



*The Centralized Lien Unit Properly Filed
Federal Tax Liens but Needs to Minimize the
Number of and Improve Controls Over Liens
Returned by Recording Offices*

July 31, 2007

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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.

Phone Number | 202-927-7037

Email Address | Bonnie.Heald@tigta.treas.gov

Web Site | <http://www.tigta.gov>



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

July 31, 2007

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION

FROM: *Michael R. Phillips*
Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices (Audit # 200630007)

This report presents the results of our review of the Internal Revenue Service (IRS) Centralized Lien Processing Unit. The overall objective of this review was to determine whether the IRS had taken appropriate actions to ensure the Centralized Lien Processing Unit is operating effectively. This audit was part of our audit coverage of the Small Business/Self-Employed Division and was included in our Fiscal Year 2006 Annual Audit Plan.

Impact on the Taxpayer

A Federal Tax Lien gives the IRS a legal claim to a taxpayer's property for the amount of his or her tax debt. Failure to file and properly record a Notice of Federal Tax Lien in the recording office¹ may jeopardize the Federal Government's priority right against other creditors. It is extremely important to protect the interests of the Federal Government, creditors, and taxpayers in general.

Synopsis

Filing a Notice of Federal Tax Lien is necessary to establish priority rights against other creditors. It is critical that recording offices ensure Federal Tax Liens are timely filed and properly recorded. The IRS Centralized Lien Processing Unit was implemented in October 2005 and has gone through numerous changes in an attempt to improve its overall effectiveness. The

¹ Recording offices are the Clerks of the Circuit Court where the IRS records its Notices of Federal Tax Lien.



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IRS has taken actions to improve the effectiveness of this unit, but additional work is still needed.

The lien processing unit generally prepared Federal Tax Liens accurately and timely. Our review of a statistically valid sample of 150 Federal Tax Liens showed unit employees accurately and timely prepared the Federal Tax Liens. However, we found problems associated with the sorting and mailing of the Notices of Federal Tax Lien and the paying of lien fees to the recording offices, which caused the recording offices not to timely file and properly record the Federal Tax Liens. These problems were a major reason recording offices returned approximately 29,000 lien documents to the IRS to be reworked.

The IRS needs to reduce the volume of returned lien documents by improving the process of paying lien fees. In addition, procedures need to be established to ensure returned lien documents rejected by the recording offices are properly controlled and corrected. Correcting returned lien documents takes additional staffing and processing time, which delay the filing or releasing of the Federal Tax Liens. Processing delays can jeopardize the collection of money owed to the Federal Government and the timely release of Notices of Federal Tax Lien after the taxpayers satisfy their tax obligations.

Recommendations

The Director, Collection, should pursue other options for paying lien fees to recording offices for processing lien documents and implement a process to ensure lien fee changes are timely and properly updated. The Director, Campus Compliance Services, should establish criteria for measuring the accuracy and timeliness of returned lien documents and ensure returned lien batches are properly maintained so the cases can be easily retrieved and reworked.

Response

The Commissioner, Small Business/Self-Employed Division, agreed with our four recommendations and will take or has taken corrective actions. IRS management will pilot a lien fee payment process directly connecting lien payments to document issuance and develop procedures to ensure lien batches are properly maintained. In addition, IRS management has developed new procedures for monitoring, reworking, and returning lien documents to the county recording offices accurately and timely

However, management disagreed with our outcome measures regarding 78 Federal Tax Liens that were not filed or timely filed, thus jeopardizing collection of \$3.4 million. Management stated the official IRS database for recording liens and releasing lien information is the



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Automated Lien System,² not a third-party database. We agree that Accurint³ is a third-party research tool and may not be totally accurate. However, our research showed discrepancies among all systems because none of the systems were completely accurate. Absent actual visits to recording offices, in our opinion, Accurint is the most reliable source available to verify lien filing information. Therefore, we believe the 58 liens may not have been filed and the collection of \$2.1 million may be in jeopardy. We also believe the 20 liens may not have been filed timely because the Automated Lien System showed it took an average of 329 days for the liens to be filed at the recording offices, thereby jeopardizing the collection of \$1.3 million. Management's complete response to the draft report is included as Appendix V.

Copies of this report are also being sent to IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs), at 202-622-5894.

² This is a comprehensive database that prints Notices of Federal Tax Lien, stores taxpayer information, and documents all lien activity.

³ Accurint is a vendor service that accesses public records nationwide.



