



*Control Weaknesses Could Allow  
Taxpayers' Delinquent Accounts to  
Be Inappropriately Closed As  
Currently Not Collectible*

**September 17, 2012**

**Reference Number: 2012-40-108**

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

### **CONTROL WEAKNESSES COULD ALLOW TAXPAYERS' DELINQUENT ACCOUNTS TO BE INAPPROPRIATELY CLOSED AS CURRENTLY NOT COLLECTIBLE**

## Highlights

**Final Report issued on September 17, 2012**

Highlights of Reference Number: 2012-40-108 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

### **IMPACT ON TAXPAYERS**

Some taxpayers try to resolve their delinquent account by working with an assistor at one of the IRS's walk-in offices called Taxpayer Assistance Centers. If the taxpayer has no ability to pay, the taxpayer account could be closed as currently not collectible. When taxpayer accounts are closed inappropriately as currently not collectible, taxpayers may be burdened and the IRS may not be able to collect taxes owed when a taxpayer's income increases.

### **WHY TIGTA DID THE AUDIT**

This audit was initiated because of a referral from the TIGTA Office of Investigations. Delinquent taxpayer accounts were closed as currently not collectible without IRS managerial approval and without detection. The objective of the audit was to determine whether controls over balance due accounts closed as currently not collectible in the Field Assistance Office are sufficient to ensure all actions are appropriate.

### **WHAT TIGTA FOUND**

An analysis of a judgmental sample of 17 cases and a statistically valid sample of 136 taxpayer accounts closed in the Taxpayer Assistance Centers as currently not collectible identified that the accounts were not worked according to procedures. Because cases lacked documentation, such as financial statements and case history notes, it could not be determined whether the correct decision was made to close the cases as currently not

collectible. The total assessed balance for the 17 cases was almost \$289,000, and the total assessed balance for the 136 taxpayer accounts was approximately \$2.5 million.

Of the 17 cases reviewed, four (24 percent) cases did not include the required financial statements, four (24 percent) cases had closing codes that were higher than warranted based on the taxpayers' financial statements, nine (53 percent) cases did not have the required tax liens, and 16 (94 percent) cases were closed without documentation of a manager's approval on the Accounts Management Services System.

Of the 136 taxpayer accounts reviewed, 13 (10 percent) had closing codes that were lower than warranted based on case documentation, and 28 (21 percent) had closing codes that were higher than warranted.

### **WHAT TIGTA RECOMMENDED**

TIGTA recommended that the IRS: 1) ensure assistors follow established procedures, 2) clarify internal guidelines requiring management approval of cases in the Accounts Management Services System history section, 3) conduct a risk analysis to determine the risk of not segregating duties, and 4) implement security reviews and reports that can be used to evaluate the assistors' use of system command codes.

The IRS agreed with the recommendations. It plans to remind assistors of their responsibility to adequately document cases and follow internal procedures, clarify guidelines requiring managerial documentation of currently not collectible cases on the Account Management Services System, and complete an analysis to assess the risks associated with the non-segregation of duties in Taxpayer Assistance Centers where staffing levels do not permit proper segregation. The IRS agreed with the need for security reviews and believes this can be done through reviews of monthly usage reports provided by the Integrated Data Retrieval System's online reports services and plans to reemphasize to managers the importance of following the security review guidelines.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

September 17, 2012

**MEMORANDUM FOR** COMMISSIONER, WAGE AND INVESTMENT DIVISION

**FROM:**

Michael E. McKenney  
Acting Deputy Inspector General for Audit

**SUBJECT:**

Final Audit Report – Control Weaknesses Could Allow Taxpayers’  
Delinquent Accounts to Be Inappropriately Closed As Currently Not  
Collectible (Audit # 201240006)

This report presents the results of our review to determine whether controls over balance due accounts closed as currently not collectible in the Field Assistance Office are sufficient to ensure all actions are appropriate. This audit was conducted as a result of a Treasury Inspector General for Tax Administration Office of Investigations referral that identified material control weaknesses that allow Internal Revenue Service assistors to place balance due taxpayer accounts in currently not collectible status without obtaining proper managerial approval. This audit is included in our Fiscal Year 2012 Annual Audit Plan and addresses the major management challenge of Tax Compliance Initiatives.

Management’s complete response to the draft report is included in Appendix VI.

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Augusta R. Cook, Acting Assistant Inspector General for Audit (Returns Processing and Account Services), at (770) 617-6434.



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*Abbreviations*

AMS	Accounts Management Services
IDRS	Integrated Data Retrieval System
IRS	Internal Revenue Service



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## *Background*

The Internal Revenue Service (IRS) has a policy that states:

*If, after taking all steps in the collection process, it is determined that an account receivable is currently not collectible, it should be so reported in order to remove it from active inventory.<sup>1</sup>*

The collection process begins with a series of delinquency notices or bills mailed to a taxpayer when the taxpayer does not file a required tax return(s) or pay taxes due. When the taxpayer fails to respond within a specified time period, a delinquent return or balance due account is generated. Generally, the IRS attempts to contact the taxpayer by telephone at this point.

