



*Payments Processed Through the  
Remittance Strategy for Paper Check  
Conversion Are Posted Accurately, but  
Deposit Timeliness Needs Improvement*

**April 16, 2010**

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This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

**Redaction Legend:**

1 = Tax Return/Return Information



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

**DEPARTMENT OF THE TREASURY**  
**WASHINGTON, D.C. 20220**

April 16, 2010

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

*Nancy A. Nakamura*

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

**SUBJECT:** Final Audit Report – Payments Processed Through the Remittance Strategy for Paper Check Conversion Are Posted Accurately, but Deposit Timeliness Needs Improvement (Audit # 200940007)

This report presents the results of our review to determine the timeliness and accuracy of processing paper remittances through the Remittance Strategy for Paper Check Conversion (RS-PCC) and to determine whether it is functioning as intended. The RS-PCC is a system that electronically processes paper checks. This audit was included in the Treasury Inspector General for Tax Administration's Fiscal Year 2009 Annual Audit Plan under the major management challenge of Providing Quality Taxpayer Service Operations.

**Impact on the Taxpayer**

The RS-PCC is a system being implemented to electronically process taxpayers' checks. It is expected to result in reduced staff hours needed to process remittances, a decrease in the Lost Opportunity Cost<sup>1</sup> on payments, and a decrease in mail costs. The RS-PCC is expected to reduce the number of instances where personally identifiable information is inadvertently disclosed. Remittances are being accurately processed through the RS-PCC, but only 13 percent of the 770,504 payments are being deposited the next business day. The Lost Opportunity Cost associated with the deposits not being timely is \$696,115. Taxpayers lose the benefit of the interest earned on timely deposits that is credited to the Department of the Treasury.

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<sup>1</sup> Lost Opportunity Cost measures the interest value of money not deposited by close of business the day after receipt. Each \$1,000,000 of deposits not processed within 24 hours or 1 business day has the opportunity to lose 8 percent interest on that specific deposit amount. The interest lost is the basis of Lost Opportunity Cost. This rate is used for comparability to prior years and is not intended to represent the current interest rate.



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### **Synopsis**

In Fiscal Year 2005, the Internal Revenue Service (IRS) began working toward the ability to electronically process paper checks. The IRS expects this will eliminate the need to manually transport and process paper checks. To move toward electronic check processing, the IRS has implemented the RS-PCC. Paper checks presented for payment of any tax obligation at an IRS Consolidated Processing Center<sup>2</sup> are scanned with a desktop scanner and the data are converted to an electronic format. Using a secure transmission over the Internet, the IRS transmits the detailed remittance information to the Financial Management Service, a bureau of the Department of the Treasury that provides central payment services to Federal agencies. The Federal Reserve Bank then debits the taxpayer's bank account.

The information is also sent to the Electronic Federal Tax Payment System for posting to the taxpayer's IRS account. The RS-PCC interfaces with the Electronic Federal Tax Payment System to post taxpayer payment information overnight to the Master File.<sup>3</sup> The scanned checks are maintained for 14 days and then destroyed as classified waste.

The RS-PCC is expected to result in reduced staff hours needed to process remittances, a decrease in the Lost Opportunity Cost on payments, and a decrease in mail costs. The RS-PCC is expected to reduce the number of instances where personally identifiable information is inadvertently disclosed. The quality performance indicator for the RS-PCC is Deposit Timeliness as measured by Lost Opportunity Cost. Deposit Accuracy and Timeliness measures are also expected to improve.

Based on a sample of 469 payments, checks are generally being posted accurately and secured both before and after processing. In addition, checks are being appropriately retained for the required 14 days.

The system that maintains the archived images of RS-PCC checks is reliable. A review of archived check images for 253 payments showed the correct archived check image for 251 (99 percent) of 253 payments. \*\*\*\*\*1\*\*\*\*\*.

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<sup>2</sup> Electronic filing has significantly reduced the number of paper tax returns received each year by the IRS, requiring fewer Submission Processing Centers to process paper returns. The Andover, Massachusetts; Brookhaven, New York; Philadelphia, Pennsylvania; and Memphis, Tennessee, Submission Processing Centers have been consolidated (closed). The work previously performed by Submission Processing at those sites is now done in other Submission Processing Centers or by the Accounts Management function in Andover, Brookhaven, Memphis, and Philadelphia.

<sup>3</sup> The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.



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Finally, from a sample of 253 payments, 83 check images included a taxpayer notation on how the payment should be applied to the taxpayer's account. In all 83 cases, the payment was applied per the taxpayers' requests.

