UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

THE STATE OF NEW YORK *ex rel.*
ERIC RASMUSEN,

Plaintiff,

- against -

Case No.: 1:15-cv-07826-LAK

CITIGROUP, INC.,

Defendant.

ERIC RASMUSEN'S MEMORANDUM IN OPPOSITION TO CITIGROUP'S MOTION TO DISMISS

HODGSON RUSS LLP
Attorneys for Eric Rasmusen
Daniel C. Oliverio, Esq.
John L. Sinatra, Jr., Esq.
Aaron M. Saykin, Esq.
The Guaranty Building
140 Pearl Street, Suite 100
Buffalo, New York 14202-4040
716.856.4000

and

1540 Broadway, 24th Floor
New York, New York 10036
212.751.4300

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INTRODUCTION

Citigroup improperly gave itself nearly a *billion-dollar* New York State tax break without first checking with the State. Instead, Citigroup took this massive tax deduction relying on a facially bogus free-pass from the IRS that was applicable only to Citigroup's *federal* taxes, in violation of federal statute and, thus, New York tax law. This false deduction cannot stand.

This kind of case is exactly what the New York False Claims Act's ("NYFCA's") tax whistleblower provisions were designed to remedy — a defendant's culpable failure to pay a significant tax liability. Without Professor Rasmusen's initiation of this case, Citigroup's New York scheme would have gone unnoticed, unchallenged, and unremedied.

Citigroup's Rule 12(b)(6) motion to dismiss must be denied. As set forth below, Citigroup's scheme is based on IRS "Notices" — issued while the U.S. Treasury owned one-third of the company's shares — which allowed the company to carry over tens of billions of dollars in net operating losses ("NOLs") in express contravention of the Internal Revenue Code. While Citigroup's reliance on the Notices may or may not put Citigroup in a safe place *vis a vis* its *federal* tax returns (which are not at issue here), the same is not true for its *New York State* tax liability. New York tax law incorporates the Internal Revenue Code, the plain and unambiguous text of which directly contradicts the Notices. It is black letter law in New York that federal administrative interpretations of statutes that contradict unambiguous statutory language must be rejected. Thus, Citigroup was forbidden from applying the federal NOL deductions at issue to its New York State returns. As a matter of law, Citigroup's citation to the Notices fails to insulate it from New York State tax liability.

Similarly deficient is Citigroup's claim that, even if the deductions were illegal under the New York tax code, it did not knowingly underpay. First, such a scienter argument is premature on a Rule 12(b)(6) motion to dismiss under Second Circuit and persuasive New York Court of Appeals case law. At this juncture, as pleaded (and as explained below), Citigroup's actions were done with sufficient culpability. Discovery into whether Citigroup knowingly claimed false deductions on its New York tax filings, as "deliberately ignorant" or with "reckless disregard," should proceed. It is unfathomable that a company of Citigroup's size, with its array of tax advisors, did not knowingly or recklessly disregard New York State tax law based on a free pass from the IRS.

Finally, Citigroup's claim that it is immune from liability here because its federal tax scheme was publicly disclosed fails for a simple reason. No allegation concerning Citigroup's New York tax liability was disclosed in public before the filing of this action. Citigroup conflates public disclosure of its federal tax behavior with its State tax liability. They are distinct, and, under well-established precedent, that distinction precludes Citigroup's invocation of the public disclosure bar. A decision on the merits of Citigroup's nearly billion-dollar New York tax dodge is required.

For these reasons, Citigroup's motion to dismiss should be denied.

FACTUAL BACKGROUND

A. New York's False Claims Act.

The NYFCA was adopted to facilitate the recovery of funds from those who, like Citigroup, have defrauded the State of New York. In 2010, New York amended its False Claims

Act to cover tax fraud. *See* N.Y. State Finance Law § 187, *et. seq.*

While similar to the federal False Claims Act, the NYFCA has critical differences relevant to this action. Notably, it permits claims for the filing of a false tax return, and it includes a whistleblower-friendly public disclosure bar.

The NYFCA encourages private persons, "relators," to blow the whistle on fraudulent tax filings by bringing qui tam lawsuits like this one on behalf of the State. *See* N.Y. State Fin. Law § 190(2)(a). NYFCA cases can be initiated by the Attorney General (or a local government), *id*. § 190(1), or by a relator who initiates the case in the hopes of a share in the recovery, *id*., § 190(2), (6).[1]

For tax cases, the NYFCA covers "claims, records, or statements made under the tax law" if three conditions are satisfied: (1) the defendant's net income or sales exceeds $1 million per year, (2) damages, as pleaded, exceed $350,000, and (3) the defendant "is alleged to have violated paragraphs (a), (b), (c), (d), (e), (f) or (g) of subdivision one of this section [189]." *Id.* § 189(4)(a). Paragraph (g) covers the case here, where Citigroup, through the filing of its New York tax returns, is alleged to have knowingly made or used "a false record or statement

[1] Contrary to the implication in Citigroup's footnote 1, the Attorney General's decision not to intervene in an FCA case has no bearing on the merits. *See, e.g.*, *United States ex rel. Feldman v. van Gorp*, 697 F.3d 78 (2d Cir. 2012). The NYFCA anticipates this, and provides a higher share of recovery to successful relators who proceed alone, as is their right. The NYFCA also permits the Attorney General to keep abreast of proceedings and *intervene later* for good cause. *See* N.Y. State Fin. Law §§ 190(2), 190(5)(a). In fact, for fiscal year 2015, $1.1 billion was recovered in federal whistleblower suits in which the Justice Department declined to intervene, compared to $1.8 billion recovered in intervened FCA cases. *See* DOJ Fraud Statistics, http://www.justice.gov/opa/file/796866/download, last visited 12/28/15.

material to" its obligation to pay its State taxes. *See id.* § 189(1)(g).[2] The NYFCA's tax provisions were designed to provide an additional enforcement tool and to deter false tax returns, while increasing recoveries to the State. *See, e.g.*, *People v. Sprint Nextel Corp*, 25 N.Y.3d 1217, 16 N.Y.S.3d 511 (2015). Actionable conduct must be "knowing," which means one of three mental states: "actual knowledge," "deliberate ignorance," or "reckless disregard." *See id*. § 188(3)(a).

The NYFCA permits whistleblower claims based on either private or publicly disclosed information, with three exceptions. In these cases, the court "shall dismiss" an action "unless opposed by the state . . . or unless the qui tam plaintiff is an original source of the information," if the same "allegations or transactions" were "publicly disclosed" in hearings to which the government is a party, in a "federal, New York state or New York local government report" or in "the news media." *See id*. § 190 (9)(b)(i)-(iii).

The NYFCA differs from its federal counterpart because it permits whistleblower claims to proceed in the face of allegations of a previous public disclosure of the issue. In particular, the State of New York "shall oppose the dismissal" of an action "solely because of an alleged public disclosure in a federal report." 13 N.Y.C.R.R. § 400.5 (emphasis added). And dismissal on such grounds is not permitted if "opposed by the state." N.Y. State Fin. Law § 190(9)(b). New York public policy thus disfavors dismissal on account of allegations disclosed in federal reports. New York was also careful to write the statute to exclude web materials from the definition of "news media." *Id.* § 190(9)(b)(iii).

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[2] Citigroup's recitation at page 22 of its brief appears to overlook the tax provision of Section 189(4)(a) and the "false record or statement" provision of Section 189(1)(g).

