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Practitioners Disagree Over Effect of UTP Reporting on Whistleblower Claims

by Jeremiah Coder

Summary by **taxanalysts**

Fortune 500 companies are sitting on almost \$200 billion in unrecognized tax benefits, a sum that may represent just the tip of the iceberg and that reflects the vast potential for whistleblower claims, according to a report by a law firm specializing in those claims.

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The study by the Ferraro Law Firm combed public financial statements to aggregate the size of each company's unrecognized tax benefit. The firm found that as of June 15, the top three companies in terms of tax reserves were General Electric Co. (\$8.719 billion), Pfizer Inc. (\$7.657 billion) and AT&T Inc. (\$7.523 billion). The authors believe that because the components of a company's tax reserve are generally not disclosed to the IRS and remain hidden in the tax accrual workpapers, the workpaper details can "make for valuable tax whistleblower submissions." (For the study, see [Doc 2010-19374](#) .)

The large size of tax reserves held by top companies puts in perspective the IRS's push this year to increase corporate transparency by requiring many business taxpayers to reveal their uncertain tax positions (UTPs) in tax filings. The IRS's proposal would require designated companies to begin reporting their UTPs for transactions in tax years beginning after December 15, 2009. (For Announcement 2010-9, 2010-7 IRB 408, see [Doc 2010-1882](#) or [2010 TNT 17-14](#) . For Schedule UTP and the accompanying instructions, see [Doc 2010-8705](#) or [2010 TNT 75-8](#) .)

But despite a potential incentive to front-load reserve charges before UTP reporting goes into effect, Gregory S. Lynam of the Ferraro Law Firm said auditing standards prevent companies from trying to beef up their reserve cushions. "The days of playing fast and loose with your tax reserve are gone," he said. In fact, Microsoft within the past few weeks recorded an additional \$1 billion tax reserve, he noted.

Lynam said that while some practitioners have speculated that the UTP reporting requirement will lower the number of whistleblower awards paid out because potential information will be disclosed to the IRS, that scenario probably will not come about because many companies do not reserve their largest tax issues. "A company's true tax exposure may be many times larger than what is reflected in the financial statements," he said. "And in many cases, those issues will have received a more likely than not opinion to prevent a reserve from being recorded." Consequently, whistleblowers are likely to report significant instances of unreported and unpaid tax liabilities, Lynam said.

But David B. Blair of Miller & Chevalier said the report brought false hope to disgruntled employees. "It is disturbing to see public information offered up in a way that intimates there is a pot of gold waiting at the end of the rainbow by simply submitting a whistleblower claim." Companies engage in good-faith decision-making when deciding what their appropriate tax reserves are, so a reserve position can't be assumed to hint at impropriety, he said.

George M. Clarke III, also of Miller & Chevalier, said the tax code's whistleblower provision serves a purpose in

uncovering taxpayers "who are hiding the ball." But in the UTP context, the disclosures that companies will make to the IRS are likely to weaken a whistleblower's claim in the absence of substantial additional original information, he said. "UTP disclosure will end up voiding a lot of whistleblower claims," he suggested, because "there is very little that won't be disclosed on Schedule UTP."

Blair said whistleblower claims are often problematic and add tension to the examination process. Whistleblower claims can damage the trust between taxpayers and the IRS by introducing a third party who is highly motivated to pursue charges of fraud and concealment, he said.

Clarke asked, "Why should a whistleblower get a reward for an issue that the IRS decided not to audit?" And in the event a new document is provided to the IRS on an issue it already is aware of, "does that minor information deserve a 30 percent reward?" he asked.

Although the reported results of the *Fortune* 500 tax reserves show large sums, Blair said that predicting the effect of UTP reporting on tax reserves is pure guesswork. "Fleshing out the details of the big round numbers companies put in their tax reserve footnotes is hard, because they contain state and international contingent claims, not just federal," he said. Just because companies may soon have a UTP reporting requirement does not mean they will make changes to their approach to SEC reports to avoid disclosure, he added.

Regarding whether the UTP reporting requirement would influence companies' decisions whether to get an opinion, Blair said it will remain "good practice" for large, sophisticated companies to get an opinion when substantial risks are involved. "When you have large issues where questions exist, companies seek an opinion to understand their potential exposure, and reserve accordingly," he said.

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