
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



The Office of Appeals Needs to Improve the Monitoring of Its Campus Operations Quality

May 10, 2007

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1 = Tax Return/Return Information

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TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

May 10, 2007

MEMORANDUM FOR CHIEF, APPEALS

FROM: 
Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Office of Appeals Needs to Improve the
Monitoring of Its Campus Operations Quality (Audit # 200510038)

This report presents the results of our evaluation of the quality and effectiveness of the Office of Appeals (Appeals) centralized campus¹ operations. During Fiscal Years 2004 and 2005, Appeals centralized certain types of case work at the Internal Revenue Service (IRS) campuses to reduce the processing time of taxpayers' appeals, enhance customer satisfaction, and improve the quality of work performed by Appeals.

Impact on the Taxpayer

Appeals does not have a statistically valid method of monitoring and reporting on the quality of work performed within the specific campus locations. We determined campus personnel did not always follow correct procedures or make correct determinations on taxpayer appeals, which could result in increased taxpayer burden, reduction of taxpayer rights and entitlements, reduction of taxpayer privacy and security, and lost revenue to the Federal Government. In addition, without an effective monitoring process, these types of errors may not be detected and could continue to occur.

¹ The data processing arm of the Internal Revenue Service. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to the taxpayer accounts.



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Synopsis

The centralization of certain types of cases into the campus operations is a major Appeals strategy for improving service to taxpayers. Appeals uses several tools to assess quality including customer satisfaction surveys, operational reviews, cycle time analysis, and the Appeals Quality Measurement System (AQMS). While all of these tools assist Appeals management in assessing some aspects of quality, the AQMS is the primary tool Appeals uses to monitor and report on the overall quality of casework. In its Strategic Plan for Fiscal Year 2006-2009, Appeals reported it would use the AQMS to measure the success of its strategies to improve quality. However, after the campus centralization, Appeals did not modify the AQMS to produce a statistically valid evaluation of the quality of casework performed within specific campuses or specific work streams. Instead, the AQMS sample is based on all Appeals functions within a geographical area, which includes all cases completed by both the field and campus operations. As a result, Appeals management may not detect areas needing improvement within the campuses or determine if its strategy for improving quality was successful.

Fiscal Year 2005 was the first full year of operations for four of the six centralized campuses. During this transition year, Appeals implemented significant new initiatives to make the campuses become fully operational. Some of this activity consisted of hiring and training new campus employees, team building efforts, revision of policies and procedures to address deficiencies as they were identified, as well as accelerating efforts to reduce inventory backlogs.

To evaluate the quality of the work performed by the campuses, we reviewed a statistical sample of cases from the campus operations. Our analysis showed that taxpayers were not always offered face-to-face hearings as required by procedures, campus employees did not always follow procedures or make the correct determinations when working taxpayer appeals, and service was not always timely. Further, taxpayer cases worked at the campus locations experienced unnecessary delays, taxpayers had not been provided adequate notifications or had not been properly informed of their rights, some taxpayers may have had unauthorized third-party contacts on their cases, and some taxpayers had erroneous abatements or refunds issued, resulting in lost revenue to the Federal Government.

Recommendations

We recommended the Chief, Appeals, revise the methodology used to select statistically valid samples of cases closed by the campus operations to measure and report on the quality of casework. The Chief, Appeals, should provide updated guidance and training sessions to ensure Appeals employees adhere to legal notification requirements for both the requesting and nonrequesting spouses when processing Innocent Spouse cases; to communicate clarifications of the penalty abatement policies, as well as emphasize the need for proper case research and



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application of penalty abatement criteria; and to ensure notification and documentation requirements for contacting third parties are followed. In addition, the Chief, Appeals, should implement a review process to ensure campus employees make the correct decisions on statute of limitations claims; adopt consistent language for Uniform Acknowledgment Letters issued for Innocent Spouse, Non-Docketed, and Offer in Compromise cases to adequately inform the taxpayer of the opportunity for requesting face-to-face hearings; revise the methods being used to monitor the aging of Penalty Appeals cases and Innocent Spouse claims; and establish a timeliness standard for issuing the Uniform Acknowledgment Letters for all Appeals casework.

Response

IRS management agreed with our recommendations. Appeals plans to review the potential benefits and costs of various sampling options and implement a new approach in Fiscal Year 2008. Appeals plans to revise and publish Internal Revenue Manual 25.15.12, "Relief from Joint and Several Liability, Appeals Procedures," with the procedures for proper legal notification; revise the Appeals letters used for Innocent Spouse cases and post them on the Centralized Database and the IRS.gov homepage; update Internal Revenue Manual 8.5.1, "Claim and Overassessment Cases," to clarify the procedures for claim cases and the statutory period of limitations; and conduct a random sample review of refund claim cases involving statute of limitations to determine if the proper decisions are being made. Further, Appeals plans to adopt consistent language and revise the Uniform Acknowledgment Letters for Innocent Spouse, Non-Docketed, and Offer in Compromise cases to ensure the taxpayer has a clear understanding of his or her options regarding a face-to-face appeals hearing. Appeals stated it will use Centralized Database real-time data to identify and address potential over-age cases before they become over-age. Management plans to flowchart the entire process to identify the "statutory suspense periods" which cannot be altered to determine areas where cycle time can be reduced, and revise processes and update the Internal Revenue Manual to further reduce cycle time when the analysis is completed. Appeals also enhanced its Centralized Database to add a new action code to ensure that the Uniform Acknowledgment Letter is timely issued and established timeliness standards for issuing the letter in the Internal Revenue Manual. Appeals plans to run a monthly report to determine if the timeliness standards are being met and send the report for follow-up when the standard is not being met. Management's complete response to the draft report is included as Appendix VI.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Nancy A. Nakamura, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.



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Abbreviations

AQMS	Appeals Quality Measurement System
CDP	Collection Due Process
FY	Fiscal Year
IRS	Internal Revenue Service
OIC	Offer in Compromise
UAL	Uniform Acknowledgement Letter



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Background

The Office of Appeals (Appeals) is an independent function within the Internal Revenue Service (IRS) whose mission is to settle tax disputes on a fair and impartial basis without litigation. Before the IRS Restructuring and Reform Act of 1998,¹ the majority of Appeals cases involved hearings for audit and penalty assessments or taxpayers who appealed to the courts (court docketed cases). The volume of Appeals cases increased significantly after the IRS Restructuring and Reform Act of 1998 was enacted because it established appeal rights for Collection Due Process (CDP),² Offers in Compromise (OIC),³ and Innocent Spouse⁴ cases.

Appeals performs work at field offices and at campuses⁵ located throughout the nation. In an effort to improve customer service, reduce the time taxpayer cases are in process (cycle time), and address aging inventories in the field offices, Appeals initiated centralized campus operations during Fiscal Year (FY) 2004 to work certain types of cases at the campuses rather than the field offices. Prior to that time, Appeals worked most cases at the field office closest to the taxpayer. FY 2005 was the first full year of operations for four of the six centralized campuses. During that transition year, Appeals implemented significant new initiatives to make the campuses become fully operational. Some of this activity consisted of hiring and training new campus employees, team building efforts, revision of policies and procedures to address deficiencies as they were identified, as well as accelerating efforts to reduce inventory backlogs.

Appeals management acknowledged the campus centralization has been challenging due to its complexity and scope, but several initiatives have been undertaken to help identify and improve the quality and effectiveness of the centralized casework. Some of the methods used by Appeals consist of specifically focused training sessions, operational reviews that are conducted at the campus team levels, and the annual Customer Satisfaction Surveys. Appeals management reported a commitment to monitoring the quality and timeliness of its campus casework and believes these methods are instrumental in helping the organization monitor and address campus related issues and concerns.

¹ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

² Taxpayers may appeal the first time a Federal Tax Lien is filed on a tax period and before the IRS levies against a taxpayer's property.

³ Taxpayers who are unable to pay their tax liability in a lump sum or through an installment agreement may file an OIC.