B. The Parties.

Eric Rasmusen is the Dan R. and Catherine M. Dalton Professor of Business Economics and Public Policy at Indiana University's Kelley School of Business. Compl. ¶ 5.

Citigroup is a global diversified financial services holding company with its principal executive offices in New York City. *Id.* ¶ 7. Citigroup incurred losses during the recession years of 2008 and 2009. Citigroup then failed to pay the State of New York approximately $800 million in taxes by improperly deducting those losses from its taxable income after undergoing ownership changes resulting from the federal government's purchase and sale of Citigroup stock. *Id.* ¶¶ 1-2.

C. The Tax Treatment of Net Operating Losses.

As alleged in paragraphs 13-15 of the complaint, the Internal Revenue Code ("IRC") sets forth a number of deductions that can be taken under federal law when computing taxable income. *See* 26 U.S.C. § 161. One is the deduction for net operating losses ("NOLs"), the excess of costs over gross income. *Id.* at § 172(c). The theory is that a taxpayer experiencing losses in one year and profits the next should be able to use the losses to offset the profits. NOLs not used up because of insufficient profits to offset can be carried forward to subsequent tax years.

Section 382 of the IRC severely limits a corporation's ability to carry forward NOLs if the corporation experiences an "ownership change" between the time it incurs the NOLs and the time it uses them as deductions. *Id.* at § 382(a), (c). Section 382 is intended to prevent loss trafficking, based on the notion that new owners, who did not own shares when the

corporation experienced losses, should not benefit from those losses. This prevents anyone from buying ownership for the deductions, reducing government revenue. Section 172 of the IRC incorporates the loss trafficking restrictions of Section 382 by reference. *See* IRC § 172(k)(2).

The prevention of loss trafficking is at the core of both the IRC's plain language and legislative history. Since 1943, the IRC has included some sort of provision to combat loss trafficking. *See* H. Rep. No. 871, 78th Cong., 1st Sess. (1943), regarding the addition to the IRC of former Section 129, the predecessor of the present Section 269. After experimentation with more subjective rules involving share buyer intent, the present Section 382 is written as a set of *bright-line rules* to determine whether a corporation with net operating loss carryforwards experienced an "ownership change," intent being irrelevant. If such a corporation (the "Loss Corporation") experiences an "ownership change," Section 382 limits future use of its NOLs. Although Section 382 provides a strictly arithmetic test for "ownership change," the arithmetic is complex because it must deal with purchases by multiple shareholders of existing and newly issued stock. If the corporation experiences an ownership change, NOL carryforwards are severely limited. *See* IRC § 382(a).

The annual limit is determined by multiplying the value of the corporation on the date of the ownership change (very low for Citigroup in 2009) by the "long term tax exempt rate" at the time of the ownership change. *See* IRC § 382(b). When a corporation experiences successive ownership changes, special rules apply that can restrict NOLs even more. *See* Treasury Regulations § 1.382-5(a)(d).

Bright-line rule "ownership changes" of Citigroup did occur under the Section

382 test because of purchases and sales by Treasury combined with a large issuance of new shares to the general public. The motion to dismiss does not argue to the contrary. What it does seem to argue is that Treasury was allowed to make an exception to the usual definition of "ownership change." *See* Citigroup's Brf. § 3(A).

In New York, the state imposes a franchise tax on banking corporations based on their net income. *See* N.Y. Tax Law §§ 1451, 1455. Unless the alternative minimum tax applies, the tax is calculated as 7 1/10% of entire net income or the portion thereof allocated to New York State. *Id*. at 1455. Like federal law, New York allows NOL deductions, and the New York NOL is the same as under section 172 of the IRC, with certain modifications. *See* N.Y. Tax Law § 1453(k-1). The franchise tax incorporates the NOL deduction under section 172 of the IRC, and thus also incorporates the NOL limitation on carryovers in Section 382.

1. The TARP Program and Citigroup.

On October 3rd, 2008, President Bush signed into law P.L. 110-343, the Emergency Economic Stabilization Act of 2008 ("EESA"). A response to the financial crisis, EESA gave Treasury authority to take steps to restore liquidity to the financial system. One program established by EESA, the Troubled Asset Relief Program ("TARP"), allowed Treasury to pursue this goal by purchasing equitable interests in publicly traded companies. In exercising this authority, EESA required that Treasury prevent the unjust enrichment of financial institutions, and generally required Treasury to maximize overall returns to taxpayers. *See* Compl. ¶ 19; EESA §§ 2(2)(C), 101(e), 113(b).

Upon passage of EESA, Treasury invested about $125 billion in the country's eight largest banks in return for preferred stock (which does not vote and does not trigger ownership changes, unlike common stock). Citigroup received $25 billion of this amount. Treasury invested an additional $20 billion in Citigroup in December 2008.

Citigroup, however, was unable to pass its stress test. To help, Treasury's $25 billion worth of Citigroup preferred stock was converted to common stock, and in December 2009, Citigroup made a large issue of new shares to the general public. These two transactions together constitute the *first* "ownership change" under Section 382's computation, since over 50% of ownership changed over a short period. In April 2010, Treasury began to sell its Citigroup common stock, and by December, it no longer owned any. Compl. ¶ 28. Treasury's stock sale, together with the earlier public issue, constitute a *second* "ownership change" because of their combined effect over a sufficiently short period. *Id.* ¶ 29.

2. The IRS Notices.

Treasury also aided Citigroup by issuing special "revenue notices" that granted waivers of corporate income tax under the guise of interpreting EESA and Section 382. In October 2008, Citigroup, with the support of the Treasury, made an offer to buy Wachovia, another troubled bank. Wachovia held valuable NOLs that would be forfeited by the ownership change. The IRS issued Revenue Notice 2008-83, 2008-42 I.R.B. 905, which interpreted Section 382 and EESA as authorizing preferential tax treatment for banks that underwent a Section 382 ownership change. *Id.* ¶ 23. In the end, Wells Fargo outbid Citigroup and acquired Wachovia without government assistance (except for Notice 2008-83), so this is commonly called "the Wells-Fargo Notice."

Congress disagreed strongly with Notice 2008-83, and repudiated it in the American Recovery and Reinvestment Act of 2009 ("ARRA"), P.L. No. 115-5. Section 1261(a)(1) says bluntly that the "delegation of authority to the Secretary of the Treasury under Section 382(m) of the Internal Revenue Code of 1986 does not authorize the Secretary to provide exemptions or special rules that are restricted to particular industries or classes of taxpayers."

Similar notices, "the IRS Notices," are at the heart of this action. On April 13, 2009, the IRS issued Revenue Notice 2009-38, 2009-18 I.R.B. 901. This Notice stated that no "ownership change" would be triggered by Treasury's purchases of stock. Thus, when Treasury bought Citigroup stock, that would not count towards an "ownership change," allowing the company to carry over its NOLs.

Revenue Notice 2010-2, 2010-2 I.R.B. 251 was issued December 11, 2009, at the same time as Citigroup's new stock issue to the public. This notice, although it superseded Revenue Notice 2009-38, reiterated Treasury's favorable treatment under IRC Section 382. It also extended that treatment to Treasury's *sale* of shares, which also would not count as an "ownership change" under the Notice. These Notices raised the price the public was willing to pay for the new Citigroup stock because the company, by carrying over its NOLs, would be effectively exempt from federal income tax for some years. A significant motivation for these private persons to buy Citigroup stock was to get the tax benefit, just what Section 382 is written to prevent. Naturally, this helped Citigroup's recovery, which was the goal of Treasury both as policymaker and shareholder.