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Abbreviations

ALS	Automated Lien System
BSV	Billing Support Voucher
IRS	Internal Revenue Service



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Background

A Federal Tax Lien gives the Internal Revenue Service (IRS) a legal claim to a taxpayer's property for the amount of his or her tax debt. The IRS sends the Notices of Federal Tax Lien to recording offices¹ that are responsible for recording the liens in public records. Usually the Federal Government is not the only creditor to whom a taxpayer owes money. Other creditors may also hold liens or secured rights against a taxpayer's assets in the amount of his or her indebtedness.

By filing the Notice of Federal Tax Lien, the IRS publicly notifies other creditors that the Federal Government has a claim against all of a taxpayer's property and any property rights owned or acquired after the lien is filed. This Notice is used by the courts to establish priority in certain situations, such as bankruptcy proceedings or sales of real estate.

It is critical that recording offices ensure Federal Tax Liens are timely filed and properly recorded. Failure to file and properly record a Notice of Federal Tax Lien in the recording office may jeopardize the Federal Government's priority rights against other creditors. This is extremely important to protect the interests of the Federal Government, creditors, and taxpayers in general.

Once a Federal Tax Lien is filed at the recording office, it cannot be released until the taxes, penalties, interest, and recording fees are paid in full. The taxpayer must pay all fees that a State or other jurisdiction charges to file and release the lien. These fees will be added to the amount owed. The IRS should issue a Release of the Notice of Federal Tax Lien within 30 calendar days after the taxpayer satisfies the tax due by paying the debt. In 2005, the IRS consolidated 33 lien operations located throughout the United States into the nationwide Centralized Lien Processing Unit at the Cincinnati, Ohio, Campus.²

The IRS pays lien fees using two methods: convenience checks (imprest checks³) and direct billing. Imprest checks are used to provide prepayment of the fees when lien documents are sent to the recording offices. Direct billing uses estimates for bulk lien documents to be processed at the recording offices.

This review was performed at the IRS National Headquarters in Washington, D.C., in the Small Business/Self-Employed Division Office of Collection Policy and the Centralized Lien Processing Unit in Cincinnati, Ohio, during the period July 2006 through March 2007. The audit

¹ Recording offices are the Clerk of the Circuit Court where the IRS records its Notices of Federal Tax Lien.

² Campuses are the data processing arm of the IRS. They process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

³ Imprest checks are payments issued by IRS cashiers to pay lien fees.



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



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Results of Review

The Lien Filing Process Was Successfully Centralized, and the New Unit Properly Filed Federal Tax Liens

In 2005, the IRS consolidated 33 lien operations located throughout the United States into a nationwide Centralized Lien Processing Unit at the Cincinnati, Ohio, Campus. Employees in this Unit send out the Notice of Federal Tax Lien to over 4,000 local recording offices for filing. In Fiscal Year 2006, the IRS filed 629,813 liens throughout the country. The lien processing unit processes requests for all Federal Tax Liens and releases. Employees handle telephone inquiries and correspondence regarding lien filings and releases from taxpayers, their representatives, and recording offices.

To implement the centralized process, management established an action plan to ensure numerous activities were implemented and coordinated. Management held biweekly conference calls to monitor the actions being accomplished. This included contacting and coordinating actions with the numerous recording offices, which is quite an extensive task because recording offices use procedures that can vary significantly. Management also established an oversight process including reviews that were conducted jointly by Headquarters Operations and the Office of Collection Policy in June 2006 and February 2007. As a result, numerous changes to procedures and policies were made as the organization stood up.

The IRS has taken actions to improve the effectiveness of the lien processing unit and generally prepared Federal Tax Liens accurately and timely. We selected a statistically valid sample of 150 Federal Tax Liens and determined the information recorded on them (taxpayer's name, address, tax period, and assessed amount) was correct. Federal Tax Liens were also prepared within 5 workdays of receipt of the lien request.

While management effectively implemented the centralized process, we found problems associated with the sorting and mailing of the Notices of Federal Tax Lien and the paying of lien fees to the recording offices. These problems contributed to the recording offices returning approximately 29,000 lien documents to the lien processing unit to be reworked. In some instances, recording offices incorrectly returned lien documents to the lien processing unit.

The lien processing unit relies on overtime to complete its regular duties. This trend will continue if the IRS does not improve its processing to reduce the workload. We have identified potential methods to increase the effectiveness of the lien processing unit by making the workload manageable and by reducing the volume of returned lien documents that need to be corrected.



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The Process of Paying Lien Fees Needs Improvement to Reduce the Volume of Lien Documents Returned by Recording Offices

The IRS needs to develop solutions to reduce the number of lien documents rejected by recording offices and returned to the lien processing unit for rework. Generally, the IRS uses two methods of payment for lien fees: imprest checks and direct billing. These are the most common methods of payment and represent the methods preferred by most of the recording offices, except those in Alaska. Imprest checks and direct billing are each used at about 2,000 local recording offices. Under the direct billing process, payments are made after the lien documents are processed by the recording offices and invoices are certified. This process is lengthy, and months can pass before recording offices receive their money. Therefore, more recording offices are requesting imprest checks because the payments are included with the lien documents when the documents are received for processing.