***Closing taxpayers' balance due accounts as currently not collectible is a high-risk action because the balances due from the taxpayers may never be collected.***

When the IRS determines that a taxpayer's account is currently not collectible, IRS personnel stop actively working the case<sup>2</sup> and suspend collection action until the taxpayer's ability to pay improves. Closing taxpayers' balance due accounts as currently not collectible is a high-risk action because the balances due from the taxpayers may never be collected.

### ***Some taxpayers try to resolve their balance due accounts by working with assistors at one of the IRS's walk-in offices, called Taxpayer Assistance Centers<sup>3</sup>***

A Taxpayer Assistance Center assistor will work with the taxpayer and determine whether the taxpayer can make payments or is unable to pay. If the taxpayer is unable to pay and the taxpayer's liability exceeds a certain dollar amount, the assistor is required to obtain and analyze information on the taxpayer's assets and financial information. If the assistor determines the taxpayer has the ability to pay or the taxpayer agrees to make payments, various collection options are considered, including installment agreements. If the taxpayer has no ability to pay, the taxpayer account is closed as currently not collectible.<sup>4</sup> The decision to place an account in currently not collectible status requires the approval of a manager.

The number of taxpayers who visit the Taxpayer Assistance Centers who are unable to pay their balance due almost tripled from Calendar Year 2011 to 2012. IRS management believes that the

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<sup>1</sup> Accounts can be declared currently not collectible for various reasons including the IRS's inability to locate or contact the taxpayer, death of the taxpayer, bankruptcy, or hardship. A hardship occurs when an individual taxpayer is unable to meet his or her basic living expenses.

<sup>2</sup> Throughout this report, we refer to taxpayer accounts closed as currently not collectible as a case.

<sup>3</sup> Taxpayer Assistance Centers are the responsibility of the IRS's Field Assistance Office.

<sup>4</sup> Most cases closed as currently not collectible in the Taxpayer Assistance Centers are hardship cases.



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increase is due to the economic downturn. Figure 1 shows the number of taxpayers with tax accounts closed as currently not collectible in the Taxpayer Assistance Centers in Calendar Years 2009 through 2012.

**Figure 1: Currently Not Collectible Closures  
in Taxpayer Assistance Centers  
for Calendar Years 2009 Through 2012**

Calendar Year	Number of Taxpayers	Amount
2009	284	\$4,707,471
2010	1,092	\$15,345,417
2011	3,952	\$71,979,183
2012	11,384	\$159,377,982
Total	16,712	\$251,410,053

*Source: Our analysis of the Taxpayer Information File<sup>5</sup> as of June 19, 2012.*

Once an individual taxpayer account is closed as currently not collectible, the account is systemically monitored, and if the taxpayer's income increases, the account is reactivated. If the account is reactivated, the taxpayer is sent a notice about taxes still owed on his or her account. These reviews can result in subsequent enforcement actions to collect the outstanding balances due or to return the account to a currently not collectible status.

This review was performed at the Wage and Investment Division's Field Assistance Office in Atlanta, Georgia; the Taxpayer Assistance Centers in Augusta, Chamblee, Dalton, and Smyrna, Georgia; the Small Business/Self-Employed Division's Field Collection function in Sandy Springs, Georgia; and the Automated Collection Service function in Chamblee, Georgia, during the period May through July 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 finding and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding 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.

<sup>5</sup> This database is the major database used within the Integrated Data Retrieval System (IDRS). It contains business and individual taxpayer information. The IDRS is the IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.



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## *Results of Review*

### ***Controls Over Currently Not Collectible Accounts Do Not Ensure All Actions Taken Are Appropriate***

Controls over balance due accounts closed as currently not collectible in the Field Assistance Office are insufficient to ensure all actions were appropriate. Tests of currently not collectible cases closed by Taxpayer Assistance Center assistors showed that the cases were not worked according to guidelines. Specifically:

- Required financial statements were not completed.
- The closing codes were not applied correctly.
- Federal tax liens were not appropriately placed on taxpayers' accounts.

However, we could not determine whether the correct decisions were made to close a case as currently not collectible because the cases did not contain sufficient documentation, such as financial statements and case history notes. This happened because the assistors did not follow procedures. Further, some cases are being closed without manager approval. Inappropriately closing taxpayer accounts as currently not collectible affects tax administration and whether taxes are collected on balance due accounts.

### ***Procedures were not followed when taxpayer balance due accounts were closed as currently not collectible***

An analysis of a judgmental sample of 17 taxpayer cases<sup>6</sup> and a statistically valid sample of 136 taxpayer accounts closed as currently not collectible on the Accounts Management Services (AMS) System<sup>7</sup> identified that procedures were not followed. The total assessed balance for the 17 cases was \$288,854, and the total assessed balance for the 136 taxpayer accounts was approximately \$2.5 million.