Treasury realized $6.85 billion in profit from buying the stock in 2009 and selling

it in 2010. *Id.* ¶ 30. However, the federal government as a whole will lose significantly more despite this paper gain because of the loss in tax revenue from the illegal NOL deductions. New York State held no Citigroup stock and gained nothing from non-application of Section 382. New York State did lose tax revenue — an estimated $800 million. New York State was not consulted in the issuance of the IRS Notices.

D. Citigroup Violated New York Tax Law.

This NYFCA case is based on the fact that the IRS Notices are irrelevant to Citigroup's New York Department of Revenue tax returns. The Notices were not approved by Congress; they are contrary to the language and purpose of Section 382; they defy ARRA's prohibition on preferential treatment of classes of taxpayers; they conflict with the requirements of EESA; and they constitute arbitrary and capricious action by the IRS. *Id.* ¶ 32. Because the Notices were improperly promulgated, they are irrelevant for New York tax. *Id.* ¶ 33. The Notices were not incorporated into New York State tax law, and Citigroup could not rely on them to reduce its New York State tax liability. *Id.* ¶ 34. Nevertheless, Citigroup did just that. *Id.* ¶ 35.

Thus, as alleged in the complaint, between 2010 and 2012, Citigroup knowingly made, used, or caused to be made, or used false records or statements material to an obligation to pay money to the State. *Id.* ¶ 36. Citigroup knowingly prepared false New York State tax returns with excessive NOL deductions to avoid the payment of state franchise tax. *Id.* ¶ 37. As a result, New York State did not receive approximately $800 million in tax revenues to which it was entitled. *Id.* ¶ 38. The complaint concludes that, as a result of Citigroup's knowingly fraudulent conduct, Citigroup is liable to the State for taxes owed to the State, trebled, plus

penalties, interest, and attorneys' fees under NYFCA. *Id.* ¶ 39.

ARGUMENT

I. CITIGROUP VIOLATED NEW YORK STATE TAX LAW BY APPLYING NOLS ON ITS NEW YORK STATE TAX RETURNS

The IRS Notices directly contravene the Internal Revenue Code. Moreover, although the IRS improperly decided not to enforce Section 382 of the Internal Revenue Code, New York State made no such decision. Further, it is black letter law that New York will disregard a federal administrative edict that directly contradicts a federal statute. Thus, the Notices are entitled to no effect with regard to Citigroup's New York State tax obligations, meaning the company violated New York law.

A. New York Law Does Not Incorporate Bogus IRS Notices.

For several reasons set forth below, the IRS Notices form no part of New York tax law — nor could they.

1. The Notices Conflict with IRC Section 382 and the Treasury Regulations.

New York law incorporates IRC Section 382's limitation on use of NOLs after an "ownership change." N.Y. Tax Law § 1453. Citigroup experienced "ownership changes" in 2009 and 2010.

New York tax law *does not* incorporate the IRS *Notices*. For federal tax purposes, the Notices eviscerate IRC Section 382 with regard to Citigroup's "ownership changes." They do this by fiat, without a reasoned explanation, declaring that "[f]or purposes of section 382, with respect to any stock . . . acquired by Treasury . . . the ownership represented by such stock . . .

shall not be considered to have caused Treasury's ownership in the issuing corporation to have increased." *See* Revenue Notice 2009-38, III D; Revenue Notice 2010-2, III D and E. Although it was nonsensical for the IRS to declare that buying shares does not lead to increased ownership, no one other than Treasury or Citigroup has standing to challenge this as a matter of federal tax liability. *See, e.g.*, *Simon v. E. Ky. Welfare Rights Org.*, 426 U.S. 26, 96 S. Ct. 1917 (1976) (dismissing for lack of standing a challenge to IRS revenue ruling giving preferable tax treatment to third parties); *Allen v. Wright*, 468 U.S. 737, 104 S. Ct. 3315 (1984) (dismissing for lack of standing a challenge to IRS guidelines granting tax-exempt status to third parties). Thus, Treasury did not anticipate having to defend the Notices in court. [3]

When New York law references provisions of the Internal Revenue Code into its own law, as with the incorporation of IRC Section 382 into N.Y. Tax Law § 1453, New York law does look to federal authority to help interpret these provisions. *See Matter of Marx v. Bragalini*, 6 N.Y.2d 322, 189 N.Y.S.2d 846 (1959); *Matter of Dreyfus Special Income Fund v. New York State Tax Comm.,* 126 A.D.2d 368, 371-2, 514 N.Y.S.2d 130, 133-4 (3d. Dep't 1987). However, it is black letter law that New York ***will disregard*** a federal administrative interpretation that directly contradicts a federal statute. *See Bosh v. Fahey*, 53 N.Y.2d 896, 440 N.Y.S.2d 626 (1981); *see also Kurcsics v. Merchants Mut. Ins. Co.*, 49 N.Y.2d 451, 459, 426 N.Y.S.2d 454, 458 (1980) (no weight to agency regulation that contradicts statute).

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[3] In 2010, the TARP's Office of Special Inspector General ("SIGTARP") did commence an evaluation into multiple aspects of Notice 2010-2 as it relates to Citigroup. *See* Engagement Memo – Review of the Section 382 Limitation Waiver for Financial Instruments Held by Treasury, Aug. 10, 2010, attached hereto as "Exhibit A." That evaluation remains open.

In *Bosh*, the New York Court of Appeals upheld the state agency's refusal to rely upon an "Action Transmittal — Interpretation" issued by the federal Department of Health and Welfare. *See Bosh*, 53 N.Y.2d 896. The case involved the Social Security Act, which requires state agencies to administer benefits in accordance with federal law. The Court determined that the federal statute was clear that state agencies must take into consideration any income or resource of eligible family members in determining a family's need, and thus, *rejected* the federal agency's directive to disregard certain benefits received by family members. The Court noted that "[w]e cannot . . . agree with petitioner's contentions that the 'scheme of cooperative federalism' implicit in the public assistance system requires States to adhere blindly to all Federal directives, no matter how irrational or inconsistent with applicable Federal law." *Id.*, 53 N.Y.2d at 900.

In *Bosh*, the New York Court of Appeals also determined that its conclusion applied to agency regulations, not just less formal pronouncements — the touchstone being whether they run counter to a clear federal statute. *Id.* at 898 n.1. Agency deference has no place in the face of clear statutory law to the contrary. *See Belmonte v. Snashall*, 2 N.Y.3d 560, 565-66, 780 N.Y.S.2d 541, 543-44 (2004) (no deference if question is merely one of statutory interpretation for the courts).

