
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



***Problems Persist When Processing
Undelivered Lien Notices and Notifying
Taxpayers' Representatives***

May 29, 2012

Reference Number: 2012-30-057

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.

Redaction Legend:

1 = Tax Return/Return Information

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HIGHLIGHTS

PROBLEMS PERSIST WHEN PROCESSING UNDELIVERED LIEN NOTICES AND NOTIFYING TAXPAYERS' REPRESENTATIVES

Highlights

Final Report issued on May 29, 2012

Highlights of Reference Number: 2012-30-057 to the Internal Revenue Service Commissioners for the Small Business/Self-Employed Division and the Wage and Investment Division.

IMPACT ON TAXPAYERS

After filing Notices of Federal Tax Lien, the IRS must notify the affected taxpayers in writing, at their last known address, within five business days of the lien filings. However, as noted in previous audits, the IRS did not always follow its own internal guidelines for notifying taxpayer representatives of the filing of lien notices. Therefore, some taxpayers may have had their rights violated when the IRS did not notify their representatives of lien filings.

WHY TIGTA DID THE AUDIT

TIGTA is required by law to determine annually whether lien notices issued by the IRS comply with the legal guidelines in Internal Revenue Code Section 6320 and related guidance in the Federal Tax Liens Handbook.

WHAT TIGTA FOUND

TIGTA reviewed a statistically valid sample of 105 Notices of Federal Tax Lien (NFTL) filed for the 12-month period ending June 30, 2011, and determined that the IRS mailed taxpayers lien notices in a timely manner as required by Internal Revenue Code Section 6320.

However, the IRS did not always follow its own regulations for notifying taxpayers' representatives of the filing of the NFTLs. IRS regulations require taxpayer representatives be given copies of all correspondence issued to the taxpayer. For four (18 percent) of the 22 sample cases for which the taxpayer had an authorized representative, the IRS did not notify the taxpayer's representative of the NFTL. TIGTA

estimated that 43,817 taxpayers may have been adversely affected because the IRS did not follow requirements to notify the taxpayers' representatives of the taxpayers' rights related to liens.

Additionally, when an initial lien notice is returned undelivered and a different address is available for the taxpayer, the IRS does not always meet its statutory requirement to send the lien notice to the taxpayer's last known address. From a judgmental sample of 250 undelivered lien notices, TIGTA identified four cases for which a new lien notice should have been sent to the taxpayer's updated address because IRS systems reflected the updated address prior to the lien preparation. These cases could involve legal violations because the IRS did not meet its statutory requirement to send lien notices to the taxpayer's last known address.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Directors, Enterprise Collection Strategy and Campus Compliance Services, Small Business/Self-Employed Division: 1) work with the Director, Compliance, Wage and Investment Division, to improve the controls and oversight for the processing of undelivered lien notices to ensure they are researched timely, and 2) ensure the use of undelivered lien notice mail status is consistent in the procedures for the Automated Collection System and the Collection Field function.

The IRS agreed with our recommendations and plans to 1) make changes to the respective Internal Revenue Manuals to improve documentation and support the timely resolution of undeliverable notices, and 2) evaluate the use of nonstatutory codes against resource demands to determine if implementation is feasible. However, in its response the IRS included general comments about taxpayer rights that TIGTA believes warrant additional comment. The IRS's comments and our response are included in the transmittal memorandum for the final report.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

May 29, 2012

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION
COMMISSIONER, WAGE AND INVESTMENT DIVISION

Margaret E. Luzzo

FROM: (for) Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Problems Persist When Processing Undelivered
Lien Notices and Notifying Taxpayers’ Representatives
(Audit # 201230001)

This report presents the results of our review to determine whether liens issued by the Internal Revenue Service (IRS) comply with legal requirements set forth in Internal Revenue Code (I.R.C.) Section (§) 6320 (a)¹ and related guidance in the Federal Tax Liens Handbook. The Treasury Inspector General for Tax Administration is required by law to determine annually whether lien notices issued by the IRS comply with the legal guidelines in I.R.C. § 6320.² This audit is included in our Fiscal Year 2012 Annual Audit Plan and addresses the major management challenge of Taxpayer Protection and Rights.

In their response to the report, IRS management concurred with our outcome measures but included some comments and assertions about our report that we believe warrant additional comment. We have included portions of management’s response and our related comments below.

Management’s Response: The IRS disagreed that any failure to send a lien notice to taxpayer representatives jeopardizes the taxpayers’ rights. In each of the four instances cited for which the taxpayer representative was not provided a notice, the lien notice was timely sent to the taxpayer, thus affording full rights of appeal.

¹ 26 U.S.C. § 6320(a) (Supp V. 2011).

² 26 U.S.C. § 7803(d)(1)(A)(iii) (Supp. V 2011).



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Office of Audit Comment: Taxpayers have a right to have representatives notified of a lien filing. As stated in the report, Department of the Treasury regulations (§ 601.506)³ provide that notices are required to be given to recognized taxpayer representatives. We identified instances in which the IRS did not send a lien notice to taxpayer representatives, thereby resulting in a potential violation of the taxpayers' right to have an authorized representative notified of the filing of a lien.

Management's Response: The IRS disagreed with the statement that the taxpayers were not provided a copy of the lien notice because in each of the four cases identified a notice was subsequently reissued to the more current address for the taxpayer and the right to appeal was extended accordingly.

Office of Audit Comment: The IRS did not comply with the statutory requirement of providing a lien notice to the taxpayer's last known address within five business days of filing the lien. Furthermore, the IRS did not reissue a lien notice to the four taxpayers' more current address until we notified them that the original lien notice was not sent to the taxpayers' last known address.

Management's complete response to the draft report is included as AppendixVIII.

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 Margaret E. Begg, Assistant Inspector General for Audit (Compliance and Enforcement Operations), at (202) 622-8510.

³ 26 C.F.R. § 601.506.



