

How the Bipartisan Budget Act Will Benefit Whistleblowers

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On February 9, 2018, President Trump signed into law the Bipartisan Budget Act of 2018. Two provisions of the law that have received little coverage in the press provide a great boon for whistleblowers seeking awards through the [SEC](#), [CFTC](#), and [IRS](#) whistleblower programs, as well as any state false claims act.

In order to understand why this new law is important, one must wade through some of the intricacies of federal income tax law. While such a journey is not exciting to most readers – which is likely part of the explanation for the lack of press coverage – the new amendments to the tax code greatly increase the financial benefit many whistleblowers may receive for providing evidence of illegal activity to the government. If [whistleblower award programs](#) are to accomplish their goal of incentivizing private individuals to assist the government in preventing fraud, the public must know what those financial incentives are.

Taxability of Attorneys' Fees

Many individuals seeking remedies through the legal system – be they car accident victims suing the driver at fault, employees bringing discrimination claims against their employers, or whistleblowers participating in a government whistleblower award program – pay trained attorneys to help them navigate the plethora of complex rules that govern our courts and administrative agencies. Whether the individual pays her attorneys' fees out-of-pocket or allows the attorney to take a percentage of what she recovers through the legal system, the money the individual uses to pay to her attorney almost always qualifies as part of that individual's "gross income" under the Internal Revenue Code. Depending on the complexity of the legal matter and the fee agreement between the client and the attorney, the amount of attorneys' fees can be extraordinarily high, sometimes matching or eclipsing the size of the recovery. If the individual is required to pay income taxes on the money she paid her attorneys, the financial benefit of her legal recovery might be little to nothing after she pays the IRS in April. If a potential litigant or whistleblower knew that most of her recovery would be consumed by attorneys' fees and tax bills, she might not even bother seeking recovery through the legal system at all.

Knowing that the taxability of attorneys' fees raises the costs for individuals seeking recovery through the legal system, Congress has historically allowed individuals to deduct their attorneys' fees from their gross income for certain types of legal claims that promote important public values, thus increasing the likelihood such claims will be brought. For instance, the Internal Revenue Code allows employees who recover money for claims of employment discrimination, retaliation, or unpaid compensation to deduct their attorneys' fees from their gross income, although the deduction may not exceed the amount of gross income the individual earned in the recovery. Similarly, a relator who recovers for a *qui tam* claim under the [False Claims Act](#) or a whistleblower who reported tax fraud to the IRS whistleblower program is allowed to deduct his or her attorneys' fees from gross income to the extent the attorneys' fees do not exceed the recovery. By removing the prospect that a

devastating tax bill will completely diminish the value of a legal recovery, Congress has made it more likely that employees and whistleblowers will utilize the legal system to seek redress for unlawful employment practices and fraud against the government.

However, as Congress passed more laws to incentivize individuals to blow the whistle on fraud in different sectors of the economy, it did not amend the Internal Revenue Code to allow these new whistleblowers to deduct their attorneys' fees from their gross income. When Congress passed the [Dodd-Frank Act of 2010](#), it created award programs for the SEC and CFTC which have paid out millions of dollars to whistleblowers. Similarly, in an effort to fight rampant Medicaid fraud throughout the country, Congress passed the Deficit Reduction Act of 2005, creating financial incentives for states to create state false claims acts. Since then, many relators have successfully brought state *qui tam* claims against healthcare providers defrauding state Medicaid programs, returning millions of taxpayer dollars to state coffers. Until now, these award recipients who hired attorneys to file their SEC or CFTC tips or state false claims act suits faced huge tax bills because they could not deduct their attorneys' fees, drastically diminishing the personal benefit they received for accomplishing important public objectives.

With the enactment of Section 41107 of the Bipartisan Budget Act of 2018, Congress has amended the Internal Revenue Code to allow these whistleblowers to deduct their attorneys' fees to the extent the deduction does not exceed the amount of income earned in the recovery. By reducing the economic burden on these whistleblowers and putting them on par with employees bringing employment discrimination claims and relators suing fraudulent government contractors under the False Claims Act, Congress has once again recognized the important values vindicated by individuals who protect the public by reporting fraud to the government. Not only will this law encourage more whistleblowers to help the government combat fraud, it will ensure that whistleblowers get the financial benefits they deserve for their courageous acts of public service.

Expanded IRS Whistleblower Program

In addition to reducing the tax burden on SEC, CFTC, and state false claims act whistleblowers, the Bipartisan Budget Act of 2018 delivered an important win for [IRS whistleblowers](#). Until now, the law provided that a whistleblower who provided original information to the IRS about tax fraud could recover an award if that information led to an IRS enforcement action which recovered at least \$2 million in "penalties, interest, additions to tax, and additional amounts." Although this list seemed expansive, IRS whistleblowers would be denied their fair share in cases in which the IRS collected money through criminal fines, civil forfeitures, and other fees for violating income reporting requirements. Such a narrow reading of the law would leave whistleblowers who helped the IRS discover offshore tax-avoidance schemes without any award, even though their information could lead to the return of millions of taxpayer dollars. Section 41108 of the Bipartisan Budget Act of 2018 has changed the law to provide an even-more expansive definition of what kinds of "proceeds" count toward a whistleblower award, ensuring that whistleblowers who expose major tax fraud can collect their fair share no matter what kind of enforcement action the IRS takes.

A Big Win for Whistleblowers

The Bipartisan Budget Act of 2018's revisions to federal income tax law represent a major victory for whistleblowers, providing greater financial incentives for individuals to cooperate with law enforcement to put an end to fraud that harms investors and taxpayers across the country.