⁴ By requesting Innocent Spouse relief, a taxpayer may be relieved of responsibility for paying tax, interest, and penalties if their spouse (or former spouse) improperly reported items or omitted items on a joint tax return.

⁵ The data processing arm of the Internal Revenue Service. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to the taxpayer accounts.



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Under campus centralization procedures, Appeals assigns cases to campuses specializing in particular types of cases. At these campus locations, Appeals works with taxpayers, or their representatives, via correspondence and telephone contact. If the taxpayer prefers a face-to-face hearing, it is Appeals' policy to transfer a case from the campus to the field office closest to the taxpayer's location. Appeals identified seven types of cases that could be processed in the campuses: CDP, OIC, innocent spouse, penalty abatement requests, non-docketed examination, S-docketed examination, and requests made through the Freedom of Information Act. See Appendix V for a description of these types of cases.

Appeals typically closes over 100,000 cases per year. As a result of the centralization, the campuses now work a greater percentage of cases than in the past. During FY 2005, the campus operations closed 24,439 (24 percent) of 102,597 cases, and during FY 2006, the campus operations closed 34,257 (33 percent) of 102,559 cases.⁶

Figure 1 shows receipts by type of case from FY 2002 through FY 2005 for the entire Appeals operation.

Figure 1: Appeals Inventory Received in FYs 2002-2005

TYPE OF CASE	FY 2002	FY 2003	FY 2004	FY 2005
CDP	26,666	31,848	28,133	29,810
OIC	7,392	16,861	16,768	14,934
Innocent Spouse	3,660	4,274	4,592	3,341
Penalties	12,092	12,561	13,047	13,703
Coordinated Industry Cases	542	608	554	552
Industry Cases	861	716	683	750
Exam/TEGE ⁷	20,309	26,607	30,239	31,536
Freedom of Information Act	456	337	236	244
Other ⁸	4,419	4,566	4,425	5,048
TOTAL	76,397	98,378	98,677	99,918

Source: Appeals Business Performance Reports.

⁶ Total cases do not agree with Figure 1 because these numbers represent "closed" cases, while Figure 1 refers to "received" cases.

⁷ Includes Exam Docketed, Non-Docketed, and S-Docketed cases. TEGE represents Tax Exempt and Government Entities Division customers.

⁸ Other includes Abatement of Interest, Collection Appeals, Director of Practice, Other Penalties, and Miscellaneous cases. Only 12 cases were included in the miscellaneous category for FY 2005.



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Figure 2 shows the types of cases that were moved to the campuses, the campus sites that process the cases, and dates the cases were centralized at each location.

Figure 2: Appeals Centralized Campuses

TYPE OF CASE	CAMPUS	DATE OF CENTRALIZATION
CDP	Fresno	October 2004
	Memphis	September 2005
OIC	Brookhaven	December 2003
	Memphis	April 2005
Innocent Spouse	Covington	October 2003
	Memphis	April 2005
Penalties	Ogden	September 2004
Non-Docketed Examination	Fresno	February 2004
	Ogden	{?} ⁹
	Philadelphia ¹⁰	1988
S-Docketed Examination	Brookhaven	June 2005
	Fresno	February 2004
	Philadelphia ¹¹	1988
Freedom of Information Act	Fresno	February 2004

Source: Director, Appeals Tax Policy and Procedure.

Appeals' campus centralization was done in an attempt to reduce the time cases are in process. Figure 3 shows the average time to process work by type of case for FY 2002 through June 2006. The length of time to process a taxpayer's case from receipt until the final resolution is known as cycle time.

⁹ We cannot determine when the Ogden Campus started working the barred statute disallowed claims from the Memphis Campus. This is a small part of all Non-Docketed examination cases.

¹⁰ Philadelphia has been working Non-Docketed examination cases that originated there since 1988 and is currently working only cases that originate there.

¹¹ Philadelphia has been working S-Docketed cases that originated there since 1988 and is currently working only cases that originate there.



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Figure 3: Appeals' Case Cycle Time – Calendar Days

TYPE OF CASE	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006 (through June)
CDP	274	253	241	242	246
OIC	331	313	253	239	234
Innocent Spouse	384	446	450	425	340
Penalties	166	194	166	117	119
Coordinated Industry Cases	836	793	782	785	847
Industry Cases	518	553	549	663	522
Examination/TEGE	391	372	333	374	341
Other	219	238	245	241	229

Source: Appeals' Business Performance Reviews November 12, 2003; May 17, 2006; and August 16, 2006.

We initiated a review of six work streams (CDP, OIC, Innocent Spouse, Penalty Abatement Requests, Examination Non-Docketed cases, and Examination S-Docketed cases) in the campus locations to determine how case cycle time and the quality of the casework were affected by the campus centralization.

This review was performed at the National Headquarters of the Office of Appeals, in Washington, D.C., during the period of January through December 2006. This audit 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

Although Appeals has centralized all seven types of casework to the six campuses, it cannot determine if its efforts have achieved its goals of “getting the right work to the right employee” and providing the highest quality of customer service. Appeals uses the Appeals Quality Measurement System (AQMS) as the primary tool for measuring the quality of its casework. However, Appeals did not modify the AQMS process to be able to monitor the quality of the cases worked at the campuses after it centralized its operations. The AQMS currently uses a sampling methodology that does not allow for statistically valid reporting of results specific to campus operations or for a specific centralized work stream. As a result, Appeals does not specifically assess the quality performance for campus operations.

To evaluate the quality and timeliness of casework, we conducted a statistical analysis of six types of cases worked in the campuses. We found the campus operations did not always follow Appeals’ procedures, make the correct determination, or complete the cases timely. Consequently, Appeals needs to take additional steps to ensure the centralization will enable it to provide efficient and effective service to taxpayers.

The Appeals Quality Measurement System Does Not Adequately Measure Quality for the Centralized Campus Operations

The centralization of certain types of cases into the campus operations is a major Appeals strategy for improving service to taxpayers. To address its goal of improving processes and meeting customer needs, Appeals created a new model to centralize its work into standard teams that perform specialized work within the campuses. In its Strategic Plan for FY 2006-2009, Appeals reported it would use the AQMS to measure the success of its strategies to improve quality. However, Appeals did not adjust the AQMS to produce a statistically valid evaluation of the quality of casework performed within specific campuses or specific work streams. As a result, Appeals management may not detect areas needing improvement within the campuses or determine if its strategy for improving quality was successful. In addition, these types of errors could continue to occur.

Appeals uses the Appeals Centralized Database System (Centralized Database) to record case activity and time charged on all closed cases. To assess quality, the AQMS randomly selects a sample of all Appeals closed cases on the Centralized Database, measures quality based on six standards,¹² and assigns an overall rating for each standard. However, the AQMS sample is

¹² Taxpayer Service and Rights, Quality of Decision, Accuracy of Computations, Appeals Case Memorandum, Time Span and Time Applied, and Procedural Compliance.



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based on all Appeals functions within a geographical area, which includes all cases completed by both the field and campus operations. Although the sample includes some cases worked by the Campuses, Appeals does not select a statistically valid independent sample of the campus and field operations. As a result, Appeals cannot use the AQMS to accurately assess the quality of work performed by the Campuses.

The Appeals organization is divided into two geographical field operations (East and West). Both the East and West operations contain Area Offices¹³ that consist of campus and field offices. While the AQMS data may be useful to propose broad corrective action plans based on the quality reported for an Area Office level, they could be used more effectively if the data were further detailed to show areas needing improvement at the campus and field level. The broad measure of quality creates a greater risk that corrective actions could be misdirected at either the campus or field operations, and an overall acceptable rating for an Area Office level may be the result of averaging the poor results from one of the operations with better results from the other.

Also, the AQMS does not make valid comparisons between campus operations and field operations on a current or historical basis. Without specific performance and quality results, Appeals does not have sufficient detail to determine if centralizing operations reduced the cycle time while maintaining the quality of its case workload, nor can it identify areas for improvement specific to the campuses or field operations. Since the AQMS does not provide statistically valid data on the quality of casework performed at the campuses and combines the results with work performed by the field operations, Appeals management may not identify errors or accurately gauge the quality of work performed within the campuses.