Liens, releases, and other lien documents are filed in more than 4,000 recording offices throughout the United States. Most lien documents (primarily Notices of Federal Tax Lien and releases) are generated using the Automated Lien System (ALS).⁴ Every Tuesday and Thursday, lien documents are printed from the ALS and sorted into batches by State and local recording office locations. A billing support voucher (BSV) is printed for each recording office; it shows a summary identifying the total number of lien documents, lien fees, and total cost the IRS will pay to the recording office for processing the lien documents in the batches. Recording offices should receive a BSV with all lien batches.

After the IRS assembles the lien batches and prepares the BSV, it sends them to 1 of the 4,000 local recording offices for processing. These lien documents for filing must be reviewed to ensure the appropriateness of the documents. The billing process is very time consuming and labor intensive. As part of its tax collection activities, the IRS reported it had filed and released a combined total of 805,973 Notices of Federal Tax Lien in Calendar Year 2006. With the high volume of lien documents the IRS prepares, errors occur. These errors have caused recording offices to return to the IRS entire lien batches unprocessed. Failure to file and properly record a Notice of Federal Tax Lien in a recording office may jeopardize the Federal Government's priority rights against other creditors.

The IRS developed a "reject log" to control the flow of returned lien batches. These batches are received by the clerical unit, which prepares the reject logs and captures certain information such as the reason the batches were rejected. The clerical unit forwards the returned lien documents to one of the five lien teams for correction. After the returned lien documents have been corrected, the batches are given to the clerical unit, which resends them to the recording offices for processing.

⁴ The ALS is a comprehensive database that prints Notices of Federal Tax Lien, stores taxpayer information, and documents all lien activity.



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Between January and September 2006, the IRS recorded receipt of 4,299 reject batches. We estimate these batches represent approximately 29,000⁵ lien documents returned from recording offices because of problems with the sorting and mailing of Notices of Federal Tax Lien and the paying of lien fees. We reviewed the reject logs for these 4,299 batches and found approximately 1,375 (32 percent) were returned to the lien processing unit because of fee-related issues, including incorrect lien fee amounts and missing or unsigned imprest checks. Also during this period, cashiers voided 2,234 imprest checks that had to be reissued. Most of the other 2,924 lien batches were returned because:

- Lien releases had incorrect or no recording information.
- Documents were missing information.
- Documents had been sent to the wrong recording offices.
- Liens were not filed by the recording office because the taxpayer did not reside in the county, even though he or she may have owned property there.
- Liens were returned for which recording fee amounts had increased but the recording office had not notified the IRS previously.

Each recording office sets the fee amounts for filing and releasing a Federal Tax Lien. Many of the fee issues occurred because the fee schedules were not updated to show the correct amount. This happened for several reasons: (1) recording offices did not always notify the IRS of fee changes and, (2) when the IRS was notified of fee changes, the lien processing unit did not always ensure the fee schedules were updated. When the lien processing unit receives notification of changes to a fee schedule from a recording office, the changes are given immediately to the manager of the team responsible for filing with that local recording office. The updates are then given to the ALS Coordinators so the fees can be revised on the ALS. The information needs to also be given to the team preparing the lien batches for that recording office, to use when updating the BSV. Other fee problems occurred because the lien processing unit did not enclose imprest checks when issuing lien batches to recording offices.

To address the fee issue, the IRS could implement a prepayment process through which it would pay a portion of the lien fees at the beginning of the fiscal year based on an estimate of lien documents to be processed by each recording office. Each month, recording offices would return invoices that the IRS certifies and the accounts would be adjusted, a process similar to that being used by recording offices in Alaska. The main difference is the recording offices receive an initial payment prior to processing the lien documents and, in each subsequent month, their accounts are adjusted after the invoices are certified. The only requirement is that the recording offices agree to be paid through electronic funds transfer.

⁵ This estimate is based on the following calculation. Our sample of 31 reject batches contained 209 lien documents, for an average of 6.742 lien documents per reject batch. We multiplied 6.742 x 4,299 reject batches for a total of 28,984.



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This prepayment method would benefit both the IRS and the recording offices. The IRS would eliminate the use of imprest checks, and recording offices would receive payments prior to processing lien documents. This method would also reduce the number of telephone calls received from recording offices inquiring about their payments. By our estimation, using the prepayment option would also eliminate approximately 12,000 returned lien documents related to fee problems. While the Federal Government would incur some interest-related costs for the prepayment method, the IRS could reduce the overtime being spent to rework the returned cases. In addition, the IRS could ensure lien priority is not lost because, at present, a recording office does not always file the liens when it returns them to the IRS.