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<sup>6</sup> A judgmental sample is a nonstatistical sample, the results of which cannot be used to project to the population. The same sample of 17 cases was used for the analysis of the financial statements, closing codes, Federal tax liens, and management approval.

<sup>7</sup> A computer-based system used to answer and resolve inquiries related to taxpayer accounts. The AMS System provides a common interface that allows users of multiple IRS systems to view history and comments from other systems and to access a variety of case processing tools without leaving the AMS System. All employees are required to use the AMS System to research, document, and resolve all account contacts, adjustments, and referrals.



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IRS guidelines state that employees are required to identify and create the appropriate issue in the AMS System and input history for all account accesses. The Government Accountability Office's *Standards for Internal Control in the Federal Government*<sup>8</sup> state that all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination. All documentation and records should be properly managed and maintained.

**Required financial statements were not always completed**

An analysis of currently not collectible cases identified that required financial statements were not always completed. Financial statements are required for total unpaid balances of \$1,500 or more. Of the 17 cases reviewed, four (24 percent) cases did not include a required financial statement.

A financial statement is an electronic statement that an assistor is required to complete using the AMS System. An assistor obtains financial information to determine the taxpayer's maximum ability to pay his or her delinquent tax debt based on the taxpayer's current financial condition. Obtaining financial information can also result in determining that a taxpayer currently has no ability to pay and that the taxpayer's account should be placed in currently not collectible status.

**Closing codes were incorrect**

Closing codes are systemically generated on the AMS System from information input into the financial statements. Assistors are also required to input a closing code to the Integrated Data Retrieval System (IDRS). The closing code equates to an amount of income the taxpayer may claim on a future tax return without being subject to additional collection action and is based on the taxpayer's current income and expenses.

An analysis of the 17 currently not collectible cases showed that closing codes were not all correctly input into the IDRS.

- 4 (24 percent) cases had closing codes higher than warranted based on the taxpayers' financial statements.
- 13 (76 percent) cases had the correct closing codes.

The amount of the total assessed balance was \$108,790 for the four taxpayers' accounts on which closing codes were input that were higher than warranted.

An analysis of the 136 currently not collectible cases identified that closing codes were not correctly input to the IDRS. Of the 136 cases, 41 (30 percent) had incorrect closing codes.

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<sup>8</sup> Government Accountability Office (formerly known as the General Accounting Office), GAO/AIMD-00-21.3.1, *Standards for Internal Control in the Federal Government*, p. 15 (Nov. 1999).



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- 13 (10 percent) had closing codes that were lower than warranted based on case documentation.
- 28 (21 percent) had closing codes that were higher than warranted based on case documentation.

The taxpayer account is systemically reviewed annually when a taxpayer files an income tax return. If a taxpayer reports increased income above the predetermined amount based on the currently not collectible closing code, the account is reactivated systemically. A *lower* than determined closing code could burden the taxpayer when the IRS takes premature collection action, and a *higher* than determined closing code could result in lost revenue.

For the 28 cases closed with a higher closing code, the total balance due was more than \$796,000, with an average of \$28,446 for each taxpayer account. For Calendar Year 2011, 3,952 taxpayer accounts were closed as currently not collectible. Of those 3,952 taxpayer accounts, there is a risk that 814<sup>9</sup> will not be reactivated. Based on the average amount of the cases closed as currently not collectible, there is potential lost revenue of \$23 million for Calendar Year 2011; projected over five years, there is a potential of \$116 million in lost revenue. We recognize that not all of this revenue will be collected because an increase in a taxpayer's income does not necessarily mean the taxes will be collected.

For the 13 cases closed with a lower closing code, there is a potential that 378 taxpayers<sup>10</sup> will be burdened as a result of taxpayer accounts being erroneously reinstated as collectible in Calendar Year 2011; projected over five years, 1,889 taxpayers could be burdened. Figure 2 provides the income and expense amounts related to closing codes.

**Figure 2: Income and Expenses Related to Closing Codes**

Income	Closing Code	Monthly Expenses
\$20,000	24	\$0 – \$1,388
\$28,000	25	\$1,389 – \$1,944
\$36,000	26	\$1,945 – \$2,500
\$44,000	27	\$2,501 – \$3,055
\$52,000	28	\$3,056 – \$3,611
\$60,000	29	\$3,612 – \$4,166
\$68,000	30	\$4,167 – \$4,722

<sup>9</sup> We multiplied the 3,952 taxpayer accounts by the higher closing code error rate of 20.59 percent to determine the number of cases that could potentially have an incorrect closing code that is higher than required.

<sup>10</sup> We multiplied the 3,952 taxpayer accounts by the lower closing code error rate of 9.56 percent to determine the number of cases that could potentially have an incorrect closing code that is lower than required.



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Income	Closing Code	Monthly Expenses
\$76,000	31	\$4,723 – \$5,277
\$84,000	32	\$5,278 or more

Source: The IRS's Internal Revenue Manual.

**Federal tax liens were not placed on taxpayers' accounts**

An analysis of the 17 currently not collectible cases identified that required Federal tax liens were not appropriately placed on taxpayer accounts with balances of more than \$10,000.

