Michael Lissack v. Commissioner of Internal Revenue, 157 T. C. No. 5 (2021)

In a significant ruling on whistleblower awards, the U. S. Tax Court upheld the IRS's denial of a whistleblower award to Michael Lissack, who alleged unreported income by a group of entities. The court ruled that Lissack was not eligible for an award because the IRS did not collect proceeds based on the information he provided. This decision clarifies the scope of IRS actions that qualify for whistleblower awards under I. R. C. § 7623(b), emphasizing the need for a direct link between the whistleblower's information and the IRS's collection of proceeds.

Parties

Michael Lissack, as the Petitioner, sought a whistleblower award under I. R. C. § 7623(b) from the Commissioner of Internal Revenue, the Respondent. The case was adjudicated at the U. S. Tax Court.

Facts

Michael Lissack filed a Form 211 with the IRS, alleging that a group of entities (collectively referred to as "Target") had failed to report millions of dollars in membership fees as gross income for the year 2008. The IRS initiated an examination based on Lissack's claim, which concluded that the membership fees were properly treated as nontaxable deposits. However, during the examination, the IRS discovered an unrelated issue concerning an erroneous deduction claimed by Target for intercompany bad debt. The IRS expanded the examination to include this issue, ultimately disallowing the deduction and assessing a $60 million adjustment. Lissack's claim for a whistleblower award was denied because the adjustment was unrelated to the information he had provided about the membership fees.

Procedural History

The IRS Whistleblower Office processed Lissack's Form 211 and referred it to a revenue agent for examination. After determining that the membership fees were properly treated, the agent discovered the unrelated bad debt issue. The IRS assessed additional taxes based on this issue but denied Lissack's claim for a whistleblower award. Lissack petitioned the U. S. Tax Court for review, and both parties filed cross-motions for summary judgment. The Tax Court reviewed the case under the administrative record and granted the Commissioner's motion for summary judgment.

Issue(s)

Whether a whistleblower is entitled to an award under I. R. C. § 7623(b) when the IRS collects proceeds from an administrative action that was expanded to include issues unrelated to the information provided by the whistleblower?

Rule(s) of Law

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I. R. C. § 7623(b)(1) provides that a whistleblower is eligible for an award only if the IRS proceeds with an administrative or judicial action "based on information" supplied by the whistleblower and collects proceeds "as a result of the action. " Treasury Regulation § 301. 7623-2(b)(1) defines "proceeds based on" as an action where the whistleblower's information "substantially contributes" to the action. The regulation also clarifies that an IRS examination may comprise multiple "administrative actions," and only the portion of the examination directly linked to the whistleblower's information qualifies for an award.

Holding

The U. S. Tax Court held that Michael Lissack was not eligible for a whistleblower award under I. R. C. § 7623(b) because the IRS did not collect any proceeds "as a result of the action" based on the information he provided. The examination of the erroneous deduction issue constituted a separate administrative action not initiated on the basis of Lissack's claim.

Reasoning

The court applied the Chevron two-step test to evaluate the validity of the Treasury Regulations. At Chevron Step One, the court found that Congress had not directly spoken to the precise question of what constitutes an "administrative or judicial action" under I. R. C. § 7623(b), leaving room for the Secretary to define the term through regulation. At Chevron Step Two, the court determined that the regulations were a reasonable interpretation of the statute, defining an "administrative action" as a portion of an IRS examination and requiring a substantial contribution from the whistleblower's information to qualify for an award. The court rejected Lissack's argument that the IRS's expansion of the examination to include the bad debt issue constituted a "related action" under the regulations, as it was not against a different person and did not involve substantially the same facts as his original claim. The court emphasized that the IRS did not proceed based on Lissack's information in disallowing the bad debt deduction, and thus, he was not entitled to an award.

Disposition

The U. S. Tax Court granted the Commissioner's motion for summary judgment and denied Lissack's cross-motion, affirming the IRS's denial of the whistleblower award.

Significance/Impact

This case significantly clarifies the scope of whistleblower awards under I. R. C. § 7623(b), emphasizing that a whistleblower's information must directly contribute to the IRS's collection of proceeds to qualify for an award. The decision upholds the validity of Treasury Regulations defining "administrative action" and "proceeds based on," providing guidance for future whistleblower claims. It also highlights the

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importance of the whistleblower’s information in triggering and contributing to the specific IRS action that leads to collected proceeds. This ruling may influence how whistleblowers frame their claims and how the IRS evaluates eligibility for awards, potentially affecting the incentives for reporting tax noncompliance.

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