Appeals justified its decision to centralize some operations at the campuses based on the expectation that it would reduce the cycle time to process cases while maintaining the quality. However, without a mechanism to measure this, Appeals cannot be held accountable for achieving this goal.

Appeals management believes it would not be cost beneficial to revise the AQMS process to obtain quality results at the campus level because it would require additional staffing to review larger sample sizes for the various work streams. However, Appeals has not conducted, and does not plan to conduct, a cost benefit analysis to support its opinion. Because Appeals reorganized its work into the campuses, we believe it should have a reliable, statistically accurate process to evaluate the quality of work done by the campus operations.

Although the AQMS is the primary tool to assess quality, Appeals uses other methods to monitor quality at the campuses, such as customer satisfaction surveys, cycle time analysis, and operational reviews. Area and Campus Directors perform operational reviews to identify training needs and monitor inventory levels and cycle time. Our analysis of the operational

¹³ A geographic organizational level used by IRS business units and offices to help their specific types of taxpayers understand and comply with tax laws and issues.



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reviews found that management can identify many issues specific to campus casework quality and address them appropriately at the local level. While these methods may provide valuable information, we believe Appeals needs to modify the AQMS to ensure it has statistically valid measurements of quality at the campuses.

Recommendation

Recommendation 1: The Chief, Appeals, should revise the methodology used to select statistically valid samples of cases closed by the campus operations to measure and report on the quality of casework.

Management's Response: IRS management agreed with our recommendation. They are considering several options and will conduct further analysis to determine the best approach to address the recommendation. Management plans to review the potential benefits and costs of various sampling options and implement a new approach in FY 2008. An alternative approach would be to keep the same methodology but eliminate the over sampling, and use those resources to conduct work stream specific reviews that were identified as a potential problem by the preliminary reviews. The third option, to conduct statistically valid samples at the work stream level in each campus with comparable field data, would cost an estimated \$2 million in staff resources. Management agreed to continue to supplement the AQMS review with data from operational reviews, data analysis, or other tools. They are now reviewing the potential benefits and costs of these various options and plan to determine which review approach to implement for FY 2008.

Appeals Campus Operations Did Not Always Follow Procedures or Make the Correct Determinations

Our review of a statistically valid sample of closed cases from each of the six types of cases determined that Appeals employees did not always follow policies and procedures or make correct determinations when processing Appeals cases at the campuses. These actions could result in increased burden, denial of rights and entitlements, loss of privacy and security for taxpayers, and loss of revenue for the Federal Government. These conditions would not have been reported to Appeals management since they were not identified in the annual AQMS results. Figure 4 summarizes the results of our analysis:



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Figure 4: Review of Appeals Campus Closures for FY 2005

Type of Error	Type of Case	Total Closures FY 2005	Sample Size	Errors in Casework	Percent Errors	Total Estimated Cases With Errors
Incorrect Determination	<i>Penalty Appeals</i>	11,615	54	17	31%	3,656
	<i>Non-Docketed</i>	1,338	53	3	6%	76
Inadequate Notification	<i>Innocent Spouse</i>	1,519	52	24	46%	701
Improper Contact With Third Parties	<i>CDP</i>	1,962	56	2	4%	70 ¹⁴

Source: Treasury Inspector General for Tax Administration review of a statistically valid sample of cases closed by Appeals campuses in FY 2005.

Appeals campus personnel did not always make the correct determination

When granting relief to the taxpayer by abating penalties, hearing officers must follow agency guidance¹⁵ and procedures, as well as the Penalty Appeals Training Guide. In our sample of 54 closed Penalty Appeals cases, we identified 17 (31 percent) cases in which the hearing officer did not adequately research the taxpayer's history; incorrectly interpreted policies, procedures, or agency guidance; or lacked proper training. When projected to the entire population of Appeals cases, we estimate that Appeals improperly abated penalties in 3,656 of the 11,615 Penalty Appeals cases closed by the campuses in FY 2005. The actual loss of revenue due to inappropriate abatements for these 17 cases was \$83,736.

In these cases, the penalties were abated although the taxpayer had not exercised proper business care, had a previous history of penalties, or had other indications of noncompliance. Agency criteria were not followed for these 17 cases and the documentation in the case files was either incomplete or did not support the determination to abate penalties. For example, 1

Taxpayers often file amended returns to claim additional credits and request refunds. However, taxpayers must file their claim for refund within set time periods (statute of limitations).

¹⁴ The numbers in this column cannot be computed due to rounding.

¹⁵ Guidance includes Internal Revenue Manual 8.11.1.3 procedures that outline various conditions for abating penalties based on Reasonable Cause criteria. The Penalty Policy Statement in Internal Revenue Manual 20.1 (P20-1) is also widely utilized by Appeals to make case determinations.



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Generally, a taxpayer may file a claim for refund within 3 years from the time the return was filed or within 2 years from the time the tax was paid, whichever is later.¹⁶ If the IRS rejects the taxpayer's claim for refund, the taxpayer may file an appeal.

In our sample of 53 Non-Docketed closed cases, we identified 3 (6 percent) cases in which hearing officers made statute-related errors by allowing refunds totaling \$24,355. Two of the errors occurred because hearing officers misinterpreted the tax law. 1.3(d)

1.3(d) The IRS attributed the incorrect determinations to newly-hired employees, the complexity of the issue, and documents being overlooked because they were stapled together. We estimate hearing officers made 76 incorrect statute of limitations determinations in the campus Non-Docketed operations for FY 2005. In FY 2006, Appeals planned to provide additional training for these types of claims, using group workshops and seminars.

Taxpayers were not properly notified of their appeal rights during innocent spouse proceedings

When a taxpayer requests tax relief using Innocent Spouse proceedings, the IRS is required to contact the nonrequesting spouse to ensure the case is fully developed and the nonrequesting spouse's rights are considered under all the Innocent Spouse provisions. However, hearing officers did not always follow procedures that require the nonrequesting spouse be offered an opportunity to participate in the appeal.¹⁷

If the IRS makes a preliminary determination to grant full or partial relief to one spouse, the IRS is required to notify the nonrequesting spouse and allow the opportunity to appeal the preliminary determination.¹⁸ If the IRS denies Innocent Spouse relief in full or in part, the requesting spouse has the right to petition the United States Tax Court. By law, the nonrequesting spouse is also allowed to participate in the court proceeding.

We identified cases where hearing officers did not send initial contact letters to the taxpayer who filed the claim or final determination letters to both spouses. In addition, hearing officers did not always send initial contact letters to the nonrequesting spouse to allow him or her to participate in the proceedings. In 24 (46 percent) of 52 cases we sampled, hearing officers did not provide proper notification to either the spouse who requested the appeal or to the nonrequesting spouse. We estimate 701 taxpayers may not have received proper notification from Appeals during FY 2005. In 19 of the 24 cases, Appeals did not contact the nonrequesting spouse to inform him

¹⁶ I.R.C. § 6511 (2007) *Limitations on Credit or Refund* sets two criteria for the allowance of claims for income tax refunds. The first criterion identifies when a claim for refund will be considered as timely filed and the second criterion establishes a look-back period, from the date of timely filing of a claim, over which taxpayers may identify payments made that are available for refund.

¹⁷ I.R.C. § 6015(h)(2)(2007) requires the nonrequesting spouse be notified and given an opportunity to participate in administrative proceedings for claims filed under I.R.C. §§ 6015(b) and (c).

¹⁸ Revenue Procedure 2003-19 and 26 C.F.R. 1.6015-6.



