FERA), a bill he sponsored and would later enforce. The measure was introduced during a statewide budget crisis and as anger toward Wall Street reached a boiling point. FERA expanded the FCA to specifically include tax fraud and to encourage whistleblowers to come forward, not just on Medicaid and contractor fraud cases, but also on tax violations.

"That put New York in a unique position," Randall Fox of Kirby McInerney LLP told Tax Analysts, adding that most states don't allow incentives for whistleblowers in any kind of tax case.

"Under the New York False Claims Act, a whistleblower can bring a *qui tam* lawsuit against an individual or business that makes more than $1 million in net income where the alleged amount New York is being defrauded via a false or fraudulent claim or statement under the state's tax laws is more than $350,000," according to Pines. "It sets limits so that you don't have as many nuisance lawsuits being brought."

Schneiderman's pursuit to hold accountable those companies engaged in tax fraud didn't end with the passage of FERA. "One of his first acts as New York attorney general was to form the Taxpayer Protection Bureau," Pines said. The creation of the bureau centralized the office's handling of non-Medicaid false claims cases, making tax cases a priority.

Fox, who served as the bureau's first chief, said that "by putting those resources in, it was a way of telling the world that New York was open for business in pursuing those kinds of cases."

FCA Criticism

Some practitioners are critical of the expanded FCA, arguing that because purposeful intent is not required, some taxpayers could plead deliberate ignorance. Others argue that different interpretations of a state's tax laws could leave the taxpayer in hot water.

Peter Faber of McDermott Will & Emery said that expanding the FCA was "unnecessary and a mistake." The state Department of Taxation and Finance "is perfectly capable of administering the tax laws," he said.

Matthew Hedstrom of Alston & Bird LLP echoed Faber's comments on the FCA expansion. "There is considerable debate on whether the use of False Claims Act statutes are appropriate at all in tax cases and the proliferation of these types of cases will, in my view, lead to pressure on the states to rethink the appropriateness of their use," Hedstrom told Tax Analysts, adding that he hopes the new attorney general will alter the way these cases are being approached.

Comiskey said he understands some of the sentiments of fellow tax practitioners. "If the cases brought were more readily apparent to be involving deliberate deception I don't think anyone would be complaining about it," he said. He disagreed that the statute's enactment was a mistake, however, arguing that if used in the right cases it is a tool that governments should embrace. "I think it needs to be judiciously and lawfully used," Comiskey said. "I think where you draw lines may be subject to debate, but they really have to be reflective of the evidence you have and the facts at your disposal."

And despite his criticism with the statute, Faber said he doesn't believe that the attorney general's office has abused its powers when going after fraudulent taxpayers, explaining that the office has been professional and evenhanded in its pursuit of tax fraud cases. "They use the tools at their disposal and that may give rise to a perception that they are 'aggressive,' but I don't think that they have been improperly aggressive."

FCA Impact

Gregory Krakower of Getnick & Getnick LLP, who helped craft the expansion of the New York FCA while serving as senior adviser to Eric Schneiderman, said that the tax provision helps keep companies in check. "There is the underreported benefit that many companies have tightened up their New York tax compliance out of fear of being caught by whistleblowers under the New York tax False Claims Act," he said.

Pines agreed, saying, "I think the New York False Claims Act impact on New York tax compliance cannot be overstated," adding that "under the act, a taxpayer can be held liable for treble damages, and the statute of limitation is 10 years and not the three years generally applicable to tax audits."

Hedstrom said that companies need to remain vigilant "by undertaking a review of their New York tax positions and carefully documenting the positions that they are currently taking, especially if there is any risk that those positions might be subject to challenge by the New York taxing authorities."

And while some companies in New York have undoubtedly lamented the FCA, practitioners agree that the act has helped New York avoid some of the pitfalls other states have encountered in whistleblower cases.

Illinois's FCA, for example, has no monetary thresholds, leaving the state open to frivolous whistleblower cases. New York avoided that problem by including monetary thresholds, Krakower said. "New York actually has a much broader tax whistleblower statute than Illinois because it covers state income taxes — and yet we have avoided the perceived abuses in Illinois because of monetary thresholds that require cases to be brought against large corporate tax cheats and millionaires," he added.

Comiskey largely agreed. "New York adopted a more reasonable statute," he said. "Could it have been better? Could it have been more precise on what kind of allegations it supported? Maybe." He also praised the attorney general's office's approach to dealing with *qui tam* cases in the tax world. "In comparison to what has happened in other states, New York has been more selective, with the attorney general's office being a check for the process," Comiskey said. "Their involvement has led to cases ending and their investigations have been thorough."

It is unclear who will ultimately become the state's next attorney general, but Fox said he thinks pursuing FCA cases will remain a priority for the office. “My expectation is that it will be attractive for any attorney general to make sure that government dollars are spent the way they’re supposed to be spent and the government is receiving the dollars it’s supposed to receive.”