



*Fiscal Year 2011 Statutory Review of
Restrictions on Directly Contacting
Taxpayers*

September 16, 2011

Reference Number: 2011-30-090

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



HIGHLIGHTS

FISCAL YEAR 2011 STATUTORY REVIEW OF RESTRICTIONS ON DIRECTLY CONTACTING TAXPAYERS

Highlights

**Final Report issued on
September 16, 2011**

Highlights of Reference Number: 2011-30-090 to the Internal Revenue Service Commissioners for the Large Business and International Division and Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

Internal Revenue Service (IRS) employees are required to stop an interview if the taxpayer requests to consult with a representative and may not bypass a representative without supervisory approval. Between October 2009 and September 2010, TIGTA's Office of Investigations closed five complaints involving allegations that IRS personnel improperly bypassed a taxpayer representative.

WHY TIGTA DID THE AUDIT

This audit was initiated because TIGTA is required to annually report on the IRS's compliance with Internal Revenue Code Sections 7521(b)(2) and (c). The overall objective of this audit was to determine whether the IRS complied with the legal guidelines addressing the direct contact of taxpayers and their representatives.

WHAT TIGTA FOUND

TIGTA varied the scope of its review this year to include discussions with, and analysis of, information received from tax representatives and personnel from the IRS's Large Business and International (LB&I) Division who reached out to TIGTA about concerns they had over potential unreported direct contact violations. TIGTA also evaluated a judgmental sample of 20 out of 2,168 large corporate audits that were open in the LB&I Division at the time of this review. TIGTA's results indicate the IRS may be at greater risk of infringing upon the direct

contact provisions during audits than the small number of complaints filed with TIGTA's Office of Investigations indicate.

Twelve tax representatives provided written accounts of their experiences where they believe examiners were starting audits without the authorized representative or insisting on interviewing taxpayers after they had secured representation. In addition, three IRS employees told TIGTA some examiners routinely contact taxpayers initially when starting an audit regardless of whether a valid Power of Attorney and Declaration of Representative (Form 2848) was filed with the IRS. Further, TIGTA's review of 20 open large corporate audits, found four instances where examiners contacted taxpayers to begin the audit even though the Form 2848 was in IRS files.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Deputy Commissioner (Operations), LB&I Division, ensure examiners use available information systems to involve tax representatives in the opening stages of the audit. TIGTA also recommended that the Deputy Commissioner (Operations), LB&I Division, and the Director, Examination, Small Business/Self-Employed Division, coordinate in initiating actions to review and revise, as needed, the language in audit initiation letters so it is clear that representatives can attend all audit appointments on behalf of the taxpayer and provide an annual refresher briefing for examiners on the importance of adhering to the processes designed to recognize taxpayer representation.

IRS officials agreed with two recommendations. The IRS plans to provide written guidance on using IRS data systems to review power of attorney information and review the audit contact letter for needed revisions. IRS officials did not concur with providing refresher training, citing recent updates to guidelines and possible changes to the audit contact letter. TIGTA believes this recommendation remains valid.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

September 16, 2011

MEMORANDUM FOR COMMISSIONER, LARGE BUSINESS AND INTERNATIONAL
DIVISION
COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION

Margaret E. Begg

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

SUBJECT: Final Audit Report – Fiscal Year 2011 Statutory Review of Restrictions
on Directly Contacting Taxpayers (Audit # 201130004)

This report presents the results of our review to determine whether the Internal Revenue Service (IRS) complied with legal guidelines addressing the direct contact of taxpayers and their representatives as set forth in Internal Revenue Code Sections 7521(b)(2) and (c). The Treasury Inspector General for Tax Administration is statutorily required to conduct this audit. This audit was conducted as part of our Fiscal Year 2011 Annual Audit Plan and addresses the major management challenge of Taxpayer Protection and Rights.

Management's complete response to the draft report is included as Appendix V.

