



*Information From State Tax Amnesty  
Programs Could Bolster Compliance  
Efforts and Ensure Federal  
Tax Obligations Are Also Met*

**September 2005**

**Reference Number: 2005-30-165**

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

September 26, 2005

**MEMORANDUM FOR** COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED  
DIVISION

**FROM:** Pamela J. Gardiner  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – Information From State Tax Amnesty Programs  
Could Bolster Compliance Efforts and Ensure Federal Tax Obligations  
Are Also Met (Audit # 200530007)

This report presents the results of our review to evaluate the effectiveness of the Internal Revenue Service's (IRS) use of information from the State tax amnesty programs. We will address the benefits and risks of implementing a Federal tax amnesty program in a subsequent review.

*Synopsis*

Tax amnesty programs are held to collect taxes owed from prior years and to place those who previously avoided taxation on the tax rolls. Over the past 23 years, at least 41 States and 2 cities have collected over \$5.7 billion from tax amnesty programs. To encourage taxpayers to participate, these programs generally forgave all civil and criminal penalties. They differed as to whether all or a portion of the interest was forgiven.

In summary, information obtained by States during their tax amnesty programs has not been used by the IRS as an ongoing tool to help ensure compliance with Federal tax laws. Consequently, the IRS is missing a unique opportunity to address noncompliant taxpayers who have acknowledged their noncompliance with tax laws to State governments and who also owe Federal taxes.

The Commissioner, Small Business/Self-Employed (SB/SE) Division, recognized the potential value of State tax amnesty information as a tool to supplement IRS enforcement information and efforts. As a result, the SB/SE Division established a team to study the potential usefulness of



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State tax amnesty information. The study found that 16 of 20 States that responded to a national survey would be willing to share tax amnesty information with the IRS. However, sharing of State tax amnesty information was generally not addressed within the IRS' existing Implementing Agreements with the States.<sup>1</sup>

Although the IRS study included considerable analysis of the tax amnesty data for individual taxpayers from two States, it did not fully explore the benefits of this information and its usefulness in IRS compliance programs. The study concluded that (1) the State tax amnesty information would not be effective in identifying unknown nonfilers or in discovering underreported income and (2) another planned FedState initiative, the Reverse Filing Match,<sup>2</sup> would yield the same information in an automated environment. The study did not address business taxpayers that participated in the State tax amnesty programs.

Our audit found the State tax amnesty information could be used effectively to bolster IRS efforts for improving compliance. We reviewed a sample of tax amnesty information from 2 States in which 24,723 individuals and 13,682 businesses participated. Our sample of income tax returns filed by 170 individuals and 149 corporations that participated in tax amnesty programs of the 2 States had the following characteristics:

- Thirty-five Federal tax returns were not filed by 18 individuals. Ten of these 18 individuals reported over \$5.5 million in Federal taxable income on 20 tax returns filed with 1 State.<sup>3</sup> The IRS received Information Returns for 17 of the 20 tax returns due from these 10 individuals. However, 13 of the 17 State tax returns reported over \$2.6 million more in Federal taxable income than was reported to the IRS on Information Returns.<sup>4</sup> The remaining 8 taxpayers in the other State reported over \$1.2 million in gross income on 15 tax returns filed.<sup>5</sup> Twelve of the 15 tax returns reported almost \$700,000 more in gross income than was reported to the IRS on Information Returns.

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<sup>1</sup> An Implementing Agreement is an agreement that complements the basic Agreement on Coordination of Tax Administration executed by the IRS and a State tax agency and contains more detailed information.

<sup>2</sup> Under the Reverse Filing Match, the IRS will obtain State extracts and match them against the IRS' databases to identify taxpayers that are Federal nonfilers.

<sup>3</sup> See Appendix I, Step IV. A. for sample details.

<sup>4</sup> Information Returns are documents filed by payers and employers to report amounts paid to or received by individuals. The IRS uses Information Returns to determine those with the best potential for substantial net tax due, in selecting nonfiler cases to work. When the tax return cannot be secured from the taxpayer, it is prepared using these Information Returns. Information Returns are also prepared for corporations but are often not required for corporate payees.

<sup>5</sup> See Appendix I, Step IV. C. for sample details.



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- Fifty-two Federal tax returns were not filed by 31 corporations. Twenty-three corporations filed 35 tax returns with 1 State, reporting net income of over \$670,000.<sup>6</sup> The IRS received Information Returns for 6 of the 35 tax returns, but net income reported to the State exceeded amounts reported to the IRS by approximately \$82,000. The remaining 8 corporations filed 17 tax returns with the second State, paying a total of approximately \$37,000 in State income taxes.<sup>7</sup> The State's tax amnesty database did not provide the IRS with the amount of income reported. The IRS received Information Returns for only 3 of these tax returns, and total income reported on these Information Returns was only \$57,913.

We believe the IRS study's conclusion that the Reverse Filing Match would yield State tax amnesty information was premature. This Match and the means to automate it are still in the testing stage.

The IRS should fully use State tax amnesty information to ensure taxpayers also meet their Federal tax obligations. Some States conducting tax amnesty programs advised taxpayers that information disclosed by the taxpayer may be shared with the IRS. These taxpayers, who did not file Federal tax returns even though they were aware of their filing obligations, warrant special attention.

