



*Fiscal Year 2010 Statutory Review
of Restrictions on
Directly Contacting Taxpayers*

June 3, 2010

Reference Number: 2010-30-060

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



HIGHLIGHTS

FISCAL YEAR 2010 STATUTORY REVIEW OF RESTRICTIONS ON DIRECTLY CONTACTING TAXPAYERS

Highlights

Final Report issued on June 3, 2010

Highlights of Reference Number: 2010-30-060 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

Internal Revenue Service (IRS) employees are required to stop an interview if the taxpayer requests to consult with a representative and may not bypass a representative without supervisory approval. Between October 2008 and September 2009, there were at least four instances in which employees improperly bypassed taxpayer representatives.

WHY TIGTA DID THE AUDIT

This audit was initiated because TIGTA is required to annually report on the IRS' compliance with Internal Revenue Code Sections 7521(b)(2) and (c). The overall objective of this audit was to determine whether the IRS complied with the legal guidelines addressing the direct contact of taxpayers and their representatives.

WHAT TIGTA FOUND

This is the twelfth year in which TIGTA has reported its inability to give an opinion on how well the IRS is complying with the Internal Revenue Code restrictions on direct contact because of limitations with the IRS' management information systems. In considering the significance of this limitation, it is important to recognize that the evidence we have obtained and evaluated over the years suggests potential direct contact violations are very small considering that thousands of IRS enforcement personnel routinely interact with millions of taxpayers and their representatives each year.

In a total of four instances, both TIGTA's Office of Investigations and Office of Audit confirmed that IRS personnel improperly bypassed taxpayer representatives. The Office of Investigations determined that the responsible IRS personnel were reprimanded for their actions. The Office of Audit determined that there was no evidence that a representative or taxpayer complaint was filed with TIGTA.

WHAT TIGTA RECOMMENDED

TIGTA is not making any specific recommendations in this report. However, a draft of the report was provided to the IRS for review and comment. The IRS had no comments on the report.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

June 3, 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 – Fiscal Year 2010 Statutory Review of Restrictions
on Directly Contacting Taxpayers (Audit # 200930043)

This report presents the results of our review to determine whether the Internal Revenue Service (IRS) complied with legal guidelines addressing the direct contact of taxpayers and their representatives, as set forth in Internal Revenue Code Sections 7521(b)(2) and (c). The Treasury Inspector General for Tax Administration is statutorily required to conduct this audit.

Although we made no recommendations in this report, we did provide IRS officials an opportunity to review the draft report. IRS management did not provide us with any report comments.

Copies of this report are also being sent to the IRS managers affected by the report results. 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.



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Abbreviations

I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
RRA 98	Restructuring and Reform Act of 1998



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Background

The Omnibus Taxpayer Bill of Rights,¹ enacted in 1988, created a number of safeguards to protect taxpayers being interviewed by Internal Revenue Service (IRS) employees as part of an examination or investigation. Specifically, IRS employees are required by the direct contact provisions of Internal Revenue Code (I.R.C.) Sections (§§) 7521(b)(2) and (c) to:

The Treasury Inspector General for Tax Administration is required to annually evaluate the IRS' compliance with the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c).

- Stop a taxpayer interview whenever a taxpayer requests to consult with a representative.
- Obtain their immediate supervisor's approval to contact the taxpayer instead of the representative if the representative is responsible for unreasonably delaying the completion of an examination or investigation.

A taxpayer can file a civil suit against the IRS if an IRS employee intentionally disregards these provisions by denying a taxpayer the right to appropriate representation.

On July 22, 1998, the President signed into law the IRS Restructuring and Reform Act of 1998 (RRA 98),² which required the IRS to revise *Your Rights as a Taxpayer* (Publication 1) to inform taxpayers of their rights to 1) be represented at interviews and 2) suspend an interview pursuant to I.R.C. § 7521(b)(2). In addition, Congress included another provision to the RRA 98 that requires the Treasury Inspector General for Tax Administration to annually evaluate the IRS' compliance with the direct contact provisions. *Senate Committee on Finance Report 105-174* (dated April 22, 1998), related to the RRA 98, stated that Congress believes taxpayers should be more fully informed of their rights to representation in dealing with the IRS and those rights should be respected.