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 Margaret E. Begg, Assistant Inspector General for Audit (Compliance and Enforcement Operations), at (202) 622-8510.



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Abbreviations

FY	Fiscal Year
I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
LB&I	Large Business and International
SB/SE	Small Business/Self-Employed
TIGTA	Treasury Inspector General for Tax Administration



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Background

This is the thirteenth year reporting that neither we nor the Internal Revenue Service (IRS) know with any degree of preciseness how well the IRS is complying with direct contact provisions of Internal Revenue Code (I.R.C.) Sections (§§) 7521(b)(2) and (c) because of limitations with its management information systems. As we reported in prior years,¹ the systems are not capable of readily identifying complaints when IRS personnel deny a taxpayer’s right to representation or bypass his or her representative without proper approval.

However, taxpayer complaints that allege IRS employees bypassed their representatives and contacted them directly are tracked by the Treasury Inspector General for Tax Administration’s (TIGTA) Office of Investigations on the Performance and Results Information System.² The Office of Investigations closed five direct contact complaints between October 2009 and September 2010 that involved an examiner and four collectors.

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The Omnibus Taxpayer Bill of Rights,³ enacted in 1988, created a number of safeguards to protect taxpayers being interviewed by IRS employees as part of an audit or investigation. Specifically, IRS employees are required by the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c) to:

- Stop a taxpayer interview whenever a taxpayer requests to consult with a representative.
- Obtain their immediate supervisor’s approval to contact the taxpayer instead of the representative if the representative is responsible for unreasonably delaying the completion of an audit or investigation.

A taxpayer can file a civil suit against the IRS if an IRS employee intentionally disregards these provisions by denying a taxpayer the right to appropriate representation.

On July 22, 1998, the President signed into law the IRS Restructuring and Reform Act of 1998,⁴ which required the IRS to revise *Your Rights as a Taxpayer* (Publication 1) to inform taxpayers

¹ See Appendix IV for a list of previous audit reports related to this review.
² The Performance and Results Information System is a management information system that provides the TIGTA with the ability to manage complaints received and investigations initiated.
³ Pub. L. No. 100-647, 102 Stat. 3730 (1988) (codified as amended in scattered sections of 5 U.S.C. and 26 U.S.C.).
⁴ 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.).



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of their rights to a) be represented at interviews and b) suspend an interview pursuant to I.R.C. § 7521(b)(2).

In addition, Congress included another provision to the IRS Restructuring and Reform Act of 1998 that requires the TIGTA to annually evaluate the IRS's compliance with the direct contact provisions. *Senate Committee on Finance Report 105-174* (dated April 22, 1998), related to the Act, stated that Congress believes taxpayers should be more fully informed of their rights to representation in dealing with the IRS and those rights should be respected.

This review was performed at the IRS National Headquarters in the offices of the Commissioner, the National Taxpayer Advocate, and the Large Business and International (LB&I) Division in Washington, D.C., and the Small Business/Self-Employed (SB/SE) Division Headquarters in New Carrollton, Maryland, during the period August 2010 through April 2011. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our 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

Because of the limitations with IRS management information systems, we varied the scope of our review this year to include discussions with tax representatives and personnel from the IRS's LB&I Division who reached out to the TIGTA about concerns they had over potential unreported direct contact violations. Despite layers of IRS management controls, our work this year surfaced evidence that suggests the IRS may be at greater risk of infringing upon the direct contact provisions during audits than the complaints filed with the TIGTA's Office of Investigations indicate.

An Array of Internal Controls Help Ensure Compliance With the Direct Contact Provisions of the Internal Revenue Code

Ultimately, the IRS relies on its examiners and collectors to properly consider and protect taxpayer rights when conducting audits and taking collection actions. To assist examiners and collectors in meeting these responsibilities, the IRS has an array of policies, procedures, and techniques (internal controls) that are in line with the Government Accountability Office's *Standards for Internal Control in the Federal Government*.⁵

The IRS's mission statement and supporting policy statements provide guidance nationwide to IRS compliance and other personnel who have contact with taxpayers. Figure 1 provides an example of IRS Policy Statement 5-2, which contains the core principles that underscore the importance of protecting taxpayer rights as well as providing the public with quality, courteous, and effective assistance in collecting unpaid taxes.