### *Recommendations*

We recommended the Commissioner, SB/SE Division, evaluate the current FedState exchange programs to determine whether State tax amnesty information will be obtained through the Reverse Filing Match or any other current program. If so, the Commissioner, SB/SE Division, should determine whether tax returns filed during State tax amnesty programs can be identified as such for use in IRS compliance programs. If not, the Commissioner should seek agreements with the States to separately obtain all State tax amnesty information. Not only should the data be used to supplement IRS compliance information, but IRS compliance programs should place emphasis on ensuring these taxpayers meet their Federal tax obligations.

### *Response*

The Commissioner, SB/SE Division, agreed with our recommendations. The office of Governmental Liaison and Disclosure (GLD) has established a multidivisional task team to determine whether the State tax amnesty information will be obtained through the Reverse Filing

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<sup>6</sup> See Appendix I, Step IV. D. for sample details.

<sup>7</sup> See Appendix I, Step IV. B. for sample details.



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Match or any other current FedState program. The team will analyze the State tax amnesty information to determine the best way to use the information in support of IRS compliance efforts from the perspective of both individual and business taxpayers. If the State tax amnesty information will not be obtained through a current FedState program, the office of GLD will determine the best method of requesting tax amnesty information from the States willing to share this information with the IRS.

The multidivisional task team will review the State tax amnesty information and explore systemic methods to leverage benefits, including matching against Federal filings, comparing to current Federal nonfilers, and determining the potential source of collection asset information. The National Fraud Program Office will assist in identifying potential fraud cases for appropriate action. Management's complete response to the draft report is included as Appendix V.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Curtis Hagan, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-3837.



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## *Background*

Tax amnesty programs are held to collect taxes owed from prior years and to place those who previously avoided taxation on the tax rolls. Over the past 23 years, at least 41 States and 2 cities have collected over \$5.7 billion from tax amnesty programs. To encourage taxpayers to participate, these programs generally forgave all civil and criminal penalties. They differed as to whether all or a portion of the interest was forgiven.

We have included a breakdown of the State tax amnesty programs provided by the Federation of Tax Administrators and supplemented with information from individual States' web sites in Appendix IV.<sup>1</sup>

The original objective of this review was to evaluate the Internal Revenue Service's (IRS) use of information from the State tax amnesty programs and to assess the potential benefits and risks of implementing a Federal tax amnesty program. Upon initiation of the audit, it became clear that we needed to concentrate on the effectiveness of the IRS' use of the information from State tax amnesty programs in IRS compliance efforts. We will address the benefits and risks of implementing a Federal tax amnesty program in a subsequent review.

This review of the IRS National Headquarters, Office of Communications and Liaison, in Washington, D.C., was performed primarily at the office of the Treasury Inspector General for Tax Administration in Holtsville, New York. Fieldwork was performed during the period February through June 2005.

The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

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<sup>1</sup> The Federation of Tax Administrators is an association of all tax agencies in the 50 States, the District of Columbia, and New York, New York. Its mission is to improve the quality of State tax administration by providing research and information exchange, training, intergovernmental and interstate coordination and by representing the interests of State tax administrators before Federal policymakers when appropriate.



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## *Results of Review*

### ***State Tax Amnesty Information Has Not Been Used As an Ongoing Tool to Help Ensure Compliance With Federal Tax Laws***

Information obtained by States during their tax amnesty programs could be used effectively to bolster IRS compliance efforts. This information has not been used by the IRS as an ongoing tool to help ensure compliance with Federal tax laws. Consequently, the IRS is missing a unique opportunity to address noncompliant taxpayers who have acknowledged their noncompliance with tax laws to State governments and who also owe Federal taxes.

The mission of the Small Business/Self-Employed (SB/SE) Division Communications, Liaison, and Disclosure function includes partnering with Federal, State and local governmental agencies to increase compliance, enforcement, and service to taxpayers. The Commissioner, SB/SE Division, recognized the potential value of State tax amnesty information as a tool to supplement IRS enforcement information and efforts. As a result, the SB/SE Division established a team to study the potential usefulness of State tax amnesty information. The team included representatives from the Nonfiler Program, Compliance Policy functions (campus and field), Centralized Delivery and Workload Selection and Delivery function, office of Governmental Liaison and Disclosure (GLD) (field), and External Liaison function staff. Although the study included considerable analysis of the tax amnesty data for individual taxpayers from two States, it did not fully explore the benefits of this information and its usefulness in IRS compliance programs.

#### ***An SB/SE Division study concluded that State tax amnesty information would not be effective in identifying nonfilers or underreported income***

The first part of the SB/SE Division study was a national survey of States under Implementing Agreements with the IRS to determine the extent to which the IRS already received State tax amnesty information.<sup>2</sup> The second phase of the study was to evaluate the data from two State tax amnesty programs. The mission of the study was limited, however, to the identification of previously unidentified nonfilers and underreporters. Also, the study did not address business

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<sup>2</sup> An Implementing Agreement is an agreement that complements the basic Agreement on Coordination of Tax Administration executed by the IRS and a State tax agency and contains more detailed information.





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taxpayers that participated in the State tax amnesty programs. Only tax amnesty information for individual taxpayers was evaluated during the study.

The IRS team compared the information for more than 2,500 unique tax amnesty participants from the first State against the Case Creation Nonfiler Identification Process system and the Discretionary Automated Examination system.<sup>3</sup>

The study found:

- Most States that responded to the national survey had not previously shared amnesty information with the IRS. Sixteen of 20 States that responded would be willing to share tax amnesty information with the IRS upon receipt of a valid written request.
- Sharing of State tax amnesty information was generally not addressed within existing IRS Implementing Agreements with the States.
- Only 2 of the tax amnesty participants were not included in the IRS nonfiler database, and 22 tax periods from these tax amnesty records were not previously identified and worked through normal IRS processes. Based on a sample selected to match income reported with Information Return Program income records,<sup>4</sup> no underreporting was found using the State data.
- Tax amnesty information for individual taxpayers from the second State was similarly analyzed with the same conclusions.

