



*Employees Are Not Always Ensuring That
Taxpayers Pay the Maximum Amount
Possible When Granting Partial Payment
Installment Agreements*

September 14, 2007

Reference Number: 2007-30-170

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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TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 14, 2007

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

Michael R. Phillips

FROM: Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Employees Are Not Always Ensuring That
Taxpayers Pay the Maximum Amount Possible When Granting Partial
Payment Installment Agreements (Audit # 200630018)

This report presents the results of our review of the Internal Revenue (IRS) Partial Payment Installment Agreement (PPIA) program. The overall objective of this review was to determine whether decisions to grant PPIAs are proper and to determine the effectiveness of the management information system¹ used to measure the PPIA program. The audit was initiated because the PPIA program was initially implemented in January 2005; this is our first review of the program.

Impact on Taxpayer

To receive a PPIA, a taxpayer has to provide to the IRS financial information that should be verified by an IRS employee to ensure the taxpayer pays the maximum amount possible. Employees are not always properly verifying the income or assets of the taxpayer, thus not collecting the maximum amount the taxpayer can pay. Inequitable treatment of taxpayers can result when employees in different functions perform varying degrees of financial verifications. Also, because the IRS did not initially establish an appropriate management information system to monitor and track performance of the PPIA program, it could not determine if the program was functioning as intended and serving taxpayers appropriately.

¹ Managers use various information system reports to ensure inventories are being processed properly, sufficient staffing is being provided and used, and programs are being worked based on established time period requirements. The reports can also give important information on the effectiveness of a specific team or employee.



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Synopsis

The American Jobs Creation Act of 2004² amended Internal Revenue Code Section 6159³ to provide the IRS the authority to enter into a PPIA when a tax liability will not be fully satisfied within the Collection Statute Expiration Date.⁴ The IRS established guidelines requiring employees to perform a financial analysis to ensure the taxpayer pays the maximum amount possible.

The IRS did not initially establish an appropriate management information system to monitor and track PPIAs. Our review indicated that 14,042 PPIAs were granted in Calendar Year 2005, based upon computer codes designated for the program. IRS management recognized the need to properly monitor and track PPIAs and has taken steps to implement a transaction code for accepted PPIAs, which should allow it to more readily identify these cases. Implementation of this code took effect in January 2007. The IRS has also submitted a Request for Information Services⁵ that will start tracking the PPIAs as part of the Installment Agreement Collection Reports and will collect pertinent information. Implementation of the new management information system is scheduled for January 2008. However, PPIAs have not been properly monitored and tracked over the past 2 years; therefore, IRS management cannot identify the actual numbers that were granted or defaulted or the number of taxpayers that had completed their payment requirements. As a result, the IRS cannot properly assess the overall performance of the PPIA program.

In 28 of 56 cases reviewed,⁶ IRS employees did not document verification of the taxpayers' income and assets in the case files or history sheets. Some employees relied upon the limited financial information provided by the taxpayers and did not properly document the verification of IRS computer records for the last tax returns filed information. As a result of not verifying income, expenses, and assets, the IRS may not be collecting the maximum amount the taxpayers can pay because these taxpayers will not have paid off the liabilities in full when the collection statutes expire.

² Pub. L. No. 108-357, 118 Stat. 1418 (2004).

³ Internal Revenue Code Section 6159 (2004) – Agreements for payment of tax liability in installments.

⁴ The Collection Statute Expiration Date is the last date on which the IRS can collect delinquent tax without filing a suit for judgment; it is usually 10 years from the tax assessment date.

⁵ A Request for Information Services is a request for automated information system support initiated within the IRS and addressed to the Information Technology Services function. It is a mandatory process for all IRS organizations to request extracts from, or make changes to, an IRS computer system, documents, software, or hardware.

⁶ There was no PPIA documentation available for 2 of the 58 PPIAs we reviewed, so we were unable to determine if these PPIAs received managerial approval or verification of income or assets.