⁵ GAO/AIMD-00-21.3.1, dated November 1999.



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Figure 1: Core Principles for Collecting Unpaid Taxes

Excerpt From IRS Policy Statement 5-2	
Principles	Description
<p style="text-align: center;"><i>OVERARCHING PRINCIPLES</i></p>	<p>All our decisions about collecting must be guided by these principles. To the extent that they are, we will succeed in our mission.</p>
<p style="text-align: center;"><i>SERVICE AND ASSISTANCE</i></p> <p>All taxpayers are entitled to courteous, responsive, and effective service and assistance in all their dealings with the Service.</p>	<p>We will actively assist taxpayers who try to comply with the law and work to continually improve the quality of our systems and service to meet the needs of our customers. All taxpayers, whether delinquent or fully compliant, are entitled to prompt and professional service whenever they deal with Service employees.</p>
<p style="text-align: center;"><i>TAXPAYER RIGHTS</i></p> <p>We will observe taxpayers' rights, including their rights to privacy and to fair and courteous treatment.</p>	<p>This affirms our commitment to observe both the spirit as well as the letter of all legal requirements, including the Taxpayer Bill of Rights I and II and the IRS Restructuring and Reform Act of 1998. Taxpayers will be protected from unauthorized disclosure of information.</p>
<p style="text-align: center;"><i>COMPLIANCE</i></p> <p>The public trust requires us to ensure that all taxpayers promptly file their returns and pay the proper amount of tax, regardless of the amount owed.</p>	<p>The public as a whole is our customer, not just delinquent taxpayers. Our customers expect us to promote voluntary compliance by ensuring that all promptly pay their fair share.</p>
<p style="text-align: center;"><i>CASE RESOLUTION</i></p> <p>While we will actively assist taxpayers to comply, we will also take appropriate enforcement actions when warranted to resolve the delinquency. To resolve a case, good judgment is needed to make sound decisions on the appropriate action needed.</p>	<p>All taxpayers are required to pay by the due date of the return. From a broad range of collecting tools, employees will select the one(s) most appropriate for each case. Case resolution, including actions such as lien, levy, seizure of assets, installment agreement, offer in compromise, substitute for return, summons, and I.R.C. 6020(b), are important elements of an effective compliance program. When it is appropriate to take such actions, it should be done promptly, yet judiciously, and based on the facts of each case.</p>

Source: Excerpt from IRS Policy Statement 5-2 – Collecting Principles.

These core principles are critical to setting the appropriate tone for agency activities and interactions with taxpayers and their representatives, especially because documentation of the interactions is controlled by examiners. To supplement agency-level mission and policy



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statements, the IRS uses, and periodically updates, the Internal Revenue Manual (IRM)⁶ and numerous taxpayer publications. Both the IRM and taxpayer publications are available online and are designed to provide guidance nationwide to IRS personnel and taxpayers alike.

The IRM and taxpayer publications are important control components

From a control perspective, both the IRM and taxpayer publications are important because they provide detailed explanations and instructions of the statutory, business, and administrative procedures the IRS follows in administering the tax laws, including the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c). For example, the IRS uses Publication 1 as the main document to keep taxpayers informed of their rights and to explain the audit, collection, appeals, and refund processes. Publication 1 also includes a contact number for the TIGTA where suspected violations of the direct contact provisions and other potential misconduct or abuse by IRS employees can be reported. In addition, Publication 1 includes the following information concerning taxpayers' rights to be represented at interviews with the IRS and to suspend an interview pursuant to I.R.C. § 7521(b)(2).