However, the codes used to track electronic payments need enhancements. The IRS uses various codes to trace and track batches of checks and individual electronic payments. One of the codes is the Remittance Processing System Identification number, which is assigned to a batch of checks in the RS-PCC unit and allows the IRS to follow the batch as it moves through payment processing. After the data from batches are uploaded to the Financial Management Service, the RS-PCC units receive a reconciliation report that indicates the status of the batch information that the Financial Management Service received. The items on the reconciliation report are not broken out or identified by RS-PCC unit. The reconciliation report also does not include the Remittance Processing System Identification number. The lack of specific batch coding makes it difficult for the IRS to know which locations are processing the most payments received from taxpayers or to identify when there is a problem with a particular location's processing of payments.

***The lack of specific batch coding makes it difficult for the IRS to know when there is a problem with a particular location's processing of payments.***

An Electronic Funds Transfer Number is also assigned to individual electronic payments and allows the IRS to track a specific payment. A test of 901,455 RS-PCC payments processed between January 22, 2008, and July 22, 2009, identified 130,951 payments (15 percent) that were inaccurately coded. Because payments were not coded according to established criteria, other payment types were erroneously included in the population and we could not identify all RS-PCC payments. The IRS stated it realized the guidance for identifying the RS-PCC payments was inaccurate so it used other ways to identify these payments.

Though checks are being accurately processed, only 13 percent of payments are being deposited the next business day through the Financial Management Service. The IRS' expectation is that all funds be deposited within 24 hours.<sup>4</sup> Analysis of the 770,504 payments processed through RS-PCC from January 22, 2008, through July 22, 2009, showed that only 99,828 payments (13 percent) met the next business day standard. The remaining 670,676 payments (87 percent) were deposited in a time period more than the next business day. The Lost Opportunity Cost associated with these deposits not being timely is \$696,115. The RS-PCC Lost Opportunity Cost is \$449.79 per \$1 million in payments. This amount is more than 2 times the cost per

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<sup>4</sup> Payments must be deposited within 24 hours (next business day). Payments received on Saturday, Sunday, and holidays need not be deposited until the next business day (the day following the weekend or holiday). Also, payments of \$100,000 or more must be deposited the same day as received.



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\$1 million in payments processed through a Submission Processing Center for Fiscal Year 2009 (\$203).

Payments of \$100,000 or more are considered timely deposited if the payments are deposited the same day as received. Of the 670,676 payments deposited untimely, 910 payments were for \$100,000 or more. None of the 910 payments were deposited on the same day as received. The Lost Opportunity Cost associated with these deposits not being timely deposited is \$316,021. While these 910 payments are less than 1 percent of the total volume of payments processed, they account for about 45 percent of the Lost Opportunity Cost.

The IRS has also not determined if the RS-PCC has reduced the staff hours needed to process remittances, decreased the Lost Opportunity Cost on payments, or decreased mail costs. The IRS stated that it plans to make this determination after Release Two has been implemented. Therefore, it could not provide us with any calculations or figures to determine if the RS-PCC is making payment processing more efficient or cost effective.

### **Recommendations**

We recommended that the Commissioner, Wage and Investment Division, further refine the RS-PCC codes to be able to track batches of payments down to the location where the batches of payments were processed and revise the internal guidelines to clarify the criteria used to identify RS-PCC payments to ensure they are properly coded.

The Commissioner should also monitor Lost Opportunity Cost and other costs such as labor and mail costs associated with the RS-PCC as it is implemented and develop a strategy to improve timeliness and reduce the Lost Opportunity Cost associated with processing payments through the RS-PCC at the Consolidated Processing Centers.

### **Response**

The IRS agreed with all of our recommendations. It has submitted a Unified Work Request for deployment of RS-PCC Release Two. Release Two will have the ability to track payments to the specific processing location and monitor costs associated with the RS-PCC, such as labor and mail costs. The IRS reviewed and revised internal guidelines for identifying the RS-PCC payments. It will also develop an action plan to improve timeliness of payments processed at Consolidated Processing Centers and to reduce Lost Opportunity Cost associated with processing payments through the RS-PCC. Management's complete response to the draft report is included as Appendix IV.

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



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Michael E. McKenney, Assistant Inspector General for Audit (Returns Processing and Account Services), at (202) 622-5916.



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## ***Abbreviations***

IRS	Internal Revenue Service
RPSID	Remittance Processing System Identification
RS-PCC	Remittance Strategy for Paper Check Conversion





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## ***Payments Processed Through the Remittance Strategy for Paper Check Conversion Are Posted Accurately, but Deposit Timeliness Needs Improvement***

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### ***Background***

The Internal Revenue Service (IRS) accepts billions of dollars in payments every year from taxpayers paying estimated tax payments in advance of filing their tax returns, submitting payments with their tax returns, and paying past due taxes. Most of these payments are made with paper checks. In Fiscal Year 2005, the IRS began working toward the ability to electronically process paper checks. The IRS expects this will eliminate the need to manually transport and process paper checks.