This review was performed at the IRS National Headquarters in the offices of the Commissioner and the National Taxpayer Advocate in Washington, D.C., and in the Small Business/Self-Employed Division Headquarters in New Carrollton, Maryland, during the period July 2009 through February 2010. 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

¹ Pub. L. No. 100-647, 102 Stat. 3730 (1988) (codified as amended in scattered sections of 5 U.S.C. and 26 U.S.C.).

² Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).



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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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Results of Review

This is the twelfth year reporting that neither we nor the IRS know with any degree of preciseness how well it is complying with direct contact provisions of the I.R.C. because of limitations with its management information systems. In considering the significance of this limitation, it is important to recognize that the evidence we have obtained and evaluated over the years suggests potential direct contact violations are very small considering that thousands of IRS enforcement personnel routinely interact with millions of taxpayers and their representatives each year. It is equally important to recognize the IRS has policies, procedures, and techniques (internal control activities) in place at the agency and operational levels that are designed to help ensure its personnel adhere to the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c).

Agency Level Internal Control Activities Help Ensure Compliance With Direct Contact Provisions

According to the Government Accountability Office *Standards for Internal Control in the Federal Government*,³ internal control activities are the policies, procedural requirements, and techniques that enforce management directives, such as complying with applicable laws and regulations. Specifically, control activities are designed to help ensure risks that could affect achieving desired outcomes are identified, evaluated, and addressed.

At the top of the agency, the IRS' mission statement and supporting policy statements provide guidance nationwide to IRS compliance and other personnel who have contact with taxpayers. Figure 1 provides an example of IRS Policy Statement 5-2, which contains the core principles that underscore the importance of protecting taxpayer rights as well as providing the public with quality, courteous, and effective assistance in collecting unpaid taxes.

³ GAO/AIMD-00-21.3.1, dated November 1999.



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Figure 1: Core Principles for Collecting Unpaid Taxes

Excerpt From IRS Policy Statement 5-2	
Principles	Description
<p style="text-align: center;"><i>OVERARCHING PRINCIPLES</i></p>	<p>All our decisions about collecting must be guided by these principles. To the extent that they are, we will succeed in our mission.</p>
<p style="text-align: center;"><i>SERVICE AND ASSISTANCE</i></p> <p>All taxpayers are entitled to courteous, responsive, and effective service and assistance in all their dealings with the Service.</p>	<p>We will actively assist taxpayers who try to comply with the law and work to continually improve the quality of our systems and service to meet the needs of our customers. All taxpayers, whether delinquent or fully compliant, are entitled to prompt and professional service whenever they deal with Service employees.</p>
<p style="text-align: center;"><i>TAXPAYER RIGHTS</i></p> <p>We will observe taxpayers' rights, including their rights to privacy and to fair and courteous treatment.</p>	<p>This affirms our commitment to observe both the spirit as well as the letter of all legal requirements, including the Taxpayer Bill of Rights I and II and the IRS Restructuring and Reform Act of 1998. Taxpayers will be protected from unauthorized disclosure of information.</p>
<p style="text-align: center;"><i>COMPLIANCE</i></p> <p>The public trust requires us to ensure that all taxpayers promptly file their returns and pay the proper amount of tax, regardless of the amount owed.</p>	<p>The public as a whole is our customer, not just delinquent taxpayers. Our customers expect us to promote voluntary compliance by ensuring that all promptly pay their fair share.</p>
<p style="text-align: center;"><i>CASE RESOLUTION</i></p> <p>While we will actively assist taxpayers to comply, we will also take appropriate enforcement actions when warranted to resolve the delinquency. To resolve a case, good judgment is needed to make sound decisions on the appropriate action needed.</p>	<p>All taxpayers are required to pay by the due date of the return. From a broad range of collecting tools, employees will select the one(s) most appropriate for each case. Case resolution, including actions such as lien, levy, seizure of assets, installment agreement, offer in compromise, substitute for return, summons, and IRC 6020(b), are important elements of an effective compliance program. When it is appropriate to take such actions, it should be done promptly, yet judiciously, and based on the facts of each case.</p>

Source: Excerpt from IRS Policy Statement 5-2 – Collecting Principles.



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To supplement agency level mission and policy statements, the IRS uses, and periodically updates, the Internal Revenue Manual (IRM)⁴ and numerous taxpayer publications. Both the IRM and taxpayer publications are available online and are designed to provide guidance nationwide to IRS personnel and taxpayers alike.