***Problems Persist When Processing Undelivered
Lien Notices and Notifying Taxpayers' Representatives***

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Abbreviations

ACS	Automated Collection System
ALS	Automated Lien System
CAF	Centralized Authorization File
FY	Fiscal Year
ICS	Integrated Collection System
IDRS	Integrated Data Retrieval System
I.R.C.	Internal Revenue Code
IRS	Internal Revenue Service
NFTL	Notice of Federal Tax Lien
SB/SE	Small Business/Self-Employed
TIGTA	Treasury Inspector General for Tax Administration



Problems Persist When Processing Undelivered Lien Notices and Notifying Taxpayers' Representatives

Background

The Internal Revenue Service (IRS) attempts to collect Federal taxes due from taxpayers by sending letters, making telephone calls, and meeting face-to-face with taxpayers. The IRS has the authority to attach a claim,¹ commonly referred to as a Federal Tax Lien, to the taxpayer's assets for the amount of unpaid tax when the taxpayer neglects or refuses to pay. The IRS files a Notice of Federal Tax Lien (NFTL)² in appropriate local government offices so that interested parties are notified that a lien exists.

Since January 19, 1999, Internal Revenue Code (I.R.C.) Section (§) 6320³ has required the IRS to notify taxpayers, in writing, within five business days of the filing of an NFTL. The IRS is required to notify taxpayers the first time an NFTL is filed for each tax period. The lien notice⁴ is used for this purpose and advises taxpayers that they have 30 calendar days, after that five-day period, to request a hearing with the IRS Appeals office. The lien notice indicates the date on which this 30-day period expires.

***Upon receiving a lien notice,
the taxpayer has 30 calendar
days to request a hearing
with IRS Appeals.***

The law also requires that the lien notice explain, in simple terms, the amount of unpaid tax, administrative appeals available to the taxpayer, and provisions of the law and procedures relating to the release of liens on property. The lien notice must be given in person, left at the taxpayer's home or business, or sent by certified or registered mail to the taxpayer's last known address.⁵

Most lien notices are mailed to taxpayers by certified or registered mail rather than being delivered in person. The IRS Automated Lien System (ALS) generates a certified mail list which identifies each notice that is to be mailed. The notices and a copy of the certified mail list are delivered to the U.S. Postal Service. A U.S. Postal Service employee ensures that all notices are accounted for, date stamps the list, and returns a copy to the IRS. The stamped certified mail list is the only documentation the IRS has that certifies the date on which the notices were mailed. A synopsis of the IRS collection and NFTL processes is included in Appendix V. Depending on employee access, NFTL requests can be generated using one of three IRS

¹ 26 U.S.C. § 6321 (Supp V. 2011).

² IRS Form 668(Y)(c), *Notice of Federal Tax Lien* (Rev. Oct. 1999), Cat. No. 60025X.

³ 26 U.S.C. § 6320 (Supp V. 2011).

⁴ IRS Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320* (Rev. Mar. 2009), Cat. No. 26767L.

⁵ The last known address is the one shown on the most recently filed and properly processed tax return, unless the IRS received notification of a different address.

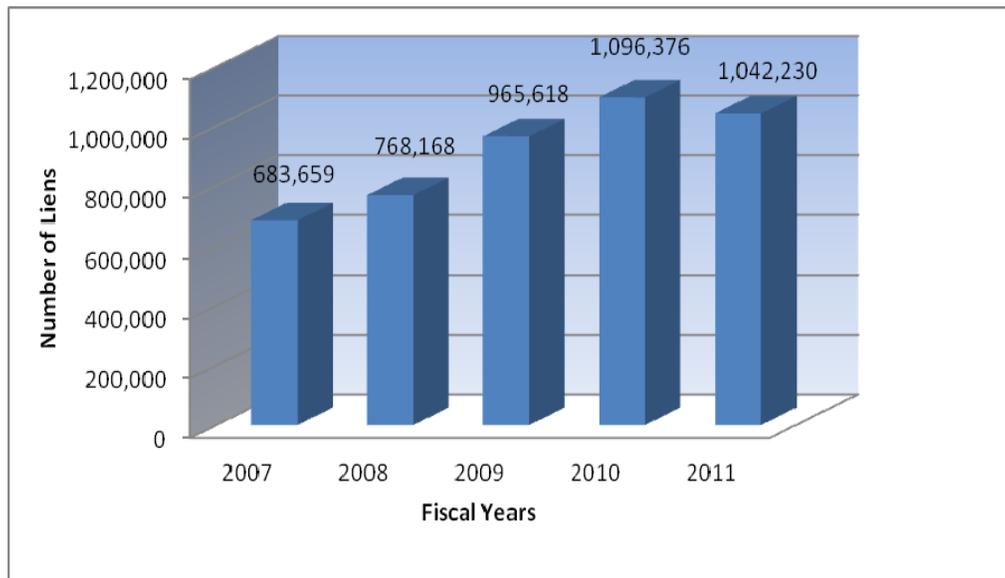


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systems: 1) the Integrated Collection System (ICS), 2) the Automated Collection System (ACS), or 3) the ALS. Appendix VI provides a description of IRS computer systems used in the mailing of lien notices.

As shown in Figure 1, the IRS has increased the number of NFTLs it has filed to protect the Federal Government's interest by 52 percent since Fiscal Year (FY) 2007.

Figure 1: Number of NFTLs Filed From FYs 2007–2011



Source: IRS Data Books published in FYs 2007 through 2011.

The Treasury Inspector General for Tax Administration (TIGTA) is required to determine annually whether, when filing NFTLs, the IRS complied with the law regarding the notifications of affected taxpayers and their representatives.⁶ This is our fourteenth annual audit to determine whether the IRS complied with the legal requirements of I.R.C. § 6320 and its own related internal guidelines for mailing lien notices. In prior years, we reported that the IRS had not yet achieved full compliance with the law and its own internal guidelines. As repeat findings, we identified potential violations of taxpayers' rights because the IRS did not timely notify their representatives. In addition, our review of a judgmental sample of undelivered lien notices found potential violations of taxpayer rights when the IRS did not use the taxpayer's last known address.