Based on the review of the individual tax return data, the study concluded that:

- Making one-time requests for State tax amnesty information would not be effective in identifying unknown nonfilers or in discovering underreported income.
- Requesting and evaluating additional State tax amnesty information on a State-by-State basis did not appear to be the best use of scarce IRS resources since another FedState initiative, the Reverse Filing Match,<sup>5</sup> would yield the same information in an automated environment.

The study recommended discontinuance of efforts to request and evaluate State tax amnesty information using written requests on a State-by-State basis.

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<sup>3</sup> The Case Creation Nonfiler Identification Process is a system that matches Information Return Program documents (see footnote 4) with the taxpayer account information stored on the IRS database to seek out taxpayers that fail to file tax returns. The Discretionary Automated Examination system is an EXCEL database that allows the automated processing of return classification without ordering unnecessary returns.

<sup>4</sup> Information Returns are documents filed by payers and employers to report amounts paid to or received by individuals. The Information Return Program processes these documents to an IRS file.

<sup>5</sup> Under the Reverse Filing Match, the IRS will obtain State extracts and match them against the IRS' databases to identify taxpayers that are Federal nonfilers.



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**Our review showed that tax amnesty information could be very useful**

Our audit found the State tax amnesty information could be used effectively to bolster IRS efforts for improving compliance. Individual taxpayers in 37 of the 43 States with an income tax must calculate the Federal Adjusted Gross Income or Federal Taxable Income to complete their State tax returns. Even in the other six States, where State income tax is computed independent of the Federal Adjusted Gross Income or Federal Taxable Income, taxpayers attest to the accuracy of “income” when they sign the State tax returns.

The IRS uses Information Returns (documents filed by payers and employers to report amounts paid to or received by individuals, sole proprietors, partnerships, or corporations<sup>6</sup>) to determine those with the best potential for substantial net tax due when selecting nonfiler cases to work. When the tax return cannot be secured from the taxpayer, it is prepared using these Information Returns.

We reviewed a sample of tax amnesty information from 2 States in which 24,723 individuals and 13,682 businesses participated. We found income reported by participants was often greater than the amount that had been reported to the IRS on Information Returns. Our sample of income tax returns filed by 170 individuals and 149 corporations that participated in the 2 State tax amnesty programs had the following characteristics:

- Thirty-five Federal tax returns were not filed by 18 individuals. Ten of these 18 individuals reported over \$5.5 million in Federal taxable income on 20 tax returns filed with 1 State.<sup>7</sup> The IRS received Information Returns for 17 of the 20 tax returns due from these 10 individuals. However, 13 of the 17 State tax returns reported over \$2.6 million more in Federal taxable income than was reported to the IRS on Information Returns (see Figure 1). The remaining 8 taxpayers in the other State reported over \$1.2 million in gross income on 15 tax returns filed.<sup>8</sup> Twelve of the 15 tax returns reported almost \$700,000 more in gross income than was reported to the IRS on Information Returns.

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<sup>6</sup> Information Returns are often not required when the payee is a corporation.

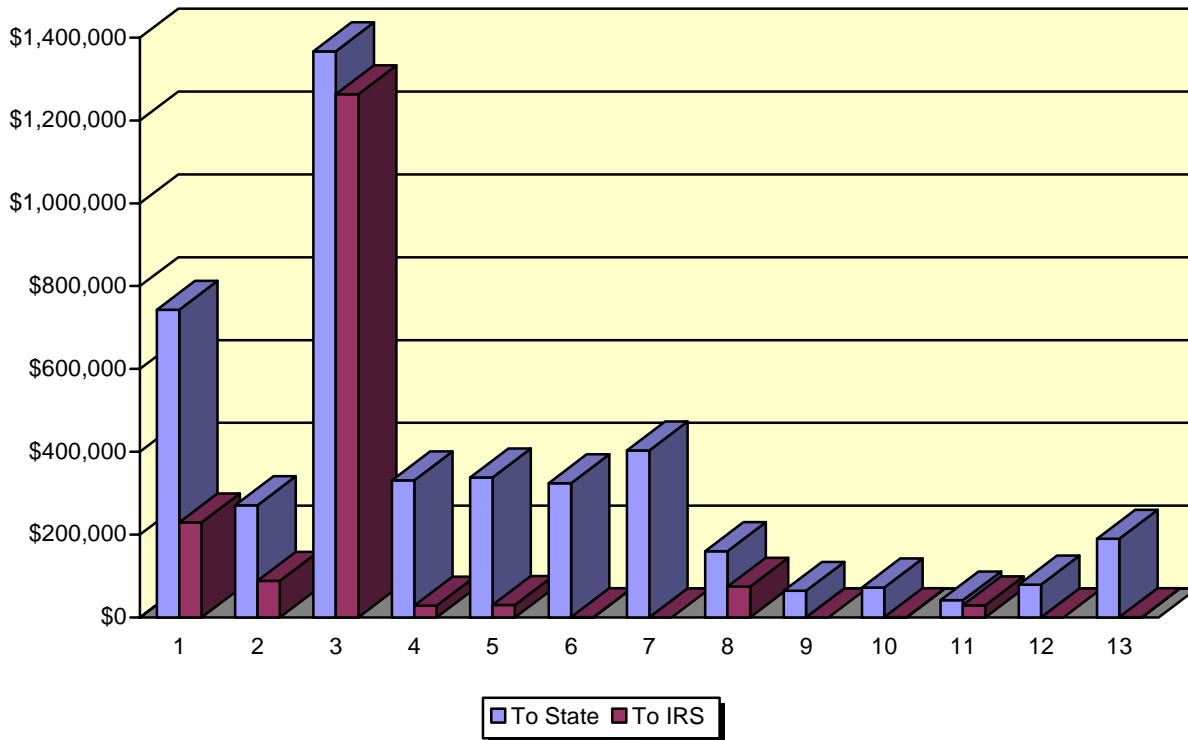
<sup>7</sup> See Appendix I, Step IV. A. for sample details.

