

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

March 12, 2010

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION

Michael R. Phillips

FROM:

Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT:

Final Audit Report – Lien Determinations Were Untimely or Not Made
Appropriately for Over \$1.4 Billion in Delinquent Taxes
(Audit #200930014)

This report presents the results of our review to determine whether Internal Revenue Service (IRS) policies and procedures for lien determinations protect the Government's interest and encourage compliance while ensuring fair and equitable treatment of taxpayers. This audit was a followup review to our report *The Internal Revenue Service Should Modify Its Federal Tax Lien Practices to Treat Taxpayers More Equitably and Better Protect the Government's Interest*.¹ This audit was included in our Fiscal Year 2009 Annual Audit Plan under the major management challenge of Tax Compliance Initiatives.

Impact on the Taxpayer

The IRS protects its claims against taxpayers who owe delinquent taxes by filing Federal Tax Liens (liens), which establishes the IRS' priority among secured creditors for the taxpayers' equity. However, lien determinations were not appropriately made or were made late for more than \$1.4 billion in delinquent taxes. Failure to protect the Government's interest on taxes that are owed creates an unfair burden on taxpayers who properly pay their taxes in full and on time.

¹ Reference Number 2002-30-106, dated June 5, 2002.

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Abbreviations

ACS	Automated Collection System
CFf	Collection Field function
ICS	Integrated Collection System
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
RO	Revenue Officer
SB/SE	Small Business/Self-Employed
TIGTA	Treasury Inspector General for Tax Administration

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Background

When initial contact between the Internal Revenue Service (IRS) and a taxpayer does not result in the successful collection of an unpaid tax, the IRS has the authority to make a determination to protect the Government's interests by attaching a claim to the taxpayer's assets for the amount of unpaid tax.¹ This claim is referred to as a Notice of Federal Tax Lien, and the following must occur for a lien notice to be filed:

- An assessment must have been made.
- A demand for payment must have been made.
- The taxpayer must have neglected or refused to pay.

The decision to file a lien notice is not an enforcement action because it does not authorize the IRS to take possession of any assets or deprive the taxpayer of the use of the assets. A lien simply protects the Government's interest by publicly recording the debt owed by the taxpayer as a notice to possible future creditors. The lien attaches to property currently owned and to property the taxpayer may acquire in the future. Therefore, a lien may be filed even though specific assets have not been identified.

***A lien protects the Government's
interest and establishes its priority
among other secured creditors.***

A lien notice may prevent taxpayers from selling assets with clear title or obtaining additional financing without payment of their tax debts.

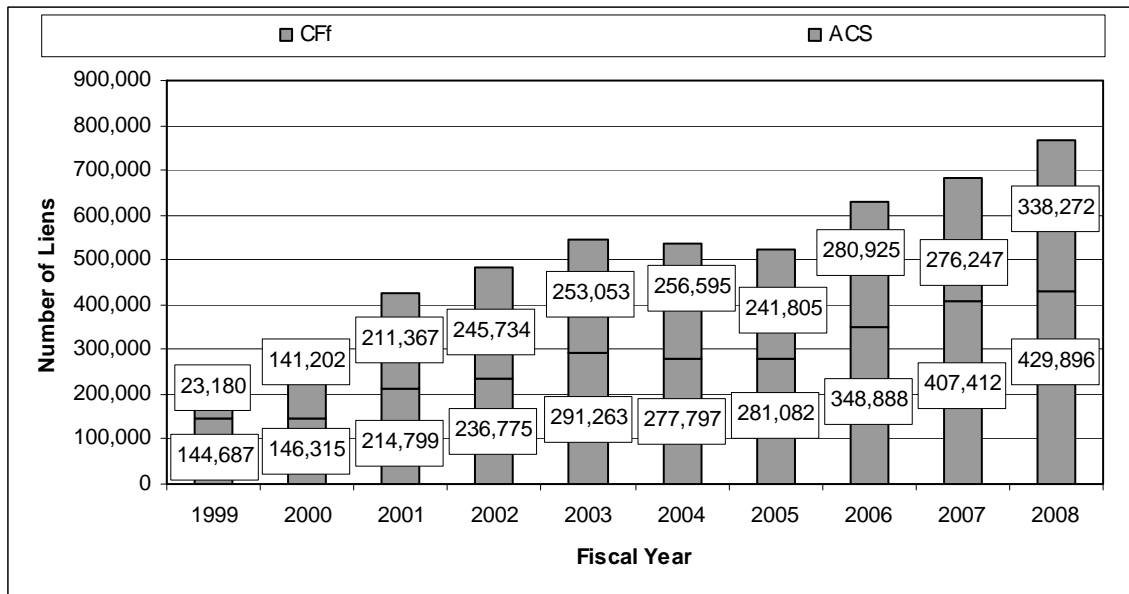
The IRS has been increasing the number of Federal Tax Liens (liens) it files to protect the Government's interest over the last several years. Figure 1 shows the total number of liens increased through Fiscal Year 2003, decreased slightly in Fiscal Years 2004 and 2005, and increased each subsequent year. From Fiscal Year 2002 to Fiscal Year 2008, the number of liens filed originating in the Collection Field function² (CFf) increased from 236,775 to 429,896 (82 percent) and in the Automated Collection System (ACS) from 245,734 to 338,272 (38 percent).