Bosh applies here because the IRS Notices directly contradict the applicable *federal statute*, which New York law incorporates. The federal statute and Treasury Regulations unambiguously require Citigroup to compute 5% shareholders' ownership percentage increases. *See* IRC § 382(g)(1); Treasury Regulations § 1.382-2T(c)(1). But Revenue Notice 2009-38 and Revenue Notice 2010-2 declare that the purchases and sales by Treasury *do not* cause increases

in ownership percentages. *The Notices either change the laws of arithmetic or directly contradict the statute and regulations.*

Because the laws of arithmetic are immutable, the Notices are in direct conflict with the statute and regulations. Therefore, they cannot stand in New York. As the Supreme Court has held, "Congress, not the (IRS) Commissioner, prescribes the tax laws . . . ." *Dixon v. United States*, 381 U.S. 68, 73, 85 S. Ct. 1301, 1304 (1965) (treasury rulings have no power to alter a statute enacted by Congress); *see also Samonds v. Commissioner*, No. 3954-91, T.C. Memo 1993-329 (Tax Ct. 1993) (rejecting an IRS notice because it was inconsistent with the Internal Revenue Code).

The Notices contradict an unambiguous statute — IRC Section 382. New York law, which incorporates the statute, therefore gives no effect to the Notices. In New York, Citigroup's NOLs are subject to statutory limitation after the "ownership changes" it experienced in 2008 and 2010. For this reason — and for the additional reasons explained below — Citigroup's New York tax position is plain wrong.

2. The Notices Defy ARRA's Prohibition On Preferential Treatment Of Classes Of Taxpayers.

The Notices also violate ARRA. Revenue Notice 2008-83 was issued by the IRS on October 1, 2008. It provided preferential treatment under IRC § 382 for banks that had experienced an "ownership change." In 2009, after considerable outcry, Congress repealed Revenue Notice 2008-83 with its enactment of ARRA. In repealing Revenue Notice 2008-83, Congress reviewed this broad delegation of authority to the IRS. It found that IRC Section 382(m) did *not* authorize the IRS to provide exemptions from the statute or special rules that are

restricted to particular industries or classes of taxpayers. In ARRA, Congress provided that Revenue Notice 2008-83 was inconsistent with its intent in enacting IRC Section 382(m). The American Recovery and Reinvestment Act of 2009, P.L. 111-5, 2/17/09, § 1261.

The Notices at issue here are similar to Revenue Notice 2008-83. They purport to trump the statute — IRC Section 382 — only for corporations whose stock has been purchased by Treasury under TARP (*i.e.*, companies "bailed out" by the federal government). *See* Revenue Notice 2009-38, III D; Revenue Notice 2010-2, III D and E.

The legislative repeal of Revenue Notice 2008-83 is dispositive federal authority prohibiting any revenue notice from bestowing preferential tax treatment on classes of taxpayers under IRC Section 382. The Notices relied on by Citigroup bestow "bailed out" corporations with favorable tax treatment.

New York law does not accord any weight to these Notices because the preferential treatment they provide to "bailed out" taxpayers is prohibited by ARRA. Therefore, Citigroup's NOLs *are* subject to limitation in New York.

3. The Notices Run Contrary To Several EESA Provisions.

The Notices also conflict with several provisions of the EESA. Section 101(e) of EESA requires Treasury, in making purchases under EESA, to "take such steps as may be necessary to prevent unjust enrichments of financial institutions participating in a program established [under TARP]." The Notices purport to trump IRC Section 382's restrictions on use of Citigroup's NOLs after the "ownership changes." The use of these NOLs, unrestricted and contrary to federal law, is manifestly unjust enrichment because it increases Citigroup's after-tax

income at the expense of other taxpayers.

Indeed, the Office of the Special Inspector General for TARP, at the request of then-U.S. Representative Dennis Kucinich, launched an ongoing inquiry into Revenue Notice 2010-2. The Inspector General is investigating what he terms the "waiver" of IRC Section 382 for Citigroup and similarly situated institutions. *See* Exhibit A.

More generally, EESA §§ 2(2)(C), 103(1) and 113(a)(1) require Treasury, in exercising its authority under EESA, to maximize overall returns to the U.S. taxpayers, to minimize the impact on the national debt, and to minimize any potential long-term negative impact on taxpayers. The Notices run afoul of all of these EESA requirements. Although Treasury's sale of Citigroup stock produced a profit, some of which is attributable to the Notices, ultimately Treasury has lost or will lose tax revenue because the Notices "waived" Section 382.

Shareholders who purchased Treasury's Citigroup common stock in 2010 paid more for that stock than they would have if Section 382 had been applied. With unrestricted use of its NOLs, Citigroup's taxes fell, leaving its profits available for dividends or reinvestment. Presumably the shareholders who bought Treasury's stock paid a premium for unrestricted use of the NOLs roughly equal to the present value of the tax on Treasury's share of Citigroup's NOLs.

The cost to the U.S. taxpayers of Citigroup's emancipation from the constraints of IRC, however, will be greater than the short term profits realized in 2010 when Treasury sold its Citigroup stock. Because the IRS, through its Notices, opted not to enforce Section 382 and to apply it to Citigroup after the "ownership changes," Treasury lost or will lose tax revenue. This lost revenue presumably will equal roughly the present value of the tax on *all* of Citigroup's

NOLs. Treasury's loss, by virtue of the Notices' evisceration of Section 382, exceeds the incremental gains realized on sale in 2010 in present value terms. The Notices cost the Treasury a significant amount of tax revenue and, thus, run afoul of several sections of EESA.

In sum, New York law is prohibited from implementing the Notices because they fly in the face of IRC Section 382 and ARRA. *See Bosh*, 53 N.Y. 2d 896. The Notices also are contrary to EESA. Thus, again, Citigroup's use of its NOLs is subject to limitation in New York.

4. Even Under Federal Standards of Deference to Agency Determinations, the Notices Would Receive No Deference.

a. Notices Are Not Afforded The Same Deference As Regulations And, Regardless, Fail The U.S. Supreme Court's Tests For Agency Action.

IRS notices are *not* regulations. They are equivalent to mere "press releases" and, as such, are not authoritative and are entitled to *no deference*. *See Stobie Creek Invests., LLC v. United States*, 82 Fed. Cl. 636, 671 (Ct. Claims 2008), *aff'd*, 608 F.3d 1366 (Fed. Cir. 2010).

Even if the Notices were more than official statements (which they are not), and had gone through the Administrative Procedure Act's stringent process of notice and comment (which they did not), they would still deserve no deference. They do not stand up to scrutiny under the *Chevron* test. *See Chevron U.S.A. Inc. v. Natural Resources Defense Council Inc.*, 467 U.S. 837, 104 S. Ct. 2778 (1984). *Chevron* provides a two-step test to determine the level of deference to be accorded an administrative agency's interpretation of a statute when it makes a regulation to implement it. To be clear, *Chevron* applies to Treasury regulations (*Mayo Found. for Med. Educ. & Research v. U.S.*, 562 U.S. 44, 131 S. Ct. 704 (2011)), not mere revenue

notices, but it is useful as a preliminary screen. If the Notices cannot pass the *Chevron* test, they cannot pass more stringent tests.

As a threshold matter, the *Chevron* test applies only where it appears that Congress has delegated to the agency authority to make rules carrying the force of law and the ruling was promulgated in the agency's exercise of that authority. *See United States v. Mead Corp.*, 533 U.S. 218, 121 S. Ct. 2164 (2001). The U.S. Supreme Court applies a "persuasiveness" standard for other agency rulings. *Id.* This higher standard determines the deference due rulings such as the Notices by analyzing their ability to persuade the court that their interpretation of the statute is correct. *Id.* at 234-35 (*citing Skidmore v. Swift & Co.*, 323 U.S. 134, 65 S. Ct. 161 (1944)).

