DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

DEPUTY COMMISSIONER

November 22, 2011

The Honorable Charles E. Grassley
Ranking Member
Committee on the Judiciary
United States Senate
Washington, DC 20510

Dear Senator Grassley:

I am writing in response to your letter of September 13, 2011, to Commissioner Shulman regarding the IRS Whistleblower Program. I appreciate your strong support of the program, and share your view that whistleblowers can provide unique and important contributions to tax compliance programs. As you noted in your letter, the program has made great progress, but there is more to be done.

As we assess the progress and direction for the Whistleblower Office, we share your vision that the Whistleblower Program should be an important tool in our overall enforcement program. Recently I held a meeting with key stakeholders in the Whistleblower representation community to ensure that IRS senior management is getting their feedback as we bring new ideas and renewed attention to the program. We intend to consider similar communications in the future as we make improvements to the program.

We believe, as you do, that the Whistleblower Program fits well with our mission. Whistleblowers can serve as an avenue of communication on newly promoted schemes and we are working to improve our timeliness to enhance this avenue. Additionally, whistleblowers can play a role in areas where there is scant or no third party information reporting and where technology may be difficult for us. Areas of little reporting have been a particular focus for the Service in recent years. Whistleblower submissions are particularly helpful, for example, when taxpayers take steps to hide their activities from the IRS, such as those who have secreted money offshore.

I will address each of your inquiries and recommendations below.

*Consideration of the Government Accountability Office (GAO) Recommendations*

You expressed concern about our response to some of the recommendations in the most recent GAO report. The GAO report contains a number of specific recommendations to enhance the data available for program management, increase attention on timely action in evaluating whistleblower information and improve

communication about program operations. We are in the process of developing a plan for addressing those recommendations and where appropriate have taken immediate action. We also are expecting TIGTA to make recommendations shortly. Thus, there are a number of program-level decisions that we plan to address once we have these findings and recommendations.

For example, after we learn the recommendations from the TIGTA review, we will finalize a plan for improving data capture in a number of areas. We are also in the process of determining whether the new data collection will be applied going forward, or can be reconstructed for cases received in prior years.

As you know, the law requires an annual report on the use of section 7623, results obtained, and any legislative or administrative recommendations regarding section 7623 and its application. The GAO has identified data which may be relevant to assessing the impact of section 7623, and the IRS will take steps to include additional data in future reports. However, some of the tables included in the GAO report cannot be created via current data systems, but require manual effort to extract and compile from an information system that was not designed to collect and report the information as presented. We are taking actions to improve our ability to collect and accurately report this information in a timely manner. However, these actions cannot be completed in time to deliver all of the requested information for the Fiscal Year 2011 report.

Case Management Information System

The IRS Whistleblower Office uses a commercial-off-the-shelf (COTS) case management information system called E-trak. Requirements for E-trak were developed and refined in FY 2007 and 2008, based on processes and expectations identified as the Whistleblower Office was getting organized and evaluating the first wave of 7623(b) submissions. The system was deployed in January 2009, initially to record new receipts. By the summer of 2009, data on 7623(b) claims received prior to January 2009 was entered into E-trak, and in the summer of 2010 data from legacy systems used to record 7623 claim data on open and closed cases (some from the 1980s) was transferred to E-trak. Plans to fully integrate the legacy data on open claims, identify additional user requirements for reports, data fields and claim tracking information, and general system updates were temporarily suspended to focus on pressing data requests, but will resume in the near future. While more significant improvements will be implemented in the future, the Whistleblower Office is currently taking the following actions to improve E-trak:

- Identifying specific changes in data fields, data definitions, screen design, drop-down lists and report formats to meet internal and external requirements.

- Recruiting new staff to assume substantial responsibilities for E-trak system maintenance and administration.
- Developing new capabilities for data entry to facilitate creation and update of records when a whistleblower submission identifies multiple taxpayers.

Improving Timeliness in Evaluating Whistleblower Submissions

The IRS is in the process of making improvements to the evaluation process that will result in more timely decisions. We recognize the need for improvement and are working on modifications to our evaluation of whistleblower information that will improve our timeliness prior to referral for audit or investigation. The 2006 amendments to section 7623 required an immediate focus on submissions alleging tax non-compliance involving more than $2 million. Processes and systems were set up to identify these submissions, and to evaluate them differently from the much larger number of submissions that do not meet that threshold. The high dollar submissions are more likely to involve taxpayers that are already under audit, whistleblowers whose relationship to the taxpayer may require analysis, and more complex technical issues regarding the alleged taxpayer liability – all of which can slow progress.