The IRM and taxpayer publications are important control components

From a control perspective, both the IRM and taxpayer publications are important because they provide detailed explanations and instructions of the statutory, business, and administrative procedures the IRS follows in administering the tax laws, including the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c). For example, the IRS uses Publication 1 as the main document to keep taxpayers informed of their rights and to explain the examination, collection, appeals, and refund processes. Publication 1 also includes the following information concerning taxpayers' rights to be represented at interviews with the IRS and to suspend an interview pursuant to I.R.C. § 7521(b)(2).

You may either represent yourself or, with proper written authorization, have someone else represent you in your place. Your representative must be a person allowed to practice before the IRS, such as an attorney, certified public accountant, or enrolled agent. If you are in an interview and ask to consult such a person, then we must stop and reschedule the interview in most cases.

The IRS has also included information on these rights in other publications, such as:

- *Your Federal Income Tax* (Publication 17).
- *Tax Guide for Small Business* (Publication 334).
- *Examination of Returns, Appeal Rights, and Claims for Refund* (Publication 556).
- *The Examination Process* (Publication 3498).

In addition, the IRS uses *Practice Before the IRS and Power of Attorney* (Publication 947) to inform taxpayers of their representatives' responsibilities and to notify taxpayers that the IRS has the authority to bypass representatives that are uncooperative. Specifically, Publication 947 states "After a valid power of attorney is filed, the IRS will recognize your representative. However, if it appears the representative is responsible for unreasonably delaying or hindering the prompt disposition of an IRS matter by failing to furnish, after repeated requests, non-privileged information, the IRS can contact you directly."

⁴ A manual containing the IRS' internal guidelines.



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Steps Have Been Taken to Strengthen Controls at the Operational Level

At the operational level, the first-line managers over IRS collectors and examiners (enforcement personnel) are a key control because they are responsible for ensuring that the personnel they supervise follow procedures and that their work meets acceptable standards. To assist managers in ensuring procedures are followed and standards are met, the IRM requires managers to conduct reviews over the work of the personnel they supervise, both while it is in process and after it is completed. These control techniques, as we have previously reported, help identify problems so prompt corrective actions, if needed, can be taken.

To its credit, the IRS recognized the critical role first-line managers have in its control activities and have taken steps to reinforce upon managers the need to address adherence to the direct contact provisions with the personnel they supervise. For example, the Small Business/Self-Employed Division issued a memorandum to its first-line managers in Fiscal Years 2001 and 2002 directing them to “take whatever steps are necessary (including discussion in group meetings, case reviews, workload reviews, on-the-job visits, and taxpayer/POA [Power of Attorney] inquiries) to ensure these requirements [the requirements mandated by I.R.C. §§ 7521(b)(2) and (c)] are understood and followed by employees.”

In August 2006, the IRS updated the IRM to include specific directions for managers in its Collection function on how to ensure compliance with the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c). In addition, the IRS committed to updating the IRM for managers of its Examination function in response to a recommendation we made in our report last year.⁵ The updates to the Examination function’s IRM are scheduled to be completed by June 2010. Assuming first-line managers adhere to the IRM guidelines, we believe there are at least three reasons that support the need and importance of emphasizing the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c) as part of the manager’s supervision over the work of enforcement personnel.

There are important reasons first-line managers should emphasize adherence to the direct contact provisions of the I.R.C.

First, thousands of enforcement personnel routinely interact with millions of taxpayers and their representatives each year to resolve a variety of tax issues. These interactions can become contentious and time consuming for both the IRS and taxpayers, especially in situations where there are strong opposing opinions on how best to resolve a particular tax issue. As a result, the sheer number and types of interactions enforcement personnel have with taxpayers are more likely to place the IRS at greater risk of jeopardizing the direct contact provisions when

⁵ *Fiscal Year 2009 Statutory Review of Restrictions on Directly Contacting Taxpayers* (Reference Number 2009-30-054, dated March 24, 2009).



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compared with the interactions that other IRS personnel have with taxpayers, such as those involved with customer service operations.

Second, the IRS cannot tell us with any degree of preciseness how well it is complying with direct contact provisions of I.R.C. §§ 7521(b)(2) and (c) because of limitations with its management information systems. As we reported in past years, neither the Taxpayer Advocate’s Management Information System⁶ nor the IRS Commissioner’s Information Tracking System⁷ is capable of readily identifying instances in which IRS personnel denied a taxpayer’s right to representation or bypassed their representative without proper approval. Despite this limitation, there is evidence that potential violations occur, although the number is a very small number compared to the millions of taxpayer interactions that can take place annually.