You may either represent yourself or, with proper written authorization, have someone else represent you in your place. Your representative must be a person allowed to practice before the IRS, such as an attorney, certified public accountant, or enrolled agent. If you are in an interview and ask to consult such a person, then we must stop and reschedule the interview in most cases.

The IRS includes information on these rights in other publications, such as:

- *Your Federal Income Tax* (Publication 17).
- *Tax Guide for Small Business* (Publication 334).
- *Examination of Returns, Appeal Rights, and Claims for Refund* (Publication 556).
- *The Examination Process* (Publication 3498).

In addition, the IRS uses *Practice Before the IRS and Power of Attorney* (Publication 947) to inform taxpayers of their representatives' responsibilities and to notify taxpayers that the IRS has the authority to bypass representatives that are uncooperative. Specifically, Publication 947 states "After a valid power of attorney is filed, the IRS will recognize your representative. However, if it appears the representative is responsible for unreasonably delaying or hindering the prompt disposition of an IRS matter by failing to furnish, after repeated requests, non-privileged information, the IRS can contact you directly."

⁶ This is a manual containing the IRS's internal guidelines.



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A number of internal controls are also in place at the operational level

At the operational level, the first-line managers over IRS collectors and examiners (enforcement personnel) are a key control because they are responsible for ensuring that the personnel they supervise follow procedures and that their work meets acceptable standards. To assist managers in ensuring procedures are followed and standards are met, the IRM requires managers to conduct reviews over the work of the personnel they supervise, both while it is in process and after it is completed. These control techniques, as we have previously reported, help identify problems so prompt corrective actions, if needed, can be taken.

In response to our reports over the years, the IRS has taken a number of steps to reinforce upon first-line managers the need to ensure the personnel they supervise are adhering to the direct contact provisions. For example, the SB/SE Division issued a memorandum to its first-line managers in Fiscal Years (FY) 2001 and 2002 directing them to “take whatever steps are necessary (including discussion in group meetings, case reviews, workload reviews, on-the-job visits, and taxpayer/POA [Power of Attorney] inquiries) to ensure these requirements [the requirements mandated by I.R.C. §§ 7521(b)(2) and (c)] are understood and followed by employees.” In August 2006, April 2010, and May 2010, the IRS updated the IRM to include specific directions for SB/SE Division managers in its Collection and Examination functions on how to ensure compliance with the direct contact provisions of I.R.C. §§ 7521(b)(2) and (c). The guidance provided in April 2010 directed that initial contact for audits must be made with an authorized representative.

Besides first-line management reviews, quality measurement staffs annually review hundreds of closed enforcement cases to measure and evaluate the quality of audits and collection actions, communicate areas of concern to upper management, identify potential training needs, and improve work processes. While these reviews do not specifically address adherence to the direct contact provisions, they do assess the degree to which enforcement personnel are complying with procedures for protecting taxpayer rights. For FY 2010 and the first quarter of FY 2011, the SB/SE Division’s quality measurement staff reported that examiners complied with the procedures for protecting taxpayer rights in 77 percent of the cases reviewed for field audits and 93 percent of cases reviewed for office audits.

In addition to reviews by first-line managers and the quality measurement staffs, mid-level managers may evaluate ongoing work in open audits and collection cases during their operational reviews. Operational reviews are required to be performed at least annually to ensure work is being done in conformance with procedures. These processes serve as a quality control by identifying managerial, technical, and procedural problems and providing a basis for corrective actions.



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Multiple Sources Suggest Additional Actions Are Needed to Reduce the Risk of Infringing Upon Taxpayer Rights During Audits

It is important to recognize that the evidence we have obtained from the TIGTA's Office of Investigations over the years suggests potential direct contact violations are small considering that thousands of IRS enforcement personnel routinely interact with millions of taxpayers and their representatives each year. However, it is also important to recognize that the rights of each taxpayer are critical to ensuring the integrity and fairness of the tax system.