A key feature of our process for evaluating high dollar submissions is a network of subject matter experts in the Operating Divisions, whose other duties provide necessary insight into potentially related IRS activities, current enforcement priorities, and the technical tax issues presented. The results, measured in timeliness of the subject matter expert reviews, vary within each Operating Division. The GAO and our own management reviews identified the need to improve timeliness in the subject matter expert review process, and we are taking the following steps to address this issue:

- Changes to the case management information system will improve our ability to identify claims that do not appear to be making adequate process, so that issues can be elevated sooner.
- A realignment of the SB/SE Informant Claims Evaluation (ICE) unit in Ogden, UT to the Whistleblower Office is scheduled for January 2012. The ICE unit has been responsible for processing whistleblower submissions that do not appear to meet the $2 million threshold, and all submissions made prior to the 2006 amendments to section 7623[1]. Merging this group into the Whistleblower Office is expected to improve efficiency and productivity in the whistleblower program, including greater attention to follow-up on aging claims.

[1] While the ICE unit has been responsible for processing whistleblower submissions that do not appear to meet the 7623(b) criteria, award decisions are made by the Whistleblower Office. This ensures that the proper award criteria are applied, particularly when an audit or investigation results in higher assessments than may have been expected when the claim was received.

- The Whistleblower Office is working with the Operating Divisions and CI to identify and implement appropriate performance targets for key steps in the evaluation of whistleblower submissions, and a more formal process for elevating concerns about aging cases.

The Whistleblower Office will work with the Operating Divisions and CI on a broad-based review of the claim evaluation procedures, including determining whether we are collecting information from whistleblowers and other sources needed to more quickly reach an appropriate conclusion.

*Assignment of an Attorney to the Whistleblower Office*

In the Spring of 2010, the Office of Chief Counsel detailed an attorney to the position of Special Counsel to the Director of the IRS Whistleblower Office. This assignment was made permanent in July 2010.

*Status of Whistleblower Claims by Identified Taxpayers by Year of Claim Receipt*

The Whistleblower Office case management information system does not capture data on the tax years represented by each submission, or specific information about applicable statutes of limitation. Submissions commonly include allegations about multiple tax years, and the scope of review by the IRS can be expanded or contracted as the facts and circumstances warrant. Your letter referred to our previous description of some of the common fact patterns. Some of those situations can be identified during initial evaluation of a submission, while others are not known until the matter is referred to the field. As we improve our data collection systems, we will consider whether changes in this area are warranted. While this information is not captured at this time, the IRS recognizes the importance of protecting the statute of limitations. Agents are instructed as to the appropriate steps that must be taken to protect the statute of limitations in all cases.

*Reconsider Priority given to Whistleblower Information.*

Potential cases identified via whistleblower information are reviewed on a case-by-case basis, and have always been given priority based on the quality and potential impact of the information presented. Given our focus on promoting the Whistleblower Program, we are considering adjusting our case selection criteria so that, for similar cases, the fact that there is whistleblower information will be favorably taken into account. However, there are a number of factors that go into case selection and assessing the potential value of cases. The fact that a whistleblower submitted the information will not, by itself, result in preferred treatment over information developed from other sources.

Your letter suggests that IRS employees be educated on the importance of the whistleblower program, and that those who work with whistleblowers be considered and rewarded as part of the annual employee performance evaluation process. In the future, the IRS plans to communicate with employees highlighting some of the successes of the Whistleblower Program and encouraging the use of whistleblower information in audits and investigations. The Whistleblower Office will re-double its internal communications efforts, reaching out through our communications and training channels to these employees. As with non-whistleblower cases, employee performance is evaluated based on a variety of criteria. As you are likely aware, prohibitions exist on the use of enforcement results in evaluations. However, as more measures are put in place relating to the movement of whistleblower cases, these measures will be evaluated and, of course, employees are evaluated on the quality and timeliness of the work they perform whether or not whistleblower information is present.

*Whistleblower Office Investigation of Issues Raised by Whistleblowers*

Your letter notes that the law provides that the Whistleblower Office shall analyze information received, "and either investigate the matter itself or assign it to the appropriate Internal Revenue Service office..." The Whistleblower Office has used this authority to request assistance from other IRS offices in evaluating information submitted by whistleblowers, and determining whether to refer that information for audit or investigation.

At this time the Whistleblower Office does not use this authority as the basis for independently conducting audits and investigations of taxpayers. This decision is based on our evaluation of a number of factors and is driven by efficiency, consistency and quality concerns discussed below.

- Whistleblower submissions typically address one or more specific allegations of tax non-compliance. An IRS audit would not be limited to those issues, and may already be in progress when the whistleblower information is received. A limited scope Whistleblower Office audit of only the issues raised by the whistleblower could deprive the taxpayer and the Service of a comprehensive review of all aspects of its liability for the years in question. A comprehensive audit by the Whistleblower Office would require that organization to be staffed like a smaller version of each IRS Operating Division.
- The practice of relying on other IRS offices to conduct audits or investigations limits the risk that the taxpayer will learn that a whistleblower submission has been made, because its interaction with the IRS is no different from that in any other audit. If the Whistleblower Office conducted the audit, the taxpayer would know from the outset that a whistleblower submission was a factor in the audit, and we could expect significant differences in the interaction between the IRS and the taxpayer.