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Recommendations

We recommended the Director, Collection, Small Business/Self-Employed Division, and the Director, Compliance, Wage and Investment Division, ensure that the new coding for PPIAs has been implemented properly and is working appropriately and that the management information system will meet their needs after its implementation. In addition, they should (1) reemphasize that when working PPIAs employees need to obtain appropriate documentation of income, verify assets, and appropriately document the verification actions in the history sheets and case files and (2) remind employees they should be asking taxpayers specific questions regarding the types of income they receive, investments they have, and real property they own and their ability to liquidate or borrow against them.

Response

IRS management agreed with the first recommendation and partially with the second recommendation. The IRS developed a method to better identify PPIAs using new transaction codes and successfully implemented it in January 2007. This new coding will allow PPIA data to be included in the Installment Agreement Collection Reports starting in January 2008. The IRS will ensure these Reports meet its needs for monitoring the program and make revisions as needed. It will be revising the campus⁷ Internal Revenue Manual to incorporate procedural changes and clarification where necessary regarding income and asset verification and analysis. It will also provide training to campus employees, including instructions relating to PPIAs. Management's complete response to the draft report is included in Appendix V.

Office of Audit Comment

IRS management disagreed with the outcome measures as described in the report. They did not agree with the number of cases for which an employee did not obtain a full financial statement and/or that higher monthly payments (or full payments) would have been realized if internal information sources had been verified. However, our analysis showed that, if the IRS had performed appropriate and accurate financial analyses, it could have realized additional revenues. IRS management also disagreed with the assumption that the rejection of an offer in compromise⁸ makes granting a PPIA on the same account inappropriate. We agree that, as

⁷ Campuses are the data processing arm of the IRS. They process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

⁸ This is an agreement between a taxpayer and the Federal Government that settles a tax liability for payment of less than the full amount owed. The IRS has the authority to settle or compromise a Federal tax liability by accepting less than full payment under certain circumstances. This is accomplished through use of an Offer in Compromise (Form 656).



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financial conditions of the taxpayer change over time, the rejection of an offer in compromise does not preclude acceptance of a PPIA; however, the financial analyses for an offer in compromise and a PPIA should be consistently applied, including consideration of special circumstances (e.g., elderly or disabled taxpayers), and similar decisions should be reached.

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 Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-5894.



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Abbreviations

CSED	Collection Statute Expiration Date
IRS	Internal Revenue Service
OIC	Offer in Compromise
PPIA	Partial Payment Installment Agreement



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Background

The American Jobs Creation Act of 2004¹ amended Internal Revenue Code Section 6159² to provide the Internal Revenue Service (IRS) the authority to enter into a partial payment agreement or a Partial Payment Installment Agreements (PPIA) when a tax liability will not be fully satisfied within the Collection Statute Expiration Date (CSED).³

Prior to enactment of the American Jobs Creation Act of 2004, taxpayers who could not immediately fully pay their tax liabilities could enter into installment agreements with the IRS to fully pay their tax liabilities within the agreement period (usually 60 months). A taxpayer who could not fully pay could also request an offer in compromise (OIC)⁴ to pay a portion of the tax liability. OICs are handled mainly by the Centralized Offer in Compromise unit.⁵

Revenue officers in the Small Business/Self-Employed Division set up (grant) PPIAs; tax examiners in the Small Business/Self-Employed Division Automated Collection System⁶ function and the Wage and Investment Division units also grant these agreements. A PPIA requires a complete financial analysis such as a monthly income and expenses comparison and verification of the taxpayer's income and assets to determine the maximum monthly payment based on the taxpayer's ability to pay. Streamlined agreements (accounts that are under a certain dollar amount that could be paid off within 36 months) do not require financial analyses.

A PPIA involves the expiration of the CSED on at least one tax period⁷ and allows the IRS to receive partial payment of the taxpayer's tax liability before the collection statute expires. Once the CSED expires on a particular tax period, the IRS can no longer pursue collection for that tax

¹ Pub. L. No. 108-357, 118 Stat. 1418 (2004).

