REPLY TO:

☐ 135 HART SENATE OFFICE BUILDING
WASHINGTON, DC 20510–1501
(202) 224–3744
e-mail: grassley.senate.gov/contact.cfm

☐ 721 FEDERAL BUILDING
210 WALNUT STREET
DES MOINES, IA 50309–2140
(515) 288–1145

☐ 150 1ST AVENUE NE
SUITE 325
CEDAR RAPIDS, IA 52401
(319) 363–6832

United States Senate

CHARLES E. GRASSLEY

WASHINGTON, DC 20510–1501

REPLY TO:

☐ 103 FEDERAL COURTHOUSE BUILDING
320 6TH STREET
SIOUX CITY, IA 51101–1244
(712) 233–1860

☐ 210 WATERLOO BUILDING
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WATERLOO, IA 50701–5497
(319) 232–6657

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SUITE 180
DAVENPORT, IA 52801–1419
(563) 322–4331

☐ 307 FEDERAL BUILDING
8 SOUTH 6TH STREET
COUNCIL BLUFFS, IA 51501–4204
(712) 322–7103

September 13, 2011

The Honorable Douglas L. Shulman
Commissioner
Internal Revenue Service
1111 Constitution Avenue NW
Washington, DC 20224

Dear Commissioner Shulman:

I am writing to express my concerns about several issues raised by the report on the whistleblower program released last week by the Government Accountability Office (GAO). I also continue to have concerns about the Internal Revenue Manual (IRM) provisions regarding whistleblower claims.

Before I address my concerns, I want to first express my appreciation for the progress in managing whistleblower claims since the 2006 reforms I authored were enacted. I am thankful that leadership at the Internal Revenue Service (IRS) is making good faith efforts to embrace whistleblowers instead of reverting to the old culture of treating them like skunks at a picnic. These actions stand in stark contrast to the sky-is-falling attitude initially taken by the leaders at the Securities and Exchange Commission (SEC) in implementing the whistleblower provisions that were included in the Dodd-Frank legislation. Those provisions, like the IRS whistleblower provisions, are based on the False Claims Act (FCA) updates, which I also authored. I hope that the IRS will take an active role, along with the Department of Justice (DOJ), in advising the SEC on its implementation of the new SEC whistleblower rules. I believe taxpayers will benefit from having a strong, coordinated, multi-agency approach to combating fraud and protecting taxpayer dollars.

While the IRS has made great progress, there is still room for improvement. The GAO report makes clear that the whistleblower program has been successful in providing good information to the IRS about big-dollar tax cheating. The data shows that IRS has received tips on more than 9,500 taxpayers from 1,400 whistleblowers in just five years while only rejecting 1,300 claims so far during that time. I remain concerned, however, about the time needed to process these claims and whether the long timeframes, combined with a lack of communication with whistleblowers, discourages current and future whistleblowers. As you know, whistleblowers often come forward at great risk, both personal and financial. With the nation facing massive deficits, both Department of Treasury (Treasury) and IRS officials need to do all they can to ensure the success of what's clearly one of the best tools available to go after tax fraud.

The next whistleblower report to Congress is due for the fiscal year (FY) 2011, which ends September 30, 2011 – just three weeks away. The GAO makes excellent recommendations

for the IRS to consider implementing for this annual report. I am disappointed that the IRS has indicated that adopting these changes is contingent upon limited resources. We know that just one tax whistleblower netted the government $20 million. This recovery alone indicates that the money collected from whistleblower tips should more than pay for improvements needed to effectively manage whistleblower claims. I understand that recoveries are not dedicated to the IRS. However, the Treasury Secretary and IRS leadership have the authority to allocate IRS resources as needed. Improved monitoring of the program and tracking of claims will comfort current and future whistleblowers, which would, in turn, ensure the continued receipt of valuable whistleblower claims. As a result, I ask that you consider the benefits of making these changes a priority.

I am also very concerned about the timeframe for addressing whistleblower claims. The Treasury Inspector General for Tax Administration (TIGTA) noted in its 2009 report that the effectiveness of the IRS Whistleblower Program could be diminished without an effective control over, and timely processing of, claims. In my June 21, 2010, letter to Secretary Geithner, I asked for an update of the information contained in Figure 1 of the 2009 TIGTA report. I did not receive this in your November, 2010, response to me. I did not pursue it at the time because the GAO had started work on its report in September, 2010. The GAOs report contains the most comprehensive and informative data on the status of whistleblower claims. As a result, I ask that the FY2011 annual whistleblower report to Congress, and all subsequent reports, FY2011, contain the Tables 3 and 4 from the GAO report.