Recommendations

The Director, Collection, should:

Recommendation 1: Pursue other options for paying lien fees to recording offices for processing lien documents. One option to consider is a prepayment process using electronic funds transfer through which the recording offices are partially paid for their services at the start of the fiscal year; then, each month, recording offices would return invoices that the IRS certifies and the accounts would be adjusted.

Management's Response: IRS management agreed with this recommendation. Although the Office of Chief Counsel and Office of Procurement determined Federal Government agencies are precluded from prepaying for goods and services, management agreed to pilot a lien fee payment process directly connecting lien payments to document issuance. The electronic payment testing, followed by a pilot, is scheduled to begin in San Bernardino, California. This fully automated method of lien fee payment will be based on a program interface built between the ALS and the Integrated Financial System in Beckley, West Virginia. The automated payment process will eliminate the current Centralized Case Processing-Lien Unit paper imprest method of making payments and will have the ability (through electronic funds transfer) to directly pay all recording offices' banks from the Integrated Financial System.

Recommendation 2: Implement a process to ensure lien fee changes are timely and properly updated once the IRS receives notification of change from the recording office. The Director should designate an individual to ensure the changes are made and reflect the correct amounts.

Management's Response: IRS management agreed with this recommendation, stating they will conduct reviews to ensure the ALS fee tables are updated timely. A written report will be submitted to the Operations Manager semi-annually. This responsibility has been assigned to the ALS Coordinator.



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Procedures Are Needed to Ensure Returned Lien Documents Rejected by the Recording Offices Are Properly Controlled and Timely Reworked

Generally, if lien documents are incomplete or contain errors, recording offices are unable to process them and return entire lien batches to the lien processing unit for resolution. The returned batches are handled by multiple employees before the lien documents are resolved and returned to the recording offices for processing. This process can take several months and delays the filing or releasing of the Federal Tax Liens. The delays occur because the lien processing unit has not established any time periods for resolving and resending corrected lien documents to the recording offices. Specifically:

- Reject logs were not properly maintained to effectively control the returned lien documents.
- Returned lien documents were not properly resolved, and no time periods were established for resolving and returning them to the recording offices.

Reject logs were not properly maintained to effectively control the returned lien documents

The lien processing unit did not adequately control the returned lien documents. To manage the returned lien documents, the unit uses reject logs to track the flow of the cases. However, the reject logs were not always properly completed. Our review of the reject logs showed they were incomplete because the lien processing unit employees did not always enter the following information for returned documents:

- Date received.
- Reason for return.
- Date resolved and returned to the recording office.

The omitted information prevented management from tracking the flow of the returned documents. Inadequate controls over the volume of returned lien documents prevented the lien processing unit from maintaining files appropriately. In addition, the unit does not have sufficient cabinet space to file the returned lien documents, and the documents were placed in bins on the floor. Therefore, the returned documents were not easily retrievable, and it was difficult for the lien processing unit employees to locate, correct, and return them to the recording offices. Files should be properly maintained to ensure lien documents are retrievable.

Without properly completed reject logs, management is unable to manage the resolution and tracking of the returned lien documents effectively, identify areas needing improvement, and provide feedback to the staff. To improve the effectiveness of the lien operation, the lien processing unit needs better procedures for controlling and processing returned lien documents.



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Returned lien documents were not properly resolved, and no time periods were established for resolving and returning them to the recording offices

Returned lien documents were not accurately and timely resolved, which causes additional processing issues for the lien processing unit. Between October 10 and October 12, 2006, we selected a judgmental sample of 31 rejected lien batches, with a total of 209 returned lien documents, and determined the lien processing unit did not properly resolve or document 86 returned lien documents (41 percent). The 86 cases involved the following errors:

- Missing BSVs (six cases).
- Not reworked (seven cases).
- Duplicate payment of lien fees (19 cases).
- Resolution not timely documented (54 cases).⁶

Without adequate controls over case files and BSVs, the lien processing unit is unable to reconcile the reworked lien batches to the original documents to determine whether any discrepancies exist and whether lien fees were paid. For example, we identified two lien filings for four taxpayers because the BSV was reworked in error. The lien processing unit is required to maintain file copies of the BSVs and annotate any discrepancies on them. Also, if the unit contacts a recording office regarding any discrepancy, it is required to annotate its findings on the file copy of the BSV.

To evaluate the impact of not timely and properly working returned lien documents, we also reviewed IRS computer systems and Accurant⁷ and determined 111 (53 percent) of the 209 cases were not properly reflected on these systems.