- Whistleblowers are understandably concerned about the particular taxpayer that is the subject of their allegations, and a Whistleblower Office charged with conducting taxpayer audits or investigations could be expected to focus on its own case inventory. Assigning the audits and investigations to be evaluated with general case inventories of CI and the Operating Divisions allows consideration of how IRS allocates resources across its overall enforcement programs. This helps ensure that taxpayers are not subject to disparate treatment, simply because of the source of the information.
- It is also our view that separating the role of making award eligibility and amount determinations from the role of conducting audits and investigations better protects the interests of whistleblowers. The current structure allows the Whistleblower Office to independently assess award related issues.

While the Whistleblower Office does not conduct audit of taxpayers, we have made, and continue to make improvements to track the aging of cases to ensure that appropriate actions are being taken within the operating divisions. It is important to recognize that the audit or investigation processes were designed to protect the rights of the taxpayer as the IRS gathers information necessary to determine the correct tax, make assessments and effect collection of any amounts due. Large case audits typically address more than one tax year, and many issues. Differences between the IRS and the taxpayer must be resolved, and appeal rights exhausted, before we can determine the extent to which whistleblower information contributed to the IRS action and make an appropriate award.

You also asked for an explanation of the manner by which conflicts between the Whistleblower Office and other IRS offices are resolved. As with matters outside of the Whistleblower Office, the starting point for conflict resolution is determining which office has the authority and responsibility to make the relevant decision. Matters related to the eligibility of a whistleblower to receive an award, and the amount of an award, are Whistleblower Office decisions. Decisions about whether to conduct an audit or investigation, the scope of an audit or investigation, and assessment and collection of tax, penalties and interest belong to the Operating Divisions, CI, Appeals and (in some cases) the courts. When the staff of one organization questions decisions made in another, they are typically raised up the management chain for an executive level decision. High level decisions are also raised to the Whistleblower Executive Board and ultimately to my attention.

*Enhance Communication with Whistleblowers*

The 2006 amendments to section 7623 did not change the limitations on disclosure of taxpayer information in section 6103 of the Internal Revenue Code. Section 6103 has been found to permit disclosure of some taxpayer information within the framework of an administrative proceeding to determine the award amount, through investigative

disclosures, and through a contract for services needed to perform a tax administration function. None of these authorities permit disclosure of information about the status of Whistleblower Office and Operating Division or CI review of a whistleblower submission, except in what are expected to be rare cases where there is a contract for services. Whistleblowers and their representatives commonly complain that the IRS provides no information on the status of open claims, other than to acknowledge that the claim remains open, and that the IRS provides no substantive explanation when a claim is denied. Under current law, the IRS cannot provide a remedy for these complaints.

The GAO suggested that more information on the average time at each stage of the evaluation, field audit or investigation, and award determination processes could help whistleblowers understand why their cases are unresolved. As we improve our ability to track and report this data, we will include it in public reports and in our communications with whistleblowers and their representatives. However, the limitations in section 6103 will not allow us to tell a whistleblower where his or her case is in the process, and expectations based on averages may be of limited relevance to the timeliness of action on a particular case. For example, a decision to expand consideration of an issue to other tax years, or a taxpayer decision to contest the matter in Appeals or in court, can render the averages irrelevant.

*IRS Position on Seeking Outside Assistance*

We believe the Treasury Regulation on contracts for services with whistleblowers reflects the position articulated in the Joint Committee on Taxation report issued in conjunction with the 2006 amendments to section 7623 which indicated that it was expected that disclosures pursuant to a 6103(n) contract would "be infrequent and w[ould] be made only when the assigned task cannot be properly or timely completed without the return information to be disclosed."

Contracts relying on the authority of section 6103(n) are to be rare, based on a finding of necessity to perform a tax administration function. If the IRS can obtain the required information or analysis using its own resources on a timely basis, including through interviews with the whistleblower, there is no basis for entering into a contract for services.

However, we recognize that there are cases where it would be beneficial for us to contract with the Whistleblower for technical assistance throughout the examination or on specific issues, such as analyzing responses to IDRs. We will be focusing on this area to assess cases for appropriateness of using section 6103(n) arrangements.

*Contacts with other Government Agencies Related to Specific Claims*

The Whistleblower Office practice, consistent with our obligations under section 6103, is to neither confirm nor deny the existence of a whistleblower claim when asked by another agency about a specific matter. These inquiries are not common, and typically occur when a whistleblower informs another agency that he or she has submitted a claim to the IRS. The Whistleblower Office may sometimes initiate an inquiry about actions of another agency that may be connected to IRS actions taken in response to whistleblower information. Any IRS contacts, and responses received, are documented in the claim file.