It is not clear from the GAO report how much time is lost because of consultations with, or delays in response, from the office of Chief Counsel. Providing independent counsel to TIGTA and the Taxpayer Advocate has been beneficial to ensuring the success of those offices As a result, please consider reassigning an attorney from another IRS office or the Office of Chief Counsel to the Whistleblower Office to help speed the resolution of any legal questions that arise.

The GAO report indicates that each operating division has different time guidelines for subject matter expert (SME) review. I am very concerned that Table 3 of the report indicates that there are over 1,000 claims listed in SME review through FY2010, which ended September 30, 2010, and almost 200 of those were received before September 30, 2009. This indicates years of languishing in a review to determine whether a taxpayer should be even audited. The numbers in audit for these years are more troubling. According to Table 3 of the report there are almost 500 cases from fiscal year 2007 in the examination stage and almost 300 from fiscal year 2008. Given that FY2007 ended September 30, 2007, we're coming up on over four years in the audit phase. This is very worrisome. Please explain why these cases are still open, what tax years they represent and how many of these claims will wind up rejected for no assessment because of the expiration of the statute of limitations (SOL).

Please note that, in my June 21, 2010, letter I asked whether the SOL was an issue for pending whistleblower claims. The IRS's November 26, 2010, response states the following:

"In some cases, the applicable limitations periods have expired before the information is submitted and the IRS is unable to act. Generally, in cases where statute of limitations dates are imminent, the IRS has little practical opportunity to act; however, some actions may be possible on an expedited basis. In some cases, the IRS may take an issue raised by the whistleblower regarding a closed year and consider it for a year that is still open. The IRS has taken steps to reduce the time required for administrative processing of section 7623 submissions, and continues to explore additional ways to reduce this time."

When I received the November 26, 2010, response, I was not aware of the number of cases outstanding for previous years. The IRS response also does not indicate how many whistleblower claims provide information about substantial errors that may result in an ***extended*** SOL or whether the IRS deems that the SOL may not apply at all because of fraud considerations. As a result, I ask that the FY2011 annual whistleblower report to Congress, and all subsequent reports, FY2011, contain the following information:

- the average time per step listed in Table 2 of the report;
- the number of cases rejected because of the expiration of the SOL;
- the number of cases for which the extended SOL applies;
- the number of SOL extensions requested by the IRS and the number of such requests denied by taxpayers; and,
- the number of cases for which the SOL may not apply.

From my understanding of various IRS compliance initiatives, it seems that audits tend to move more quickly when IRS management prioritizes an issue. I understand that the IRS has decided that audits from whistleblower claims should not be prioritized over other audits. Given the large dollar claims the IRS is receiving as a result of the 2006 law changes and the problems presented by the expiration of the SOL for these claims, I ask for this decision to be reconsidered and an explanation for this policy. Please also inform me what steps have been, or will be taken, to educate IRS employees about the importance of the whistleblower program, whether and how employees that review whistleblowers claims are considered and rewarded for working with whistleblowers as part of the annual employee performance evaluation process.

The GAO report highlights that the whistleblower office does not have a process to check in with the operating divisions concerning the time in each step listed in Table 2. I am concerned that the Whistleblower Office is viewed as a delivery service – responsible only for delivering whistleblower claims to IRS offices.

The Whistleblower Office was intended to be an advocate for the whistleblower and should be raising the alarm if meritorious whistleblower claims are being ignored or overlooked by an IRS office. This larger role – of ensuring that good whistleblower claims receive appropriate attention – is one of the reasons why the Whistleblower Office consults as an equal with other IRS offices.

The independence of the Whistleblower Office was made clear in the statute because of the historic treatment of whistleblowers by the IRS, which was similar to that at other

government agencies. The IRS previously often had little to no understanding, sympathy or interest in whistleblowers. As is well known, the IRS whistleblower program was severely underutilized and extremely ineffective prior to the 2006 reform. Whistleblower claims were lost, ignored, relegated to the backroom or forgotten by the responsible divisions at the IRS. On those rare occasions when claims were considered, the IRS would form a committee made up of senior IRS managers to review these whistleblower cases and consider possible awards. In practice this internal committee was the place where whistleblower claims went to die. That is why the 2006 statute gave sole authority to the Whistleblower Office to decide awards for whistleblowers. The Congress recognized that the independence of the Whistleblower Office is vital to the success of the program.

The director of the Whistleblower Office reports directly to the IRS Commissioner, has the authority to contract or establish working relationships with whistleblowers and their advisors, and, most importantly, has the authority to either investigate whistleblower claims itself *or assign them to the appropriate IRS office. There should be no doubt the Whistleblower Office* has the authority to investigate whistleblower claims even if those claims fall within the jurisdiction of another division at the IRS.