<sup>8</sup> See Appendix I, Step IV. C. for sample details.



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**Figure 1: Federal Taxable Income Reported to the State vs. Income Reported to the IRS on Information Returns**



**State Tax Returns and IRS Information Returns**

*Source: Tax amnesty information from one State. In our judgmental sample of income tax returns filed by 71 individual taxpayers under the tax amnesty program in 1 State, 10 taxpayers failed to file 20 tax returns to report over \$5.5 million in Federal taxable income that was reported to the State. Thirteen of the 20 State tax returns (first column) reported over \$2.6 million more in Federal taxable income than was reported to the IRS on Information Returns (second column).*

- Fifty-two Federal tax returns were not filed by 31 corporations. Twenty-three corporations filed 35 tax returns with 1 State, reporting net income of over \$670,000.<sup>9</sup> The IRS received Information Returns for 6 of the 35 tax returns, but net income reported to the State exceeded amounts reported to the IRS by approximately \$82,000. The

<sup>9</sup> See Appendix I, Step IV. D. for sample details.



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remaining 8 corporations filed 17 tax returns with the second State, paying a total of approximately \$37,000 in State income taxes.<sup>10</sup> The State's tax amnesty database did not provide the IRS with the amount of income reported. The IRS received Information Returns, reporting income of \$57,913, for only 3 of these tax returns.

Information Returns filed with the IRS had reported minimal income for some of the taxpayer accounts appearing in State tax amnesty information. This may have influenced the determination of how the cases were worked. The outcome of the cases may have been different had the State tax amnesty information been taken into consideration. For example:

- One taxpayer filed returns for several years under the State's tax amnesty program but failed to file Federal tax returns for those tax years. Although the taxpayer reported income ranging from \$8,000 to over \$50,000 to the State, no Information Returns were filed with the IRS for those tax years and the IRS assessed no tax. The only Federal tax returns filed in over 10 years were prepared under the Substitute For Return program.<sup>11</sup> Also, the taxpayer's last name and address reported to the State (and to the IRS on Information Returns in more recent years) are different from those shown on IRS records of the taxpayer's account.
- The balance due in excess of \$60,000 for another Federal tax return, prepared under the IRS Substitute For Return program, was determined to be uncollectible. No tax return has been filed by the taxpayer or spouse since that time. However, income reported to the State for several subsequent years was \$30,000 to \$180,000 higher than the amounts reported on the Information Returns (in this case Wage and Tax Statement (Form W-2)) for the taxpayer and spouse.

Some taxpayers were listed in the State tax amnesty databases for multiple years. Furthermore, some taxpayer accounts "previously identified and being worked through the Service's [IRS'] normal processes" had been identified 4 to 5 years ago yet remained unresolved 2 years after the taxpayers participated in the State tax amnesty program.

### **The status of the Reverse Filing Match**

The IRS team concluded that requesting and evaluating additional State tax amnesty information on a State-by-State basis did not appear to be the best use of scarce resources since the Reverse Filing Match would yield the same information in an automated environment. However, the Reverse Filing Match, and the means to automate it, are still in the testing stage.

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<sup>10</sup> See Appendix I, Step IV. B. for sample details.

<sup>11</sup> The Substitute For Return program deals with taxpayers who have not filed tax returns voluntarily and for whom income information is available to substantiate a significant income tax liability.



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Results of a limited test conducted in Fiscal Year 2004 were very positive, with over \$1.5 million in tax realized from approximately 300 tax returns for 1 State. In that test, the IRS used copies of Federal tax returns attached to delinquent tax returns secured by the State to encourage taxpayers to file. Tax returns were prepared for those who did not. Multiple-year cases were referred to the Criminal Investigation function.

More extensive testing of the Reverse Filing Match has been initiated, but the results are not available at this time. Potentially, the Reverse Filing Match will be a good use for the State tax amnesty information. However, it is premature to expect this program to effectively use all of the available tax amnesty information because it is still being tested and excludes the use of tax amnesty information from businesses.

### **Benefits of using State tax amnesty information**

Sometimes taxpayers file State tax returns without filing Federal tax returns because they do not have the funds to pay both State and Federal taxes due. In addition, some risk suspension of licenses or permits if they do not file with the State. The IRS is missing out on taxpayer compliance information from the State tax amnesty programs that could prove very useful in its own enforcement programs. Benefits include the following:

- Identification of income received by self-employed nonfilers that is not currently reported on Information Returns sent to the IRS.
- Identification of income received by small business corporations (S corporations),<sup>12</sup> where filing noncompliance is at an unacceptably high level. Failure to file might circumvent scrutiny of income both at the corporate level and for the individual shareholders.
- Availability of current addresses for taxpayers the IRS could not locate.
- Availability of tax amnesty information without having to incur the costs borne by the States, such as the waiving of penalties and interest, disruption to other programs, and many other expenses.<sup>13</sup>

For current and future State tax amnesty programs, the IRS needs to determine (1) whether current FedState information exchanges and an IRS Reverse Filing Match will, in fact, capture State tax amnesty information and (2) whether FedState agreements need to specifically address the tax amnesty information.