Despite layers of management controls, available evidence suggests the IRS may be at greater risk of infringing upon the direct contact provisions than the complaints filed with the TIGTA's Office of Investigations indicate. Between October 2009 and September 2010, the TIGTA's Office of Investigations closed five complaints involving allegations that IRS personnel improperly bypassed a taxpayer representative. The National Taxpayer Advocate's *2010 Annual Report to the Congress* documented practitioner concerns from the Low Income Taxpayer Clinics and American Institute of Certified Public Accountants about IRS personnel in various functions bypassing representatives without reason and without regard for the bypass procedures.

Additionally, our contacts with tax representatives and LB&I Division personnel during this review showed that some examiners may not be appropriately involving tax representatives in audits and other tax administration matters. As summarized below, 2 tax representatives provided written accounts collected from 12 other representatives where they believe examiners may have attempted to bypass the representative.

- Three representatives described events where examiners or collectors initially contacted only the taxpayer when a Power of Attorney and Declaration of Representative (Form 2848) had been previously filed with the IRS.
- Nine representatives related events in audits where examiners were insisting on interviewing the taxpayer, often in the initial interview, when it had not yet been determined that the representatives could not complete the audit themselves. In four of these instances, the representatives noted that examiners indicated they would use a summons to compel taxpayers to appear for an interview at the beginning stages of audits.

Due to time constraints, we did not attempt to verify the accuracy of the accounts the representatives submitted by retrieving and evaluating IRS case files during this review. However, we did share the accounts with IRS officials after redacting the personal identifying information contained in the documents. As reflected in the following IRS statements, the officials believe there may be some misunderstanding among the representatives about IRS audits.

Review of the representative's written accounts indicates there may be some misunderstandings among the representatives related to the Service's rights,



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responsibilities and policies regarding interviewing individuals who possess appropriate knowledge of the business; summoning when appropriate; and conducting a tour of the business. Internal Revenue Code Section 7521(c) states that an examiner cannot require a taxpayer to accompany an authorized representative to an examination interview in the absence of an administrative summons; however, that does not prevent examiners from requesting the taxpayer's voluntary presence at the interview as a means to facilitate the examination process. Examiners should not conduct the interview with representatives who are not knowledgeable regarding the taxpayer's business practices and merely serve as a courier, shuttling questions and answers between the examiner and the taxpayer. This type of arrangement may obstruct the flow of the examination. If the representative and taxpayer will not consent to the taxpayer being interviewed for those cases where it is determined to be appropriate, the examiner and group manager should consider issuing a summons. The issuance of a summons is not a "threat" as referenced by some of the representatives but rather an enforcement action which is sometimes necessary to secure information to resolve a case.

Additionally, a tour of the business and/or the physical observation of the taxpayer's operations serve as an integral part of the examination process. Treasury Regulation section 301.7605-1(d)(3)(iii) states: "regardless of where an examination takes place, the Service may visit the taxpayer's place of business or residence to establish facts that can only be established by direct visit, such as inventory or asset verification. The Service generally will visit for these purposes on a normal workday of the Service during the Service's normal tour of duty hours." From the review of the written accounts the Service's requests for tours of the taxpayer's business were appropriate.

Besides the representative accounts, three IRS employees working in its LB&I Division reached out to the TIGTA this year with concerns that some examiners routinely contact taxpayers initially when starting audits regardless of whether a valid Form 2848 was filed with the IRS. Interviewing taxpayers initially without the presence of the representative presents an opportunity to obtain more spontaneous and unrehearsed responses from taxpayers that might not have otherwise been provided about their financial situation, tax records, and business operations. IRS personnel also told us that the practice of initiating audits with taxpayers, rather than involving tax representatives, was emphasized by instructors in an examiner training class. Moreover, our review of a judgmental sample of 20 out of 2,168 large corporate audits that were open in the LB&I Division at the time of this review seemed to corroborate the assertions of IRS personnel about LB&I Division examiners initiating audits with taxpayers. Of the 20 cases reviewed, 4 were initiated with the taxpayer even though a Form 2848 was recorded in IRS files.