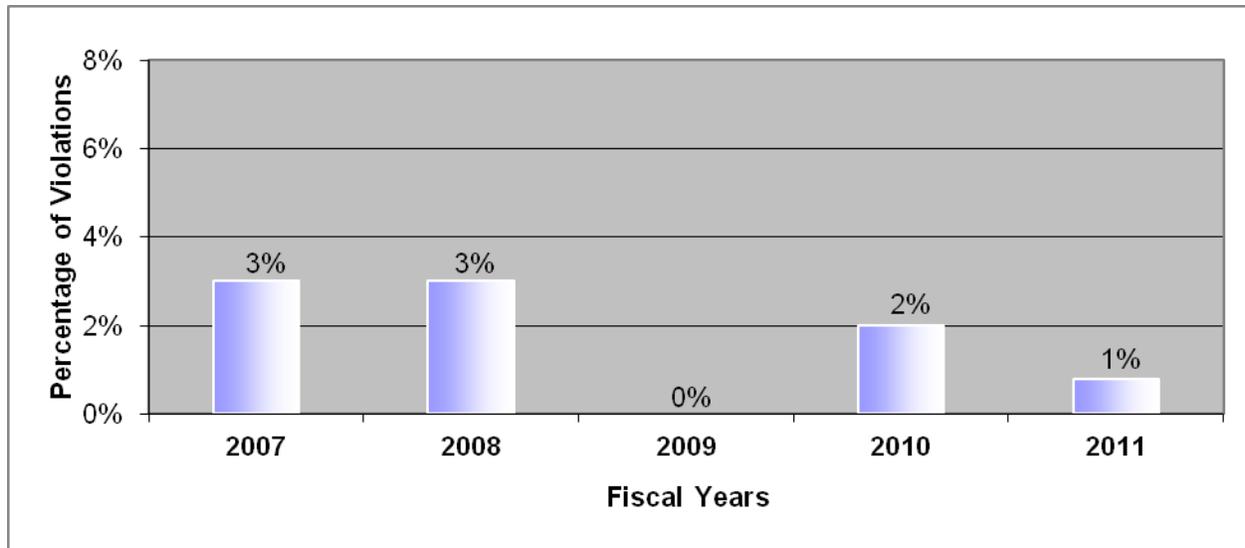
⁶ 26 U.S.C. § 7803(d)(1)(A)(iii) (Supp. V 2011).



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Figure 2 shows the percentages of potential violations of taxpayer rights we identified during our prior annual audits.

Figure 2: Potential Violations of Taxpayer Rights Based on Timely Notification



Source: TIGTA statutory lien reports issued during FYs 2007–2011.⁷

This review was performed at the Small Business/Self-Employed (SB/SE) Division Office of Collection Policy in New Carrollton, Maryland, and the Centralized Case Processing – Lien Unit and the ACS Support function in Covington, Kentucky, and the Wage and Investment Division ACS Support function in Fresno, California, during the period September 2011 through January 2012. 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.

⁷ See Appendix VII for a list of prior reports.



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Results of Review

Lien Notices Were Mailed Timely

I.R.C. § 6320 requires the IRS to notify taxpayers in writing, at their last known address,⁸ within five business days of the filing of an NFTL. We randomly sampled 105 NFTLs from the 1,150,049 NFTLs filed between July 1, 2010, and June 30, 2011. For all 105 cases, the IRS timely and correctly mailed lien notices as required. We determined that the law was complied with by confirming the mail date using the proof of mailing. Proof of mailing consists of certified mail lists showing a U.S. Postal Service date stamp. The certified mail list is produced by the ALS along with the taxpayer notice and stamped by the U.S. Postal Service with the date of mailing. The certified mail list is then forwarded to the Centralized Case Processing – Lien Unit for record keeping.

The Internal Revenue Service Did Not Comply With Regulations for Notifying Taxpayer Representatives

Taxpayer representative information is contained on the Centralized Authorization File (CAF)⁹ that is located on the Integrated Data Retrieval System (IDRS).¹⁰ Using the IDRS, employees can research the CAF to identify the types of authorization given to taxpayer representatives.

Department of the Treasury regulations (§ 601.506)¹¹ provide that notices are to be given to recognized taxpayer representatives. Specifically, any notice or other written communication (or a copy thereof) required or permitted to be given to a taxpayer in any matter before the IRS must be given to the taxpayer and, unless restricted by the taxpayer, to the representative. Accordingly, IRS procedures require the requestor of a lien to ensure he or she notifies the Centralized Case Processing – Lien Unit of all powers of attorney and co-obligors that are to be notified. More specifically, IRS procedures require that a copy of the notice be sent to the taxpayer's representative no later than five business days after the notice is sent to the taxpayer when an NFTL is filed.

⁸ 26 U.S.C. § 6320 (Supp V. 2011) also allows the IRS to provide written notice in person or left at the taxpayer's usual place of business.

⁹ The CAF contains information about the type of authorizations taxpayers have given their representatives for their tax returns.

¹⁰ IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.

¹¹ 26 C.F.R. § 601.506.



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Our review of the random sample of 105 liens included 22 taxpayers with representatives authorized to receive notifications at the time the liens were filed. For four (18 percent) of the 22 taxpayers, ALS records did not indicate that the IRS had sent copies of the lien notices to their representatives. Specifically:

- Three of the four liens were initiated by revenue officers¹² using the ICS, but the revenue officers did not ensure that the power of attorney information available on the ICS and the IDRS was sent to the ALS before the notices were mailed to the taxpayers.

- *****1*****¹³*****
*****1*****

We project¹⁴ that 43,817 taxpayers may have been adversely affected because the IRS did not follow requirements to notify the taxpayers' representatives of the taxpayers' rights related to liens. We are 95 percent confident that the range of potential violations is between 11,961 and 108,910. In addition to this year's results, Figure 3 shows the error rates reported on the notification of taxpayer representatives in our last five reports.