- 8 (47 percent) accounts did not require a tax lien.
- 9 (53 percent) accounts with a total assessed balance of \$253,774 did not have the required tax liens placed on the accounts.

When unpaid balances are equal to or exceed \$10,000, a Federal tax lien is to be placed on a currently not collectible taxpayer account. A lien is placed on an account as security for an outstanding tax liability.

**Management approval is not always documented or appropriate**

An analysis of the 17 currently not collectible cases showed that cases were closed on the AMS System but frequently did not have the required managerial approval.

- \*\*\*\*\*1\*\*\*\*\*
- \*\*\*\*\*1\*\*\*\*\*

To place an account in currently not collectible status requires the approval of a manager. However, the manager is not required to document the approval in the AMS System. There are two options for management approval: the assistor routes a Form 4442, *Inquiry Referral*, to the manager for approval or the manager directly accesses the AMS System account and inputs a comment in the history section.

- Managers are required to thoroughly evaluate the currently not collectible taxpayer account and research it before making a decision regarding the account's collectability status. Once the manager has made the determination, Form 4442 is routed back to the employee approved or disapproved. The Form 4442 and routing history is retained on the AMS System for approximately 90 days and then is systemically deleted. Form 4442 has no place for a manager to sign to indicate approval of the case. Once deleted, there is no longer evidence of the manager's approval.



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- Managers can access the AMS System and input comments in the history section. These comments are permanently retained. Managers are required to use this method for mirrored cases<sup>11</sup> closed as currently not collectible and taxpayer accounts not approved to be closed as currently not collectible. Information on the history section is permanently retained.

The Government Accountability Office's *Standards for Internal Control in the Federal Government* state that transactions and other significant events should be authorized and executed only by persons acting within the scope of their authority. This is the principal means of assuring that only valid transactions are initiated or entered into. Authorizations should be clearly communicated to managers and employees.

**Systemic controls do not prevent assistors from approving their own case closings and updating the taxpayer's account to currently not collectible status on the IDRS**

The Taxpayer Assistance Center assistors are required to use the AMS System to determine if a taxpayer's delinquent account(s) is uncollectible. The assistor must manually update the taxpayer's account in the IDRS. The assistors can accomplish both of these tasks without managerial approval and without detection. The Treasury Inspector General for Tax Administration's Office of Investigations and Office of Audit identified 28 taxpayer accounts for which assistors did not obtain management approval on currently not collectible closures.

There were 30 taxpayer accounts accessed by Taxpayer Assistance Center assistors with no associated cases on the AMS System. The tax accounts were updated by inputting the currently not collectible status directly to the IDRS. No determination could be made whether the taxpayer accounts were updated by Taxpayer Assistance Center assistors or employees from other offices or functions. In addition, there were no associated IRS employee numbers on transactions input to tax accounts. The total assessed balance for these inappropriately closed accounts was \$338,536.

**There are no preventive controls**

Assistors can close a case on the AMS System without managerial review or approval. Additionally, assistors use the IDRS command code REQ77<sup>12</sup> to input a currently not collectible status on a taxpayer account and do not need approval to input this command code.

IRS management stated that currently there are 187 Taxpayer Assistance Centers with only one or two technical employees, making it unrealistic to segregate duties in those locations (for example, separating the acceptance of payments and inputting transactions into the computer for

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<sup>11</sup> These are cases in which one taxpayer on a jointly filed tax return needs to be treated separately from the other taxpayer and is unable to pay the assessed balance.

<sup>12</sup> This code is used to input a transaction, Notice of Action for Entry, on the Master File/IDRS. 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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the same taxpayers). The IRS stated these Taxpayer Assistance Centers processed 271,010 payments totaling approximately \$432 million from October 1, 2011, through June 15, 2012. However, the IRS has not conducted a risk analysis to determine if it can sufficiently minimize the risk associated with this lack of segregation of duties.

The Government Accountability Office's *Standards for Internal Control in the Federal Government* state that management needs to comprehensively identify risks and should consider all significant interactions between the entity and other parties as well as internal factors at both the entity wide and activity levels. Risk identification methods may include qualitative and quantitative ranking activities, management conferences, forecasting and strategic planning, and consideration of findings from audits and other assessments. Once risks have been identified, they should be analyzed for their possible effect. Risk analysis generally includes estimating the risk's significance, assessing the likelihood of its occurrence, and deciding how to manage the risk and what actions should be taken.

In the Examination function, tax auditors are prohibited from inputting transactions to taxpayer accounts and have read-only access to the IDRS. Adjustments to accounts under examination are conducted by a different function. In addition, some IRS functions use Form 3177, *Notice for Action of Entry on Master File*, to maintain separation of duties. This form is completed with the required currently not collectible information and is sent to the Accounting Operations branch for entries to be input to the taxpayer account. However, Form 3177 has not been revised since November 2005 and does not require management approval.