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<sup>12</sup> A corporation that can avoid the corporate tax by electing to be taxed in a manner similar to partnerships.

<sup>13</sup> For example, the State of New York waived over \$100 million in penalties and interest on returns filed under its 2002-2003 tax amnesty program and spent over \$16 million in expenses to bring in \$527,479,783 (including known accounts receivables).



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The IRS should fully use State tax amnesty information to ensure participants also meet their Federal tax obligations. These are taxpayers that are admittedly noncompliant, often for multiple years. Also, some of the States conducting tax amnesty programs advised taxpayers that information disclosed by the taxpayers may be shared with the IRS. These taxpayers, who did not file Federal tax returns even though they were aware of their filing obligations, warrant special attention.

## ***Recommendations***

The Commissioner, SB/SE Division, should:

**Recommendation 1:** Analyze the current FedState exchange programs to determine whether State tax amnesty information will be obtained through the Reverse Filing Match or any other current program. If so, determine whether tax returns filed under State tax amnesty programs can be identified as such for use in IRS compliance programs.

**Management's Response:** The office of GLD has taken the lead to establish a multidivisional task team to determine whether State tax amnesty information will be obtained through the Reverse Filing Match or any other current FedState program. If so, the team will determine if tax returns filed under the State tax amnesty programs can be identified as such and will analyze and evaluate State tax amnesty information to determine the best way to use the information in support of IRS compliance efforts from the perspective of both individual and business taxpayers.

**Recommendation 2:** Seek agreements with the States to separately obtain all State tax amnesty information, if tax amnesty information is not obtained through current programs.

**Management's Response:** If the State tax amnesty information will not be obtained through the Reverse Filing Match or any other current FedState program, the office of GLD will determine the best method of requesting tax amnesty information from the States willing to share this information with the IRS. The method could be a specific request, a memorandum of understanding, or an addendum to Implementing Agreements with the States.

**Recommendation 3:** Supplement IRS compliance information with that from State tax amnesty programs. Once State tax amnesty information is obtained, place emphasis on ensuring these taxpayers also meet their Federal tax obligations.

**Management's Response:** The multidivisional task team led by the office of GLD will review the State tax amnesty information and explore systemic methods to leverage benefits, including matching against current Federal filings, comparing to current Federal nonfilers, and determining the potential source of collection asset information. In addition, the National Fraud Program Office will assist the multidivisional task team in



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identifying and classifying potential fraud cases as a result of the analysis of State tax amnesty program information and will take appropriate action in coordination with the IRS operating divisions.





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## Appendix I

### *Detailed Objective, Scope, and Methodology*

The overall objective of this review was to evaluate the effectiveness of the Internal Revenue Service's (IRS) use of information from the State tax amnesty programs. To accomplish this objective, we:

- I. Determined whether the results of the State tax amnesty programs were shared with the IRS by contacting the IRS Communications and Liaison, Customer Liaison Branch, and reviewing the consolidation of responses by States to a national survey performed under the IRS' study on the potential usefulness of State tax amnesty information.
- II. Determined why the IRS decided not to use this information by reviewing the testing and results of the IRS' study on the potential usefulness of State tax amnesty information.
- III. Determined, where possible, the benefit yield of tax amnesty programs to the States through research of the Federation of Tax Administrators and State web sites.<sup>1</sup>
- IV. Evaluated whether the IRS could have used more information available from the States or obtained more benefits from the information obtained. We compared the tax amnesty data provided by two States against the IRS' records of the taxpayers' accounts and available Information Returns received by the IRS.<sup>2</sup>
  - A. In 1 State that did not allow tax liabilities previously billed to be included in its tax amnesty program, 2,534 individual taxpayers filed 4,452 tax returns in the State tax amnesty program. We reviewed 89 tax returns reporting State tax in excess of \$10,000 filed by 71 individual taxpayers. We researched the IRS records to determine whether a Federal tax return had been filed and if so, compared the Federal taxable income reported to the IRS against the amount reported to the State. If no Federal tax return had been filed, we researched IRS records for available Information Returns or Case Creation Nonfiler Identification Process (CCNIP) records.<sup>3</sup>

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<sup>1</sup> The Federation of Tax Administrators is an association of all tax agencies in the 50 States, the District of Columbia, and New York City. Its mission is to improve the quality of State tax administration by providing research and information exchange, training, intergovernmental and interstate coordination and by representing the interests of State tax administrators before Federal policymakers when appropriate.

<sup>2</sup> Information Returns are documents filed by payers and employers to report amounts paid to or received by individuals. The Information Return Program processes these documents to an IRS file.

<sup>3</sup> The CCNIP is a system that matches Information Returns Program documents with the taxpayer account information stored on the IRS database to seek out taxpayers that fail to file tax returns.