- Accurant showed 58 Notices of Federal Tax Lien were not filed at the recording offices.⁸
- Accurant showed 14 Notices of Federal Tax Lien were not released at the recording offices after the taxpayers had satisfied their tax liabilities.
- Recording information for 20 Notices of Federal Tax Lien had not been entered in the ALS within 90 calendar days of the lien prepared date.
- Incomplete or no court recording information had been entered in the ALS for six Notices of Federal Tax Lien.
- No lien release indicator was shown on the Integrated Data Retrieval System⁹ for 13 cases.

⁶ Case resolution took more than 45 calendar days.

⁷ Accurant is a vendor service that accesses public records nationwide.

⁸ The ALS showed the liens were filed at the recording offices.

⁹ This is an IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.



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Our Accurant research showed that, for 78 of the 111 cases, Federal Tax Liens were either not or untimely filed at the recording offices, which could jeopardize the collection of \$3.4 million owed to the Federal Government. Also, certificates of release were not found in recording offices, which may cause additional burden on 14 taxpayers.¹⁰

Improper or untimely resolution of returned lien documents can delay the filing of liens at the recording offices. If lien filings are delayed and the recording information is not entered in the ALS within 90 calendar days of the lien prepared date, a mismatch will occur and the lien will appear on the “lost lien report.” The lost lien report identifies each prepared lien older than 90 calendar days for which there is no record that the lien was filed at the recording office. As of March 27, 2007, the lost lien report contained 63,322 liens that need to be resolved, some more than 10 years old.

To resolve the lost lien inventory, on December 4, 2006, the Office of Collection Policy issued a memorandum instructing the lien processing unit not to replace liens that are over a specified age. It also instructed the unit to issue replacement liens for those lost liens meeting specified age and dollar limits. The lien processing unit has determined these procedures should eliminate about 31,300 of the 63,322 liens from the lost lien inventory.

Processing delays generate additional telephone inquiries from taxpayers, their representatives, recording offices, and revenue officers regarding information about the liens. During Fiscal Year 2006, the lien processing unit received more than 3,000 telephone calls per week; additional resources and overtime have been authorized to handle new issues to prevent backlogs.

Management reviews identified similar issues

Management has performed two reviews of the lien processing unit activities. The reviews were conducted jointly by Headquarters Operations and the Office of Collection Policy in June 2006 and February 2007. Normally, these reviews are an analysis to determine if the IRS timely notified taxpayers, business partners, spouses, and taxpayer representatives of the filing of Notices of Federal Tax Lien.

The scope of these reviews was expanded to provide a status update of the unit’s operation. The draft reports of the IRS reviews showed results similar to those identified in our review. For example, controls over returned lien documents are lacking. In reviewing 50 reject logs, the IRS found 12 batches were sent to the wrong counties and 14 batches were sent back for not having impress checks attached. In addition, the IRS identified batches of lien documents on the floor that contained impress checks that were not properly safeguarded.

¹⁰ See Appendix IV for details.



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Recommendations

The Director, Campus Compliance Services, should:

Recommendation 3: Establish criteria for measuring the accuracy and timeliness of the processing of returned lien documents. For example, record the dates to track the processing of the returned lien documents from date of receipt to date of rerouting to the recording offices.

Management's Response: IRS management agreed with this recommendation. The Centralized Lien Unit has created a new Rejected Document Form and implemented new procedures for accurately monitoring, reworking, and returning documents to county recorders' offices. The Department Manager will review the open Rejected Document Forms monthly and issue a written report to the Operations Manager on trends in rejected work and timeliness of resolving issues.

However, management disagreed with our outcome measures regarding 78 Federal Tax Liens that were not filed or timely filed, thus jeopardizing collection of \$3.4 million. Management stated the official IRS database for recording liens and releasing lien information is the ALS, not a third-party database (i.e., Accurint).

Office of Audit Comment: We agree that Accurint is a third-party research tool and may not be totally accurate. However, the IRS uses Accurint to verify certain information regarding the filing and releasing of Federal Tax Liens. We also relied on Accurint to verify the lien information. In addition, we researched IRS computer systems to verify the lien information for the 209 cases that needed to be reworked by the lien processing unit and returned to the recording offices to be processed.

Our research showed discrepancies among all systems because none of the systems were completely accurate. For example, the ALS research showed no lien filed and Accurint showed a lien filed. Based on its comment, the IRS would rely on its official computer system and the result would show no lien filed. This disparity can occur because the recording office may not have returned the recorded lien information or the IRS has not entered the recorded information into the ALS, when in fact the lien has actually been filed.