The Collection Field function uses the Integrated Collection System<sup>13</sup> to input taxpayer interview notes, prepare financial statements, and assess the taxpayer's ability to pay balances due. The system does not allow the employee to approve his or her own work and the employee has read-only access to the IDRS.

There are no detective controls

The AMS System does not generate daily or weekly reports showing cases closed as currently not collectible. No other reports are available listing the cases closed as currently not collectible in the Taxpayer Assistance Centers. Although an employee may obtain manager approval, there is no review process to ensure employee entries to the AMS System and the IDRS are accurate and complete.

Inappropriately closing taxpayer accounts as currently not collectible creates a high risk of not collecting unpaid taxpayer account balances. A process should be implemented to systemically notify managers of the accounts that are closed currently not collectible, and managers need to access the AMS System history section and approve the currently not collectible cases.

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<sup>13</sup> An information management system designed to improve revenue collections by providing revenue officers access to the most current taxpayer information, while in the field, using laptop computers for quicker case resolution and improved customer service.



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Taxpayer Assistance Center assistors need read-only access to the IDRS, and any adjustments to accounts should be sent to the Account Resolution branch to be input to the taxpayer's account. In addition, a procedure should be implemented whereby the manager is required to review currently not collectible closures and approve the entries that are sent to the Account Resolution branch. If Form 3177 is used, the form should be revised requiring management approval.

On June 25, 2012, the Government Accountability Office reported<sup>14</sup> that two clerks in a campus support unit had the ability to make adjustments to a taxpayer's account through the IDRS while also maintaining physical possession of hard-copy receipts. IRS procedures did not specifically prohibit access to the IDRS commands for certain employees who were responsible for processing payments, and IRS procedures did not require monitoring these particular employees' system accesses. The Government Accountability Office recommended that the IRS direct the appropriate IRS officials to update the Internal Revenue Manual to specify steps to be followed to prevent campus support clerks from making adjustments to taxpayer accounts. The IRS agreed with the recommendation. Taxpayer Assistance Center assistors process payments and can adjust accounts by placing the accounts in currently not collectible status.

The Government Accountability Office's *Standards for Internal Control in the Federal Government* state that key duties and responsibilities should be segregated among different people to reduce the risk of error or fraud. The standards further state that this segregation of duties should include dividing the responsibilities for authorizing, recording, and reviewing transactions as well as handling any related assets. No one individual should be in a position to both cause and conceal an error or irregularity by controlling certain key aspects of a transaction or event. Internal controls should generally be designed to assure that ongoing monitoring occurs in the course of normal operations and includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties.

IRS guidelines state that front-line managers of IDRS users are responsible for day-to-day implementation and administration of IDRS security<sup>15</sup> in their unit, which includes ensuring the command code usage of employees with sensitive command codes are reviewed at least monthly. A lack of sufficient segregation of duties over the Taxpayer Assistance Center activities increases the risk of unauthorized access to taxpayer information, which can lead to the loss, theft, or misuse of this information.

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<sup>14</sup> Government Accountability Office, GAO-12-683R, *Management Report: Improvements Are Needed to Enhance the Internal Revenue Service's Internal Controls and Operating Effectiveness* (June 2012).

<sup>15</sup> Each employee who uses the IDRS is assigned a command code profile that determines the types of transactions he or she can process.



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## **Recommendations**

The Commissioner, Wage and Investment Division, should:

**Recommendation 1:** Ensure assistors thoroughly document cases and follow established procedures when closing taxpayer accounts as currently not collectible. This should include procedures for completing financial statements, documenting correct closing codes on taxpayer accounts, and ensuring required liens are filed.

**Management's Response:** IRS management agreed with the recommendation and will ensure assistors are reminded of their responsibility to adequately document cases and follow Internal Revenue Manual procedures when closing taxpayer accounts as currently not collectible. E-mail communications will be distributed to the field as a reminder of the currently not collectible procedures for completing financial statements, closing codes, and the filing of required liens. In addition, IRS Fiscal Year 2013 Continuing Professional Education includes a currently not collectible refresher lesson for all Individual Tax Advisory Specialist employees.

**Recommendation 2:** Clarify internal guidelines requiring that management document approval of balance due cases in the AMS System history section. This should ensure that appropriate manager approvals are completed and retained on the AMS System.

**Management's Response:** IRS management agreed with the recommendation and will clarify guidelines requiring managerial documentation of currently not collectible cases on the AMS System. E-mail reminders will be distributed to the IRS field regarding these requirements.

**Recommendation 3:** Conduct a risk analysis to evaluate the risk of not segregating duties in the Taxpayer Assistance Centers. The risk analysis should include the costs associated with separating duties when processing payments, taking case actions (including closing cases as currently not collectible), and making account adjustments. It should also include any potential effect on taxpayer burden and the risk associated with lost revenue. As needed, implement controls and revise IRS guidelines to ensure appropriate separation of duties.