Figure 3: Error Rates Reported on Notification of Taxpayer Representatives

Report FY	Sampled Lien Cases Requiring Representative Notification	Sampled Lien Cases Not Receiving Representative Notification	Error Rate
2007	25	15	60%
2008	30	12	40%
2009	27	8	30%
2010	31	8	26%
2011	30	4	13%
2012	22	4	18%

Source: Prior and current year results of TIGTA tests of taxpayer representative notification.

While the error rate has been reduced from 60 percent in our FY 2007 report to 18 percent in our FY 2012 report, the potential for violations still exists in cases requiring taxpayer representative notification.

In our FY 2009 statutory lien report, we recommended that the IRS enhance its systems by establishing a systemic upload of CAF data to the ALS to ensure taxpayer representatives timely

¹² Employees in the Collection Field function who attempt to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses or the ACS. Campuses are 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.

¹³ The Advisory Unit provides technical guidance to revenue officers regarding liens, levies, and litigation.

¹⁴ Two-sided 95 percent confidence interval projection using the exact Binomial method.



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received lien notices. However, the implementation of the IRS corrective action¹⁵ was indefinitely delayed. Therefore, on December 29, 2011, the Director, Collection Policy, SB/SE Division, submitted a request to have the implementation of the corrective action rescheduled. Because these corrective actions may be scheduled to occur before the FY 2013 sample selection, this process will be evaluated during next year's statutory review.

Ineffective Working of Undelivered Lien Notices Resulted in Potential Violations of Taxpayers' Rights

IRS procedures require that employees send another lien notice to a new address if: 1) the originally mailed notice is returned as undelivered mail, 2) research confirms the original lien notice was not sent to the last known address, and 3) the new address was effective prior to or during the same cycle¹⁶ the NFTL was prepared that caused the lien notice to be issued. Collection function employees are responsible for certain actions when notices are returned as undelivered. For example, ACS Support function employees are required to research the IDRS within 14 calendar days of receipt to ensure that the address on the original lien notice is correct. If the employee cannot find a new address on the computer system, the undelivered lien notice will be destroyed and a new notice is not issued.

If the address on the notice is not the last known address and a different address was in effect prior to preparation of the original lien notice, employees should issue a new notice to the new address. A new notice is created by using an option in the ALS.

We selected a judgmental sample¹⁷ of 250 undelivered lien notices returned to the Cincinnati (125 lien notices) and Fresno (125 lien notices) Campuses in October 2011. The sample included only returned lien notices identified as undelivered and did not include returned mail identified as refused or unclaimed. We selected the Cincinnati and Fresno Campuses because the lien notices issued by the SB/SE and Wage and Investment Divisions' ACS sites returned as undelivered are sent to these locations. This sample provided a sufficient volume to evaluate the procedures.

IRS procedures require address verification and, if applicable, resolution (request to have the lien notice reissued) of undelivered lien notices within 14 calendar days of receipt. For these 250 notices, we reviewed computer system audit trails to assess whether IRS employees performed timely research to determine whether the addresses were correct on the originally mailed notices. Figure 4 shows how the 250 returned notices were handled by employees.

¹⁵ The IRS corrective action included a tool within the ALS to verify taxpayer representative information on the CAF prior to printing the lien notice.

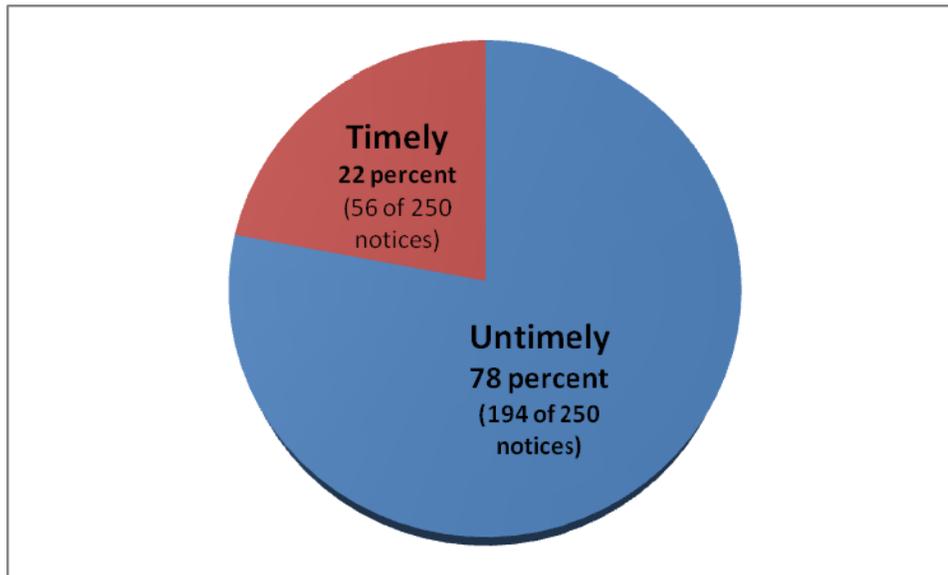
¹⁶ Cycle refers to the IRS method of documenting dates (*i.e.*, Processing Cycle 201102 is the second week of January 2011).

¹⁷ A judgmental sample is a nonstatistical sample, the results of which cannot be used to project to the population.



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Figure 4: Timeliness of Employee Research of Sampled Undelivered Lien Notices



Source: TIGTA analysis of sampled undelivered lien notices.

Our test of undelivered lien notices identified 15 of 250 lien notices for which the address on the IRS computer system and the original lien notice did not agree. For 11 (73 percent) of the 15 notices, the address on the IRS computer system was updated after the original lien notice was sent to the taxpayer. Therefore, no additional action was required. However, for four (27 percent) of the 15 notices, the address was updated prior to the cycle the NFTL was prepared in the ALS. According to IRS procedures, employees are required to send the taxpayer a new lien notice using the updated address. However, the IRS did not send notices to the four updated addresses.¹⁸ The four notices not reissued could involve potential violations of taxpayer rights because the IRS did not meet its statutory requirement of sending each lien notice to the taxpayer's last known address. For example, in a case filed in March 2010, the U.S. Tax Court¹⁹ found that an IRS lien notice was invalid because it was not mailed to the individual's last known address.