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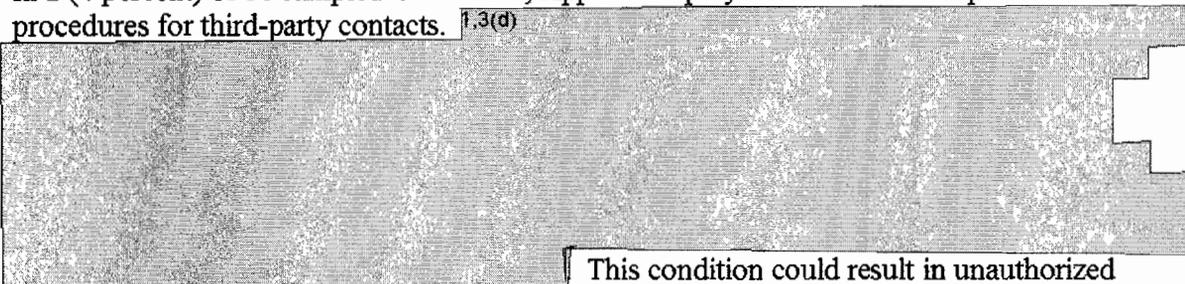
or her of the appeals process. Notably, in 5 of these 19 cases, Appeals found the nonrequesting spouse fully or partially liable for the tax liability but did not give the nonrequesting spouse the opportunity to be a party to the proceedings.

Although Appeals management agreed that procedures required the hearing officers to send the appropriate notifications to the requesting and nonrequesting spouse, it believed it was not necessary to do so because hearing officers do not usually agree to grant relief, and the nonrequesting spouse would not be harmed. However, this is a potential violation of taxpayer rights. We believe the nonrequesting spouse's right to protest the determination or petition the United States Tax Court should not be compromised based on an assumption that the risk is low that they will be affected by an Appeals decision.

Taxpayers were not always notified before the IRS contacted third parties

The IRS is required to provide reasonable notice to taxpayers when contacts with third parties are necessary to complete an investigation of the taxpayer's financial situation.¹⁹ For example, the IRS may need to contact third parties such as financial institutions, mortgage companies, or the taxpayer's neighbors to resolve a collection case. When third-party contact is necessary, the case file must be documented accordingly.

In 2 (4 percent) of 56 sampled CDP cases, Appeals employees did not follow policies and procedures for third-party contacts. ^{1.3(d)}



This condition could result in unauthorized disclosure of taxpayer returns or return information. During FY 2005, we estimate hearing officers may not have followed procedures for communicating with third parties for 70 cases.

Taxpayers were not offered face-to-face hearings

As part of our analysis, we determined whether and how the taxpayers were informed about the opportunity for a face-to-face Appeals hearing, if desired. We also determined if the information provided to taxpayers in contact letters adequately explained the option of requesting a face-to-face hearing.

¹⁹ Section 3417 of the IRS Restructuring and Reform Act of 1998 revised I.R.C. §7602(c) (2007) to require that IRS employees provide taxpayers with notice of contact of third parties. Under this section, the IRS must provide taxpayers with prior notification that third parties may be contacted during the determination or collection of that specific taxpayer's Federal tax liability.



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All of the Appeals' work streams require a Uniform Acknowledgment Letter (UAL), the initial contact letter, be sent to taxpayers to inform them their cases have been received by Appeals and the various options for a hearing. The purpose of the UAL is to introduce the taxpayer to Appeals and the hearing process. We reviewed the UALs sent for all of the campus operations work streams to determine what information was provided to taxpayers regarding the option for having a face-to-face hearing.

The UAL sent by the CDP campus operations contained specific language informing the taxpayer of the option to request a face-to-face hearing. However, the letters used for OIC rejection, Innocent Spouse claim, Non-Docketed, S-Docketed, and Penalty Appeals hearing requests in FY 2005 stated, "We conduct our reviews by: (1) telephone, (2) mail, and/or (3) personal interviews." In our opinion, this statement does not explicitly inform the taxpayer of the option to request a face-to-face hearing.

In August 2006, the UALs for the S-Docketed and Penalty Appeals work streams were revised to include specific language explaining the taxpayer's options, including a face-to-face hearing, if desired. However, the UALs for the Non-Docketed, Innocent Spouse, and OIC work streams had not been revised. We could not determine why Appeals was inconsistent in how it informed taxpayers of the option for face-to-face hearings between the various work streams. During FY 2005, Appeals closed 1,338 Non-Docketed cases, 1,519 Innocent Spouse cases, and 5,146 OIC cases. We estimate that 8,003 (100 percent) of these cases involved UALs that did not contain specific wording explaining the taxpayer's option to request a face-to-face hearing, which may have resulted in taxpayers being denied rights or entitlements.

Recommendations

Recommendation 2: The Chief, Appeals, should provide updated guidance and training sessions to:

- Ensure Appeals employees adhere to legal notification requirements for both the requesting and nonrequesting spouses when processing Innocent Spouse cases.
- Communicate clarifications of the penalty abatement policies, as well as emphasize the need for proper case research and application of penalty abatement criteria.
- Ensure notification and documentation requirements for contacting third parties are followed.

Management's Response: IRS management agreed with our recommendation and plans to revise and publish Internal Revenue Manual 25.15.12, "Relief from Joint and Several Liability, Appeals Procedures," with the procedures for proper legal notification. Management also plans to revise the Appeals letters used for Innocent Spouse cases and post them on the Centralized Database and the IRS.gov homepage. Management will also communicate clarifications of the penalty abatement policies as well as emphasize the need



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for proper case research and application of penalty abatement criteria. The policies and procedures relating to penalty abatement were updated in September 2006, and Appeals will further clarify them in the cross-functional Internal Revenue Manual 20.1. Management plans to update Internal Revenue Manual 8.7.2 to clarify notification and documentation requirements for contacting third parties.

Recommendation 3: The Chief, Appeals, should implement a process to review claims involving statute of limitations to confirm that decisions made by Appeals employees are correct.

Management's Response: IRS management agreed with our recommendation and plans to update Internal Revenue Manual 8.5.1, "Claim and Overassessment Cases," to clarify the procedures for claim cases and the statutory period of limitations. Management also plans to conduct a random sample review of refund claim cases involving statute of limitations to determine if the proper decisions are being made.

Recommendation 4: The Chief, Appeals, should adopt consistent language in the UAL for Innocent Spouse, Non-Docketed, and OIC cases to explicitly inform the taxpayer he or she may request a face-to-face hearing when certain conditions are met.

Management's Response: IRS management agreed with our recommendation. Management plans to adopt consistent language and revise the UALs for Innocent Spouse, Non-Docketed, and OIC cases to ensure the taxpayer has a clear understanding of his or her options regarding a face-to-face appeals hearing.

Appeals Campus Operations Did Not Always Provide Timely Service

Timely service is important to taxpayers. Based on an Appeals Customer Satisfaction Survey,²⁰ taxpayers felt the Appeals process was too lengthy and they were not updated about the status of their cases. The National Taxpayer Advocate also expressed concerns about the lengthy time period to complete the Appeals process. In the *National Taxpayer Advocate 2004 Annual Report to Congress*, the National Taxpayer Advocate reported that unreasonable delays during the Appeals process can limit taxpayer access to Appeals and potentially compromise Appeals' independence.

We identified excessive delays that ranged from 1 to 13 months in acknowledging taxpayers' appeals and providing final responses to taxpayers. Figure 5 summarizes the results of our review of timeliness:

²⁰ Internal Revenue Service Customer Satisfaction Survey, Appeals National Report, April through September 2005 issued February 2006.



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Figure 5: Delays in Acknowledging and Processing Taxpayers' Appeals in FY 2005

Type of Error	Type of Case	Number of Closures	Sample Size	Length of Delay	Untimely Actions in Sample	Percent Untimely Actions	Total Estimated Untimely Actions
Untimely Initial Response	CDP	1,962	56	1-3 months	6	11%	210
	OIC	5,146	55	1-10 months	23	42%	2,152
Untimely Final Response	Penalty Appeals	11,615	54	6-8 months	5	9%	1,076
	Innocent Spouse	1,519	52	7-13 months	7	13%	204 ²¹

Source: Treasury Inspector General for Tax Administration review of a statistically valid sample of cases closed by Appeals campuses in FY 2005.