For example, taxpayer complaints that allege IRS employees bypassed their representatives and contacted them directly are tracked on the Performance and Results Information System⁸ by the Treasury Inspector General for Tax Administration Office of Investigations. The Office of Investigations closed 13 direct contact complaint/investigation cases between October 2008 and September 2009. In three substantiated complaints, *****1*****
*****improperly bypassed taxpayer representatives and were counseled or reprimanded for their actions. In addition, we judgmentally sampled 30 of 12,155 examinations that were closed by IRS field examiners in Fiscal Year 2009 and found *****1*****

*****.

Third, the requirement of having first-line managers emphasize the direct contact provisions is consistent with the Government Accountability Office *Standards for Internal Control in the Federal Government*. Among other things, the standards specify that control activities should include techniques that ensure management directives are followed.

⁶ The Taxpayer Advocate Management Information System is an electronic database and case inventory control system used by Taxpayer Advocate Service function employees.

⁷ The Information Tracking System is a system used by the IRS to control and track information and correspondence.

⁸ The Performance and Results Information System is a management information system that provides the Treasury Inspector General for Tax Administration with the ability to manage complaints received and investigations initiated.



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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether the IRS complied with legal guidelines addressing the direct contact of taxpayers and their representatives as set forth in I.R.C. §§ 7521(b)(2) and (c).

To accomplish this objective, we:

- I. Interviewed IRS management personnel in the Small Business/Self-Employed Division to determine that the IRS neither has, nor plans to implement, a system or process to identify or track cases in which taxpayers have requested to consult with a representative or in which an IRS employee bypassed a representative.
 - A. Reviewed a judgmental sample of 30 Fiscal Year 2009 closed individual Small Business/Self-Employed cases where taxpayers had a Power of Attorney on file during their examination. Our sample was selected from a population of 12,155 taxpayers meeting the criteria above. We chose a judgmental sample because we did not intend to project our results to the population.
- II. Interviewed various IRS and Treasury Inspector General for Tax Administration personnel responsible for the Taxpayer Advocate Management Information System,¹ the Information Tracking System,² and the Performance and Results Information System³ to determine if there is a system to track taxpayer complaints relating to violations of the direct contact provisions of the law.
 - A. Identified 13 direct contact complaint/investigation cases on the Performance and Results Information System closed by the Treasury Inspector General for Tax Administration Office of Investigations between October 2008 and September 2009.
 - B. Obtained and reviewed the closed Office of Investigations case files to determine their validity and what actions were taken by the IRS as a result of the complaints/investigations.

¹ The Taxpayer Advocate Management Information System is an electronic database and case inventory control system used by Taxpayer Advocate Service function employees.

² The Information Tracking System is a system used by the IRS to control and track information and correspondence.

³ The Performance and Results Information System is a management information system that provides the Treasury Inspector General for Tax Administration with the ability to manage complaints received and investigations initiated.



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- III. Obtained information on the actions taken by the IRS in response to I.R.C. §§ 7521(b)(2) and (c) to determine the impact on IRS programs.
- A. Reviewed all prior Treasury Inspector General for Tax Administration audit reports for the statutory direct contact reviews and summarized the audit results, recommendations, and corrective actions taken by the IRS.
 - B. Reviewed historic and current IRM⁴ sections to identify any updates made in response to I.R.C. §§ 7521(b)(2) and (c).
 - C. Reviewed the IRWeb (i.e., IRS Intranet) to identify the impact I.R.C. §§ 7521(b)(2) and (c) have had recently on any IRS programs.
 - D. Reviewed IRS.gov (the public IRS Internet site) and related IRS publications to identify how the IRS informs taxpayers of its prohibition against directly contacting taxpayers in certain situations.

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:

- Agency level internal control activities.
 - a. The IRS' mission statement, supporting policy statements, and IRM guidelines that provide guidance to IRS employees to ensure compliance with direct contact provisions.
 - b. Numerous publications that keep taxpayers informed of their rights.
- Operational level internal control activities. First-line managers are required under IRM guidelines to address adherence to the direct contact provisions by the personnel they supervise.

⁴ A manual containing the IRS' internal guidelines.



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Appendix II

Major Contributors to This Report

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

Frank Dunleavy, Director

Steven Stephens, Audit Manager

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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, Communications, Liaison, and Disclosure, Small Business/Self-Employed Division
SE:S:CLD
Director, Examination, Small Business/Self-Employed Division SE:S:E
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