Lien notices are not sent to the most current addresses because, in part, employees are not always following established procedures for verifying the current address of the taxpayer prior to preparing a lien request. Also, the ALS does not currently perform an automated verification of the taxpayer's last known address prior to printing the lien notice. In our FY 2009 statutory lien

¹⁸ IRS reissued the notices to the four taxpayers after we brought this observation to their attention.

¹⁹ *Roberts v Comm'r, T.C. Summ.Op. 2010-21*. The U.S. Tax Court found that the lien notice issued with respect to a taxpayer's 2002 tax return was not mailed to the taxpayer's last known address, nor was it received and, therefore, it is invalid. Consequently, the IRS is required, under the provisions of § 6320 and the accompanying regulations, to issue to the taxpayer a substitute lien notice and provide him or her with an opportunity to request a lien hearing.



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report, we recommended that the IRS enhance its systems by establishing an automated check of a taxpayer's last known address prior to the printing of lien notices. However, the implementation of this enhancement was indefinitely delayed. Therefore, on December 29, 2011, the Director, Collection Policy, SB/SE Division, submitted a request to have the implementation of the enhancement rescheduled. Because these corrective actions may be scheduled to occur before the FY 2013 sample selection, this process will be evaluated during next year's statutory review.

In addition, IRS management indicated that the routing of the undelivered lien notices could have contributed to the untimely research of the undelivered mail. Specifically, all returned mail received at the Cincinnati and Fresno Campuses is extracted and sorted by mail type in their respective mail rooms. The undelivered lien notices are routed to the ACS Support functions that are located in different buildings. ACS Support function employees then perform the research on IRS computer systems to identify the last known addresses. We allowed three additional calendar days for the undelivered lien notices to be routed from the campus mailroom to the ACS Support functions. We were advised that, in some instances, it takes longer than three calendar days for the undelivered mail to be received in the ACS Support functions.

Notably, after we reported this issue in last year's report, IRS increased the number of days in which research should be completed, from within seven calendar days to within 14 calendar days. In addition, ACS Support function management does not consider the time spent routing mail as part of the 14 calendar days in which the research is required to be completed. Specifically, ACS Support function management believes research is timely if it is performed within 14 calendar days of the time the notice is received by the ACS Support functions, not the date on which it was received by the IRS. Furthermore, the IRS does not track the amount of time it takes to internally route undelivered lien notices, so it is uncertain what is causing the delays.

The requirement to research undelivered mail timely (now within 14 calendar days) is presumably to ensure taxpayers do not experience burdensome delays, particularly when they have provided the IRS with proper notice of an address change. However, IRS procedures appear to focus on processing times within each function instead of the overall amount of time expended from the taxpayer's perspective. When the IRS does not research the taxpayer's address timely, it makes little difference to the taxpayer if the IRS delays occurred in the mailroom or in the ACS Support functions.



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Employees are still not following procedures designed to monitor undelivered lien notices

In August 2007, procedures for handling undelivered lien notices were revised to return the undelivered lien notice directly to the requesting employee or function. The IRS procedures for Federal Tax Liens were also revised to require employees handling undelivered lien notices to input a specific IDRS transaction code with an appropriate action code. The transaction code signifies that the lien notice was returned and the action code indicates the reason (*i.e.*, undelivered, unclaimed, or refused). The IRS procedures for Federal Tax Liens require these codes to be entered into the IDRS after appropriate research of the returned lien notice is performed to record the mail status of the lien notices. On December 22, 2011, the Director, Collection Policy, SB/SE Division, issued interim guidance that emphasized the requirement for Collection Field function employees to input this specific IDRS transaction code with the appropriate action code to reflect the status of the returned lien notice.

In August 2009, the ALS was enhanced to perform a weekly systemic extract to send the appropriate undeliverable status (transaction code and action code) of lien notices to the IDRS using a specific command in ALS. When this command is used to update the status of the lien notice, no additional input is necessary to update the IDRS. When a lien notice is returned undelivered and research has been completed regarding an updated address, the employee can request the lien notice screen on ALS be updated with the undelivered status or go to the lien notice screen themselves and indicate undelivered status.

Our test of undelivered lien notices determined that the IRS is still not complying with this procedure of updating the undelivered status. None of the 250 undelivered lien notices that we sampled had a transaction code or associated action code input to the IDRS. For our sample, the ALS was not updated with the status of the undelivered lien notices and, therefore, the upload to the IDRS (via the ALS) did not occur. As a result, there is no record of the mail status of these lien notices. Management advised us that the requirements to enter these codes do not apply to the ACS. However, the ACS Support function has been designated by the SB/SE and Wage and Investment Divisions to receive all undelivered lien notices that were filed by the ACS since the address verification process was decentralized in August 2007. Accordingly, the IRS procedures for Federal Tax Liens provide that the person designated the responsibility of processing undelivered lien notices will also check the IDRS for a last known address and request the input of the transaction code with the appropriate action code or the command code enhancement via the ALS.

Because the ACS Support function was not following the IRS procedures for Federal Tax Liens, we recommended, in our FY 2011 statutory lien report, that Collection and Campus Compliance Services, SB/SE Division, and Compliance, Wage and Investment Division, ensure the procedures that address the handling of undelivered lien notices are consistent and include the same requirements for timely research of undelivered notices and when a new notice should be sent. Management agreed to reevaluate procedures to ensure they are consistent across the



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functions and support the timely resolution of undelivered notices. While some changes were made, the procedures pertaining to the campus were not changed to include the requirement to input the specific transaction code and the applicable action code.

Compliance with these procedures is important because it allows management to review the handling of undelivered lien notices. Undelivered lien notices are being sent back to more than 450 Collection Field function groups throughout the country where the employees or functions that requested the liens are located. The combination of decentralizing the handling of undelivered lien notices and the failure of employees to update taxpayers' data in the IDRS has not provided management with the information needed to ensure and enforce the timely resolution of undelivered lien notices. Figure 5 shows this situation has contributed to the number of undelivered lien notices that were not researched timely over the past five years.