#### ***The RS-PCC is designed to:***

- Create and utilize digitized images of the front and back of the remittances/checks.
- Provide the capability to capture taxpayer information through manual operator entry and to capture remittance data through scanning.
- Transmit remittance transactions to the Financial Management Service Electronic Verification and Imaging System<sup>1</sup> to facilitate deposit of the remittance.
- Interface with the Electronic Federal Tax Payment System<sup>2</sup> to enable the crediting of taxpayer accounts and receive a Document Locator Number and a Trace Identifier for each transaction.
- Transmit all information necessary for long-term storage to the Remittance Transaction Research system.
- Retain data and images for 14 days on the server to accommodate downstream balancing and correction activities.

To move toward electronic check processing, the IRS has implemented the Remittance Strategy for Paper Check Conversion (RS-PCC). Paper checks presented for payment of any tax obligation at an IRS Consolidated Processing Center<sup>3</sup> are scanned with a desktop scanner and the data are converted to an electronic format. Using a secure transmission over the Internet, the IRS transmits the detailed remittance information to the Financial Management Service, a bureau of the Department of the Treasury that provides central payment services to Federal agencies. The Federal Reserve Bank then debits the taxpayer's bank account.

The information is sent to the Electronic Federal Tax Payment System for posting to the taxpayer's IRS account. The RS-PCC interfaces with the Electronic Federal Tax Payment System to post taxpayer payment

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<sup>1</sup> The host application where all check images are stored.

<sup>2</sup> A tax payment system provided free by the United States Department of the Treasury to allow individuals to pay Federal taxes electronically via the Internet or telephone.

<sup>3</sup> Electronic filing has significantly reduced the number of paper tax returns received each year by the IRS, requiring fewer Submission Processing Centers to process paper returns. The Andover, Massachusetts; Brookhaven, New York; Philadelphia, Pennsylvania; and Memphis, Tennessee, Submission Processing Centers have been consolidated (closed). The work previously performed by Submission Processing at those sites is now done in other Submission Processing Centers or by the Accounts Management function in Andover, Brookhaven, Memphis, and Philadelphia.



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information overnight to the Master File.<sup>4</sup> The scanned checks are maintained for 14 days and then destroyed as classified waste.

The RS-PCC is expected to result in reduced staff hours needed to process remittances, a decrease in the Lost Opportunity Cost<sup>5</sup> on payments, and a decrease in mail costs. The RS-PCC is expected to reduce the number of instances where personally identifiable information is inadvertently disclosed. The quality performance indicator for it is Deposit Timeliness as measured by Lost Opportunity Cost. Deposit Accuracy and Timeliness measures are also expected to improve. Although the IRS stated in its business case that RS-PCC would bring about a decrease in Lost Opportunity Cost on payments and chose Deposit Timeliness as its quality performance indicator, it stated this measure does not accurately reflect the performance of the RS-PCC. However, it continues to calculate the Lost Opportunity Cost for comparability purposes.

The IRS has stated that the delays in depositing taxpayer payments result in \$13 million annually of Lost Opportunity Cost. After full implementation, annual savings on mail costs are expected to be approximately \$2.8 million. Annual savings in labor costs are expected to be 144 Full-Time Equivalents<sup>6</sup> or \$6.4 million (calculated using Fiscal Year 2006 data).

***After implementation of the RS-PCC, the IRS expects to save \$13 million annually in Lost Opportunity Cost, \$2.8 million in mail costs, and \$6.4 million in labor costs.***

Currently, the RS-PCC is converting paper remittances received only at Consolidated Processing Centers. The following centers are currently using the RS-PCC:

- The Philadelphia, Pennsylvania, Consolidated Processing Center began use on January 14, 2008, to process insolvency trustee checks for single cases and on May 20, 2008, to process perfect payments.<sup>7</sup>
- The Brookhaven, New York, Consolidated Processing Center began use on May 28, 2008, to process perfect payments and on October 22, 2008, to process Offer in Compromise payments.

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<sup>4</sup> The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

<sup>5</sup> Lost Opportunity Cost measures the interest value of money not deposited by close of business the day after receipt. Each \$1,000,000 of deposits not processed within 24 hours or 1 business day has the opportunity to lose 8 percent interest on that specific deposit amount. The interest lost is the basis of Lost Opportunity Cost. This rate is used for comparability to prior years and is not intended to represent the current interest rate.