Taxpayers did not receive timely acknowledgment of their appeal requests in CDP and OIC cases

More than 40 percent of the work closed by the campuses involves collection type cases such as CDP and OIC. The Appeals CDP procedures require that the employee assigned to work the taxpayer's case send a UAL within 1 month. Although Appeals contacts taxpayers by sending the UAL, it is not always timely or the case may not be worked expeditiously.

We found significant delays, ranging from 1 to 3 months, after case assignment for issuing UALs for 6 (11 percent) of 56 sampled CDP cases. Appeals management advised us that UALs were not issued timely because the employees initially assigned the cases were focused on case-related research, preparing the cases for quick closeout, or forwarding the cases to a hearing officer for final resolution. Delays beyond 1 month to acknowledge the taxpayer's hearing request are excessive and may cause the taxpayer to contact the IRS to inquire about the status of their CDP request. While Appeals conducts quality reviews through its AQMS, the issue of untimely UALs sent by the campuses was not identified because the AQMS does not report results based on specific campus performance. We estimate that, potentially, 210 taxpayers were burdened because the UALs were not issued timely.

When the IRS rejects a taxpayer's OIC, the taxpayer may appeal. Unlike the procedures for CDP cases, Appeals' procedures do not specify the time period in which the UAL must be sent to taxpayers for OIC cases. In 23 (42 percent) of 55 sampled cases, Appeals employees took from 1 to 10 months to send the UAL. Appeals explained that some of the delays were attributable to reassignment or transferring of the cases during that time period. In our opinion,

²¹ The numbers in this column cannot be computed due to rounding.



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delays beyond 1 month to acknowledge the taxpayer's appeal are unreasonable and could increase taxpayer frustration with the Appeals process as well as cause undue taxpayer burden. During that elapsed time, the taxpayer's financial condition could change, which could affect the feasibility of the OIC. We estimate approximately 2,152 taxpayers who requested an appeal of their OICs may have experienced excessive delays because the UALs were not timely issued. Since the AQMS data analysis does not report results based on specific campus performance, Appeals management was not aware of this condition and had not taken action to correct it.

There were excessive delays in processing Penalty Appeals cases and Innocent Spouse claims

Appeals' policies and procedures do not contain specific time periods for processing Penalty Appeals cases and Innocent Spouse claims. However, we noted the procedures require that "every effort should be made to resolve penalty appeal cases as expeditiously as possible, given the complexity of the issues and workload constraints."

Our analysis of Penalty Appeals cases and Innocent Spouse claims identified long periods of inactivity. In 5 (9 percent) of 54 sampled cases in which taxpayers requested abatement of penalties, Appeals took between 6 and 8 months to contact taxpayers during the Appeals process. Appeals management was not monitoring the aging of assigned cases adequately to ensure there were not excessive periods of inactivity. During FY 2005, we estimate 1,076 taxpayers may have had unexplained delays exceeding 6 months during the Penalty Appeals process for cases closed by Appeals campus operations.

In 7 (13 percent) of 52 sampled Innocent Spouse claims, taxpayers experienced delays during the Appeals process ranging from 7 to 13 months. Appeals told us this situation occurred because some cases were assigned to employees who were working higher priority cases and were not immediately available. In addition, some employees assigned these cases were working developmental assignments or were in training. Appeals agreed that better monitoring of the aging of these cases would help to identify cases that should be reassigned or transferred to other employees. We estimate 204 taxpayers whose Innocent Spouse claims were closed during FY 2005 may have experienced unnecessary delays exceeding 7 months.

Recommendations

Recommendation 5: The Chief, Appeals, should revise the methods being used to monitor the aging of Penalty Appeals cases and Innocent Spouse claims so that long periods of inactivity are promptly identified and addressed to ensure cases are worked timely.

Management's Response: IRS management agreed with our recommendation and plans to use Centralized Database real-time data to identify and address potential over-age cases before they become over-age. Management stated they will also flowchart the entire process to identify the "statutory suspense periods" which cannot be altered and then



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determine areas where cycle time can be reduced. Management will also revise the processes and update the Internal Revenue Manual to further reduce cycle time when the analysis is completed.

Recommendation 6: The Chief, Appeals, should establish a timeliness standard for issuing the UALs for all Appeals case work. Further, this standard should be monitored on the Centralized Database to ensure policies and procedures are being followed and the letters are timely issued.

Management's Response: IRS management agreed with our recommendation and on August 23, 2006, enhanced the Centralized Database to add a new action code, CO-UAL, to the Case Activity Record, which is a system-generated action code that is automatically input when the first UAL is generated. On October 5, 2006, management established a timeliness standard for issuing UALs in the Internal Revenue Manual. The Internal Revenue Manual provides that the Appeals Team Manager must make every attempt to generate and issue the UAL in the shortest time possible, but no later than 30 days from when the case is received in Appeals. On February 22, 2007, management enhanced the Centralized Database to automatically populate the "ACKLTR" field so Appeals can monitor whether UALs were properly and timely generated. The Appeals Team Manager must prepare the letter using the Centralized Database Forms Generator, and then the current date is recorded in the "ACDLTR" field on the Centralized Database to show the date the letter was generated. A report will be run monthly to determine if timeliness standards are being met and the report will be sent to the field for follow-up action where it is not met.



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Appendix I

Detailed Objective, Scope, and Methodology

The objective of this audit was to evaluate the quality and effectiveness of Appeals centralized campus¹ operations. To accomplish our objective, we:

- I. Obtained a computer extract of all closed campus cases between October 2004 and September 2005 from the Centralized Database file maintained at the Treasury Inspector General for Tax Administration Data Center Warehouse. We validated the reliability of the computer extract using table descriptions from the Data Center Warehouse, reviewed appropriateness of data within fields requested, and compared population totals to information obtained from Appeals officials.
- II. Selected statistically valid random samples from each of six separate work streams. The total sample was 376 cases and was selected based on a confidence level of 90 percent, precision rate of 6.5 percent, expected error rate of 10 percent, and included an additional 10 percent random selection to help account for lost or unobtainable cases. The samples were obtained from the total population of 24,153 cases closed from 6 work streams by campus operations in FY 2005.
- III. Obtained and reviewed case files for each sample for the six work streams for three attributes we determined were quality indicators. The following attributes were evaluated:
 - A. Case file documentation sufficiently supported the determination.
 - B. Written correspondence or phone conversations with the taxpayer were adequate before a determination was made on a case.
 - C. Appeals offered and, if necessary, allowed taxpayers the option of a face-to-face hearing with field operations.
- IV. Discussed with Appeals officials (national/area/local managers and analysts) policies at the centralized campus operations that affected the quality of taxpayer hearings. This included:
 - A. Identifying the policies related to written correspondence or phone conversations with taxpayers before determinations; using the updated contact letter; and offering

¹ The data processing arm of the Internal Revenue Service. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to the taxpayer accounts.



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- face-to-face hearings and, if necessary, allowing taxpayers the option of a face-to-face hearing with field operations.
- B. Interviewing Appeals team managers about their policies and procedures related to how a request is handled when a taxpayer requests a face-to-face hearing.
 - C. Confirming case review exceptions from Step III. and discussing the causes.
- V. Determined how centralized campus case quality is monitored by Appeals and whether the level of oversight is appropriate to provide useful feedback for conditions found.
- A. Evaluated the AQMS review process for the extent of the quality analysis related to centralized campus operations. This included the method of selecting samples, case rating standards, results or feedback provided to various management levels, and if any conditions or recommendations are monitored.
 - B. Obtained the recent AQMS quality report to determine if it had been adapted to reflect quality specifically related to the centralized campus operations. We discussed any plans to revise the report for centralized campus operations with Appeals officials.
 - C. Discussed with Appeals officials (national/area/local managers and analysts) any quality reviews, which were in addition to the AQMS, in place at centralized campus operations and the results of these reviews.