² Internal Revenue Code Section 6159 (2004) – Agreements for payment of tax liability in installments.

³ The CSED is the last date on which the IRS can collect delinquent tax without filing a suit for judgment; it is usually 10 years from the tax assessment date.

⁴ This is an agreement between a taxpayer and the Federal Government that settles a tax liability for payment of less than the full amount owed. The IRS has the authority to settle or compromise a Federal tax liability by accepting less than full payment under certain circumstances. This is accomplished through use of an Offer in Compromise (Form 656).

⁵ These are the IRS units located in the Holtsville, New York, and Memphis, Tennessee, Campuses that complete initial processing and work less complicated OICs to completion. Campuses are the data processing arm of the IRS. They process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

⁶ This is a telephone contact system through which telephone assistants collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.

⁷ This refers to each tax return filed by the taxpayer for a specific period (year or quarter) during a calendar year for each type of tax.



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liability. Because the IRS will not collect the full tax liabilities, the taxpayers must agree to the maximum monthly payments based on their abilities to pay.

This review was performed at the IRS Centralized Case Processing Site in Philadelphia, Pennsylvania, during the period February through October 2006. The 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

A Sufficient Management Information System Was Not Initially Implemented to Identify and Track the Partial Payment Installment Agreement Program

The IRS did not initially develop an appropriate management information system⁸ to properly identify the volume of or track all PPIAs granted at the onset of the program. Without an appropriate management information system, the IRS cannot monitor and assess the performance of the program or determine if the program is functioning as intended.

On January 17, 2005, the IRS began using Agreement Locator Numbers⁹ ending in “12” on a computer database to identify taxpayer accounts in PPIA status. Prior to January 17, 2005, Agreement Locator Numbers ending in “12” were used to identify other types of installment agreements. IRS management informed us the number of installment agreement accounts in this program was very limited and that was why it was chosen for the PPIA program. Our computer extract of all taxpayer accounts with the Agreement Locator Number ending in “12” from January 17 through December 16, 2005, identified 14,042 PPIAs.

Management relied on a computer program that would identify installment agreements ending in “12” to determine the number of PPIAs that are still current. While this program would identify the majority of accounts in PPIA status that are still current, the IRS could not identify the actual numbers of PPIAs that had been granted or defaulted or the number of taxpayers that had completed their payment requirements because it did not have an appropriate management information system in place. The IRS also cannot determine the actual amounts collected through the PPIA program or the amounts of liabilities remaining after the CSEDs have expired.¹⁰

After establishing a short-term method, IRS management focused on a method for a long-range management information system for PPIAs. In August 2006, it created a PPIA Design Document to implement changes to both the Integrated Collection System¹¹ and the IRS

⁸ Managers use various information system reports to ensure inventories are being processed properly, sufficient staffing is being provided and used, and programs are being worked based on established time period requirements. The reports can also give important information on the effectiveness of a specific team or employee.

⁹ The Agreement Locator Number is a four-digit code indicating the specific type of processing that will occur at the campus level.

¹⁰ See Appendix IV for details.

¹¹ The Integrated Collection System is a computer application used by Compliance function employees to monitor inventory. Histories of OIC investigations conducted by Area Office employees are maintained on this System.



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computer system. The changes will implement a transaction code for accepted PPIAs, which should allow the IRS to more readily identify these cases. The implementation date for the new transaction code was January 2007.

The IRS also has submitted another Request for Information Services¹² that will start tracking the PPIAs on the Installment Agreement Collection Reports and will track the number of agreements, the amount of the liabilities, the payments received per the agreements, the number of defaults, and other pertinent information so the IRS can appropriately assess the performance of the program. The scheduled implementation date for tracking PPIAs is January 2008.

Recommendation

Recommendation 1: The Director, Collection, Small Business/Self-Employed Division, and the Director, Compliance, Wage and Investment Division, should ensure that the new coding for identifying PPIAs has been implemented properly and is working appropriately and that the new section of the Installment Agreement Collection Reports meets their needs for an appropriate management information system to monitor performance of the overall PPIA program.