The requirement of consultation and coordination is to ensure that the Whistleblower Office is not isolated; that all IRS offices benefit from information provided by whistleblowers and that the Whistleblower Office benefits from the expertise of all the IRS offices. It is likely that an operating division may be more efficient at conducting the actual examination. However, *it is the responsibility of the Director of the Whistleblower Office to ensure that each claim is* being decided on the merits. For the whistleblower program to succeed, whistleblowers need to have confidence that the IRS Whistleblower Office will ensure that a well-grounded claim will receive ***objective and timely consideration***.

Please inform me what steps you will take to ensure that the Whistleblower Office is operating under its full authority, including making clear to managers the role of the Office. Please also explain how conflicts between the Whistleblower Office and other IRS offices are resolved. If they do not already exist, I ask that you develop procedures outlining the when, what, why, and how for investigations conducted by the Whistleblower Office. For example, consider sending back to the Whistleblower Office those claims that are languishing in one of the steps identified in Table 2, such as those FY2007 claims still in SME review.

I also ask that the FY2011 annual whistleblower report to Congress, and all subsequent reports, contain the following information:

- the number of investigations conducted directly by the Whistleblower Office; and,
- the number of claims in which there is a disagreement between the Whistleblower Office and other IRS offices.

The GAO report indicates that communications with whistleblowers regarding the status of their claims remains an issue. As I stated above, the IRS should be very concerned that current and future whistleblowers will become disheartened by the snail's pace for processing claims. The IRS should develop communication guidelines that fit within the privacy restrictions to communicate with whistleblowers at every step. At each of these stages the whistleblower

should be given an estimate of the time to the next step and also provided periodic updates as appropriate. Such basic information will do much to assure whistleblowers of the IRS's commitment to processing their claim. At a minimum, the Whistleblower Office should widely disseminate the information in Table 2 of the GAO report with average expected time per step.

Further, every effort should be made to provide whistleblowers who have submitted substantive claims an opportunity to meet and discuss with IRS officials responsible about the claim and its problems and merits. I am very disappointed to learn from the GAO report that the IRS has not used the authority provided to it under Internal Revenue Code (IRC) section 6103(n) to enter into contracts when processing whistleblower claims.

When first considering updates to the IRS whistleblower statute, I had drafted an amendment to IRC section 6103 to permit communications with a whistleblower. However, my Finance Committee staff was informed by the IRS directly that such statutory changes were unnecessary because the IRS would use its contract authority under 6103 to communicate with whistleblowers. The IRS has failed to date to meet its commitment to me. This is especially troubling after learning about the number of claims outstanding from FY2010 and before.

It is the utilization of outside attorneys and advisors of whistleblowers that has been a key to the success of Department of Justice with FCA claims. The Committee report language for the updated IRS whistleblower law was intended to replicate the success of the FCA.

Sec. 406(b) of the statue reads as follows:

"(b) Whistleblower office.

. . .

"(C) in its sole discretion, may ask for additional assistance from such individual or any legal representative of such individual.

"(2) Request for assistance. The guidance "issued under paragraph (1) shall specify that any assistance requested under paragraph (1)(C) shall be under the direction and control of the Whistleblower Office or the office assigned to investigate the matter under paragraph (1)(A). No individual or legal representative whose assistance is so requested may by reason of such request represent himself or herself as an employee of the Federal Government."

The Committee Report placed additional emphasis on the IRS benefitting from outside assistance:

"Under the provision, the Whistleblower Office may seek assistance from the individual providing information or from his or her legal representative, and may reimburse the costs incurred by any legal representative out of the amount of the reward. To the extent the disclosure of returns or return information is required to render such assistance, the disclosure must be pursuant to an IRS tax administration contract."

The IRM section 25.2.2.7(10) assumes a very narrow view of permissible assistance from whistleblowers and their advisors:

> "The law requires the Whistleblower Office to analyze 7623(b) claims, and authorizes the Whistleblower Office to request assistance from the whistleblower or their counsel. In most cases, the IRS should be able to receive information from a whistleblower, conduct a debriefing to ensure the information provided is fully understood and that the IRS has all relevant information the whistleblower can offer, and then proceed with an investigation or examination without further assistance from the whistleblower. In some cases, there may be a need to pose additional questions to the whistleblower."

The intent of the law, contrary to the position taken in the IRM, was not to simply ensure that all relevant information is provided by the whistleblower. Rather, the statute envisions having whistleblowers and their advisors helping to pull the oars in the examination and investigation – as is the successful practice for years with the FCA. For example, the IRS could bring in experts on a difficult valuation question.

The IRS should be using all tools available to it to speed up the processing of whistleblower claims. Such dialogue will also improve the quality of information that the IRS receives from whistleblowers and their attorneys. As a result, in order to speed up the processing of whistleblower claims, I ask you to reconsider the IRS's position on when to seek outside assistance.