Another example occurred on lien releases. Lien releases are systemically generated, but the IRS does not know whether a recording office actually released a lien. Typically, once taxpayers satisfy their tax obligations, the lien releases are systemically generated and the ALS is updated, showing the lien release date. Unless a recording office is physically visited, Accurint is researched, or the IRS receives a complaint from a taxpayer, the IRS does not know whether a lien was actually released. The ALS could show a lien has been released, even though it may still be filed at the recording office.



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Absent actual visits to recording offices, in our opinion, Accurint is the most reliable source available to verify lien filing information. Therefore, we believe the 58 liens may not have been filed and the collection of \$2.1 million may be in jeopardy. We also believe the 20 liens may not have been filed timely because the ALS showed it took an average of 329 days for the liens to be filed at the recording offices, thereby jeopardizing the collection of \$1.3 million.

Recommendation 4: Ensure returned lien batches are properly maintained so the cases can be easily retrieved and reworked.

Management's Response: IRS management agreed with this recommendation, stating they will implement procedures to ensure (1) all issues on a returning BSV are resolved prior to closing a Rejected Document record and (2) the completed Rejected Document Form is associated with the BSV file. The Department Manager will review a 10 percent sample of the closed Rejected Document Forms to ensure copies have been associated with the BSV files. A written report will be provided to the Operations Manager on trends and timeliness of resolving issues.



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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this audit was to determine whether the IRS had taken appropriate actions to ensure the Centralized Lien Processing Unit is operating effectively. To accomplish our objective, we:

- I. Determined whether Notices of Federal Tax Lien were filed timely and accurately.
 - A. Obtained an ALS¹ extract containing 504,020 lien records for the first 10 months of Fiscal Year 2006.
 - B. Selected a statistical sample of 150 liens for our case review. We used attribute sampling to calculate the minimum sample size (n), which we rounded to 150:

$$n = (Z^2 p(1-p))/(A^2)$$

Z = Confidence Level: 90 percent (expressed as 1.65 standard deviation)

p = Expected Rate of Occurrence: 5 percent

A = Precision Rate: ± 3 percent

1. Validated the ALS extract by comparing the sampled records to online data from the Integrated Collection System² and the Automated Collection System³ because Small Business/Self-Employed Division management stated they had no data checks ensuring reliability, completeness, and accuracy.
2. Determined whether the lien processing unit prepared the Notices of Federal Tax Lien timely. For each sample case, we compared the lien prepared date from the ALS extract to the lien request date obtained from the Integrated Collection System, the Automated Collection System, Referral Forms, emails, or faxes to determine whether Notices of Federal Tax Lien were created within 5 calendar days, as required by IRS guidelines.

¹ The ALS is a comprehensive database that prints Notices of Federal Tax Lien, stores taxpayer information, and documents all lien activity.

² The Integrated Collection System is a 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.

³ The Automated Collection System is a telephone contact system through which telephone assistants collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.



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3. Determined whether the liens were properly notated on the ALS as being filed at the recording offices.⁴ In those instances for which the recording information did not exist, we traced back to the lost lien report and determined the status of the lien filings.
 - C. From October 10-12, 2006, selected a judgmental sample of 31 reject packages containing 209 lien documents returned by the recording offices and determined whether the lien documents were reworked according to the Internal Revenue Manual guidelines and accurately prepared. We used a judgmental sample because the IRS did not control the receipt of returned lien documents. The returned lien documents were stored on the floor, and we could not readily identify the documents that needed to be reworked; therefore, we were unable to determine the population. Also, the test was conducted to show control weaknesses for which management needed to take corrective action.
- II. Determined whether IRS management had implemented an effective quality review program to ensure Notices of Federal Tax Lien were accurately prepared.
 - A. Reviewed IRS procedures and determined whether they adequately measure the accuracy of the Notices of Federal Tax Lien.
 - B. Interviewed managers and determined the process used to ensure Notices of Federal Tax Lien were accurately prepared.
 - C. Reviewed checksheets to determine whether sufficient information was recorded and the Notices of Federal Tax Lien were accurate.
 - D. Determined whether a sufficient number of cases were reviewed and an accuracy problem existed.
 - E. Reviewed trend, feedback, or problem reports prepared and determined the sufficiency of the information gathered to address the problems.
- III. Evaluated the controls implemented over the cashier operation for processing lien payments and paying lien fees.
 - A. Discussed procedures with management.
 - B. Obtained and analyzed established policies and procedures for making lien payments and for processing taxpayer payments.
 - C. Determined whether managers performed operational reviews.
 - D. Discussed with management the benefits and drawbacks of centralizing the cashier operation.

⁴ Recording offices are the Clerks of the Circuit Court where the IRS records its Notices of Federal Tax Lien.