**Management's Response:** IRS management agreed with the recommendation and will complete an analysis to assess the risks associated with the non-segregation of duties in Taxpayer Assistance Centers where staffing levels do not permit proper segregation. The IRS will use the results of the assessment to determine appropriate steps to mitigate risks that exceed acceptable levels.

**Recommendation 4:** Implement security reviews and reports that can be used to evaluate the assistors' use of IDRS command code REQ77.

**Management's Response:** IRS management agreed with the intent of this recommendation and believes it can be met through reviews of monthly usage reports



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provided by the IDRS Online Reports Services, which includes all REQ77 command code activity. The IRS will reemphasize to their managers the importance of following the security review guidelines provided by IRM 10.8.34, *IDRS Security Controls*.



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## Appendix I

### *Detailed Objective, Scope, and Methodology*

Our objective was to determine whether controls over balance due accounts closed as currently not collectible in the Field Assistance Office are sufficient to ensure all actions are appropriate. To accomplish our objective, we:

- I. Identified the procedures and processes the Field Assistance Office had in place to work and close currently not collectible cases and determined whether they were sufficient to protect revenue and reduce the risk of fraud.
- II. Assessed the Field Assistance Office's processes for working and approving currently not collectible cases to ensure all case actions were appropriate.
  - A. Selected and reviewed a judgmental sample<sup>1</sup> of closed currently not collectible cases to determine if all required actions were taken. To identify the currently not collectible cases, we queried the Taxpayer Information File<sup>2</sup> for the period January 1, 2009, through April 30, 2012. We matched the results to the AMS System<sup>3</sup> user table and then matched those results to the list of Taxpayer Assistance Center assistors to identify the transactions entered into the AMS System and the IDRS. From a population of 16,712 taxpayer accounts, we selected 17 cases for review and analysis.
  - B. Selected a statistically valid sample<sup>4</sup> of 136 taxpayer accounts from a population of 3,952 taxpayer accounts that were closed as currently not collectible in the Taxpayer Assistance Centers in Calendar Year 2011. We used a confidence level of 90 percent, an error rate of 15 percent, and a precision level of  $\pm 5$  percent to determine our sample size. We oversampled by three taxpayer accounts. We used the sample to determine the number of taxpayer accounts that showed an incorrect closing code in the IDRS.

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<sup>1</sup> A judgmental sample is a nonstatistical sample, the results of which cannot be used to project to the population. We used a judgmental sample because we did not plan to project our results.

<sup>2</sup> This database is the major database used within the IDRS. It contains business and individual taxpayer information. The IDRS is the IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records

<sup>3</sup> A computer-based system used to answer and resolve inquiries related to taxpayer accounts. The AMS System provides a common interface that allows users of multiple IRS systems to view history and comments from other systems and to access a variety of case processing tools without leaving the AMS System. All employees are required to use the AMS System to research, document, and resolve all account contacts, adjustments, and referrals.

<sup>4</sup> We used a statistically valid sample because we planned to project our results for this test.



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- III. Determined whether the Field Assistance Office had sufficient reports to monitor and track currently not collectible cases to ensure guidelines were followed.
- IV. Obtained data from the Taxpayer Information File and the AMS System to determine the number of cases closed by Taxpayer Assistance Center assistors and the amount of assessed balances.
- V. Ensured all data used during the audit was valid, complete, and accurate. We assessed the reliability of data extracted from the Taxpayer Information File and the AMS System by (1) performing electronic testing of required data elements, (2) reviewing existing information about the data and the system that produced them, (3) interviewing agency officials knowledgeable about the data, and (4) selecting a judgmental sample of ten accounts from each system and verifying that the data elements extracted matched the taxpayer account information on the IDRS and the cases on the AMS System. We determined that the data were sufficiently reliable for purposes of this report.

**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 internal controls relevant to our audit objective include the IRS's internal guidelines used by the Taxpayer Assistance Center assistors to close currently not collectible cases and the management information systems used to control currently not collectible cases. We evaluated controls by reviewing cases, interviewing management, and reviewing policies and procedures. We selected a judgmental sample of 17 cases and a statistically valid sample of 136 cases.



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**Appendix II**

*Major Contributors to This Report*

Michael E. McKenney, Assistant Inspector General for Audit (Returns Processing and Account Services)

Augusta R. Cook, Acting Assistant Inspector General for Audit (Returns Processing and Account Services)

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Kathy Coote, Auditor

Nelva Usher, Auditor

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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 Operations Support OS  
Deputy Commissioner for Services and Enforcement SE  
Commissioner, Small Business/Self-Employed Division SE:S  
Deputy Commissioner, Small Business/Self-Employed Division SE:S  
Deputy Commissioner, Services and Operations, Wage and Investment Division SE:W  
Director, Customer Assistance, Relationships and Education SE:W:CAR  
Director, Field Collection, Small Business/Self-Employed Division SE:S:FC  
Director, Field Assistance SE:W:CAR:FA  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Office of Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis RAS:O  
Chief, Program Evaluation and Improvement, Wage and Investment Division SE:W:S:PEI  
Office of Internal Control OS:CFO:CPIC:IC  
Audit Liaison: Chief, Program Evaluation and Improvement, Wage and Investment Division  
SE:W:S:PEI



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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:**

- Increased Revenue – Potential; \$115,725,586 for 814 taxpayer accounts (see page 3).<sup>1</sup>

#### **Methodology Used to Measure the Reported Benefit:**

From a statistically valid sample of 136 taxpayer accounts,<sup>2</sup> 28 accounts were identified with incorrect closing codes that were higher than required. The total balance due on these accounts was approximately \$796,492, with an average of \$28,446 for each taxpayer account.