Management's Response: IRS management agreed with the recommendation and is taking appropriate actions. The IRS developed a method to better identify PPIAs using new transaction codes and successfully implemented it in January 2007. This new coding will allow PPIA data to be included in the Installment Agreement Collection Reports starting in January 2008. The IRS will ensure these Reports meet its needs for monitoring the PPIA program and make revisions as needed.

Some Employees Did Not Perform Sufficient Financial Analyses When Granting Partial Payment Installment Agreements

Some IRS employees granted PPIAs without following procedures for analyzing taxpayer financial information. Our conclusion is based upon review of a statistically valid sample of 61 PPIAs from a computer extract of 14,042 cases initiated between January 17 and December 16, 2005.¹³ We reduced our sample size to 58 because 3 cases were not part of the PPIA program.

¹² A Request for Information Services is a request for automated information system support initiated within the IRS and addressed to the Information Technology Services function. It is a mandatory process for all IRS organizations to request extracts from, or make changes to, an IRS computer system, documents, software, or hardware.

¹³ The statistical sample was selected using a 95 percent confidence level, a precision level of ± 10 percent, and an estimated error rate of 20 percent.



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The 58 agreements were granted by the following functions:

- Wage and Investment Division – 46.
- Small Business/Self-Employed Division Automated Collection System – 9.
- Small Business/Self-Employed Division revenue officers – 3.

The Internal Revenue Manual¹⁴ requires completion of a full Collection Information Statement and that equity in assets be addressed and, if appropriate, used to make payments on the liability. IRS employees must request a copy of a document, statement, etc. to verify income or an expense claimed by the taxpayer when determining his or her ability to pay. The employees should also check IRS computer records to determine income reported on the taxpayer's last filed income tax return.

In 28 of the 56 cases we reviewed,¹⁵ the IRS employee did not obtain a full financial statement and did not properly document verification of the taxpayer's assets and income in the case file or history sheet. Employees relied upon the limited financial information provided by the taxpayer and did not document verification of IRS computer records for last return filed information in the case file or history sheet.

We determined that, if IRS employees had verified the income of the taxpayers, 24 of the 56 taxpayers could have paid higher monthly payments and as many as 14 of these taxpayers could have made payments sufficient to fully pay the balances due by the CSEDs. As a result, these 14 taxpayers would not have qualified for a PPIA. We based our analysis on information from IRS computer records. While some of these records may not have been available to the IRS employee at the time the PPIA was initiated, the discrepancy in the income figures could have been identified if the employee had requested verification from the taxpayer.

Some of these PPIAs were granted by employees who worked streamlined agreements and were not trained on financial analysis. However, PPIA procedures require that employees not trained "on financial analysis, transfer the call to the Non-Streamline Installment Agreement Application." Eighty percent of the PPIAs granted in our sample were obtained by Wage and Investment Division employees. As a result of not always verifying income and assets, the IRS may not be collecting the maximum amounts the taxpayers can pay because these taxpayers will not have paid off the liabilities in full when the CSEDs expire. In addition, taxpayers are not treated equitably when employees in different functions perform varying degrees of financial verifications.

In three cases in which verification of income and assets was properly documented, revenue officers granted the PPIAs. Because there were only three revenue officer cases in our sample,

¹⁴ Internal Revenue Manual Sections 5.19.5.5.1 (1), 5.14.2.2 (2), and 5.14.2.2.1 (1).

¹⁵ There was no PPIA documentation available for 2 of the 58 PPIAs we reviewed, so we were unable to determine if these PPIAs received managerial approval or verification of income or assets.



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IRS management wanted a further review of these cases and asked us to perform a separate review of PPIAs granted by revenue officers. Our review of a judgmental sample of 20 cases being monitored at the Philadelphia Centralized Case Processing site showed that revenue officers usually properly verified assets and income. While this indicates revenue officers are generally performing effective financial analyses, our statistically valid sample showed PPIAs obtained by revenue officers represent only about 7 percent of the cases coded as PPIAs.

