

GAO Faults IRS Whistleblower Program for Award Delays

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The IRS's handling of the tax whistleblower program suffers from a lack of complete data and a failure to adequately communicate with whistleblowers, leading to lengthy case processing times and reducing the appeal of the program, the Government Accountability Office said in a report released September 9.

The report focuses on case processing for tax whistleblower claims made under section 7623(b). Enacted as part of the Tax Relief and Health Care Act of 2006, the program provides for higher award payments to whistleblowers if a reported individual's gross income for the year exceeds \$200,000 and the amount of tax (plus penalties, interest, and additions to tax) in dispute exceeds \$2 million. Under section 7623(b), the IRS must issue an award amount of between 15 and 30 percent of the collected proceeds from a successful administrative or judicial action based on information submitted by a whistleblower. The GAO reported that through May 2011, the IRS Whistleblower Office had received roughly 1,300 submissions under section 7623(b) that cover allegations of nearly 9,500 noncompliant taxpayers. (For GAO-11-683, see *Doc 2011-19195*.)

The report notes that it can take years for a submitted claim to receive final disposition by the IRS. In fact, more than 60 percent of claims submitted in 2007 and 2008 are still being processed, the GAO said. The report cites the lack of controls on the review process undertaken by the IRS operating divisions as one reason claims can remain pending for so long without an award determination, and it recommends that the Whistleblower Office establish better procedures for checking on outstanding claim reviews.

The GAO described the six intermediate steps undertaken by the IRS from the time a claim is first filed by a whistleblower until an award payment might be made: initial review by the Whistleblower Office; subject matter expert review; classification and examination; appeals and collections; taxpayer right to request refund; and final Whistleblower Office review.

To shorten the amount of time it takes for the IRS to process a tax whistleblower claim, the Service should make changes to its tracking system to collect "complete data on the length of time claims spend at each step of the review process to inform the decision making for establishing appropriate review time targets," the GAO said. Expanding the type of information collected "could help the Whistleblower Office make some program management or resource allocation decisions and in reporting information," the GAO said.

According to the GAO, the IRS cited several factors that contribute to the time a whistleblower claim may remain under review. The complexity of many cases, the

numerous demands on subject matter experts' time, review of information for applicable privilege, and arranging debriefings with whistleblowers all add to how long a claim may be in process, the IRS said.

Although prohibitions on the release of taxpayer information limit some interaction between the Whistleblower Office and whistleblowers and their representatives, the GAO said greater efforts could be made to improve external outreach. And while the IRS is required to submit an annual report to Congress on whistleblower activity, the absence of numerous relevant data "limits Congress's ability to effectively oversee the program," the report says.

Policies adopted by the IRS impede constructive operation of the whistleblower program, according to practitioners interviewed by the GAO. For example, the narrow definition of collected proceeds and the practice of withholding on award payments cause whistleblowers to view the program as unfair. (For prior coverage, see *Doc 2011-8602* or *2011 TNT 78-1* and *Doc 2011-10213* or *2011 TNT 92-1*.)

According to information provided by the IRS's whistleblower case management system, the IRS has dismissed more than 90 percent of the submitted section 7623(b) claims. A substantial number of claims filed in fiscal 2010 averaged more than 200 days in the Whistleblower Office's initial review stage. Of the 8,200 claims currently being processed by the IRS, only 36 had arrived at the level of an award evaluation by the Whistleblower Office, the GAO said.

Improving Communication

"The GAO has done a good service by providing a road map for how to improve the IRS whistleblower program and go after big-dollar tax cheating," Senate Finance Committee member Chuck Grassley, R-Iowa, author of the changes to the 2006 whistleblower law, said in a release. "For the benefit of honest taxpayers, I intend to ensure that the IRS follows that map." (For the release, see *Doc 2011-19220*.)

Grassley called on the IRS to take the GAO report's recommendations seriously. "The challenge is for the IRS and Treasury to make the changes needed to provide assurance to existing and future whistleblowers so they're not discouraged by the time needed to process their claims," he said. "The IRS needs to do a better job of communicating with whistleblowers."

Practitioners contacted by Tax Analysts agreed that the lack of communication by the IRS with whistleblowers is hurting the program. Erika A. Kelton of Phillips & Cohen LLP said that the recommendations made by the GAO are helpful "but don't get to the real problems." One problem is "the refusal of the IRS to use the statutory exceptions to section 6103 to allow whistleblowers to provide crucial help when needed with investigations and the complete lack of information provided to whistleblowers about the status of their claims," she said.

The relatively small number of whistleblower claims that get referred to the operating divisions for examination raises concerns that perhaps some valid claims are being dropped because the IRS doesn't seek additional information from the whistleblowers

to support the claims, Kelton said. Another issue is the number of suspended claims -- "a limbo status that deserves further inquiry" because "that category is particularly suspect," she said.

Gregory S. Lynam, a tax partner at the Ferraro Law Firm, said the IRS already has plenty of rights it could use without waiting for congressional modifications to section 6103. "The report confirmed that the IRS has yet to enter into a single section 6103(n) information sharing agreement with a whistleblower to get their help with a case," he said, expressing surprise that none has happened despite the existence of so many claims. "Are we supposed to believe that out of the 9,540 total claims, not one of those cases could benefit from the exam team talking to the tax whistleblower?" he asked.