*The Centralized Lien Unit Properly Filed Federal Tax Liens but
Needs to Minimize the Number of and Improve Controls Over
Liens Returned by Recording Offices*

Appendix II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs)
Parker F. Pearson, Director
Edward Gorman, Audit Manager
Marcus Sloan, Lead Auditor
Darryl Roth, Senior Auditor
Denise Gladson, Auditor
Stephen Elix, Student Trainee



*The Centralized Lien Unit Properly Filed Federal Tax Liens but
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Appendix III

Report Distribution List

Acting 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, Campus Compliance Services, Small Business/Self-Employed Division SE:S:CCS
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



The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices

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:

- Increased Revenue – Potential; not filing 58 Federal Tax Liens at the recording offices¹ could jeopardize the collection of \$2.1 million owed to the Federal Government (see page 7).

Methodology Used to Measure the Reported Benefit:

From a judgmental sample of 31 rejected lien packages containing 209 lien documents, we identified 58 Federal Tax Liens totaling \$2.1 million that were not shown as being filed at the recording offices. A Notice of Federal Tax Lien gives the IRS a legal claim to a taxpayer's property for the amount of his or her tax debt. Not filing Federal Tax Liens at the recording offices may jeopardize the Federal Government's priority right against other creditors.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; not timely filing 20 Federal Tax Liens at the recording offices could jeopardize the collection of \$1.3 million owed to the Federal Government (see page 7).

Methodology Used to Measure the Reported Benefit:

From a judgmental sample of 31 rejected lien packages containing 209 lien documents, we identified 20 liens that took an average of 329 days for the liens to be filed at the recording offices, thereby jeopardizing the collection of \$1.3 million.

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; 14 taxpayers did not have their Federal Tax Liens released at the recording offices after satisfying their tax obligations (see page 7).

¹ Recording offices are the Clerks of the Circuit Court where the IRS records its Notices of Federal Tax Lien.



The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices

Methodology Used to Measure the Reported Benefit:

From a judgmental sample of 31 rejected lien packages containing 209 lien documents, we identified 14 taxpayers that did not have their Federal Tax Liens released at the recording offices after satisfying their tax obligations. The IRS issues a Release of the Notice of Federal Tax Lien within 30 calendar days after the taxpayer satisfies the tax due by paying the debt. Taxpayer burden could be affected because a Federal Tax Lien gives the IRS a legal claim to a taxpayer's property for the amount of the tax debt that the taxpayer no longer owes.



The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices

Appendix V

Management's Response to the Draft Report

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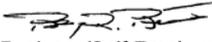


DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D. C. 20224

SMALL BUSINESS/SELF-EMPLOYED DIVISION

July 11, 2007

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:  Kathy K. Petronchak
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number and Improve Controls over Liens Returned by Recording Offices (Audit # 200630007)

We reviewed your draft report "Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number and Improve Controls over Liens Returned by Recording Offices." While we agree additional efforts are needed by the IRS to reduce the volume of liens returned by recording offices, we appreciate your acknowledgement of the multiple actions we have taken to improve the effectiveness of the lien processing unit.

We agree with both of your recommendations and our comments are attached. However, we would like to clarify two items in the report. First, the report states the IRS uses three methods for paying lien fees: convenience checks (imprest), direct billing, and payment purchase cards. The IRS does not utilize payment purchase cards to pay lien fees.

Second, the report references the use of Accurint as a research tool used to secure lien filing and lien release data. Accurint is one of many tools used to perform research and not all county recorders post lien information to this site. The Accurint Website includes the following disclaimer on the accuracy of their data:

"The Public Records and commercially available data sources used in the system have errors. Data is sometimes entered poorly, processed incorrectly and is generally not free from defect. This system should not be relied upon as definitively accurate. Before relying on any data this system supplies, it should be independently verified. For Secretary of State documents, the following data is for information purposes only and is not an official report. Certified copy may be obtained from that individual state's Department of State."

We disagree with the outcome measure in this report. The official IRS database for recording and releasing lien information is the Automated Lien System (ALS), not a third party database. Since all but 20 county recordings were input to ALS timely, we cannot



The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices

agree with the outcome measure stating 78 Federal Tax Liens were not filed or timely filed jeopardizing collection of \$3.4 million.

If you have questions or concerns, please contact me at (202) 622-0600 or Brenda A. Dial, Acting Director, Campus Compliance Services at (202) 283-2518.

Attachment



The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices

Attachment

RECOMMENDATION 1:

Pursue other options for paying lien fees to recording offices for processing lien documents. One option to consider is a prepayment process using electronic funds transfer through which the recording offices are partially paid for their services at the start of the fiscal year; then, each month, recording offices would return invoices that the IRS certifies and the accounts would be adjusted.