Figure 5: Error Rates Reported on Undelivered Lien Notices

Report FY	Sampled Undelivered Lien Notices	Sampled Undelivered Lien Notices Untimely Researched	Error Rate
2008	400	133	33%
2009	283	234	83%
2010	300	252	84%
2011	250	204	82%
2012*	250	194	78%

Source: Prior and current year results of the TIGTA's tests of undelivered lien notices

**The IRS changed the definition of timely from within seven calendar days to within 14 calendar days of receipt for undelivered liens reviewed for our FY 2012 report.*

Cases sampled for our FY 2008 report were selected prior to the decentralization. The cases sampled for our FY 2009 report were selected after decentralization, when the error rate increased from 33 percent to 83 percent. It has remained near 80 percent since that time. Further, because employees are not following the procedures to enter the undelivered notice status into the IDRS via transaction and action codes, the information about the undelivered notice is limited to only those employees working the undelivered mail. IRS management, including Accounts Management organization²⁰ employees and Centralized Case Processing – Lien Unit employees who have access to the ALS, do not have access to information on

²⁰ The Accounts Management organization is responsible for providing taxpayers with information on the status of their returns and refunds and for resolving the majority of issues and questions to settle their accounts.



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undelivered lien notices. As a result, Taxpayer Assistance Center²¹ employees would be unable to answer taxpayer questions about these Federal Tax Liens.

Recommendations

Recommendation 1: The Directors, Enterprise Collection Strategy and Campus Compliance Services, SB/SE Division, and the Director, Compliance, Wage and Investment Division, should improve the controls and oversight over the processing of undelivered lien notices to ensure they are researched timely.

Management's Response: IRS management agreed with this recommendation. The IRS will make changes to the respective Internal Revenue Manuals to provide guidance for improved documentation and support the timely resolution of undeliverable notices.

Office of Audit Comment: In their response, the IRS disagreed with the statement that the taxpayers were not provided a copy of the lien notice because in each of the four cases identified, a notice was subsequently reissued to the more current address for the taxpayer and the taxpayers' appeal rights were extended. However, the IRS did not comply with the statutory requirement of providing a lien notice to the taxpayer's last known address within five business days of filing the lien. Furthermore, the IRS did not reissue a lien notice to the four taxpayers' more current address until we notified them that the original lien notice was not sent to the taxpayers' last known address.

Recommendation 2: The Directors, Enterprise Collection Strategy and Campus Compliance Services, SB/SE Division, should ensure the use of undelivered lien notice mail status is consistent in the procedures for the ACS and the Collection Field function.

Management's Response: IRS management agreed with this recommendation. The use of the status codes for all functions will be evaluated against resource demands to determine if implementation of the nonstatutory codes across all functions is feasible.

²¹ IRS offices with employees who answer questions, provide assistance, and resolve account-related issues for taxpayers face to face.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to determine whether liens issued by the IRS comply with legal guidelines set forth in I.R.C. Section (§) 6320 (a)¹ and related guidance in the Federal Tax Liens Handbook. To accomplish the objective, we:

- I. Determined whether taxpayer lien notices related to 105 Federal Tax Liens filed by the IRS complied with legal requirements set forth in I.R.C. § 6320 (a) and related internal guidelines.
 - A. Selected a random sample of 105 Federal Tax Lien cases from the ALS² extract of the 1,150,049 liens filed by the IRS nationwide between July 1, 2010, and June 30, 2011. We selected a random sample because we wanted to project the number of cases with errors. We used the formula below to calculate the minimum sample size, which we rounded to 105:

Population:	1,150,049
Confidence Level:	95 percent
Expected Rate of Occurrence:	2 percent ³
Precision Rate:	±3 percent
 - B. Validated the ALS extract by comparing the sampled records to online data.
 - C. Determined whether the sampled liens adhered to legal guidelines regarding timely notifications of lien filings to the taxpayer, the taxpayer's spouse, or business partners by reviewing data from the ALS and the certified mail list.
 - D. Evaluated the controls and procedures established for transferring, storing, and safeguarding certified mail lists at the Centralized Case Processing – Lien Unit.
 - E. Determined whether taxpayers' representatives were provided a copy of the lien due process notice by reviewing data from the ALS, IDRS, ICS, and ACS.
 1. Reviewed IDRS screens for CAF indicators for all sampled cases.

¹ 26 U.S.C. § 6320 (Supp V. 2011).

² See Appendix VI for descriptions of IRS computer systems used in the filing of Notices of Federal Tax Lien.

³ Expected rate of occurrence based on error rates in prior years – no errors in FY 2009, 2 percent in FY 2010, and 1 percent in FY 2011.



Problems Persist When Processing Undelivered Lien Notices and Notifying Taxpayers' Representatives

2. Reviewed ALS history screens for accounts with CAF indicators to see if lien notices were mailed to taxpayers' representatives within five business days of mailing the taxpayers' notices.
 - F. Reviewed the ACS and the ICS for taxpayer representative/power of attorney indicators and matched tax periods to ensure that all taxpayer representatives/powers of attorney listed on the ACS and the ICS were provided notification per the ALS.
 - G. Provided all exception cases to the Office of Collection Policy, SB/SE Division, for agreement to potential violations and corrective actions if appropriate.
- II. Evaluated the procedures for processing lien notices⁴ that are returned undelivered.
- A. Selected a judgmental sample⁵ of 250 unprocessed (unopened) and recently processed (opened) mail containing undelivered lien notices received during October 2011 in the Cincinnati (125) and Fresno (125) Campuses⁶ and recorded the taxpayer's name, address, Social Security Number, and serial lien identification number. We used a judgmental sample because we could not determine the population of undelivered lien notices at these two campuses.
 - B. For each sampled case:
 1. Researched IDRS Master File (Command Codes INOLE, IMFOL, and BMFOL) and determined if the address on the Master File⁷ matched the address on the undelivered lien notice for each sampled case.
 2. Reviewed taxpayer audit trails to determine whether lien employees performed the required IDRS research during creation of the lien.
 3. Reviewed IDRS taxpayer audit trails to determine whether employees performed the required IDRS research for resolution of the undelivered lien notices within 14 calendar days of receipt.
 - a. If appropriate research was completed for resolution of the undelivered lien notices, verified the appropriate transaction code and action code was entered into the IDRS.