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- We also reviewed the information for other years (where the State tax was not in excess of \$10,000) included in the State's tax amnesty program for these taxpayers.
- B. The tax amnesty data for this State included the State tax, but not the income, for 115 corporate tax returns filed by 49 taxpayers under the State's tax amnesty program. We researched the IRS' records to determine whether the Federal corporate tax returns had been filed and whether the IRS had Information Returns available for the tax returns not filed.
  - C. For a second State that included accounts receivable in its tax amnesty program, 22,189 individual taxpayers that participated in the State's tax amnesty program filed 31,790 State tax returns. We selected a random sample of 99 of 10,216 individual taxpayers participating in the State's tax amnesty program who filed 14,839 tax returns reporting gross income in excess of \$50,000 to the State. We did not include five tax returns that did not reflect a taxpayer identification number. We researched the IRS' records for the 167 tax returns (reporting any amount of income) included in the State's tax amnesty program for these 99 individual taxpayers to determine whether a Federal tax return had been filed. If a Federal tax return had been filed, we compared the gross income reported to the State against the income reported to the IRS and attempted to determine the explanation for any differences. If a tax return had not been filed, we researched IRS records for Information Returns or the CCNIP records.
  - D. In this second State, 13,633 corporations participating in the tax amnesty program filed 25,354 corporate income tax returns. We selected a random sample of 100 of 3,945 corporations that filed 5,975 income tax returns to report a positive income to the State. We researched the IRS' records for the 153 tax returns included in the State's tax amnesty program for these 100 corporate taxpayers to determine whether a Federal tax return had been filed. If no tax return had been filed, we researched the IRS' records for available Information Returns.



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**Appendix II**

*Major Contributors to This Report*

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Richard J. Dagliolo, Director

Robert K. Irish, Audit Manager

Dolores Castoro, Lead Auditor

Stephen A. Wybaillie, Senior Auditor



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## **Appendix III**

### *Report Distribution List*

Commissioner C  
Office of the Commissioner – Attn: Chief of Staff C  
Commissioner, Wage and Investment Division SE:W  
Deputy Commissioner, Small Business/Self-Employed Division SE:S  
Deputy Commissioner, Wage and Investment Division SE:W  
Director, Communications, Liaison, and Disclosure SE:S:CLD  
Acting Director, Strategy and Finance, Wage and Investment Division SE:W:S  
Acting Chief, Performance Improvement, Wage and Investment Division SE:W:S:PI  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Office of Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis RAS:O  
Office of Management Controls OS:CFO:AR:M  
Audit Liaisons:  
    Commissioner, Small Business/Self Employed Division SE:S  
    Commissioner, Wage and Investment Division SE:W  
    Acting Senior Operations Advisor, Wage and Investment Division SE:W:S



*Information From State Tax Amnesty  
Programs Could Bolster Compliance Efforts  
and Ensure Federal Tax Obligations Are Also Met*

**Appendix IV**

*State Tax Amnesty Programs*

*November 22, 1982 -- Present*

STATE	TAX AMNESTY PERIOD	MAJOR TAXES COVERED	ACCOUNTS RECEIVABLE INCLUDED	COLLECTIONS (\$ Millions) (a)	NOTES
ALABAMA	1/20/84 - 4/1/84	All	No	3.2	
ARIZONA	11/22/82 - 1/20/83 1/1/02 - 2/28/02 9/1/03 - 10/31/03	All Ind. Income All (m)	No No Unknown	6.0  73.0	
ARKANSAS	9/1/87 - 11/30/87 7/1/04 - 12/31/04	All All	No Unknown	1.7 0.8	(r)
CALIFORNIA	12/10/84 - 3/15/85 2/1/05 - 3/31/05	Ind. Income Sales Income, Franchise, Sales	Yes No Unknown	154.0 43.0 188.0	(c)(r)
COLORADO	9/16/85 - 11/15/85 6/1/03 - 6/30/03	All All	No Unknown	6.4 18.4	
CONNECTICUT	9/1/90 - 11/30/90 9/1/95 - 11/30/95 9/1/02 - 12/2/02	All All All	Yes Yes Unknown	54.0 46.2 109.0	
FLORIDA	1/1/87 - 6/30/87 1/1/88 - 6/30/88 7/1/03 - 10/31/03	Intangibles All All	No No Unknown	13.0 8.4 80.0	(b)
GEORGIA	10/1/92 - 12/5/92	All	Yes	51.3	
IDAHO	5/20/83 - 8/30/83	Ind. Income	No	0.3	
ILLINOIS	10/1/84 - 11/30/84 10/1/03 - 11/17/03	All(n) All	Yes Unknown	160.5 532.0	