Just as I am concerned that the IRS Whistleblower Office makes its award decisions independently and without interference from IRS offices, I am similarly concerned that other government agencies not be allowed to interfere with the decisions of the Whistleblower Office. Please explain the procedures for documenting contacts with other government agencies related to specific whistleblower claims.

Table 3 of the GAO report highlights another very troubling data set – the number of claims for FY2007 through FY2009 sitting at Whistleblower Office in final review, award evaluation or suspended status. I would expect that the SOL for taxpayers to request refunds has expired for many if not all of these. It is important that the Whistleblower Office lead by example and quickly dispose of claims. Please explain why there are so many cases in these statuses for these years, the process for these cases including the expected timeline for making a determination and a final award and the expected timeline to make decisions for these cases in general. In addition, please provide the following information:

- the number of claims for which IRS has received payment from the taxpayer and for which the SOL for a taxpayer to file a refund request has expired; and,
- the number of weeks, for each case, that a claim case has been awaiting determination by the IRS Whistleblower Office and whether the whistleblower has been notified of an award determination.

I ask that you provide me a monthly update until these claims are closed. I also ask that you inform me of the communication that IRS provides to whistleblowers and their advisors during this time, particularly when the SOL for refund filings has expired.

On a similar note, the IRS should make it a priority to have a final determination on any issues brought forward by a whistleblower. For example, if a whistleblower has brought forward information on issue X and it is subject to exam and resolved – the matter should be subject to a closing agreement and payment made to the whistleblower. The IRS already has a form for this Form 906, *Closing Agreement on Final Determination Covering Specific Matters,* or a Form 870-AD in Appeals. Currently, it appears whistleblowers must wait for all issues related to a taxpayer to be resolved and all rights of appeal exhausted before receiving a payment, even if a closing agreement is an effect. Please explain why, when a closing agreement is in effect, it is still necessary for the SOL on taxpayer refund requests to expire before a whistleblower award is paid.

In addition to concerns raised by the GAO report, I wanted to take this opportunity to express my concerns about other provisions in the IRM. In my June 21, 2010, letter, I expressed concerns about the IRS's decision, through the IRM, to limit the type of transactions eligible for whistleblower awards. I appreciate the IRS's decision to reconsider these provisions and to issue regulations in this area.

I understand a number of considered comments about the proposed regulations have been submitted by practitioners and organizations. These comments raise important points about what payments and fines should be encompassed by the awards that Treasury needs to consider given its inappropriately narrow reading of the legislation. It is important for whistleblower confidence – and tax administration – that whistleblowers be rewarded for providing information about income being reduced by net operating losses (NOLs). I understand that this is a difficult issue as IRS does not collect payments of tax in such cases and so a whistleblower award likely could not be made until a taxpayer's NOLs are fully utilized and pays taxes. Please provide an update on the status of these regulations.

Separately, I am in receipt of the letter from several advocacy organizations, a copy of which is attached. I ask that you give serious consideration to the points raised in their letter. As they note, there is a long and established history regarding the meaning of "planned and initiated." The IRS should consider this history and practice at other federal agencies and not attempt to create its own policy that could conflict with this longstanding practice.

On a related matter, in IRM section 25.2.2.9.2.13.C, the IRS attempts to categorize a "whistleblower's role as a planner and initiator as significant, moderate, or minimal." As stated in the letter from the three organizations, limitations for planners and initiators was intended to apply to the ***chief architect*** or the ***chief wrongdoer***. I ask that you take into consideration the established law in this area with respect to FCA claims.

Finally, I wanted to express my disappointment with the content of the annual whistleblower report to Congress and with the extreme delays in issuing the report. I have provided my comments on the content above. In addition, given the minimal content of the reports to date, there is no reason for the report to be issued several months after the close of the fiscal year. I ask that the report be provided to Congress by November 30 each year – 60 days from the end of the fiscal year should be more than sufficient to provide the requested data.

Separately, the discussion of "Legislative and Administrative Issues" in the latest report is vague and unclear. Keeping in mind the independence of the Whistleblower Office, I ask that the FY2011 whistleblower report, and all subsequent annual reports, include the Director of the Whistleblower Office's recommendations for legislative and administrative fixes.

The GAO has done a good service by providing a road map for how the IRS can improve the IRS whistleblower program and go after big-dollar tax cheating. Now 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 or by the issuance of rules that contradict well-established rules for compensation of non-tax whistleblowers. The vast majority of taxpayers are honest. They're the ones who benefit from a successful whistleblower program. More tax compliance means more fairness for hardworking families who pay what they owe.

I appreciate your prompt response to the questions raised above. If you have any questions, please contact my staff at (202) 224-3744.

Sincerely,

Chuck Grassley

Charles E. Grassley
Ranking Member

cc: The Honorable Max Baucus
The Honorable Orrin Hatch
The Honorable Dave Camp
The Honorable Sander Levin