⁴ IRS Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320* (Rev. Mar. 2009), Cat. No. 267671.

⁵ A judgmental sample is a nonstatistical sample, the results of which cannot be used to project to the population.

⁶ Campuses are 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.

⁷ 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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- III. Determined if IRS internal guidelines have been modified since our last review by discussing procedures and controls with appropriate IRS personnel in SB/SE Division Collection Policy function.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for 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 timely notifying taxpayers of lien filings and timely verifying addresses of undelivered lien notices. We evaluated these controls by interviewing management and reviewing samples of lien notices sent to taxpayers and lien notices returned to the IRS as undelivered.



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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
Michael J. Della Ripa, Lead Auditor
Steven Stephens, Senior Auditor
Stephen Elix, Auditor
Frank Maletta, Auditor
Kevin O' Gallagher, Information Technology Specialist
Joseph L. Katz, Ph.D., Contractor, Statistical Sampling Consultant



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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
Deputy Commissioner, Wage and Investment Division SE:W
Director, Campus Compliance Services SE:S:CCS
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Compliance, Wage and Investment Division SE:W:CP
Director, Enterprise Collection Strategy SE:S:ESC
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 Liaisons:
 Commissioner, Small Business/Self-Employed Division SE:S
 Commissioner, Wage and Investment Division SE:W



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Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to Congress.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 43,817 taxpayers whose representatives may not have been provided Letters 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320*,¹ resulting in potential violations of taxpayers' rights (see page 4).

Methodology Used to Measure the Reported Benefit:

From a random sample of 105 NFTL cases, we identified 22 cases with taxpayer representatives authorized to receive notifications at the time the NFTLs were filed. From those 22 cases, we identified four (18 percent) cases for which IRS employees did not provide lien notices to taxpayer representatives, resulting in potential violations of taxpayers' rights. The sample was selected based on a confidence level of 95 percent, a precision rate of ± 3 percent, and an expected rate of occurrence of 2 percent.

- Error rate = Four cases out of 105 (3.81 percent) in which the taxpayer representative was not provided Letter 3172
- Population = 1,150,049 NFTLs generated by the ALS between July 1, 2010, and June 30, 2011.
- Projection = $1,150,049 \times 3.81$ percent = 43,817 taxpayers whose representatives may not have been provided Letters 3172.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Actual; four taxpayers were not provided a Letter 3172, resulting in potential legal violations of taxpayers' rights (see page 6).

¹ IRS Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320* (Rev. Mar. 2009), Cat. No. 267671.



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Methodology Used to Measure the Reported Benefit:

In a judgmental sample of 250 undelivered lien notices, we determined that the IRS did not send lien notices to the updated addresses of four taxpayers. The four lien notices not sent to the updated addresses could involve potential violations of taxpayer rights because the IRS did not meet its statutory requirement of sending each lien notice to the taxpayer's last known address.



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Appendix V

***Synopsis of the Internal Revenue Service
Collection and Notice of Federal Tax Lien Processes***

The collection of unpaid tax begins with a series of letters (notices) sent to the taxpayer advising of the debt and asking for payment of the delinquent tax. IRS computer systems are programmed to mail these notices when certain criteria are met. If the taxpayer does not respond to these notices, the account is transferred for either personal or telephone contact.

- IRS employees who make personal (face-to-face) contact with taxpayers are called revenue officers and work in various locations. The ICS¹ is used in most of these locations to track collection actions taken on taxpayer accounts.
- IRS employees who make only telephone contact with taxpayers work in call sites. The ACS is used in the call sites to track collection actions taken on taxpayer accounts.

When these efforts have been taken and the taxpayer has not paid the tax liability, designated IRS employees are authorized to file a lien by sending an NFTL² to appropriate local government offices. Liens protect the Federal Government's interest by attaching a claim to the taxpayer's assets for the amount of unpaid tax. The right to file an NFTL is created by I.R.C. Section 6321 when:

- The IRS has made an assessment and given the taxpayer notice of the assessment, stating the amount of the tax liability and demanding payment.
- The taxpayer has neglected or refused to pay the amount after the notice and demand for payment.

When designated employees request the filing of an NFTL using either the ICS or the ACS, the ALS processes the NFTL filing requests from both systems. In an expedited situation, employees can manually prepare the NFTL. Even for manually prepared liens, the ALS controls and tracks the liens and initiates subsequent lien notices³ to notify responsible parties of the lien filings and of their appeal rights. The ALS maintains an electronic database of all open NFTLs and updates the IRS's primary computer records to indicate that an NFTL has been filed.

¹ See Appendix VI for detailed descriptions of IRS computer systems used in the filing of Notices of Federal Tax Lien.

² IRS Form 668(Y)(c), *Notice of Federal Tax Lien* (Rev. Oct. 1999), Cat. No. 60025X.

³ IRS Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320* (Rev. Mar. 2009), Cat. No. 267671.



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Most lien notices are mailed to taxpayers by certified or registered mail, rather than delivered in person. To maintain a record of the notices, the IRS prepares a certified mail list (U.S. Postal Service Form 3877), which identifies each notice that is to be mailed. The notices and a copy of the certified mail list are delivered to the U.S. Postal Service. A U.S. Postal Service employee ensures that all notices are accounted for, date stamps the list, and returns a copy to the IRS. The stamped certified mail list is the only documentation the IRS has that certifies the date on which the notices were mailed. IRS guidelines require that the stamped certified mail list be retained for 10 years after the end of the processing year.



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Appendix VI

***Internal Revenue Service Computer Systems
Used in the Mailing of Lien Notices***

Automated Collection System (ACS) is 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. Lien notices requested using the ACS are uploaded to the ALS, which generates the Notices of Federal Tax Lien¹ and related lien notices and updates the IRS's primary computer files to indicate that Notices of Federal Tax Lien have been filed.