Scott A. Knott, also a tax partner at the Ferraro Law Firm, said that although the IRS acknowledged that a section 6103(n) agreement might be helpful when a taxpayer provides potentially false information during discovery that contradicts the whistleblower's information, "we had that exact situation occur, and no agreement or additional information was requested from the whistleblower." He argued that "apparently there is an institutional resistance to asking for help despite us having many other cases involving sophisticated corporate transactions and issues in which the IRS could benefit from the continuing assistance of a knowledgeable insider."

Dean Zerbe, national managing director at Alliantgroup LP and a former tax counsel to Senate Finance Committee Republicans, said the IRS must find a path to improving communication with whistleblowers, because "the failure to communicate with the whistleblower is putting a lot of sand in the gears and discouraging good whistleblowers."

Institutional Resistance?

Zerbe said the report appropriately highlights specific IRS procedures that are "holding the whistleblower program back." In particular, it is "very concerning that the GAO report highlights about a dozen times during the process when an IRS employee can deny a whistleblower claim and not once in the process can the IRS Whistleblower Office appeal that denial when it disagrees," he said.

Grassley also cautioned that the Whistleblower Office needs to act more independently at times. "I'm concerned that the IRS management still might have too many opportunities to say 'no' to a whistleblower, even when the whistleblower office believes a claim has merit," he said. "The IRS commissioner has to make it clear that he expects the director of the IRS whistleblower office to speak up if it thinks an IRS office is foot-dragging on a good whistleblower claim. The law I wrote gives the IRS whistleblower office the power to investigate claims on its own."

While the IRS may have limited resources to devote to whistleblower claims, Grassley said more can be done to leverage the Whistleblower Office's resources. "The tax cheats shouldn't be the only ones who can take advantage of outside legal talent. The IRS can't ask for more resources while ignoring the free resources available," he said.

It would help for the IRS to develop specific goals and priorities for the whistleblower program and then communicate those goals throughout the operating divisions, said Bryan C. Skarlatos of Kostelanetz & Fink LLP. "There continues to be a sense among some IRS personnel that the whistleblower program is not a good idea," he said. "Good or not, the program is law and appears to be here to stay, and the emphasis should be on how to make it as effective as possible. To do this will require complete buy-in from the operating divisions and the examining agents."

But Kelton was more skeptical. "The IRS whistleblower program is broken and desperately needs to be fixed," she said. Unless the IRS makes major changes to its program and eliminates the institutional resistance to whistleblowers, "I would expect the number of whistleblowers filing claims to continue to decrease," she said.

Claims Languishing

Lynam said the IRS's use of subject matter experts has been an inefficient procedure in evaluating whistleblower claims. The best people to evaluate those claims are the revenue agents directly, he said. "Often the subject matter expert who is evaluating these cases isn't even in the same industry group as the taxpayer. Revenue agents at the exam level are highly skilled tax professionals who can tell good issues from bad issues and can ask privilege questions of chief counsel just as well or better than subject matter experts," he said.

Knott said that with almost 1,300 section 7623(b) cases awaiting decision by a subject matter expert, "it is shocking that 192 of those cases have been stuck there for more than two years, and 933 more are still there from fiscal 2010, which ended September 30, 2010."

"No one needs three years to determine if a case could be valid. In point of fact, waiting three years pretty much ensures that it won't be because the statute of limitations would have expired," Lynam said. "If a revenue agent lets the statute of limitations run on an exam, there would be significant consequences, including potential job termination. But if the subject matter expert or chief counsel employee lets the statute of limitations run, it is just another day at the office."

Knott also questioned the metrics used by the Whistleblower Office to track how long a case sits at each review stage. "The current IRS system of tracking whistleblower cases does not put any responsibility on either the subject matter expert or chief counsel for delaying a case because their evaluation time gets lumped together, such that they can each blame the other for taking too long and not be held accountable to their supervisors," he said. "In fact, the study says that the subject matter expert and chief counsel supervisors can't even see how long their staff are taking to process a case."

Hope for the Future

Despite the criticisms contained in the report, Zerbe said that the expanded whistleblower program "is a winner." Data provided in the GAO report show that whistleblower claims "are receiving active consideration by the IRS" and that overall they are "well-grounded and have already led to significant recovery of taxes."

Skarlatos said the report's recommendation that the IRS should collect more information throughout the claims process "makes a lot of sense." If the information can be released to the public, "it will help taxpayers, whistleblowers, and their representatives understand how the process works and, in the long run, will enhance the quality of submissions and the deterrent effect of the whistleblower program," he said. "In particular, it would help to have more information about why claims are rejected so people can know what does and does not make a good claim."

"Eventually, the IRS whistleblower program will become an important component of tax enforcement as more awards become public and taxpayers become more aware of the whistleblower program, with the mere existence of the program generally deterring tax noncompliance, much like the fear of an IRS audit does today," Skarlatos predicted.

The IRS did not comment on the report, other than to refer to a letter included in the GAO report provided by IRS Deputy Commissioner (Service and Enforcement) Steven T. Miller. In the letter, the IRS said it generally agreed with the GAO's recommendations and was taking steps to improve information tracking in some areas and to increase timely review by the operating divisions.