Some taxpayers had an OIC rejected and then received a PPIA

To further evaluate whether employees are effectively verifying assets and income, we reviewed a judgmental sample of 12 taxpayers that had OICs rejected because the Centralized Offer in Compromise units determined the taxpayers had the ability to fully pay; then, within 90 calendar days, the IRS granted PPIAs. In all 12 cases, the IRS employee did not properly document verification of the taxpayer's assets and in 5 cases did not document verification of the taxpayer's income in the PPIA case. For the 12 PPIAs (6 granted by the Wage and Investment Division, 5 granted by the Small Business/Self-Employed Division Automated Collection System, and 1 granted by the Collection Field function¹⁶), we determined that:

- Six taxpayers had an ability to fully pay the accounts based upon financial information in the OIC case files.
- Two taxpayers had sufficient equity in assets to fully pay. [REDACTED]
- Four taxpayers qualified for a PPIA: [REDACTED]

The 7 taxpayers who did not qualify for a PPIA had an aggregate current tax liability of \$343,308. The Centralized Offer in Compromise units determined the combined reasonable collection potential¹⁷ for these taxpayers was \$801,064. We determined the current liability of \$343,308 would accrue to approximately \$2,013,564 by the CSEDs, and the IRS would receive payments totaling \$142,621 (7.1 percent) during this same time period. Therefore, if the IRS had continued to pursue regular collection actions against these taxpayers with the ability to fully pay, it would have potentially collected a minimum of an additional \$200,687 (if the taxpayers would fully pay immediately) to a maximum of \$1,870,943¹⁸ by the CSEDs.

¹⁶ This is the unit in the Area Offices consisting of revenue officers who handle personal contacts with taxpayers to collect delinquent accounts or secure unfiled returns.

¹⁷ Reasonable collection potential is the amount the IRS determines could reasonably be collected from the taxpayer. It equals the total realizable value of the taxpayer's assets plus future income.

¹⁸ See Appendix IV for details.



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Recommendation

Recommendation 2: The Director, Collection, Small Business/Self-Employed Division, and the Director, Compliance, Wage and Investment Division, should reemphasize that when working PPIAs employees need to obtain appropriate documentation of income, verify assets, and appropriately document the verification actions in the history sheets and case files. Employees should also be reminded that they should be asking taxpayers specific questions regarding the types of income they receive (wage earner or self-employed), investments they have, and real property they own and their ability to liquidate or borrow against them.

Management's Response: IRS management partially agreed with this recommendation, stating the perceived weaknesses in the program that the recommendation seeks to correct were isolated to the PPIAs granted in the campuses. The IRS is revising the campus Internal Revenue Manual Section 5.19.1 to incorporate procedural changes and clarification where necessary regarding income and asset verification and analysis. It will provide training to campus employees, including instructions relating to PPIAs.

Office of Audit Comment: IRS management disagreed with the outcome measures as described in the report. They did not agree with the number of cases for which an employee did not obtain a full financial statement and/or that higher monthly payments (or full payments) would have been realized if internal information sources had been verified. However, our analysis showed that, if the IRS had performed appropriate and accurate financial analyses, it could have realized additional revenues. IRS management also disagreed with the assumption that the rejection of an OIC makes granting a PPIA on the same account inappropriate. We agree that, as financial conditions of the taxpayer change over time, the rejection of an OIC does not preclude acceptance of a PPIA; however, the financial analyses for an OIC and a PPIA should be consistently applied, including consideration of special circumstances (e.g., elderly or disabled taxpayers), and similar decisions should be reached.