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Appendix II

Major Contributors to This Report

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Appendix III

Report Distribution List

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Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Chief, Appeals AP



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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 the Congress.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 701 taxpayers may have had their rights violated because they did not receive proper notification from Appeals on Innocent Spouse cases (see page 7).

Methodology Used to Measure the Reported Benefit:

In 24 (46.15 percent) of 52 sampled Innocent Spouse case reviews, taxpayers did not receive the required notification as the requesting or nonrequesting spouse. Appeals campus groups closed a total of 1,519 Innocent Spouse appeals cases in FY 2005. We estimate that, potentially, 701 (1,519 population x 46.15 percent error rate) of those cases may not have provided the proper notifications to the requesting or nonrequesting spouse. Our reviews of 52 randomly selected Innocent Spouse cases for this attribute resulted in a 46.15 percent actual error rate and a ± 11.18 percent precision rate based on a 90 percent confidence level.

Type and Value of Outcome Measure:

- Protection of Revenue – Actual; \$83,736 was not collected due to inappropriate abatements of post assessment penalties for 17 taxpayers (see page 7).
- Protection of Revenue – Potential; 3,656 Penalty Appeals cases may have inappropriate abatements of post assessment penalties resulting in potential lost revenue during FY 2005 (see page 7).

Methodology Used to Measure the Reported Benefit:

Penalties were erroneously abated in 17 (31.48 percent) of 54 post assessment penalty cases closed by campus Appeals. The IRS could have protected assessments totaling \$83,736 for these 17 cases if policies and procedures were followed, adequate research was conducted, and proper training had been provided for proper penalty abatement. Appeals campus groups closed a total of 11,615 post assessment penalty appeals during FY 2005. We estimate that 3,656 (11,615 population x 31.48 percent error rate) of those cases could have erroneous penalty abatements. Our reviews of 54 randomly sampled cases for this attribute resulted in



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a 31.48 percent actual error rate and a \pm 10.37 percent precision rate based on a 90 percent confidence level.

Since our sample was based on a review of quality attributes, we did not project the potential dollars of revenue protected for the population of campus Penalty Appeals cases.

Type and Value of Outcome Measure:

- Taxpayer Privacy and Security – Potential; 70 taxpayers may have had their privacy and security violated by unauthorized disclosures of taxpayer return information (see page 7).

Methodology Used to Measure the Reported Benefit:

In 2 (3.57 percent) of the 56 sampled CDP cases, Appeals made unauthorized third-party contacts. As a result, there is the potential that there may have been unauthorized disclosures of taxpayer returns or return information to unauthorized third parties. We estimate that, potentially, 70 taxpayers (1,962 population x 3.57 percent error rate) had their privacy and security violated by inappropriate third-party contacts which could have resulted in unauthorized disclosures of return information. Our reviews of 56 randomly selected samples of CDP campus closures for this attribute resulted in an actual error rate of 3.57 percent and a \pm 4.02 percent precision rate based on a 90 percent confidence level.

Type and Value of Outcome Measure:

- Protection of Revenue – Actual; \$24,355 was erroneously refunded due to inappropriate allowances of claims which were barred by the statute of limitations (see page 7).
- Protection of Revenue – Potential; 76 accounts with erroneous refunds that were barred by the statute of limitations (see page 7).

Methodology Used to Measure the Reported Benefit:

In 3 (5.66 percent) of the 53 sampled Non-Docketed campus cases, there were erroneous refunds that were barred from refund by the statute of limitations. These 3 cases resulted in the issuance of \$24,355 in erroneous refunds. Appeals campus groups closed a total of 1,338 Non-Docketed cases during FY 2005. We estimate that 76 (1,338 population x 5.66 percent error rate) accounts contained erroneous refunds. Our reviews of 53 randomly selected Non-Docketed cases for this attribute resulted in an actual error rate of 5.66 percent and a \pm 5.12 percent precision rate based on a 90 percent confidence level.

Since our sample was based on a review of quality attributes, we did not project the potential dollars of revenue protected to the population of campus Non-Docketed cases.



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Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 8,003 taxpayers may have had their rights violated due to the lack of adequate notification of the right to a face-to-face hearing (see page 7).

Methodology Used to Measure the Reported Benefit:

The UALs used in FY 2005 for the Non-Docketed, Innocent Spouse, and OIC work streams did not contain adequate language informing taxpayers of the option to request a face-to-face hearing in a local Appeals office. Appeals campus groups closed 1,338 Non-Docketed cases, 1,519 Innocent Spouse cases, and 5,146 OIC cases for a total of 8,003 taxpayers who were potentially denied their rights because of the inadequate UALs.

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; 210 taxpayers may have experienced excessive delays in the issuance of the UALs for CDP cases (see page 12).

Methodology Used to Measure the Reported Benefit:

In 6 (10.71 percent) of the 56 sampled CDP cases, taxpayers experienced excessive delays in issuance of the UALs. As a result, the taxpayers may have been unnecessarily burdened by not timely knowing the status of their Appeals requests. Appeals campus groups closed a total of 1,962 CDP cases in FY 2005. We estimate that, potentially, 210 taxpayers (1,962 population x 10.71 percent error rate) were burdened when the UALs were not timely issued. Our reviews of 56 randomly selected samples of CDP campus closures for this attribute resulted in an actual error rate of 10.71 percent and a ± 6.7 percent precision rate based on a 90 percent confidence level.

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; 2,152 taxpayers who requested an appeal of their OICs may have experienced excessive delays because their UALs were not timely issued (see page 12).

Methodology Used to Measure the Reported Benefit:

In 23 (41.82 percent) of the 55 sampled OIC case closures, Appeals did not timely issue UALs to the taxpayers. Appeals campus groups closed a total of 5,146 OIC cases in FY 2005. We estimate that 2,152 (5,146 population x 41.82 percent error rate) of those cases did not have UALs timely issued. Our reviews of 55 randomly selected OIC campus closures for this attribute resulted in a 41.82 percent actual error rate and a ± 10.88 percent precision rate based on a 90 percent confidence level.



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Type and Value of Outcome Measure:

- Taxpayer Burden –Potential; 1,076 taxpayers who requested post assessment Penalty Appeals may have been burdened by unexplained delays exceeding 6 months during the Appeals process (see page 12).

Methodology Used to Measure the Reported Benefit:

In 5 (9.26 percent) of 54 sampled post assessment Penalty Appeals case reviews, timely contact was not made with the taxpayer during the Appeals process after the initial acknowledgment letter was sent. Appeals campus groups closed a total of 11,615 post assessment Penalty Appeals during FY 2005. We estimate 1,076 (11,615 population x 9.26 percent error rate) of those cases could have resulted in burden to taxpayers due to the unnecessary delays. Our reviews of 54 randomly sampled post assessment Penalty Appeals cases for this attribute resulted in a 9.26 percent actual error rate and a ± 6.47 percent precision rate based on a 90 percent confidence level.

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; 204 taxpayers involved in Innocent Spouse cases may have been burdened by unnecessary delays exceeding 7 months during the Appeals process in obtaining a final case resolution (see page 12).

Methodology Used to Measure the Reported Benefit:

In 7 (13.46 percent) of 52 sampled Innocent Spouse case reviews, taxpayers may have been burdened by unnecessary delays exceeding 7 months during the Appeals process in receiving a final case resolution from Appeals. Appeals campus groups closed a total of 1,519 Innocent Spouse appeals cases in FY 2005. We estimate 204 (1,519 population x 13.46 percent error rate) taxpayers could have been burdened by unnecessary delays. Our reviews of 52 randomly selected Innocent Spouse cases for this attribute resulted in a 13.46 percent actual error rate and a ± 7.65 percent precision rate based on a 90 percent confidence level.