For Calendar Year 2011, 3,952 taxpayer accounts were closed as currently not collectible in the Taxpayer Assistance Centers. Using the error rate of 20.59 percent (28 accounts divided by 136 total accounts sampled), we determined that there is a potential that 814 accounts (20.59 percent of 3,952 accounts) are at risk of not being reactivated. Based on the average amount of the balance due, we determined \$23,145,117 may be at risk of not being collected; projected over five years, \$115,725,586 may be at risk. The dollar value could range from \$56 million to \$176 million. We recognize that not all of this revenue will be collected because increases in taxpayers' income do not necessarily mean the taxes owed will be collected.

#### **Type and Value of Outcome Measure:**

- Taxpayer Burden – Potential; 1,889 taxpayers affected (see page 3).

#### **Methodology Used to Measure the Reported Benefit:**

From our sample of 136 taxpayer accounts, 13 accounts were identified with a lower closing code than required. Using the error rate of 9.56 percent (13 accounts divided by 136 total accounts sampled), we determined that there is a potential 378 taxpayers (9.56 percent of 3,952 accounts) may be burdened; projected over five years, 1,889 taxpayers may be burdened. The estimated number of taxpayers burdened could range from 926 to 2,852.

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<sup>1</sup> Totals may not calculate due to rounding.

<sup>2</sup> We selected a statistically valid sample of 136 accounts from a population of 3,952 taxpayer accounts. We used a confidence interval of 90 percent, an error rate of 15 percent, and a precision level of  $\pm 5$  percent.



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**Appendix V**

*Controls and Tolerances Concerning  
Currently Not Collectible Accounts*

Closing Code	Definition	Dollar Criteria	Manager Approval Required	Exception Cases
<p>Accounts Management (to include the Field Assistance Office) and Compliance assistors are limited to closing IMF and out-of-business BMF sole proprietor accounts as unable to pay up to \$100,000 for all outstanding balances including accounts previously reported as currently not collectible. IRM 5.19.1.7 (11/03/2010).</p>				
03	<b>Unable to Locate.</b> Inability to locate the taxpayer or assets.	IMF < \$25,000 and BMF if the aggregate assessed balance is < \$10,000 if trust funds are involved, < \$25,000 if trust funds are not involved.	More Than \$5,000	Form 433-A, <i>Collection Information Statement for Wage Earners and Self-Employed Individuals</i> , is required unless it is an exception case.
08	<b>Decedent.</b> Death of an individual with no collection potential from the decedent estate or no collection potential for estate taxes.	No dollar criteria.	More Than \$5,000	MANAGERIAL APPROVAL REQUIRED FOR ALL EXCEPTION CASES.  Exception cases have an aggregate assessed balance of less than \$10,000, including prior currently not collectible amounts, <u>and</u> one or more of the following conditions exist:
09	<b>Below Tolerance.</b>	Accounts may be closed as currently not collectible where the aggregate unpaid balance, including accruals, is less than \$100.00 for IMF and BMF accounts.	No	<ul style="list-style-type: none"> <li>• Taxpayer has a terminal illness or excessive medical bills.</li> <li>• Taxpayer is incarcerated.</li> <li>• Taxpayer's only source of income is Social Security, welfare, or unemployment.</li> <li>• Taxpayer is unemployed with no source of income (excluding the seasonal unemployed which fall under normal currently not collectible consideration and processing).</li> </ul>
12	<b>Inability to Contact.</b> Inability to contact a taxpayer although the address is known and there is no means to enforce collection.	IMF < \$25,000 and BMF if the aggregate assessed balance is < \$10,000 if trust funds are involved, < \$25,000 if trust funds are not involved.	More Than \$5,000	<ul style="list-style-type: none"> <li>• Taxpayer is unemployed with no source of income (excluding the seasonal unemployed which fall under normal currently not collectible consideration and processing).</li> </ul>
24-32	<b>Hardship.</b> Collection of the liability would create a hardship for taxpayers by leaving them unable to meet necessary living expenses.	< \$100,000 where the aggregate assessed balance is less than \$100,000.	More Than \$1,500	Lien determinations must be conducted for accounts over \$10,000.

Source: IRS Internal Revenue Manual. BMF = Business Master File. IMF = Individual Master File.