¹ Internal Revenue Code Section 6321 (1994).

² See Appendix V for a glossary of terms.

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Figure 1: Number of Liens Filed From Fiscal Years 1999 to 2008



Source: Prior Treasury Inspector General for Tax Administration (TIGTA) report.³

Depending on the type and amount of tax liability, some delinquent taxpayer accounts are assigned to the ACS, where contact is generally initiated by the taxpayer and where employees do not maintain a personal inventory of cases. Cases that are not resolved by or assigned to the ACS are sent to the Cff for contact by revenue officers (RO). ROs generally maintain a caseload of assigned cases and initiate contact with taxpayers. Both ACS and Cff employees have the authority to make a determination of whether or not to file a lien notice.

All cases assigned to the Cff are controlled on the Integrated Collection System (ICS). Upon assignment of the case in the ICS, the system automatically calculates a due date for initial contact. The ICS also generates a lien determination due date at this time. If the RO has not recorded a lien determination by this due date or has not extended the determination date, the ICS gives the RO a lien determination reminder notice. The ICS case summary screen for each taxpayer account also displays the status of the lien determination for each module, showing whether a lien has been filed or requested, the determination date was extended, a nonfiling determination was made, or no action has been taken regarding a lien determination.

Cff group managers use the ENTITY Case Management System (Entity system) to ensure that lien determinations are being made properly. The Entity system is a versatile tool that allows managers to extract and organize information about case activity and casework quality. The

³ Trends in Compliance Activities Through Fiscal Year 2008 (Reference Number 2009-30-082, dated June 10, 2009).

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information in the Entity system comes both from day to day recordation of employees' activities and from Integrated Data Retrieval System account information channeled through the ICS. The system offers both pre-established and customizable queries, several sort options, and preprogrammed reports. These tools allow the user a great deal of flexibility in requesting data from the system.

This audit was a followup review to our report *The Internal Revenue Service Should Modify Its Federal Tax Lien Practices to Treat Taxpayers More Equitably and Better Protect the Government's Interest*.⁴ The prior report determined that liens were being filed to protect the Government's interest in a large portion of the CFf cases that meet the criteria, but were not always filed in accordance with procedures. In addition, CFf managers were not using the Entity system to monitor lien determinations on open cases assigned to ROs. The audit also determined that the IRS was not filing liens against a substantial number of delinquent accounts closed as excess inventory (shelved).

The review was performed at the Philadelphia ACS call site located at the Philadelphia, Pennsylvania, Campus, the CFf groups located in Phoenix, Arizona, and Baltimore, Maryland, and at the Small Business/Self-Employed (SB/SE) Division Headquarters in New Carrollton, Maryland, during the period April 2009 through November 2009. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

⁴ Reference Number 2002-30-106, dated June 5, 2002.

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Recommendations

The Director, Collection, SB/SE Division, should:

Recommendation 1: Establish procedures for group managers to use the Entity system as a proactive tool in ensuring lien determinations are made timely. For example, managers could produce reports that show how many days have elapsed since initial contact with the taxpayer was attempted.

Management's Response: The IRS agreed with this recommendation and has requested enhancements to the Entity system lien report that will improve managers' ability to identify those cases without a lien filing and ensure lien determinations are timely.

Recommendation 2: Request programming changes to enable the Entity system lien reports to identify subsequent modules. For example, tying the lien report and lien query to taxpayer contact and the most recent calendared touch on a module may assist managers in proactively identifying situations where a lien determination has not been made.

Management's Response: IRS management agreed with this recommendation and an enhancement to the Entity system has been requested as described in their response to Recommendation 1.

Recommendation 3: Request programming changes to the ICS to ensure action is taken in response to the ICS lien determination reminder notifications.

Management's Response: IRS management agreed with the premise of this recommendation, but believes the Entity system enhancements that have been requested in response to Recommendation 1 will increase management oversight and followup, which will be more effective.

Recommendation 4: Ensure guidance and respective IRM sections are consistent between employment tax and nonemployment tax subsequent modules.

Management's Response: IRS management agreed with this recommendation and has published updated guidance in the IRM.

Recommendation 5: Request programming changes to the ICS to ensure lien determination reminder notifications are sent to ROs for subsequent modules, in accordance with the guidance established in Recommendation 4.

Management's Response: IRS management agreed with this recommendation and the change to the ICS has been implemented.

Recommendation 6: Ensure lien determinations are completed on the 210 modules with no lien determinations that we identified at the 2 CFf locations.