Here, the Notices fail to meet the Supreme Court's threshold "persuasiveness" standard. They provide, contrary to Section 382 and the rules of arithmetic, that purchases and sales by Treasury do not increase the buyer's percentage ownership interest in Citigroup. They contradict the statute they purport to interpret and make no effort to persuade. The Notices, therefore, fail the "persuasiveness" standard.

But even if the Notices were to clear this persuasiveness test (which they do not), they still fail to survive either part of the *Chevron* test. Step one of the *Chevron* test asks whether Congress has directly spoken to the precise question at issue. *Chevron*, 467 U.S. 843. The analysis begins with the words Congress has used to draft the statute "because if [the statute's] language is unambiguous, no further inquiry is necessary." *N.Y. ex rel. N.Y. State Office of Children & Family Servs. v. U.S. Dep't of Health & Human Servs. Admin. for Children*

& Families, 556 F.3d 90 (2d Cir. 2009). Thus, if the statute contains no ambiguous language, that is the end of the inquiry. The Court and the IRS "must give effect to the unambiguously expressed intent of Congress" and the agency cannot insert its own interpretation. *Chevron*, 467 U.S. 843.

Conversely, if the language of the statute is ambiguous, then analysis under step two of the *Chevron* test must occur. In these situations, the Court determines whether the agency's interpretation is based on a permissible construction of the statute. *Id*. When a statute explicitly leaves a gap for an agency to fill by regulation, such regulations are given controlling weight. *Id*. However, if a proposed regulation is "arbitrary, capricious, or manifestly contrary to the statute," a court cannot defer to the regulation. *Id*.

First, the Notices do not survive part one of the *Chevron* test. Both the IRC (Section 382(g)(1)) and the Treasury Regulations (Section 1.382-2T(c)(1)) require Citigroup to calculate the increases in its "5% shareholders' " percentage ownership. A 5% shareholder is a shareholder of the company who owns at least 5% of its shares. *See* Section 382 (k)(7). And Treasury purchased in excess of 5% of Citigroup. The language of the statute is unambiguous. The Notices contradict this language, stating that when Treasury buys and sells, there is no ownership change. But someone owned those shares, and that someone was the U.S. Government. There is no exception in Section 382 for federal, state, or foreign governments, nor for trusts, non-profits, especially deserving people, or anyone else. A shareholder is a shareholder. As such, the IRS cannot create its own statutory exceptions by fiat, in direct contravention of a statute's plain language. But that is precisely what the IRS did here. Thus, the Notices are of no merit under the first part of the *Chevron* test.

Because the statute is unambiguous, there is no need to proceed to step two of *Chevron*. The Court and the IRS "must give effect to the unambiguously expressed intent of Congress." *Chevron*, 467 U.S. at 843.

Nevertheless, even assuming that the Court reads the statute to be ambiguous, Treasury's interpretation still fails under step two of the *Chevron* test. Here, Treasury's interpretation and subsequent regulation is arbitrary and capricious because it is unsupported by any argument. Further, it is contrary to the purpose of the statute, which was to provide a bright-line rule for loss trafficking. The intent of Section 382 is precisely to eliminate the need to ask whether loss trafficking is the motive of a sale of stock by creating a bright-line, numerical test. If a non-profit entity had acquired Citigroup, it would not have escaped Section 382 even though it pays no income tax and could not possibly have loss trafficking as a motive.

Indeed, it is common for corporate acquisitions to occur and be subject to Section 382 even though loss trafficking cannot be the motive — because any loss trafficking is prevented by Section 382 itself. Ironically enough, however, the tax consequences of acquiring Citigroup shares were very likely high on the list of the concerns of both Treasury and the buyers of the new shares issued when they decided to buy the stock. Treasury was buying to resell, and it would be politically embarrassing to sell at a loss. By waiving Section 382, Treasury raised Citigroup's value — and the value of its stock — by billions of dollars.

The Notices are contrary to the unambiguous language of the statute; they run contrary to the purpose of the statute; and they are unreasoned, making their adoption arbitrary and capricious in violation of the second part of the *Chevron* test. For Citigroup, that means the

Notices are null and void and, thus, will be accorded no weight at all in New York. The Notices purport to defeat IRC Section 382 on an issue that the statute directly addresses. They fail the "persuasiveness" test that applies to these type of agency rulings. They also fail both steps of the deferential *Chevron* test. New York cannot defer to the Notices, and Citigroup cannot utilize its NOLs on its New York State taxes.

b. The Notices Are Arbitrary And Capricious Under The Administrative Procedure Act.

The Notices violate the Administrative Procedures Act (the "APA"), P. L. No. 79–404, the provisions of which apply to IRS revenue notices. *See Cohen v. United States*, 650 F.3d 717, 723, 736 (D.C. Cir. 2011). Much like step two of the *Chevron* test, Section 706 of the APA provides, in part, that a reviewing court shall hold unlawful and set aside agency actions found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[4] *See* 5 U.S.C. § 706(2)(A).

In *Motor Vehicle Mfrs. Ass'n. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 103 S. Ct. 2856 (1983), the Supreme Court reviewed an action by the National Highway Traffic Safety Administration (the "NHTSA"). In applying the APA's "arbitrary or capricious" standard to the NHTSA's action, the Court emphasized previous Supreme Court rulings regarding this standard. "We have frequently reiterated that an agency must cogently explain why it has exercised its discretion in a given manner . . . and we reaffirm this principle again today." *Id.* at

[4] The Supreme Court has confirmed that the APA's "arbitrary or capricious" standard involves the same analysis as step two of the Supreme Court's *Chevron* standard (in which the court reviews whether an agency ruling is a permissible construction of the statute). *See Judulang v. Holder*, 132 S. Ct. 476, 484 n.7 (2011).

48-49, 2869 (citations omitted). The Court determined that the action was arbitrary and capricious and therefore invalid because the NHTSA failed to articulate a satisfactory explanation for its action.[5] *Id.* at 34, 2862.

Here, the Notices offer no explanation, cogent or otherwise, of their evisceration of IRC Section 382 for the benefit of "bailed out" taxpayers like Citigroup. The Notices did not go through a notice-and-comment period, and they do not argue for their position. The closest thing to a legal argument in Notice 2009-14, for example, is: "Section 382(m) of the Code provides that the Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of sections 382 and 383. Section 101(c)(5) of EESA provides that the Secretary is authorized to issue such regulations and other guidance as may be necessary or appropriate to carry out the purposes of EESA." An agency's "necessary and appropriate" powers do not extend to replacing the courts and Congress in interpreting and amending statutes.

Thus, because their lack of reasoned argument fails to meet the minimum requirements of APA Section 760(2)(A), the Notices are arbitrary and capricious and New York law does not respect them.

Treasury's interpretation of Section 382 also runs contrary to Congress's intent to replace a subjective standard with a bright-line rule for loss trafficking. Section 382's intent is precisely to eliminate the need to ask whether loss trafficking is the motive. If a non-profit entity

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[5] *See also Dominion Resources, Inc. v. U.S.*, 681 F.3d 1313 (Fed. Cir. 2012). In that case, the court struck down former Treasury Regulation Section 1.263A-11(e)(1)(ii)(B). The Federal Circuit based its decision, in part, on APA Section 706(2). It held that the regulation was arbitrary and capricious because Treasury failed to articulate a satisfactory or cogent explanation.

had acquired Citigroup, it would not escape Section 382 even though it pays no income tax and could not have loss trafficking as a motive.