<sup>6</sup> A measure of labor hours in which 1 Full-Time Equivalent is equal to 8 hours multiplied by the number of compensable days in a particular Fiscal Year. For Fiscal Year 2009, 1 Full-Time Equivalent was equal to 2,088 staff hours.

<sup>7</sup> A perfect payment is a payment received for one taxpayer with one Taxpayer Identification Number for one amount and one tax period.



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- The Memphis, Tennessee, Consolidated Processing Center began use on June 10, 2008, to process perfect payments and on October 20, 2008, to process Offer in Compromise payments.
- The Andover, Massachusetts, Consolidated Processing Center began use on June 29, 2009, to process perfect payments.

In Fiscal Year 2010, the IRS will begin expanding the use of the RS-PCC to IRS walk-in offices called Taxpayer Assistance Centers.

### **The RS-PCC is being implemented in phases called releases**

The pilot, called Release One, has been implemented at the Brookhaven, Memphis, and Philadelphia Consolidated Processing Centers; Brookhaven and Memphis Centralized Offer in Compromise Operations; and Philadelphia Centralized Insolvency Operations. Release One provides the capacity of single check processing. A portion of Release One of the RS-PCC was deployed June 2009 at the Andover Consolidated Processing Center.

The IRS recently received funding to begin Release Two activities and is currently updating the schedule to reflect a new start date and update additional pilot sites. Release Two will:

- Process split remittances (one check received for more than one return/document and/or more than one tax period) and multiple payments (two or more remittances received with a single return/document).
- Be piloted at 10 Taxpayer Assistance Centers beginning in April 2010. The pilot will provide Release One functionality within the following Taxpayer Assistance Centers: San Francisco, California; Hartford, Connecticut; Detroit, Michigan; Kansas City, Missouri; Las Vegas, Nevada; Newark, New Jersey; Charlotte, North Carolina; Guaynabo, Puerto Rico; Dallas, Texas; and San Antonio, Texas.
- Equip all Taxpayer Assistance Centers with the RS-PCC Release Two functionality to process remittances. The RS-PCC will be fully deployed at all Taxpayer Assistance Centers between November 2010 and February 2011.

Currently, the IRS field offices are not equipped to process and deposit checks. Checks received in field locations must be logged and mailed to a Submission Processing Center for processing. The receiving site verifies the payments received in the mail and forwards the checks for processing. This process of mailing the remittances can take 3 or more days; thus the checks are not deposited within 24 hours. The Wage and Investment and Small Business/Self-Employed Division Collection functions are in the planning stage of developing RS-PCC functionality for the Small Business/Self-Employed Division Collection function field offices in Release Three.

This review was performed at the IRS Submission Processing Center in Ogden, Utah, and the Consolidated Processing Centers in Philadelphia, Pennsylvania, and Memphis, Tennessee, during the period July through December 2009. We conducted this performance audit in



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accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed 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***

### ***Payments Are Being Accurately Posted to Taxpayer Accounts and Maintained in a Secure Environment***

The RS–PCC Release One has been implemented at the planned Consolidated Processing Centers. Based on a sample of 469 payments,<sup>8</sup> checks are generally being posted accurately and secured both before and after processing. In addition, checks are being appropriately retained for the required 14 days.

#### **The processing workflow**

Several times a day checks extracted from the mail are delivered to the RS–PCC unit for processing. The checks are sorted into various categories, such as payments from individual taxpayers or businesses, or single checks without a posting document. Batches of 20 to 25 checks are created. The batch number is entered on a batch sheet and the batch is placed on a cart, indicating it is ready to be scanned.

Employees in the RS–PCC unit sign out a batch from the cart by initialing the batch sign-out sheet. From the signed-out batch, the employee manually enters the following items into the RS–PCC system for each check:

- Received Date.
- Name Control.
- Taxpayer Identification Number Type.<sup>9</sup>
- Remittance Processing System Identification (RPSID) Number.
- Tax Period.

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<sup>8</sup> The sample included: 1) a statistical sample of 203 payments; 2) all 14 payments equal to or greater than \$2.5 million; 3) a sample of 50 payments equal to or greater than \$100,000 but less than \$2.5 million; 4) a sample of 50 payments equal to or less than \$5; 5) 76 payments pulled from 3 batches of perfect payments during our visit to Memphis; and 6) 76 payments pulled from 4 batches (3 batches of perfect payments and 1 batch of insolvency payments) during our visit to Philadelphia. See Appendix I for details of our sampling method.

<sup>9</sup> The IRS associates taxpayers with tax records using a Taxpayer Identification Number, be it an Individual Taxpayer Identification Number, Social Security Number, or Employer Identification Number. An Employer Identification Number is a Federal Tax Identification Number used to identify a business entity, including estates and trusts.













