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STATE	TAX AMNESTY PERIOD	MAJOR TAXES COVERED	ACCOUNTS RECEIVABLE INCLUDED	COLLECTIONS (\$ Millions) (a)	NOTES
IOWA	9/2/86 - 10/31/86	All	Yes	35.1	
KANSAS	7/1/84 - 9/30/84	All	No	0.6	
	10/1/03 - 11/30/03	All	Yes	53.7	
KENTUCKY	9/15/88 - 9/30/88	All	No	100.0	
	8/1/02 - 9/30/02	All	No	100.0	
LOUISIANA	10/1/85 - 12/31/85	All	No	1.2	
	10/1/87 - 12/15/87	All	No	0.3	
	10/1/98 - 12/31/98	All	No (k)	1.3	
	9/1/01 - 10/30/01	All	Yes	173.1	
MAINE	11/1/90 - 12/31/90	All	Yes	29.0	
	9/1/03 - 11/30/03	All	Unknown	37.6	
MARYLAND	9/1/87 - 11/2/87	All	Yes	34.6	(d)
	9/1/01 - 10/31/01	All	Yes	39.2	
MASSACHUSETTS	10/17/83 - 1/17/84	All	Yes	86.5	
	10/1/02 - 1/30/02	All	Yes	96.1	
	1/1/03 - 2/28/03	All	Yes	22.7	(c)(r)
MICHIGAN	5/12/86 - 6/30/86	All	Yes	109.8	
	5/15/02 - 6/30/02	All	Yes	81.9	(r)
MINNESOTA	8/1/84 - 10/31/84	All	Yes	12.1	
MISSISSIPPI	9/1/86 - 11/30/86	All	No	1.0	
	9/1/04 - 12/31/04	All	No	7.9	
MISSOURI	9/1/83 - 10/31/83	All	No	0.9	
	8/1/02 - 10/31/02	All	Yes	76.4	
	8/1/03 - 10/31/03	All	Yes	20.0	
NEBRASKA	8/1/04 - 10/31/04	All	No	7.5	
NEVADA	2/1/02 - 6/30/02	All	Unknown	7.3	
NEW HAMPSHIRE	12/1/97 - 2/17/98	All	Yes	13.5	
	12/1/01 - 2/15/02	All	Yes	13.5	
NEW JERSEY	9/10/87 - 12/8/87	All	Yes	186.5	
	3/15/96 - 6/1/96	All	Yes	359.0	
	4/15/02 - 6/10/02	All	Yes	276.9	



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STATE	TAX AMNESTY PERIOD	MAJOR TAXES COVERED	ACCOUNTS RECEIVABLE INCLUDED	COLLECTIONS (\$ Millions) (a)	NOTES
NEW MEXICO	8/15/85 - 11/13/85	All (e)	No	13.6	
	8/15/99 - 11/12/99	All	Yes	45.0	
NEW YORK	11/1/85 - 1/31/86	All (f)	Yes	401.3	
	11/1/96 - 1/31/97	All	Yes	253.4	
	11/18/02 - 1/31/03	All	Yes	582.7	
NEW YORK CITY	10/20/03 - 1/23/04	All (o)	Yes (p)	40.0	(c)(r)
NORTH CAROLINA	9/1/89 - 12/1/89	All (g)	Yes	37.6	
NORTH DAKOTA	9/1/83 - 11/30/83	All	No	0.2	
	10/1/03 - 1/31/04			6.9	
OHIO	10/15/01 - 1/15/02	All	No	48.5	
OKLAHOMA	7/1/84 - 12/31/84	Income, Sales	Yes	13.9	
	8/15/02 - 11/15/02	All (l)	Yes	38.8	(r)
PENNSYLVANIA	10/13/95 - 1/10/96	All	Yes	N.A.	(q)
RHODE ISLAND	10/15/86 - 1/12/87	All	No	0.7	
	4/15/96 - 6/28/96	All	Yes	7.9	
SOUTH CAROLINA	9/1/85 - 11/30/85	All	Yes	7.1	
	10/15/02 - 12/2/02	All	Yes	66.2	
SOUTH DAKOTA	4/1/99 - 5/15/99	All	Yes	0.5	
TEXAS	2/1/84 - 2/29/84	All (h)	No	0.5	
	3/11/04 - 3/31/04	All (h)	No	379.0	(r)
VERMONT	5/15/90 - 6/25/90	All	Yes	1.0	(c)
VIRGINIA	2/1/90 - 3/31/90	All	Yes	32.2	
	9/2/03 - 11/3/03	All	Yes	98.3	
WEST VIRGINIA	10/1/86 - 12/31/86	All	Yes	15.9	
	9/1/04 - 10/31/04	All	Unknown	10.4	
WISCONSIN	9/15/85 - 11/22/85	All	Yes (i)	27.3	
	6/15/98 - 8/14/98	All	Yes	30.9	
DIST. OF COLUMBIA	7/1/87 - 9/30/87	All	Yes	24.3	
	7/10/95 - 8/31/95	All (j)	Yes	19.5	

*Source: The Federation of Tax Administrators with additional entries from individual State web sites made by the Treasury Inspector General for Tax Administration*



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*Information From State Tax Amnesty  
Programs Could Bolster Compliance Efforts  
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**NOTES:**

- (a) Where applicable, figure includes local portions of certain taxes collected under the State tax amnesty program.
- (b) Does not include intangibles tax and drug taxes. Gross collections totaled \$22.1 million, with \$13.7 million in penalties withdrawn.
- (c) Preliminary figure.
- (d) Figure includes \$1.1 million for the separate program conducted by the Department of Natural Resources for the boat excise tax.
- (e) The severance taxes, including the six oil and gas severance taxes, the resources excise tax, the corporate franchise tax, and the special fuels tax were not subject to amnesty.
- (f) Availability of amnesty for the corporation tax, the oil company taxes, the transportation and transmissions companies tax, the gross receipts oil tax, and the unincorporated business tax restricted to entities with 500 or fewer employees in the United States on the date of application. In addition, a taxpayer principally engaged in aviation, or a utility subject to the supervision of the State Department of Public Service, was ineligible.
- (g) Local taxes and real property taxes were not included.
- (h) Texas does not impose a corporate or individual income tax. In practical effect, the amnesty was limited to the sales tax and other excise taxes.
- (i) Waiver terms varied depending upon the date the tax liability was assessed.
- (j) Does not include real property taxes. All interest was waived on tax payments made before July 31, 1995. After this date, only 50 percent of the interest was waived.
- (k) Exception for individuals who owed \$500 or less.
- (l) Except for property and motor fuel taxes.
- (m) All taxes except property, estate, and unclaimed property.
- (n) Does not include the motor fuel use tax.
- (o) All New York City (NYC) taxes administered by the NYC Department of Finance are covered except for Real Estate Tax. NYC Sales and Use Tax and NYC Resident Personal Income Tax also are not covered because they are administered by the New York State Department of Taxation and Finance.
- (p) Taxpayers under audit as of March 10, 2003, are ineligible; taxpayers with an existing installment agreement are ineligible; taxpayers under criminal investigation are ineligible; and taxpayers party to an administrative or court proceeding must withdraw as a condition of amnesty.
- (q) N.A. (not applicable): The amount collected is not available.
- (r) The amount was inserted in the chart by the Treasury Inspector General for Tax Administration. Amounts were obtained from the State web site, where available. In some cases, the amounts were preliminary and not the final amount.