5. If, Somehow, New York Determined That The Notices Were Effective For Federal Tax Purposes, It Would Still Give Them No Weight For New York Tax Purposes Because Of Their Disparate Effect On New York's Treasury.

Even if federal law were to deem the Notices valid for federal purposes, that would still not give effect to them for New York tax purposes. The Notices allow Citigroup to realize substantial benefits from its NOLs, despite "ownership changes" under Section 382. This has already cost New York several hundred million dollars in tax revenue (and may cost an additional $1.3 billion), and it jeopardizes New York's interest in preserving its fiscal health.

Where federal authority economically favors Treasury, but hurts the New York fisc, New York does not follow this federal authority. In *Isabella Geriatric Cent., Inc. v. Novello*, 2005 WL 3816962, at *6 (Sup. Ct., New York County. Dec. 9, 2005), *aff'd*, 38 A.D.3d 356, 833 N.Y.S.2d 5 (1st Dep't 2007), the court rejected petitioners' reliance on a 2004 letter from the United States Department of Health and Human Services. The letter provided that the New York Department of Health was under-reimbursing nursing homes. However, the court held that the federal government's "report is of no moment because [NY]DOH is not statutorily obligated to rely on HHS's suggestions regarding state reimbursement procedures. Indeed, the federal government has its own interest in having DOH pay more to nursing homes: it shares the financial responsibility of reimbursing nursing homes with DOH." *Id.*

Here, like the HHS reimbursement suggestions in *Isabella Geriatric Cent.*, the Notices allowed Treasury to realize immediate economic gain from its sale of its Citigroup

common shares. New York, on the other hand, had no Citigroup stock to sell. If New York recognized the Notices, it would not share the benefits reaped by Treasury *and* it would suffer lost tax revenue. Consequently, New York law gives no weight to the Notices.

Even if New York determined the Notices were valid for federal purposes, it would not respect them for New York tax purposes because of the significantly different economic effect on the two governments. New York does not defer to the Notices.

II. THE COMPLAINT PROPERLY ALLEGES SCIENTER

A. The Law Rejects Citigroup's Position.

Citigroup gave itself a free pass in New York in derogation of federal and state statutes. The Internal Revenue Code does not allow Citigroup's NOL deductions, and Citigroup does not even argue for the merits of the Notices, just for their authority as IRS pronouncements. Citigroup stuck its head in the sand and now asks this Court to bless that reckless strategy.

As a matter of New York law, Citigroup's NOLs are not allowed. *See* Point I, *supra*. Citigroup and its advisors should have known this — or did know this. Under these circumstances, and given Citigroup's sophistication, its decision to deduct the NOLs in its New York tax returns evidences at least recklessness or deliberate ignorance. Billions of dollars were at stake and, as Citigroup's brief says, there were numerous claims in the media that the federal NOLs were improper despite the IRS Notices. *See* Citigroup's Brf. § II(A). Citigroup's advisors should have understood the weaknesses of the Notices as well as — or better than — Professor Rasmusen. Moreover, it is inconceivable that Citigroup's army of tax lawyers and advisors did

not flag this issue, yet it seems Citigroup proceeded without getting pre-clearance with the New York State Department of Taxation and Finance through an Advisory Opinion.

Citigroup argues for a free pass in this New York False Claims Act case, claiming that there is uncertainty in the law and, as such, Citigroup did not have the knowledge required for a NYFCA violation. Citigroup is wrong again. The NYFCA's "knowledge" requirement is met by any one of three things: (a) actual knowledge, (b) deliberate ignorance, or (c) reckless disregard. *See* N.Y. State Fin. Law § 188(3)(a). Moreover, "no proof of specific intent to defraud" is required. *See id.* § 188(3)(b).

The "reasonableness" of a legal interpretation *can* be relevant to whether a False Claims Act defendant acted knowingly. *See United States ex rel. Oliver v. Parsons Co.*, 195 F.3d 457, 464 (9th Cir. 1999) ("A contractor relying on a good faith interpretation of a regulation is not subject to liability, not because his or her interpretation was correct or 'reasonable' but because the good faith nature of his or her action forecloses the possibility that the scienter requirement is met").

But a reasonableness claim is *not dispositive*, and certainly not on a motion to dismiss. If it were, a False Claims Act defendant would be permitted to submit a false claim or false tax return, knowing it was false, and avoid liability by claiming that its false return was based upon a "reasonable interpretation" of the law.

That is not the law. *See id.* at 463 n.3, 464 (denying defendant summary judgment where defendant relied on its "reasonable interpretation" of the applicable regulations, but relator's evidence showed that defendants acted purposely to defraud the government); *see*

also Minnesota Assoc. of Nurse Anesthetists v. Allina Health Sys. Corp., 276 F.3d 1032, 2053 (8th Cir. 2002) (reversing summary judgment to defendants who had argued that regulations were "susceptible" to their interpretation; relator's evidence showed that defendants certified compliance with regulation while knowing that the agency interpreted the regulation differently).

Indeed, in *United States ex rel. K & R Ltd. Partnership v. Massachusetts Housing Fin. Agency*, 530 F.3d 980, 983 (D.C. Cir. 2008), the court expressly noted that the reasonableness of a defendant's interpretation is "merely evidence, the absence of which does not preclude a finding of knowledge" (citation omitted); *see also United States v. Kellogg Brown & Root Servs*., No. 4:12-cv-4110-SLD, 2014 U.S. Dist. Lexis 43000, at *23-*28 (C.D. Ill., March 31, 2014) (rejecting a "reasonable interpretation" argument on a motion to dismiss and distinguishing summary judgment cases; an objectively reasonable interpretation may be knowingly false); *United States ex rel. Chilcott v. KBR, Inc.*, No. 09-cv-4018, 2013 U.S. Dist. Lexis 153331, at *21-*28 (C.D. Ill., Oct. 24, 2013) (same and, on a motion to dismiss, drawing the reasonable inference that the relator's interpretation was the correct one). Simply put, "[c]ontractors should not be permitted to escape liability for knowingly choosing [what may be] a 'reasonable,' but incorrect, interpretation of a contract or regulation." *See Chilcott*, 2013 U.S. Dist. Lexis 153331, at *31 (emphasis in original).

United States v. Newport News Shipbuilding, Inc., 276 F. Supp. 2d 539, 560-66 (E.D. Va. 2003), is similar. There, the court rejected a summary judgment argument that ambiguity in the regulation rendered it impossible for the defendant to have knowingly submitted false claims. Even though the regulation was subject to "agency and industry dispute and doubt," the plain language and legislative history of the regulation suggested that the defendant's

interpretation was incorrect. With respect to the Government's argument that the defendant acted recklessly by charging costs based on a "tenuous interpretation" of the regulation without disclosing its interpretation, the court noted that "both the clarity of the regulation and the reasonableness of a contractor's interpretation are relevant in deciding whether a failure to disclose charging practices is indicative of a reckless disregard of their falsity." *Id.*

Citigroup's New York State tax position is objectively *unreasonable*. Further, in this case, the issue of Citigroup's scienter is simply not one that can be adjudicated on a motion to dismiss as a matter of settled FCA law. *See generally United States ex rel. Cantekin v. University of Pittsburgh*, 192 F.3d 402, 411 (3d Cir. 1999) (citation omitted) ("we must heed the basic rule that a defendant's state of mind typically should not be decided on summary judgment") (superseded by statute on other grounds).