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Appendix V

Types of Cases Worked by the Campuses

- **CDP:** The IRS is required to notify taxpayers in writing that a lien¹ has been filed or that it intends to levy.² A taxpayer is allowed to appeal a lien or levy action through the CDP by filing a hearing request.
- **OIC:** An OIC is an agreement between a taxpayer and the IRS that resolves the taxpayer's tax debt. The IRS has the authority to settle, or "compromise," Federal tax liabilities by accepting less than full payment under certain circumstances. When the IRS rejects a taxpayer's OIC, the taxpayer may appeal.
- **Innocent Spouse:** A husband and wife are generally liable jointly and individually for the entire tax on a joint return. The IRS may collect the entire amount of tax, penalties, and interest due on a joint return from either spouse. However, the IRS Restructuring and Reform Act of 1998 made substantial changes to the tax law by including provisions to allow expanded relief for married taxpayers from the burden of tax liability. Taxpayers who have requested relief and disagree with the IRS' decision may file a Statement of Disagreement (Form 12509)³ and elect to forward the claim to Appeals or file a petition with the Tax Court.
- **Penalty Abatement Requests:** Penalties are effective tools used by the IRS to encourage voluntary tax compliance. The IRS may request payment from a taxpayer for some types of penalties before the taxpayer has an opportunity to dispute the penalties. These are considered post assessment penalties.⁴ Taxpayers who disagree with these post assessment penalties can choose to protest the penalty through an appeal.
- **Non-Docketed Examination:** Non-Docketed examination cases are those in which the taxpayer has not filed a petition in the United States Tax Court. If the IRS identifies a deficiency on a taxpayer's return, the IRS will send the taxpayer a letter, accompanied by

¹ When initial contacts by the IRS do not result in the successful collection of unpaid tax, the IRS has the authority to attach a claim, commonly referred to as a lien, to the taxpayer's assets.

² The IRS has the authority to work directly with financial institutions and other parties to obtain funds owed by a taxpayer. This process is commonly referred to as a levy.

³ This form is used to explain why taxpayers disagree with the IRS determination concerning relief from joint and several liability for a joint return under Internal Revenue Code (I.R.C.) sections (§§)6015(b), 6015(c), or 6015(f) (2007).

⁴ Post assessment penalties include the failure to pay tax penalty and the failure to file penalty under I.R.C. § 6651 (2007).



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the Revenue Agent's Report, which gives the taxpayer 30 days to request an Appeals conference. If the taxpayer does not request an Appeals conference, then the IRS will send the taxpayer a Notice of Deficiency. If the taxpayer files a petition with the Tax Court and has not had an Appeals conference, the IRS will send the case to Appeals to investigate a possible settlement.

- S-Docketed Examination: These are examination audit assessments under \$50,000 that have been petitioned to the Tax Court.
- Freedom of Information Act:⁵ Whenever a Freedom of Information Act request is denied, the requester has the right to appeal the denial. A requester may appeal the withholding of a document, the denial of a fee waiver request, the type or amount of fees that were charged, or any other type of adverse determination under the Freedom of Information Act. A requester can also appeal because the IRS failed to conduct an adequate search for the documents that were requested. However, a requester may not file an administrative appeal for the lack of a timely response.

⁵ 5 U.S.C.A. § 552 (West Supp. 2003). This Act provides public access to agency records unless protected from disclosure by one of the Freedom of Information Act's nine exemptions or three exclusions.



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Appendix VI

Management's Response to the Draft Report



CHIEF, APPEALS

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

APR 11 2007

RECEIVED
APR 11 2007

MEMORANDUM FOR TREASURY INSPECTOR GENERAL FOR TAX
ADMINISTRATION

FROM: Sarah Hall Ingram *Sarah Hall Ingram*
Chief, Appeals

SUBJECT: Response to Draft Report – Audit 2005-10-038
Appeals Needs to Improve the Monitoring of its
Campus Operations Quality

I have reviewed the subject draft audit report and appreciate your efforts in evaluating the initial quality of the Appeals Campus Operation. Appeals requested this review because we are committed to continuously improving our overall campus operation and the way we monitor timeliness, quality of work, the protection of taxpayer rights, and customer satisfaction. Our mission is to provide effective and efficient service to taxpayers wishing to resolve their disputes without litigation. We value all input about how we can further improve and look forward to follow-up evaluations of the effectiveness of our campus operation.

Establishing an effective Appeals Campus Operation is one of our principal strategies for improving service to taxpayers. By centralizing campus-sourced work on the campus and by developing specialized cadres of employees, we are able to get the right work to the right employee more quickly and improve timeliness and efficiency in operations. Our stakeholders have repeatedly made it clear that timeliness, measured as getting to their cases more quickly and resolving them more efficiently, is a key element of good customer service and their measured satisfaction levels. Data shows that our Appeals Campus Operation has made a big difference in reducing inventory backlogs and working efficiently with taxpayers.

As Appeals began the construction of our campus operation, we encountered a number of challenges that start-ups of this scope and complexity typically experience. As we identified some of the same challenges mentioned in your draft report, we responded with targeted procedures and training. Within the last eighteen months, Appeals has been analyzing data, tackling timeliness issues, training and re-training campus employees, balancing workloads, revising Internal Revenue Manuals (IRM), delivering Continuing Professional Education (CPE) at all campus locations, and improving the currency of our inventory. The cases reviewed in this audit were closed in FY 2005, during the first year of operation for four of the six campus offices. Although we believe you would find a different picture today, we recognize that there are always additional steps that can and will be taken to strengthen operations.



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You asked us to include in our response our concurrence or nonconcurrence with the findings and recommendations in this report. Although Appeals generally agrees with your findings and recommendations, we offer a few comments as background to the attached action plan.

We use open- and closed-case information from many sources to continuously assess our operations, identify opportunities for improvement and track the impact of our efforts. The Appeals Quality Measurement System (AQMS) provides case quality data from the review of a limited pool of closed cases. While we agree that it would be interesting to see this data at a more detailed site and work stream level, we have conducted a cost analysis and determined we would need three times as many resources (additional staff at a cost of approximately \$2 million) to review a sample that was statistically valid at both the campus and work stream levels. As those resources would have to come from front-line operations, we will also be evaluating a number of less expensive alternatives to increase available data on quality without adversely impacting other operations.

We take very seriously our mission to provide quality dispute resolution services, which includes accuracy, timeliness, and the protection of taxpayers' rights. On some of your findings, such as timeliness of uniform acknowledgement letters, we had already identified the same issues and begun implementing changes. We will continue to assess and improve those activities. On others, we have reviewed your observations and built new actions into the attached plan.

For a few, we would size the problem differently even while we continue to implement improvements. For example, Revenue Procedure 2003-19 (Innocent Spouse cases) provides that if Appeals proposes to change the IRS's preliminary determination to a result less favorable to the non-requesting spouse, then Appeals is required to notify that spouse and provide him or her with the opportunity to present his or her position including any relevant additional information before the final determination. After reviewing your concerns, I am comfortable that Appeals employees correctly followed the revenue procedure in most cases and that we can address the few remaining items through our action plan.

We appreciate your input on opportunities to further improve our communication tools. We want our website, publications, and case correspondence to correctly inform taxpayers about the Appeals mission and procedures and about their options and rights during their interactions with us. We have found that the vast majority of taxpayers do not choose to interact with us in face-to-face conferences. For example, in FY 2006, only 21% of taxpayers whose cases were considered in the field (our more complex work) opted for a face-to-face conference. Moreover, we had 5,943 taxpayers whose cases originated in the campus (our less complex work) specifically request a transfer to a field Appeals office for a face-to-face conference. Only 17.5 % of those taxpayers actually appeared face-to-face. Nonetheless, we agree that communications should be clear and we will adopt consistent language in all of our letters to ensure taxpayers have a clear understanding of options regarding face-to-face Appeals hearings.