*Information From State Tax Amnesty  
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**Appendix V**

*Management's Response to the Draft Report*



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

RECEIVED  
SEP 14 2005

September 14, 2005

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Kevin M. Brown *KMB*  
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report - Information from State Tax Amnesty  
Programs Could Bolster Compliance Efforts and Ensure Federal  
Tax Obligations are Also Met (Audit # 200530007)

We have reviewed your report and agree with the recommendations. We appreciate your acknowledgement that we have recognized the potential value of state tax amnesty information as a tool to supplement our enforcement efforts. The IRS places great value on the relationships it has cultivated with the states in the pursuit of mutual federal and state tax administration goals. IRS and the states both benefit from opportunities to share information and save government resources. We continue to look for opportunities to leverage federal and state resources to improve federal tax compliance.

You concluded that our determination regarding the usability of the Reverse Filing Match information was premature and warranted further consideration. We agree and will continue to evaluate the Reverse Filing Match program.

The report also pointed out, and we agree, that we did considerable analysis of state tax amnesty information for individual taxpayers but that we need to further explore the benefits of the information from the perspective of both individual and business taxpayers. We will further evaluate the usefulness of state tax amnesty information as a tool for federal tax compliance.

Finally, the report highlights the fact that current Implementing Agreements (IAs) with states generally do not address the sharing of state tax amnesty information. It is important to note that this alone does not preclude the regular sharing of tax amnesty information. However, we will consider instituting agreement provisions that specifically address the exchange of state tax amnesty information.

Our responses to your specific recommendations follow:





*Information From State Tax Amnesty  
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**RECOMMENDATION 1:**

Analyze the current exchange programs to determine whether the state tax amnesty information will be obtained through the Reverse Filing Match, or any other current program. If so, determine whether tax returns filed under state tax amnesty programs can be identified as such for use in IRS compliance programs.

**CORRECTIVE ACTION:**

Governmental Liaison and Disclosure (GLD) has taken the lead to establish a multi-divisional task team to determine whether amnesty information will be obtained through the Reverse Filing Match or any other current FedState program, and if so, determine if tax returns filed under state amnesty programs can be identified as such. The team will also analyze and evaluate state tax amnesty program data to determine how best to use it in support of IRS compliance efforts.

**IMPLEMENTATION DATE:**

March 31, 2006

**RESPONSIBLE OFFICIAL:**

Director, Governmental Liaison and Disclosure, SB/SE Division

**CORRECTIVE ACTION MONITORING PLAN:**

Director, Governmental Liaison, will advise the Director GLD, of any delays.

**RECOMMENDATION 2:**

If tax amnesty information is not obtained through current programs, seek agreements with the states to separately obtain all state tax amnesty information.

**CORRECTIVE ACTION:**

If state tax amnesty information will not be obtained through the Reverse Filing Match or any other current FedState program, Governmental Liaison and Disclosure will determine the best method of requesting amnesty information from states, whether via specific request, memorandum of understanding, or addendum to Implementing Agreements with states that wish to share state tax amnesty information with IRS.

**IMPLEMENTATION DATE:**

March 31, 2006

**RESPONSIBLE OFFICIAL:**

Director, Governmental Liaison and Disclosure, SB/SE Division

**CORRECTIVE ACTION MONITORING PLAN:**

Director, Governmental Liaison, will advise the Director, GLD, of any delays



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*Information From State Tax Amnesty  
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**RECOMMENDATION 3:**

Supplement IRS compliance information with that from state tax amnesty programs. Once state tax amnesty information is obtained, place emphasis on ensuring that these taxpayers also meet their Federal tax obligations.

**CORRECTIVE ACTION:**

The multi-divisional task team led by GLD will review state amnesty information and explore systemic methods to leverage benefits, including matching against current federal filings, comparing to current federal nonfilers, and determining the potential source of collection asset information. In addition, the National Fraud Program Office will assist the multi-functional task team in identifying and classifying potential fraud cases as a result of the analysis of state amnesty program data and will take appropriate action in coordination with IRS' operating divisions.

**IMPLEMENTATION DATE:**

August 31, 2006

**RESPONSIBLE OFFICIAL:**

Director, Governmental Liaison and Disclosure, SB/SE Division

**CORRECTIVE ACTION MONITORING PLAN.**

Director, Governmental Liaison, will advise the Director, GLD, of any delays in implementation of the corrective action.

If you have any questions, please call me at (202) 622-0600 or Beth Tucker, Director SB/SE Communications, Liaison and Disclosure at (202) 283-7407.