*Status of Claims in Final Review, Award Evaluation, or Suspended Status*

Your letter asks for an explanation for the status of claims in final review, award evaluation and suspended status for claims received in 2009 and prior. With respect to the final review and award evaluation statuses, the inventory is constantly changing as the Whistleblower Office receives completed case information from the Operating Divisions and CI, and as the Whistleblower Office is able to reach a conclusion on eligibility for an award. The timeline for award evaluation is also affected by the potential for the taxpayer to file a claim for refund (discussed below). We are not currently collecting the data necessary to report cycle time for final review and award determination, but will include this in our information system enhancements. However, the Whistleblower Office staff gives cases in these statuses their highest priority. The only work that has a comparable level of attention is the initial evaluation of new receipts for referral to Operating Division and CI subject matter experts.

The "claim suspended" status currently does not distinguish the reason for suspension—an issue we are addressing in our improvements of the case management information system. A claim may be suspended when there are questions about how the issues presented will be addressed. For example, we have received a number of submissions that identify large numbers of taxpayers. These claims have been recorded and suspended as the Operating Divisions and CI work to coordinate actions, deciding which taxpayers will be investigated or audited, whether efforts need to be sequential or parallel, and whether there is a need to consider impact on other compliance priorities. A claim may also be suspended if action on a particular taxpayer is complete, but actions on other taxpayers identified in the submission are still open. This is most common when there is no award payable with respect to the completed actions, but it could also be used to protect the interests of the whistleblower when the amount in dispute on completed claims is below the $2 million threshold. Aggregation of the completed claims with others in process could satisfy the threshold requirement, permitting the whistleblower to participate in the administrative proceeding for making award determinations in 7623(b) claims, and preserving an opportunity to appeal to Tax Court.

*Two Year Refund Statute of Limitations*

The IRS rule requiring that award claims not be made until after the two year period for filing a claim for refund has expired or has been waived recognizes that IRS action is not final until taxpayer rights have been exhausted. Awards are paid from collected proceeds, but we cannot be sure that amounts collected will stay collected if the taxpayer has the right to challenge the IRS assessment or collection action. In some closing agreements, the taxpayer waives its right to appeal. In those cases, a determination of award eligibility and amount can proceed. In others, a much less common action by the taxpayer could waive the right to appeal on an issue or group of issues, while reserving the right to appeal other matters for the relevant tax period. Such a waiver may not be the final word with respect to proceeds from the agreed issue(s). For example, in some cases a change in the taxpayer's favor on an unagreed issue could affect the base from which the liability on the agreed issue is computed. Furthermore, though some issues may be agreed, a taxpayer might not make full payment on those issues until the unagreed issues are resolved and the total additional liability (if any) is known. There are cases, however, in which awards can be paid before the running of the two year refund statute. The Whistleblower Office practice is to look at the two year refund statute issue on a case-by-case basis and to move forward with payment when the facts of the particular case warrant doing so.

*Status of the Collected Proceeds Regulation*

Public comments have been received and considered, and a final regulation is being prepared and cleared for publication.

*Application of the "Chief Architect or Chief Wrongdoer" Criteria to Determine Whether the "Planned and Initiated" Provision Applies*

The IRS is reviewing the issue and expects to clarify its position on the "planned and initiated" criteria in the IRM.

*Annual Whistleblower Report Requests*

You identified a number of areas in which you would like additional data included in the annual Whistleblower Report to Congress. As previously discussed, most of the data-related recommendations cannot be implemented for the Whistleblower Office FY 2011 annual report because information system changes are needed. We also need to determine whether the new data collection will be applied going forward, or can be reconstructed for cases received in prior years. As we work through the issues and set priorities, the Whistleblower Office is reaching out to other IRS organizations to be sure their needs are incorporated into system and process changes. We are also maintaining lines of communications with external groups.

*Request for Legislative and Administrative Recommendations from Director of the Whistleblower Office.*

You requested that the FY 2011 Whistleblower Report include the Director of the Whistleblower Office's recommendations for legislative and administrative fixes. The Fiscal Year 2010 annual report described some of the issues that the IRS faces as it develops internal and external guidance to implement section 7623. For example, as is noted in the 2010 report, the term "collected proceeds" is undefined, and its relationship to the Victims of Crime Act (which dedicates funds from criminal fines to the Victim of Crimes Fund) is not addressed. The annual report on section 7623 will include proposals or issue discussions that have been prepared by the Whistleblower Office, in consultation with the Treasury Department Office of Tax Policy.

My staff is available to meet with your staff and discuss any additional questions you may have. If you have any questions, please contact me or a member of your staff may contact Floyd Williams at (202) 622-3720.

Sincerely,

Steven T. Miller
Deputy Commissioner for
Services and Enforcement