

Economics Professor Uses New York FCA to Sue Citigroup for \$2.4 Billion

POSTED ON OCT. 22, 2015

By

 DAVID SAWYER

An economics professor from Indiana University is using New York's False Claims Act (FCA) to bring a \$2.4 billion lawsuit against Citigroup, alleging that the bank failed to pay \$800 million in taxes to the New York State Department of Taxation and Finance.

The plaintiff, Eric Rasmusen, initially filed his complaint  in New York state court under seal in 2013 and served the complaint on Citigroup in September 2015 after New York Attorney General Eric Schneiderman (D) declined to pursue the case.

Citigroup moved  the case to the U.S. Federal District Court for the Southern District of New York on October 2.

In the complaint Rasmusen said that Citigroup's unpaid tax liability arose from its participation in the federal Troubled Asset Relief Program (TARP), which was set up in accordance with the Emergency Economic Stabilization Act of 2008 following the financial crisis.

As part of the program, the U.S. Treasury Department purchased equity interests in Citigroup that ultimately amounted to a \$45 billion investment in the company. These investments, according to the complaint, constituted a change in ownership of the corporation for purposes of IRC section 382, which establishes limitations on the use of net operating losses.

According to the complaint, starting in 2009, the IRS waived the restrictions on the use of NOLs for companies that benefited from the Treasury's actions under TARP by issuing Notice 2009-38, 2009-18 IRB 901  and Notice 2010-2, 2010-2 IRB 251  to stipulate that NOL limitations did not trigger upon a change of ownership caused by either the Treasury's purchase or sale of stock in the companies.

In 2010, the complaint said, Citigroup repurchased \$20 billion of its stock from the government, and the government sold off its remaining \$25 billion worth of stock on the open market. These transactions, the complaint said, constituted a second change in ownership of Citigroup under section 382.

Because it did not consider section 382 NOL limitations to apply, Citibank was able to use losses to reduce not only its federal tax burden but also its New York state franchise tax obligation because the state's tax code conforms to the IRC, the complaint said.

"Like federal law, New York allows a corporation to take a NOL deduction and, for taxable years beginning on or after January 2001, the New York NOL is 'presumably' the same as the federal NOL," with certain

modifications made to it for state purposes, the complaint said. New York's tax law incorporates the IRC's NOL deduction, the complaint said, and in so doing "also incorporates the NOL limitation on carryovers in section 382 of the IRC."

The notices issued by the IRS, which Citigroup relied on to avoid limiting its use of NOLs, were issued in contradiction to express orders of Congress and so were improperly promulgated, according to the complaint. Because of this, the complaint said, Citigroup "was not entitled to rely upon them to reduce its taxable income for purposes of the IRC or, for that matter, the New York Tax Law."

Further, the complaint said, even if the IRS notices were valid, they were not adopted by New York or incorporated into the state's tax laws, meaning that Citigroup could not rely on them for state tax purposes.

Despite this, the complaint said, Citigroup between 2010 and 2012 "knowingly made, used, or caused to be made or used, or is knowingly making, using or causing to be made or used, false records or statements material to an obligation to the state" to file tax returns with improperly excessive NOL deductions to avoid paying approximately \$800 million in taxes owed to New York under the state tax code.

In his complaint, Rasmusen said that he is seeking treble damages, civil penalties, and attorney fees under the state's FCA, all of which would drive the total amount at issue in the suit to \$2.4 billion.

In a press release , Rasmusen said that "based on what I have been able to uncover, I can't understand why Citigroup and its team of tax lawyers have been allowed to take advantage of New York State this way."

Rasmusen added that he is disappointed that the state attorney general decided not to join the suit. "While we are confident we can convince the court that Citigroup owes millions to New York State, when you're facing a company this big, it would be helpful to have the attorney general on the taxpayers' side," he said.

The federal district court has asked Citigroup to respond to, answer, or move to dismiss Rasmusen's complaint by December 7.

However, in the meantime the New York Court of Appeals on October 20 decided the first tax-related FCA case to make its way to the high court. In that case, *New York v. Sprint Nextel Corp.* , the court found that the attorney general had a cause of action under the FCA to bring suit against telecommunications giant Sprint Nextel Corp. in pursuit of \$100 million in New York sales tax obligations that the attorney general claims the company knowingly and improperly avoided paying. (Prior coverage )

Rasmusen told Tax Analysts that the court's decision in *Sprint* applies to his suit as well because it clarifies the *scienter* requirement under the state's FCA.

"We claim that section 382 of the Tax Code unambiguously contains no exception for tax-exempt shareholders such as a charity or the U.S. Treasury, and that Citigroup knows this," Rasmusen said. "Thus, it, like Sprint 'will have to substantiate in further proceedings that it actually held such reasonable belief,' and in

our case, we are 'entitled to discovery, and there are factual issues that must be fleshed out in further proceedings,' to quote from the Sprint decision," he added.

Rasmusen added that it is noteworthy that the court in *Sprint* cited a 2011 case, *Matter of New York State Superfund Coalition Inc. v. New York State Dept. of Env'tl. Conservation*, "to reiterate that under New York state law, the courts only defer to a state agency (and, *a fortiori* to the federal IRS), in a case 'where interpretation or application involves knowledge and understanding of underlying operational practices or entails an evaluation of factual data and inferences to be drawn therefrom.'"

"Our case is not about operational practices in the slightest," Rasmusen said, "thus, Citigroup cannot rely on IRS notices for interpretation of New York state law."

"We believe the claims are without merit," Kamran Mumtaz, a spokesman for Citigroup Inc., told Tax Analysts.

Peter Faber of McDermott Will & Emery said that the suit against Citigroup illustrates the mischief that can happen if citizens decide to act as vigilantes.

"We don't generally allow citizens to usurp the role of competent government agencies," Faber said. "If someone thinks that a corporation is not meeting its tax obligations, he should go to the IRS or state tax department and let them decide whether to pursue it," he added.

Further, Faber said, "treble damages is an awful remedy."

"The tax laws already contain severe penalties for fraud, often 50 percent or 100 percent of the tax," Faber said. "Why should the penalty be dramatically more severe if the proceeding starts at a private person's initiative?" Either way, he said, the taxpayer's conduct is the same.

Faber said the plaintiff apparently does not like that Citigroup accepted the IRS's interpretation of the law. "If Citi had not taken the position that it did, would he have brought a shareholders' derivative suit against Citi for failing to take legal deductions?" Faber said.

"The fact that a politically aggressive AG who is no fan of big banks declined to get involved should tell us something," he added.

DOCUMENT ATTRIBUTES

CODE SECTIONS

SECTION 382 -- NOL CARRYOVERS

SECTION 172 -- NET OPERATING LOSS

JURISDICTIONS

[NEW YORK](#)

SUBJECT AREAS

CARRYBACKS AND CARRYFORWARDS

INDUSTRY GROUPS

BANKING, BROKERAGE SERVICES, AND RELATED
FINANCIAL SERVICES

AUTHORS

[DAVID SAWYER](#)

INSTITUTIONAL AUTHORS

TAX ANALYSTS

TAX ANALYSTS DOCUMENT NUMBER

DOC 2015-23417

TAX ANALYSTS ELECTRONIC CITATION

2015 STT 204-2