Rather, Citigroup's intent should be explored in discovery. At this juncture, it is sufficient that the amended complaint states a *prima facie* case that Citigroup's actions were false and fraudulent: Citigroup filed its returns knowingly relying on bogus IRS Notices that fly in the face of the federal tax code. Regardless of its federal tax obligations, Citigroup knew that, if the matter reached a New York court, it could not rely on the Notices. Indeed, a dispositive motion based upon a defendant's supposed lack of scienter is disfavored if interpretation issues are involved. *See, e.g.*, *United States ex rel. Feldman v. Van Gorp*, 674 F. Supp. 2d 475, 481 (S.D.N.Y. 2009) (denying summary judgment).

B. <u>The Second Circuit's Policy of Leniency on Scienter Issues Governs Here.</u>

Scienter may be alleged generally. *See Gold v. Morrison-Knudsen Co.*, 68 F.3d

1475, 1477 (2d Cir. 1995); N.Y. State Fin. Law § 188(3)(b) (liability requires no specific intent to defraud).

Indeed, the Second Circuit's stated policy of "leniency" on scienter issues at pre-trial stages such as on a Rule 12(b)(6) motion should be *dispositive* here. *See, e.g., Meijer, Inc. v. Ferring B.V.*, 585 F.3d 677, 693 (2d Cir. 2009) ("We are, however, 'lenient in allowing scienter issues to withstand summary judgment based on fairly tenuous inferences,' because such issues are 'appropriate for resolution by the trier of fact'") (citations omitted). Thus, "Rule 9(b) requires only the *circumstances* of fraud to be stated with particularity; knowledge itself can be alleged generally." *Id.* at 695 (emphasis in original).

Citigroup's *intent* should be explored in discovery. Scienter is premature under the Second Circuit's lenient approach.

C. Citigroup's *Sprint* Decision Proves the Point that Dismissal for Lack of Scienter is Premature.

Citigroup's citation to *People v. Sprint Nextel Corp.*, 25 N.Y.3d 1217, 16 N.Y.S.3d 511 (2015), is curious. In that case, Sprint moved to dismiss under CPLR 3211 (the Rule 12(b)(6) analog), arguing that it held a reasonable interpretation of a disputed tax law provision, so there could be no "knowing" violation, *i.e.*, no scienter. *Id.* at *13-14. The Court of Appeals *rejected* this argument, stating, "[t]his is not the stuff that a CPLR 3211 dismissal is made of." *Id.* at *14. Rather, the Court determined that Sprint would have to substantiate, in further proceedings — after discovery — that it actually held such a reasonable belief and actually relied on it. *Id.* Denying the motion to dismiss, the Court of Appeals concluded that dismissal was premature, and that the state was entitled to discovery and the benefit of every possible inference at this juncture. *Id.* at *16.

Discovery into Citigroup's decision-making will shed significant light on the issue of scienter. As in *Sprint*, discovery should proceed.

III. CITIGROUP'S NEW YORK TAX DODGE WAS NOT "PUBLICLY DISCLOSED"

The NYFCA requires the Court to dismiss an action "if substantially the same allegations or transactions as alleged in the action were publicly disclosed" in public hearings to which the government is a party, in "a federal, New York state, or New York local government report, audit, or investigation" or in "the news media." N.Y. State Fin. Law § 190(9)(b).

The purpose of the NYFCA is to incentivize actions against tax fraud that would not be brought by the Attorney General without it. NYFCA does this by rewarding private parties who alert the Attorney General to fraud, and who, if the Attorney General declines to join the suit, act as relators and bring the action themselves at their own risk. This purpose would not be furthered by the filing of fraud allegations that the Attorney General already knew about or was investigating. Thus, the statute seeks to bar actions brought on the basis of information likely to be known to the Attorney General.

Citigroup argues that the facts underlying this NYFCA case were publicly disclosed in a Congressional report, SEC filings, and scholarly publications. This claim ignores a critical distinction. The public allegations that Citigroup evaded its *federal* tax obligations *did not* encompass Citigroup's *New York* tax dodging. That dodge can be discovered only by careful reading of the footnotes in Citigroup's annual report and 10-Ks for the relevant years.

Further, unlike the federal False Claims Act, the NYFCA — and the whistleblower-friendly policy behind it — bars dismissal based on one of the types of public disclosure — federal government reports — alleged by Citigroup.

A. Any Public Disclosures Pertained To Citigroup's Federal Taxes, Not Its New York State Taxes.

While the IRS Notices and Citigroup's NOLs in its federal tax returns were publicly discussed in 2009 and 2010, the possibility of New York State tax fraud was not. The allegations in this NYFCA case are not "substantially the same" as the allegations of federal tax fraud that were made. *See* N.Y. State Fin. Law § 190(9)(b). Cheating on your federal tax returns is not substantially the same act as cheating on your state tax returns. It is a separate allegation. Maybe this point is lost on Citigroup because it conflates the federal and state governments. *See* Citigroup's Brf., at 27-28.

Any public disclosure of allegations concerning Citigroup's federal taxes does not address New York franchise taxes, does not imply that Citigroup filed its New York tax returns claiming New York NOLs, and is not "substantially the same" as this NYFCA action.

Instructive cases include *United States ex rel. Aflatooni v. Kitsap Physicians Servs.*, 163 F.3d 516, 522-23 (9th Cir. 1998), where the Ninth Circuit Court of Appeals reversed that part of the District Court's dismissal on public disclosure grounds because the public disclosure about one group of defendants did not address a separate group of defendants. Here, there is even more reason to reject this defense, namely, that there are two distinct governments at issue — the federal government, which might be concerned with the federal disclosures, and

the State government, which is not concerned with Citigroup's federal tax strategy and its special relationships with the IRS.

In *United States ex. rel. Springfield Term. Ry. v. Quinn*, 14 F.3d 645, 653-55 (D.C. Cir. 1994), the District of Columbia Circuit Court of Appeals vacated a District Court dismissal on public disclosure grounds because only some — but not all — relevant detail had been publicly disclosed. The D.C. Circuit provided an illustration that applies equally here: if X + Y = Z, where Z is the allegation of fraud and X and Y are its essential elements, a public disclosure must involve either Z (*i.e.*, the entire allegation of fraud) or both X and Y, the essential elements from which Z can be inferred. *Id.* at 654. If only one element exists in one of the barred information sources (*e.g.*, X), then the relator's case may proceed by alleging Y or Z. *Id.* at 655. That is the case here, where Citigroup's *New York* filing (Y) and *New York* tax fraud (Z) were not revealed in public and, instead, *only* its federal filing per the notices (X) was revealed.

Desperate to avoid a determination on the merits, Citigroup reaches into the weeds when it claims that a law student note supplies the missing link to Citigroup's New York State tax fraud. *See* Citigroup's Brf., at 18. The entirety of the note's mention of state taxes consists of:

> Notice 2008-83 had a significant impact on the tax revenues of the federal government, as well as many state governments. Lower tax revenues may mean that federal and state governments will be forced to impose a higher tax on their citizens to make up the lost revenues. Alternatively, federal and state governments may be forced to cut programs and services, which could disproportionately impact needy populations.