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We agree that timely communication and actions are a vital part of effective customer service and operational performance. Indeed, FY 2004 and 2005 Customer Satisfaction feedback highlighted taxpayer expectations clearly--that Appeals substantially reduce the time it takes to consider cases. The Appeals campus sites and specialization have allowed us to make considerable progress towards meeting that expectation. For instance, since FY 2004, we have reduced the number of cases over one year old by 68% in the Penalty Appeals work stream and 96% in our Innocent Spouse work stream. Also, we have seen a substantial reduction in cycle time in certain campus work streams. For instance, the campuses have improved OIC cycle time by 19% (154 days in FY 2005 to 125 days in FY 2006), and examination case cycle time by 29% (261 days in FY 2005 to 185 days in FY 2006). Although the campus results for the Penalty Appeals and Innocent Spouse work streams are not as dramatic, both campus cycle times are roughly half of that for the field – an impressive achievement even considering the relative complexity of the inventories.

Your review occurred during the start-up phase of our campus areas. As those operations have matured and gained experience they have continued to improve across the spectrum of business/customer service measures. We see many of your recommendations as opportunities for further improvements and will be interested in inviting a follow-up review to further assess operational improvements.

Attached is a detailed response outlining our planned corrective actions to address your recommendations. If you have any questions, please contact me at (202) 435-5600.

Attachment



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Attachment

RECOMMENDATION 1

The Chief, Appeals should revise the methodology used to select statistically valid samples of cases closed by the Campus Operations to measure and report the quality of casework.

Proposed Corrective Action 1:

We believe we could conduct a statistically valid sample of each campus (but not each work stream) with our current resources by adjusting the number of cases selected for review at each site (Field vs. Campus) and eliminating over sampling and ad hoc studies. An alternative approach would be to maintain our current sampling process and eliminate the over sampling, and use those resources to conduct work stream specific reviews that have been identified as a potential problem through our review process. As stated in our response, to conduct statistically valid samples at the work stream level in each campus with comparable field data, would cost an estimated \$2 million in additional staffing. However, we will continue to supplement our AQMS review with data from operational reviews, data analysis, or other tools. We are now reviewing the potential benefits and costs of these various options and will determine which review approach to implement for FY 2008.

Implementation Date: October 15, 2007

Responsible Official: Director, Strategy and Finance

Corrective Action Monitoring Plan: The Director, AQMS will inform the Director, Strategy and Finance of any delays in performing the analysis and making a determination of approach.

RECOMMENDATION 2

The Chief, Appeals should provide updated guidance and training sessions to:

- Ensure Appeals employees adhere to legal notification requirements for both the requesting and non-requesting spouses when processing Innocent Spouse cases.
- Communicate clarifications of the penalty abatement policies, as well as emphasize the need for proper case research and application of penalty abatement criteria.
- Ensure notification and documentation requirements for contacting third parties are followed.



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Proposed Corrective Action 2a:

We will revise and publish IRM 25.15.12, *Relief from Joint and Several Liability, Appeals Procedures* with the procedures for proper legal notification. We will also revise the Appeals letters used for Innocent Spouse cases and post them on ACDS and the irs.gov homepage.

Implementation Date: January 15, 2008

Responsible Official: Director, Technical Services

Corrective Action Monitoring Plan: The Director, Tax Policy and Procedure (Collection and Processing) will inform the Director, Technical Services, of any delays in implementing this corrective action.

Proposed Corrective Action 2b:

We will continue to communicate clarifications of the penalty abatement policies, as well as emphasize the need for proper case research and application of penalty abatement criteria. In September 2006, we updated IRM 8.11.1, *Penalties*, and in October 2006, we posted an article on the Appeals web site to clarify when it is appropriate to abate an assessed penalty.

We will further clarify the penalty abatement policies when we update and move the material contained in IRM 8.11.1 into an Appeals section of cross-functional IRM 20.1, *Penalty Handbook*.

Implementation Date: January 15, 2008

Responsible Official: Director, Technical Services

Corrective Action Monitoring Plan: The Director, Tax Policy and Procedure (Exam) will inform the Director, Technical Services, of any delays in implementing this corrective action.

Proposed Corrective Action 2c:

Appeals will update IRM 8.7.2 to clarify notification and documentation requirements for contacting third parties.

Implementation Date: January 15, 2008

Responsible Official: Director, Technical Services



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Corrective Action Monitoring Plan: The Director, Tax Policy and Procedure (Collection and Processing) will inform the Director, Technical Services, of any delays in implementing this corrective action.

RECOMMENDATION 3

The Chief, Appeals should implement a process to review claims involving statute of limitations to confirm that decisions made by Appeals employees are correct.

Proposed Corrective Action 3a:

Appeals will update IRM 8.5.1, Claim and Overassessment Cases, to clarify the procedures and the statutory period of limitations for claim cases.

Implementation Date: January 15, 2008

Responsible Official: Director, Technical Services

Corrective Action Monitoring Plan: The Director, Tax Policy and Procedure (Exam) will inform the Director, Technical Services, of any delays in implementing this corrective action.

Proposed Corrective Action 3b:

During FY 2008 we will conduct a random sample review of refund claim cases involving statute of limitations to determine if the proper decisions are being made. Based on the results of the random sample review, we will assess the need for further reviews.

Implementation Date: September 15, 2008

Responsible Official: Director, Technical Services

Corrective Action Monitoring Plan: The Director, Tax Policy and Procedure (Exam), will inform the Director, Technical Services of any delays in implementing this corrective action.

RECOMMENDATION 4

The Chief, Appeals should adopt consistent language in the UAL for Innocent Spouse, Non-Docketed, and OIC cases to explicitly inform the taxpayer he or she may request a face-to-face hearing when certain conditions are met.



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Proposed Corrective Action 4:

We will adopt consistent language and revise the UALs for Innocent Spouse, Non-Docketed, and OIC cases to ensure the taxpayer has a clear understanding of his or her options regarding a face-to-face appeals hearing.

Implementation Date: January 15, 2008

Responsible Official: Director, Technical Services

Corrective Action Monitoring Plan: The Directors, Tax Policy and Procedure (Exam) and Tax Policy and Procedure (Collection and Processing) will inform the Director, Technical Services, of any delays in implementing this corrective action.

RECOMMENDATION 5

The Chief, Appeals should revise the methods being used to monitor the aging of Penalty Appeals cases and Innocent Spouse claims so that long periods of inactivity are promptly identified and addressed to ensure cases are worked timely.

Proposed Corrective Action 5:

We will use ACDS real time data to identify and address potential overage cases before they become overage. We will also flowchart the entire process to identify the "statutory suspense periods" which we cannot alter and then determine areas where we are able to further reduce cycle time. After we have completed our analysis, we will revise our processes and update our IRM to further reduce cycle time.

Implementation Date: January 15, 2008

Responsible Official: Director, Technical Services

Corrective Action Monitoring Plan: The Directors, Tax Policy and Procedure (Exam) and Tax Policy and Procedure (Collection and Processing) will inform the Director, Technical Services, of any delays in implementing this corrective action.

RECOMMENDATION 6

The Chief, Appeals should establish a timeliness standard for issuing the UALs for all Appeals case work. Further, this standard should be monitored on the Appeals Centralized Database System to ensure policies and procedures are being followed and the letters are timely issued.



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Proposed Corrective Action 6:

On August 23, 2006, Appeals enhanced ACDS, specifically the Case Activity Record and added a new action code CO-UAL which is a system generated action code that is automatically input when the first UAL is generated.

On October 5, 2006, Appeals established a timeliness standard for issuing UALs in IRM, 8.1.4.3.1, *Assignment of Work Units and Issuance of Letter 4141(CG), Uniform Acknowledgment Letter (UAL)*. It provides that the Appeals Team Manager (ATM) must make every attempt to generate and issue the UAL in the shortest time possible, but no later than 30 days from when the case is received in Appeals.

On February 22, 2007, Appeals enhanced ACDS to automatically populate the "ACKLTR" field so we can monitor whether UALs were properly and timely generated. The ATM must prepare the letter using the ACDS Forms Generator, and then the current date is recorded in the "ACKLTR" field on ACDS to show the date the letter was generated.

We will run a monthly report to determine if we are meeting the timeliness standard and send the report to the field for follow-up action where it is not met.

Implementation Date: Implemented

Responsible Official: Director, Technical Services