

GAO Highlights

Highlights of [GAO-22-104180](#), a report to the Ranking Member, Committee on the Judiciary, U.S. Senate

Why GAO Did This Study

Tax evasion schemes involving offshore insurance are complex and resource-intensive for IRS to pursue, making it important for IRS to conduct compliance programs effectively.

GAO was asked to review how IRS conducts enforcement on offshore insurance compliance issues. This report evaluates to what extent IRS (1) reviews its guidance on offshore insurance to ensure that the guidance has its intended effect; (2) aligns oversight of its audit activities on taxpayers who may be abusing micro-captive insurance tax shelters with IRS audit policies and guidance; and (3) reviews its investigation activities on promoters who market abuses of offshore insurance tax shelters.

GAO reviewed IRS procedures on issuing guidance and on reviews of audits and promoter investigations, reviewed files on audits related to micro-captive insurance tax schemes, interviewed IRS officials, and compared IRS procedures with IRS policies and selected federal standards for internal control.

What GAO Recommends

GAO is making seven recommendations to improve how IRS oversees, through managerial reviews and independent quality reviews, its taxpayer audits and promoter investigations involving micro-captive insurance arrangements. IRS disagreed with the recommendations, stating that its current procedures are sufficient and citing resource constraints. However, GAO maintains that IRS's procedures should be refined and can be done so with minimal use of resources.

View [GAO-22-104180](#). For more information, contact Jessica Lucas-Judy at (202) 512-6806 or lucasjudj@gao.gov.

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ABUSIVE TAX SCHEMES

IRS Could Improve Its Reviews of Offshore Insurance Audits and Investigations

What GAO Found

To encourage voluntary compliance with tax laws concerning offshore insurance arrangements, the Internal Revenue Service (IRS) uses feedback from internal stakeholders and the public to review and modify applicable guidance. Offshore insurance has legitimate uses but also can be structured to hide U.S. taxpayers' assets or falsely claim tax benefits. Treasury and IRS have opportunities to better solicit public input on certain guidance, including for offshore insurance, as GAO recommended in its April 2021 report. Treasury neither agreed nor disagreed with the recommendation, but GAO maintains that the recommendation remains valid.

One offshore insurance issue that IRS has prioritized with enforcement is micro-captive insurance arrangements—that is, when small insurance companies insure related business entities. For example, micro-captive insurance has been included on IRS's "Dirty Dozen" tax schemes list. To ensure micro-captive insurance audits are conducted properly, IRS generally uses two approaches:

- **Managerial reviews:** These consist of various types of written reviews, including in-process case reviews and workload reviews, among others, performed by the managers overseeing the audit.
- **Quality reviews:** These are conducted by independent reviewers outside of the audit work-stream to ensure that all processes meet IRS's standards.

IRS officials said that current oversight practices were sufficient to ensure that micro-captive audits were conducted accurately. For example, IRS cited that from fiscal years 2016 through 2020, the Small Business and Self Employed Division's (SB/SE) managerial reviews found that performance on attributes of micro-captive insurance audits were conducted appropriately about 97 percent of the time, compared to about 92 percent for all audits in general.

However, IRS's application of its review approaches could be enhanced. For example, SB/SE's managers have little guidance in the Internal Revenue Manual for when an audit should be subjected to managerial review and Large Business and International Division (LB&I) managers lack systems through which to record and analyze certain managerial reviews. By clarifying guidance and establishing a formal review system, SB/SE and LB&I would have better assurance that they are effectively auditing micro-captive insurance.

IRS also investigates whether promoters of micro-captive insurance schemes violate tax law. IRS's oversight of promoter investigations has no systematic method that would enable IRS to evaluate the effectiveness of its micro-captive promoter investigation program. For example, SB/SE lacks a systematic method to identify micro-captive promoter investigations for quality review. From fiscal years 2016 through 2020, LB&I did not apply quality reviews to any micro-captive insurance promoter investigations. Conducting formal reviews more systematically would better assure the quality of IRS's promoter investigations on micro-captive arrangements.