The note is about the wrong Notice (2008-83, not 2009-14), and it suggests no connection between *Citigroup* in particular and the question of whether *Citigroup* planned to, or did, take NOL deductions in *New York* as a result of its *2009* ownership change. In sum, the note is irrelevant. So, too, is Citigroup's reliance on the note's footnote 103, where the law student discussed a possible modification to the *federal* False Claims Act to challenge federal tax issues. *See* Citigroup's Brf., at 21. This obscure note does not dictate the result in this important NYFCA case.

Citigroup's proposed public disclosure bar would leave its internal tax accountants as the only possible whistleblowers in this case. That is not the law. The law does not require a relator to be a current or former corporate insider, nor does it bar publicly disclosed information outside of the three enumerated sources. Is Citigroup claiming that its New York State fraud is not actionable because its federal fraud was no secret? One violation's notoriety should not be a free pass for a second one.

B. Regardless, A NYFCA Case Cannot Be Dismissed Based On Certain Publically Disclosed Government Reports.

1. The NYFCA Does Not Categorize SEC Reports As Publically Disclosed.

The NYFCA includes a public disclosure exception for information obtained from government reports like SEC filings. Under Section 190(9)(b)(ii) of the NYFCA, a "federal… government report… shall not be deemed 'publicly disclosed'" when disclosure stems from "any… federal… law, rule, or program enabling the public to review… documents in the possession of … public agencies." Put another way, if a statute mandates that the public has the

right to review certain documents of public agencies, then the NYFCA's public disclosure bar does not apply to a relator's claims based on those documents

An SEC filing fits within the definition of the public disclosure exemptions in § 190(9)(b)(ii). The SEC is a public agency of the United States Government. Further, under the Securities and Exchange Act of 1934 (15 USCS § 78a), companies/corporations with more than ten million in assets whose securities are held by more than five hundred (500) owners must file annual and other periodic reports with the SEC. These reports, in turn, must be made available to the public. *See* 15 U.S.C. § 78m ("Promptly after the filing of any such report, the Commission shall make the information contained therein conveniently available to the public for a reasonable fee").

Citigroup is a corporation that fits this description, and its reports to the government are available on the SEC website. Citigroup makes them convenient for investors by incorporating them in its annual reports. Therefore, because the law requires these documents to be publicly available, even if one were to term a report *to* a government as "a federal, New York state or New York local government report, hearing, audit, or investigation," a relator such as Professor Rasmusen can use them in his complaint unaffected by the NYFCA's public disclosure bar. This is precisely what he did here.

2. The NYFCA Bars Dismissal Based On Certain Types of Public Disclosures.

Even if SEC filings did not fit within the definition of the public disclosure exemptions in § 190(9)(b)(ii) (although they do), the NYFCA still bars dismissal of this claim.

New York has an express public policy against dismissal based on public disclosure. In particular, the New York Attorney General's own regulation governing public disclosure motions requires his office to oppose such a motion in a relator's case if dismissal is sought solely because of alleged public disclosures in federal reports. *See* 13 N.Y.C.R.R. § 400.5(b). And in such a case, where dismissal is opposed by the State (as required), dismissal is improper under the express terms of the NYFCA. *See* N.Y. State Fin. Law § 190(9)(b). Citigroup ignores this statutory and regulatory language and the policy behind it.

Without Professor Rasmusen, this suit would not have been brought. The passage of time from 2010, when the violations began, to 2013, when the suit was filed, to 2015, when the Attorney-General declined to join and the suit was unsealed contained no rush of relators trying to be first. The Attorney General has the power to police frivolous NYFCA cases by moving to dismiss them as needed. *See* N.Y. State Fin. Law § 190(5)(b)(i).

CONCLUSION

Citigroup has already dodged $800 million in New York taxes by carrying forward losses from periods before its "ownership changes." And these losses have the potential to offset an additional $1.3 billion in New York taxes in the future. Congress, by statute, has prohibited the use of these losses, and New York law incorporates that statutory prohibition. While the IRS has issued Notices lifting the ban for Citigroup for federal purposes, these Notices have no bearing on New York taxes.

New York tax law pays no deference to these Notices because they are invalid. Citigroup's use of its losses is restricted in New York. To suggest that Citigroup was *expected*

(by whom it is unclear) to rely on IRS Notices that directly contravene the applicable federal statute and incorporating state statute when submitting its New York tax return is fanciful and unsupportable. *See* Citigroup's Brf., at 23. In sum, Citigroup's *New York* tax position is wrong as a matter of law.

Citigroup, with its vast army of tax professionals, surely should have understood its obligation to pay New York taxes and that the IRS's largesse in publishing the Notices does not apply to Citigroup's New York tax liability. Citigroup's failure to apply the law properly was knowing and, accordingly, entitles this case to proceed under the NYFCA.

Dated: February 4, 2016

HODGSON RUSS LLP
Attorneys for Eric Rasmusen

By: s/John L. Sinatra, Jr.
Daniel C. Oliverio, Esq.
John L. Sinatra, Jr., Esq.
Aaron M. Saykin, Esq.
The Guaranty Building
140 Pearl Street, Suite 100
Buffalo, New York 14202-4040
716.856.4000

and

1540 Broadway, 24th Floor
New York, New York 10036
212.751.4300

EXHIBIT A

OFFICE OF THE SPECIAL INSPECTOR GENERAL
FOR THE TROUBLED ASSET RELIEF PROGRAM
1801 L STREET, NW, 4TH FLOOR
WASHINGTON, D.C. 20220

AUG 10 2010

MEMORANDUM FOR: Herbert M. Allison, Jr., – Assistant Secretary for Financial Stability, Department of Treasury

Douglas H. Shulman – Commissioner of Internal Revenue

FROM: Neil M. Barofsky, Special Inspector General for the Troubled Asset Relief Program

SUBJECT: Engagement Memo – Review of the Section 382 Limitation Waiver for Financial Instruments Held by Treasury

As part of our continuing oversight of the Troubled Asset Relief Program ("TARP"), and at the request of Representative Dennis Kucinich, we are initiating an evaluation to assess the decision-making process regarding the waiver to Revenue Code Section 382 (IRS Notice 2010-2, hereafter the "Waiver") for institutions, such as Citigroup Inc., whose securities are acquired or disposed of by the Department of the Treasury ("Treasury") under TARP.

Our specific objectives are to determine (1) the rationale behind Treasury's decision to issue the Waiver; (2) whether Treasury was aware of any tax effect that may result from the issuance of the Waiver; (3) determine the principal decision makers involved in issuing the Waiver; and (4) the extent to which Treasury's policy to timely dispose of TARP investments factored into the decision to issue the Waiver.

We plan to start work on this engagement immediately. This work will be conducted under evaluation engagement code 002. We expect to perform audit work at both the Internal Revenue Service and Office of Financial Stability. A member of my staff will contact you shortly to arrange an entrance conference. At that time, we will discuss our scope, methodology, and timeframes in more detail. If you have any questions in the meantime, please contact Mr. Kurt Hyde, Deputy Special Inspector General for Audit, at 202-622-4633.

cc: Timothy Massad, Chief Counsel, Office of Financial Stability
Jennifer Williams, Oversight Liaison, Office of Financial Stability
Michael Phillips, Deputy Inspector General for Audits, Treasury Inspector General for Tax Administration