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**Appendix VI**

*Management's Response to the Draft Report*



COMMISSIONER  
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
ATLANTA, GA 30308

August 31, 2012

MEMORANDUM FOR MICHAEL E. MCKENNEY  
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Peggy Bogadi   
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Control Weaknesses Could Allow  
Taxpayers' Delinquent Accounts to Be Inappropriately Closed  
As Currently Not Collectible (Audit # 201240006)

Taxpayer Assistance Centers (TAC) complement the services available to taxpayers through IRS.gov and Toll-free telephone service by providing a venue for face-to-face assistance from IRS personnel. In many cases, taxpayers may obtain one-stop resolution of their account issues at the TACs, especially when those issues involve increased levels of complexity, or when the review of documentation or the exchange of information can be facilitated when done in person. One of the services the TACs provide is assisting taxpayers who owe taxes but are unable to pay. The assistance provided can include assessing the ability to pay the taxes due and establishing payment plans. In some cases, when taxpayers do not have the financial ability to commit to installment payments of their tax debt, a determination may be made that the account is Currently Not Collectible (CNC). In recent years, we have noticed an increase in the number of taxpayers who seek assistance at TACs when they are unable to pay their taxes owed. The resulting increase in the volume of accounts determined to be CNC has affected the workload performed at the TACs and has illustrated a need to reinforce existing procedural controls with our employees and to reevaluate the effectiveness of those controls.

We will remind our employees and managers of the procedures to be followed in evaluating the collectability of balance-due accounts and reinforcing expectations for adequate documentation of decisions made and approvals granted in updating accounts to CNC status. We are also initiating a comprehensive review of existing procedures and internal controls, and will perform an assessment of risks present and the effectiveness of controls in mitigating those risks.



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As we discussed during the audit, there are 187 TAC locations staffed by just one or two employees. At those sites, the limited number of staff available and the high expectations of our stakeholders for the services to be provided present significant challenges in achieving a true separation of duties. We have compensated for this risk with a security review process to be performed by the managers of these locations. This review process will also be assessed as part of the aforementioned risk assessment.

Attached are our comments to your recommendations. If you have any questions, please contact me, or a member of your staff may contact Leslye Baronich, Director, Field Assistance, Wage and Investment Division, at (404) 338-7149.

Attachment



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Attachment

**RECOMMENDATIONS**

The Commissioner, Wage and Investment Division, should:

**RECOMMENDATION 1**

Ensure assistors thoroughly document cases and follow established procedures when closing taxpayer accounts as currently not collectible. This should include procedures for completing financial statements, documenting correct closing codes on taxpayer accounts, and ensuring required liens are filed.

**CORRECTIVE ACTION**

We will ensure assistors are reminded of their responsibility to adequately document cases and follow Internal Revenue Manual (IRM) procedures when closing taxpayer accounts as Currently Not Collectible (CNC). Email communications will be distributed to the field as a reminder of the CNC procedures for completing financial statements, closing codes, and the filing of required liens. In addition, our Fiscal Year 2013 Continuing Professional Education includes a CNC refresher lesson for all Individual Tax Advisory Specialist employees.

**IMPLEMENTATION DATE**

March 15, 2013

**RESPONSIBLE OFFICIAL**

Director, Field Assistance, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 2**

Clarify internal guidelines requiring that management document approval of balance due cases in the AMS System history section. This should ensure that appropriate manager approvals are completed and retained on the AMS System.

**CORRECTIVE ACTION**

We will clarify our guidelines requiring managerial documentation of CNC cases on the Account Management Services system. Email reminders will be distributed to the field regarding these requirements.

**IMPLEMENTATION DATE**

March 15, 2013

**RESPONSIBLE OFFICIAL**

Director, Field Assistance, Wage and Investment Division



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**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 3**

Conduct a risk analysis to evaluate the risk of not segregating duties in the Taxpayer Assistance Centers. The risk analysis should include the costs associated with separating duties when processing payments, taking case actions (including closing cases as currently not collectible), and making account adjustments. It should also include any potential effect on taxpayer burden and the risk associated with lost revenue. As needed, implement controls and revise IRS guidelines to ensure appropriate separation of duties.

**CORRECTIVE ACTION**

We will complete an analysis to assess the risks associated with the non-segregation of duties in Taxpayer Assistance Centers where staffing levels do not permit proper segregation. We will use the results of the assessment to determine appropriate steps to mitigate risks that exceed acceptable levels.

**IMPLEMENTATION DATE**

October 15, 2014

**RESPONSIBLE OFFICIAL**

Director, Field Assistance, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 4**

Implement security reviews and reports that can be used to evaluate the assistors' use of IDRS command code REQ77.

**CORRECTIVE ACTION**

We agree with the intent of this recommendation and believe it can be met through reviews of monthly usage reports provided by the Integrated Data Retrieval System (IDRS) Online Reports Services, which includes all REQ77 command code activity. We will reemphasize to our managers the importance of following the security review guidelines provided by IRM 10.8.34, *IDRS Security Controls*.

**IMPLEMENTATION DATE**

March 15, 2013



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**RESPONSIBLE OFFICIAL**

Director, Field Assistance, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.