Automated Lien System (ALS) is a comprehensive database that prints Notices of Federal Tax Lien and lien notices, stores taxpayer information, and documents all lien activity. Lien activities on both ACS and ICS cases are controlled on the ALS by Technical Support or Case Processing functions at the Cincinnati, Ohio, Campus.² Employees at the Cincinnati Campus process Notices of Federal Tax Lien and lien notices and respond to taxpayer inquiries using the ALS.

Integrated Collection System (ICS) is an 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. Lien requests made using the ICS are uploaded to the ALS. The ALS generates the Notices of Federal Tax Lien and related lien notices and updates the IRS's primary computer files to indicate Notices of Federal Tax Lien have been filed.

Integrated Data Retrieval System (IDRS) is an online data retrieval and data entry system that processes transactions entered from terminals located in campuses and other IRS locations. It enables employees to perform such tasks as researching account information, requesting tax returns, entering collection information, and generating collection documents. The IDRS serves as a link from campuses and other IRS locations to the Master File³ for the IRS to maintain accurate records of activity on taxpayers' accounts.

¹ IRS Form 668(Y)(c), *Notice of Federal Tax Lien* (Rev. Oct. 1999), Cat. No. 60025X.

² Campuses are 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.

³ The Master File is 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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Appendix VII

***Statutory Lien Reports Issued During
Fiscal Years 2007 Through 2011***

TIGTA, Ref. No. 2007-30-051, *Fiscal Year 2007 Statutory Review of Compliance With Lien Due Process Procedures* (Mar. 2007).

TIGTA, Ref. No. 2008-30-082, *Fiscal Year 2008 Statutory Review of Compliance With Lien Due Process Procedures* (Mar. 2008).

TIGTA, Ref. No. 2009-30-089, *Additional Actions Are Needed to Protect Taxpayers' Rights During the Lien Due Process* (Jun. 2009).

TIGTA, Ref. No. 2010-30-072, *Actions Are Needed to Protect Taxpayers' Rights During the Lien Due Process* (Jul. 2010).

TIGTA, Ref. No. 2011-30-051, *Challenges Remain When Processing Undeliverable Mail and Preventing Violations of Taxpayers' Rights During the Lien Due Process* (May 2011).



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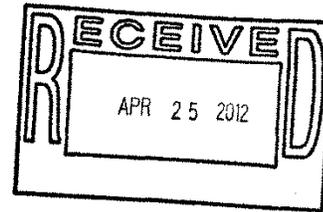
Appendix VIII

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/Self-EMPLOYED DIVISION

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



APR 25 2012

MEMORANDUM FOR MICHAEL R. PHILLIPS
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Faris R. Fink *Faris R. Fink*
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – Problems Persist When Processing
Undeliverable Mail and Notifying Taxpayers' Representatives
(Audit No. 201230001)

Thank you for the opportunity to review your draft report titled: "Problems Persist When Processing Undeliverable Mail and Notifying Taxpayers' Representatives." We agree with your recommendations as stated in the report. We continue to take strides to ensure the processes for handling lien notices, including those returned as undeliverable, are consistent across all functions, and comply with statutory requirements. We also continue to explore alternative methods to improve our systems relative to the notification process.

We concur with your Outcome Measure relative to the number of taxpayer representatives that may not have been notified; however, we disagree that any failure to notify the representative jeopardizes the taxpayers' rights. In each of the four instances cited where the taxpayer's representative was not provided a notice, the lien notice was timely sent to the taxpayer, thus affording their full rights of appeal.

We also concur with the Measure regarding the number of taxpayers from the judgmental sample where the initial notice may have been sent to an outdated address. We disagree, however, with the statement that the taxpayers were not provided a notice because, in each of the four cases identified, a notice was subsequently reissued to a more current address for the taxpayer and the taxpayers' right to appeal was extended accordingly. In addition, although stated in the report, it should be emphasized that these four cases were taken from a batch of notices that were returned as undeliverable, which represents a small percentage of the overall number of notices issued.

We appreciate your noting that, of the statistically-valid sample of 105 cases, all notices were timely and correctly mailed to the taxpayers. This finding, which follows three years where we had a total of only two instances of late notices, demonstrates our ongoing commitment to protecting taxpayers' rights while enforcing the tax laws.



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2

Attached is a detailed response outlining our corrective actions to address your recommendations.

If you have any questions, please contact me, or a member of your staff may contact Michael Julianelle, Director, Enterprise Collection at (202) 622-3480.

Attachment



***Problems Persist When Processing Undelivered
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Attachment

RECOMMENDATION 1:

The Directors, Enterprise Collection Strategy and Campus Compliance Services, SB/SE Division, and the Director, Compliance, Wage and Investment Division, should improve the controls and oversight over the processing of undelivered lien notices to ensure they are researched timely.

CORRECTIVE ACTION:

We will make additional changes to the respective IRMs to provide guidance for improved documentation and support the timely resolution of undeliverable notices.

IMPLEMENTATION DATE:

September 15, 2012

RESPONSIBLE OFFICIAL(S):

Director, Collection Policy (SB/SE)
Director, Campus Compliance Services (SB/SE)
Director, Compliance (W&I)

CORRECTIVE ACTION MONITORING PLAN:

IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 2:

The Directors, Enterprise Collection Strategy and Campus Compliance Services, SB/SE Division, should ensure the use of undelivered lien notice mail status codes are consistent in the procedures for the ACS and the Collection Field function.

CORRECTIVE ACTION:

The use of the status codes for all functions will be evaluated against resource demands to determine if implementation of the non-statutory codes across all functions is feasible.

IMPLEMENTATION DATE:

December 15, 2012

RESPONSIBLE OFFICIAL(S):

Director, Collection Policy (SB/SE)
Director, Campus Compliance Services (SB/SE)
Director, Compliance (W&I)

CORRECTIVE ACTION MONITORING PLAN:

IRS will monitor this corrective action as part of our internal management system of controls.