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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether decisions to grant PPIAs are proper and to determine the effectiveness of the management information system¹ used to measure the PPIA program. To accomplish this objective, we:

- I. Determined if PPIAs were appropriate and were based on accurate and consistent financial analyses.
 - A. Held discussions with analysts in and managers of the PPIA program and determined:
 1. Procedures and guidelines used in conducting PPIA evaluations.
 2. Trends identified through quality reviews conducted and use of the information developed through these reviews.
 3. Internal systems used to verify information provided on Collection Information Statements.
 - B. Obtained from the IRS Integrated Data Retrieval System² Taxpayer Information File³ a computer extract of taxpayer accounts (cases) with the Agreement Locator Number⁴ ending in “12” initiated between January 17 and December 16, 2005. The computer extract contained 14,042 records. We were unable to assess the reliability of the extracted computer data. We relied on this information because this was the only source for the data and the IRS did not have a tracking system to determine an actual number of PPIAs. We took our sample from the entire universe and indicated which cases in our selection were not PPIAs.
 - C. Selected a statistically valid sample of 61 cases from our initial extract of 14,042 cases based on a 95 percent confidence level, a precision level of ± 10 percent,

¹ Managers use various information system reports to ensure inventories are being processed properly, sufficient staffing is being provided and used, and programs are being worked based on established time period requirements. The reports can also give important information on the effectiveness of a specific team or employee.

² The Integrated Data Retrieval System is a computer system with the capability to instantaneously retrieve or update stored information.

³ A Taxpayer Information File is a file containing entity and tax data processed by a given IRS campus for all Taxpayer Identification Numbers. Campuses are the data processing arm of the IRS. They process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

⁴ The Agreement Locator Number is a four-digit code indicating the specific type of processing that will occur at the campus level.



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- and an estimated error rate of 20 percent. Our sample was reduced to 58 after we identified 3 cases that were not part of the PPIA program.
- D. Reviewed the IRS Desktop Integration⁵ narrative prints supporting the IRS determination to accept the PPIA for the 58 sample cases. We analyzed the available data and used the IRS Decision IA⁶ program to determine if the cases qualified for PPIA status and if the payment amounts were appropriate.
- II. Evaluated the IRS PPIA management information systems used to measure the program's effectiveness and to identify and evaluate trends.
- A. Discussed with IRS management present and future plans for a management information system for the PPIA program.
 - B. Determined the current status of the tax accounts of taxpayers who were granted a PPIA within 90 calendar days of a rejected OIC by comparing the cases on the IRS Automated Offer in Compromise system⁷ to our PPIA computer extract.
 - C. Selected a judgmental sample of 12 cases meeting the above criteria by comparing the 14,042 cases from our computer extract to the cases in Step II.B.
 - D. Obtained and reviewed the Desktop Integration narrative prints along with the history sections of the IRS' Automated Offer in Compromise system maintained by the Treasury Inspector General for Tax Administration Data Central Warehouse.⁸

⁵ Desktop Integration is the current system used by IRS employees in multiple functions to document actions taken on taxpayer accounts.

⁶ Decision IA is an IRS program employees use to determine the type of installment agreement to set up for the taxpayer.

⁷ An IRS computer system used to control offers in compromise.

⁸ The Treasury Inspector General for Tax Administration maintains electronic files of certain IRS computer systems on computers at its Data Center Warehouse.



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Appendix II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs)
Parker F. Pearson, Director
Amy L. Coleman, Audit Manager
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Appendix III

Report Distribution List

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Deputy Commissioner, Wage and Investment Division SE:W
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Compliance, Wage and Investment Division SE:W:CP
Chief Counsel CC
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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:

- Reliability of Information – Potential; 14,042 taxpayer accounts affected (see page 3).

Methodology Used to Measure the Reported Benefit:

Our objective was to determine if the IRS had a management information system¹ to identify the number of PPIAs that had been granted, the number that had defaulted, the amounts the IRS was collecting, and the amounts the IRS could not collect before the CSEDs.² We interviewed IRS management and determined the IRS did not have an appropriate management information system initially that would identify the performance of the program. Our computer extract for the period of January 17 through December 16, 2005, identified 14,042 PPIA cases. Because there was no appropriate management information system initially, we concluded there was a lack of reliable information for all 14,042 taxpayer accounts.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; \$1,870,943 (see page 4).

