



## Treasury Inspector General for Tax Administration Office of Audit

### DESPITE THE SUCCESS ACHIEVED, THE SON OF BOSS SETTLEMENT HAD LITTLE IMPACT ON INVESTOR FILING AND PAYMENT COMPLIANCE

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## Highlights

Highlights of Report Number: 2009-30-018 to the Internal Revenue Service Commissioners for the Large and Mid-Size Business Division and the Small Business/Self-Employed Division.

### IMPACT ON TAXPAYERS

The ability of the Internal Revenue Service (IRS) to successfully administer the nation's tax system is heavily dependent upon the public's perception about its fairness. Many involved in tax administration believe that abusive tax shelters can give the appearance that the tax system is unfair, which in turn can undermine voluntary compliance. The fairness issue might be further aggravated when a tax shelter settlement allows participating taxpayers to deduct a portion of the costs associated with investing in the abusive tax shelter even when they fail to meet their tax return filing and payment obligations.

### WHY TIGTA DID THE AUDIT

The objective of the review was to evaluate whether participants and non-participants in the Son of Boss (Bond and Option Sales Strategies) settlement are meeting their Federal tax obligations. The review was initiated as part of our planned Fiscal Year 2008 audit coverage.

### WHAT TIGTA FOUND

The IRS has a long history of using incentives as a tax administration tool to resolve controversy and foster compliance. The Son of Boss settlement was one such incentive that provided participating taxpayers and the IRS with the opportunity to save time and money that might otherwise have been spent on a protracted dispute over the Son of Boss abusive tax shelter. Investors participating in the settlement were also allowed to deduct a portion of their transaction costs, typically promoter and professional fees, and, in some instances, avoid tens of thousands of dollars in penalties that could have been imposed.

The Offer in Compromise is another incentive that is, perhaps, more widely known to the public due to IRS

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outreach efforts and the considerable amount of advertising appearing in the media about taxpayers settling their tax liabilities for much less than the amounts actually owed.

While there are differences between the Son of Boss settlement and an Offer in Compromise, both incentives ultimately resolve issues for less than the amounts that could have been owed and are promoted as being in the best interest of the Federal Government and the taxpaying public. Because of these similarities, TIGTA analyzed features in each incentive and has observations that the IRS might find useful in designing future tax shelter settlements. Specifically, our analysis suggests that incorporating greater transparency as well as filing and payment compliance commitments in tax shelter settlements might help alleviate any potential fairness concerns associated with abusive tax shelters.

With respect to filing and payment compliance commitments, taxpayers who have their liabilities compromised face losing the benefits they receive under an Offer in Compromise because the IRS can reinstate the debt and resume collection actions if they fail to meet all their filing and payment obligations in the succeeding 5 years. In contrast, taxpayers who participated in the Son of Boss settlement were not required to make a similar commitment as a condition for keeping the settlement's benefits.

Both our work and that of the IRS suggest that the prospect of losing benefits contributes to a high level of voluntary filing and payment compliance, which is key to reducing the annual tax gap. Our evaluation of voluntary filing and payment compliance in the 3 years following the Son of Boss settlement showed that 27 percent (300) of the 1,103 taxpayers who participated in the settlement did not meet their filing and payment obligations. Comparatively, TIGTA reported in 2004 that virtually all of the 84 taxpayers (96 percent) evaluated in a statistical sample of 28,018 Offers in Compromise were in compliance with their filing and payment obligations at the time of our review.

### WHAT TIGTA RECOMMENDED

TIGTA made no recommendations for specific corrective actions. Because our review focused only on the Son of Boss settlement, TIGTA has no basis for knowing whether the filing and payment compliance issues were unique to the participants in the Son of Boss settlement or are prevalent among participants in other tax shelter settlements. IRS officials reviewed and provided comments on a draft of this report. TIGTA incorporated the comments where appropriate.

### READ THE FULL REPORT

To view the report, including the scope and methodology, go to:

<http://www.treas.gov/tigta/auditreports/2009reports/200930018fr.pdf>.

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