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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to determine whether IRS policies and procedures for lien determinations protect the Government's interest and encourage compliance while ensuring fair and equitable treatment of taxpayers. This audit was a followup review to our report, *The Internal Revenue Service Should Modify Its Federal Tax Lien Practices to Treat Taxpayers More Equitably and Better Protect the Government's Interest*.¹ To accomplish our objective, we:

- I. Evaluated IRS policies, procedures, goals, and monitoring of the lien program.
 - A Reviewed revisions to IRM procedures and other guidance issued.
 - B Assessed the IRS' corrective actions in response to the prior TIGTA report by reviewing Joint Audit Management Enterprise System documents and management responses to evaluate whether the corrective actions were timely and effectively implemented.
 - C Determined the goals of the lien program and methods used to monitor the program based on a review of IRS lien filing documentation, lien cost data, and interviews of executives and analysts in the SB/SE Division Compliance function. We also:
 1. Analyzed Collection function reports to determine the number of liens filed by the CFF² and the ACS for Fiscal Years 2002 to 2008.
 2. Obtained IRS cost data from the Automated Financial System to determine annual expenditures for lien fees for Fiscal Years 2002 to 2008.
 - D Contacted the IRS Office of Research Analysis and Statistics to discuss any studies performed of the lien program since our prior review and any current or planned lien studies.
- II. Established the validity of the ICS, ACS, and Taxpayer Service and Returns Processing Categorization data being used in our review.
 - A Established the completeness of ICS and ACS open case data by reconciling information from a selected number of cases to Integrated Data Retrieval System Master File data.

¹ Reference Number 2002-30-106, dated June 5, 2002.

² See Appendix V for a glossary of terms.

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planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective: the SB/SE Division Collection function's policies, procedures, and practices for documenting lien determinations in ICS case histories and Collection function group managers' review of Entity system reports to identify when lien determinations have not been made timely. We evaluated these controls by interviewing management, reviewing Entity system reports, and reviewing a sample of the ICS case histories for open taxpayer modules from two CFf offices.

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Appendix II

Major Contributors to This Report

Margaret E. Begg, Assistant Inspector General for Audit (Compliance and Enforcement Operations)

Carl Aley, Director

Timothy Greiner, Audit Manager

Curtis Kirschner, Lead Auditor

Michael Della Ripa, Auditor

Cristina Johnson, Auditor

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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Collection Policy, Small Business/Self-Employed Division SE:S:C:CP
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 Internal Control OS:CFO:CPIC:IC
Audit Liaison: Commissioner, Small Business/Self-Employed Division SE:S

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Appendix V

Glossary of Terms

Automated Collection System - A computerized call site inventory system that maintains balance due accounts and return delinquency investigations. ACS function employees enter all of their case file information (online) on the ACS.

Campus - The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

Collection Field function - Units in the Area Offices consisting of ROs who handle personal contacts with taxpayers to collect delinquent accounts or secure unfiled tax returns.

Currently Not Collectible - Taxpayers who are unable to pay their balance due may have their accounts temporarily placed in a currently not collectible status until their financial conditions change. Penalties and interest continue to accrue until the balance is paid in full.

Data Center Warehouse - A TIGTA function responsible for obtaining, storing, and securing numerous IRS data files, as well as developing interfaces allowing users to access the data.

Entity Case Management System - A tool that allows SB/SE Division Collection function group managers to extract and organize information about case activity and casework quality. The system offers both preprogrammed and user programmable queries, several sort options, and preprogrammed reports. This allows the user a great deal of flexibility in requesting data from the system. The information in the Entity system comes both from the day to day recordation of employees' activities and from Integrated Data Retrieval System account information channeled through the ICS. This information, together with information routed to the system from the Integrated Data Retrieval System through the ICS, creates a unique database which combines employee casework activity, employee time, and taxpayer account information.

Integrated Collection System - The IRS computer system with applications designed around each of the main collection tasks, such as opening a case, assigning a case, building a case, performing collection activity, and closing a case. The ICS is designed to provide management information, create and maintain case histories, generate documents, and allow online approval of case actions.

Integrated Data Retrieval System - The IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.

Master File - The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

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Module - Refers to one specific tax return filed by the taxpayer for one specific tax period (year or quarter) and type of tax.

Nonfiling lien determinations - A lien determination that results in no lien being filed.

Queue - An automated holding file for unassigned inventory of delinquent cases for which the Collection function does not have enough resources to immediately assign for contact.

Revenue Officer - Employees in the CFF who attempt to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses (formerly known as service centers) or the ACS.

Taxpayer Delinquent Account - A balance due account of a taxpayer. A separate Taxpayer Delinquent Account exists for each tax period.

Taxpayer Service and Returns Processing Categorization - A monthly extract from the IRS main computer files of all accounts with a balance due as of the date of the extract. Accounts are categorized for statistical analyses according to their current collection status.

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Appendix VI

Management's Response to the Draft Report

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