Methodology Used to Measure the Reported Benefit:

Our objective was to determine if taxpayers applying for OICs³ and PPIAs were treated equitably by the two programs. We selected a judgmental sample of 12 OICs that had been rejected by the

¹ Managers use various information system reports to ensure inventories are being processed properly, sufficient staffing is being provided and used, and programs are being worked based on established time period requirements. The reports can also give important information on the effectiveness of a specific team or employee.

² The CSED is the last date on which the IRS can collect delinquent tax without filing a suit for judgment; it is usually 10 years from the tax assessment date.

³ This is an agreement between a taxpayer and the Federal Government that settles a tax liability for payment of less than the full amount owed. The IRS has the authority to settle or compromise a Federal tax liability by accepting less than full payment under certain circumstances. This is accomplished through use of an Offer in Compromise (Form 656).



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Centralized Offer in Compromise⁴ units and the taxpayers had been granted PPIAs within 90 calendar days of the rejected OICs. We reviewed the OIC case histories and determined all 12 OICs had been rejected because the Centralized Offer in Compromise units had determined the taxpayers had the ability to fully pay their liabilities. We calculated that, in 7 of the 12 cases, the IRS would receive PPIA payments totaling \$142,621 on the aggregate current tax liability of \$343,308 at the time each PPIA was granted. The total accrued tax liabilities at the CSEDs for these taxpayers would be \$2,013,564. If these taxpayers would fully pay their tax liabilities immediately, the IRS would collect \$200,687 in additional revenue. If these taxpayers would fully pay their tax liabilities by the CSEDs, the IRS would potentially collect a maximum of \$1,870,943 in additional revenue.

⁴ These are the IRS units located in the Holtsville, New York, and Memphis, Tennessee, Campuses that complete initial processing and work less complicated OICs to completion. Campuses are the data processing arm of the IRS. They process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.



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Appendix IV

Management's Response to the Draft Report

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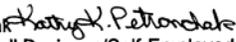


COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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

August 16, 2007

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

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

SUBJECT: Draft Audit Report – Employees Are Not Always Ensuring That Taxpayers Pay the Maximum Amount Possible When Granting Partial Payment Installment Agreements (Audit # 200630018)

We have reviewed the draft report titled "Employees Are Not Always Ensuring That Taxpayers Pay the Maximum Amount Possible When Granting Partial Payment Installment Agreements." We generally concur with your recommendations to implement an appropriate Management Information System to monitor Partial Payment Installment Agreements (PPIA), and that proper income and asset verification and documentation are necessary when considering granting PPIAs.

We appreciate your report on this new program that was developed and implemented within a short timeframe after the American Jobs Creation Act of 2004 was passed in October 2004. The report confirms we have made significant progress and our long term plans are consistent with your recommendations. We are also pleased the report acknowledges Revenue Officers are performing effective financial analysis when considering PPIAs.

We agree with Recommendation 1 to implement an appropriate Management Information System. This has been part of our implementation plan since PPIAs were first initiated. We immediately implemented a quarterly data extract as an interim method of monitoring PPIA performance pending creation of a long-term Management Information System. Programming limitations delayed the implementation of the final Management Information System that is scheduled for January 2008. We developed a better method for identifying these agreements using new transaction codes and successfully implemented it in January 2007. This coding has been applied to all accounts that were granted PPIAs from the start of the program. The coding will allow PPIA data to be included on the Installment Agreement Collection Reports starting in January 2008 as noted in the draft report. We will ensure that these reports meet our performance monitoring needs and revisions will be made as necessary.



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We are in partial agreement with Recommendation 2. We will emphasize to employees that proper income and asset verification and documentation are required when considering a PPIA, as well as remind employees to ask specific questions related to income and assets. The perceived weaknesses in the program that this recommendation seeks to correct were isolated to PPIAs granted in the campuses. We are revising the campus Internal Revenue Manual 5.19.1 to incorporate procedural changes and clarification where necessary regarding income and asset verification and analysis. This IRM revision is scheduled to be completed in October 2007. We are also providing training to campus employees, including instructions related to PPIAs, which is scheduled for completion by December 2007.