CORRECTIVE ACTIONS:

1. Following consultation with Counsel and Procurement regarding the legality and feasibility of large scale lien fee (prepayment) draw down accounts, we determined government agencies are generally precluded from prepaying for goods and services (see 31 U.S.C § 3321).
2. Programming is currently underway for a pilot lien fee payment process directly connecting lien payments to document issuance. The electronic payment testing followed by a pilot is scheduled to begin in San Bernardino, California. This fully automated method of lien fee payment will be based on a program interface built between the Automated Lien System (ALS) and the Integrated Financial System (IFS) in Beckley, West Virginia. The automated payment process will eliminate the current Centralized Case Processing-Lien Unit paper imprest method of making payments and have the ability to pay all recording offices through electronic funds transfer directly to their bank from the IFS system. We plan to start the streamlined electronic payment process with a state that currently pays with imprest funds. Further, the E-Lien Release 3 Website will be capable of receiving lien fee schedule changes from the recording offices as well as providing links for recording officials to sign up for electronic payment, changing banking information, and linking to other sites. Upon successful completion of the testing, we will establish a recording office outreach plan and rollout schedule.

IMPLEMENTATION DATE:

1. Completed
2. June 30, 2009

RESPONSIBLE OFFICIAL:

Director, Collection, Small Business/Self-Employed Division

CORRECTIVE ACTION(S) MONITORING PLAN:

The Director, Collection Policy will monitor programming, testing, and piloting of the interface system and will provide a status report to the Director, Collection, Small Business/Self-Employed Division.



The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices

RECOMMENDATION 2:

Implement a process to ensure lien fee changes are timely and properly updated once the IRS receives notification of change from the recording office. The Director should designate an individual to ensure the changes are made and reflect the correct amounts.

CORRECTIVE ACTIONS:

IRM 5.19.12.10 (01-01-07) requires the Centralized Lien Unit (CLU) to update the ALS (Automated Lien System) fee table within three days following referral by the recording office, a field employee, or the Governmental Liaison. To further enhance this requirement, CLU will also conduct a review to ensure the ALS fee table is updated timely and a written report will be submitted to the Operations Manager semi-annually. This responsibility has been assigned to the ALS Coordinator.

IMPLEMENTATION DATE:

August 30, 2007

RESPONSIBLE OFFICIAL:

Director, Campus Compliance Services, Small Business/Self-Employed Division

CORRECTIVE ACTION(S) MONITORING PLAN:

The SB/SE Director, Campus Filing and Payment Collection, will monitor the status and advise the SB/SE Director, Campus Compliance Services, of any delays in implementing.

RECOMMENDATION 3:

Establish criteria for measuring the accuracy and timeliness of the processing of returned lien documents. For example, record the dates to track the processing of the returned lien documents from date of receipt to date of rerouting to the recording offices.

CORRECTIVE ACTIONS:

1. The CLU created a new Rejected Document Form and implemented new procedures for accurately monitoring, reworking, and returning documents to county recorders offices.
2. The Department Manager will review the open Rejected Document Form monthly and issue a written report to the Operations Manager on trends in rejected work and timeliness of resolving issues.

IMPLEMENTATION DATE:

1. Completed
2. August 30, 2007

RESPONSIBLE OFFICIAL:

Director, Campus Compliance Services, Small Business/Self-Employed Division



The Centralized Lien Unit Properly Filed Federal Tax Liens but Needs to Minimize the Number of and Improve Controls Over Liens Returned by Recording Offices

CORRECTIVE ACTION(S) MONITORING PLAN:

The SB/SE Director, Campus Filing and Payment Collection, will monitor the status and advise the SB/SE Director, Campus Compliance Services, of any delays in implementing.

RECOMMENDATION 4:

Ensure returned lien batches are properly maintained so the cases can be easily retrieved and reworked.

CORRECTIVE ACTIONS:

1. CLU will implement procedures to ensure that all issues on a returning Bill Support Voucher (BSV) are resolved prior to closing a Rejected Document record, and that the completed Rejected Document Form is associated with the BSV file.
2. The Department Manager will review a 10 percent sample of the closed Rejected Documents to ensure that a copy has been associated with the BSV files. A written report will be provided to the Operations Manager on trends and timeliness of resolving issues.

IMPLEMENTATION DATE:

1. July 30, 2007
2. August 30, 2007

RESPONSIBLE OFFICIAL:

Director, Campus Compliance Services, Small Business/Self-Employed Division

CORRECTIVE ACTION(S) MONITORING PLAN:

The SB/SE Director, Campus Filing and Payment Collection, will monitor the status and advise the SB/SE Director, Campus Compliance Services, of any delays in implementing.