We do not concur with the outcome measures as reported in Appendix IV for the number of cases where the employee purportedly did not obtain a full financial statement, and/or that higher monthly payments (or full payment) would have been realized if internal information sources were verified. The income and asset data to arrive at this conclusion was not available to the employees at the time the PPIA was considered. While we do not agree with the numbers cited we do agree that procedures need to be clarified and training provided to the employees.

We disagree with the assumption in the report that the rejection of an Offer in Compromise (OIC) makes granting a PPIA on that same account inappropriate. In an OIC determination, the reasonable collection potential is calculated using the monthly ability to pay, multiplied by a set number of months, added to the net equity in assets. In an OIC it is possible that this reasonable collection potential calculation may result in an amount in excess of the tax liability, therefore showing an ability to pay in full. The net equity in assets must be included in the calculation of reasonable collection for an OIC, even if only potentially available over time. In a PPIA, the asset equity must only be considered and immediate liquidation of assets is required only if appropriate to an individual's circumstances. There are situations where requiring immediate payment of asset equity would be inappropriate (elderly or disabled taxpayers for instance). The unique ability to pay determination we use to decide whether to compromise the amount of a liability cannot be applied across the board to general collection decisions including whether to grant a PPIA.

Attached is a detailed response outlining our corrective actions. If you have any questions, please call me at (202) 622-0600 or David Alito, Director, Collection, Small Business/Self-Employed Division, at (202) 283-4941, or James Grimes, Director Compliance, Wage & Investment Division at (404) 338-9904.

Attachment



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Attachment

RECOMMENDATION 1:

The Director, Collection, Small Business/Self-Employed Division, and the Director, Compliance, Wage and Investment Division, should ensure that the new coding for identifying PPIAs has been properly implemented, is working appropriately, and that the new section of the Installment Agreement Collection Reports meets their needs for an appropriate Management Information System to monitor performance of the overall PPIA program.

CORRECTIVE ACTIONS:

The new identification codes for PPIAs were implemented in January 2007 and are working correctly. The applicable Collection Activity Reports are being revised to include monthly and cumulative PPIA data. This will provide the appropriate means to measure and monitor performance of the PPIA program.

IMPLEMENTATION DATE:

January 15, 2008

RESPONSIBLE OFFICIAL:

The Director, Collection, Small Business/Self-Employed Division

CORRECTIVE ACTION(S) MONITORING PLAN:

The Director, Collection, Small Business/Self-Employed Division will advise the Commissioner, Small Business/Self-Employed Division of any delays in implementing this corrective action.

RECOMMENDATION 2:

The Director, Collection, Small Business/Self-Employed Division and the Director, Compliance, Wage and Investment Division, should reemphasize that when working a PPIA, employees need to obtain appropriate documentation of income and also verify assets and appropriately document the history sheets and case files of the verifications. Employees should also be reminded that they should be asking taxpayers specific questions regarding the type of income they receive (wage earner or self-employed), investments they have, and real property they own; and their ability to liquidate or borrow against them.

CORRECTIVE ACTIONS:

Internal Revenue Manual 5.19 is being revised to clarify instructions and emphasize documentation and verification of income and assets when working PPIAs. The revised version will be published by December 15, 2007. Training will be provided to campus employees to further educate and emphasize appropriate case actions for PPIAs.

IMPLEMENTATION DATE:

January 15, 2008



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RESPONSIBLE OFFICIAL:

The Director, Small Business/Self-Employed Campus Compliance Services Division
and the Director, Compliance, Wage and Investment Division

CORRECTIVE ACTION(S) MONITORING PLAN:

The Director, Small Business/Self-Employed Campus Compliance Services Division
and the Director, Compliance, Wage and Investment Division, will advise their
respective Commissioners of any delays in implementing this corrective action.