A combination of at least three factors likely contributed to the concerns

First, our review of the 20 cases showed that examiners are not taking advantage of the IRS's automated information systems to identify and involve tax representatives during the initial stages of audits. In reviewing the 20 audit case files, we accessed the IRS's automated



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information systems⁷ to determine if the taxpayers filed a Form 2848 with the IRS. For 12 of the 20 audits, we saw no documentation that this resource was used to determine if a Form 2848 was on file with the IRS before the audit was initiated. In addition, we found that only 5 of 20 examiners involved in the cases we reviewed had the capability to access the systems. IRS officials told us that it is common for examiners to have clerical personnel access the IRS automated systems and secure needed documentation for them.

Second, the language in the audit contact letter (Letter 2205) used by field examiners to initiate audits could be confusing taxpayers and examiners alike because it seemingly creates an expectation that taxpayers need to attend the first appointment. For example, in addition to identifying and including sources of information that explain the rules, procedures, and processes the IRS follows during the audits, the Letter informs taxpayers that they may have someone represent them during any part of the audit. However, the Letter also requests taxpayers to submit a completed Form 2848 at the first appointment, or prior to it, if they want someone to represent them during the audit. In contrast, the language in the audit contact letter (Letter 2202) used by office examiners informs taxpayers that if they are not attending their first audit appointment, they must submit a completed Form 2848 in advance.

Third, there is a concern that some examiners may believe it is more efficient to initiate audits directly with taxpayers rather than involve tax representatives. Field examiners typically conduct detailed interviews during the first appointment and request to see the business facilities of the taxpayer under audit. From an examiner perspective, the interview process and business tour are critical components of the audit process because they are designed to provide information about the taxpayer's financial condition, business operations, and books and records. They also help set the scope and depth of the audit and are used to obtain leads, develop information, and establish evidence. However, despite the importance to field examiners, taxpayers have the right under the tax laws to have a representative attend the first appointment and all other appointments on their behalf.

The National Taxpayer Advocate's report expressed the need to provide annual training for IRS employees who routinely interact with taxpayers and representatives. Given the risk that a number of potential direct contact violations may be occurring and not being reported, we believe the National Taxpayer Advocate's recommendation to provide annual training could be a cost-effective solution to help alleviate these concerns. This training would be in-line with the IRS learning and education policy, which requires all employees to complete short, mandatory refresher training in critical areas of tax administration such as ethics and information security. It would also be consistent with internal control standards, which require all personnel to possess and maintain a level of competence that allows them to accomplish their assigned duties.

⁷ These include, among others, IRS Business Master File and Centralized Authorization File. The Business Master File is a database that consists of Federal tax-related transactions and accounts for businesses. The Centralized Authorization File is a computerized system of records which houses authorization information from both powers of attorney and tax information authorizations.



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Recommendations

Recommendation 1: The Deputy Commissioner (Operations), LB&I Division, should ensure examiners and their immediate managers take advantage of the IRS's automated information systems to identify and involve tax representatives during the initial stages of audits.

Management's Response: IRS officials agreed with this recommendation. The Deputy Commissioner (Operations), LB&I Division, will provide written guidance to examiners and frontline managers on their responsibility to take proper steps to review the power of attorney information from the IRS data systems prior to contacting taxpayers.

The Deputy Commissioner (Operations), LB&I Division, and the Director, Examination, SB/SE Division, should coordinate in initiating actions:

Recommendation 2: To review the language in Letter 2205 and use the review results to revise the language, as needed, so it is clear that tax representatives can attend all audit appointments on behalf of taxpayers.

Management's Response: IRS officials agreed with this recommendation. The Director, Examination, SB/SE Division, will coordinate with the Deputy Commissioner (Operations), LB&I Division, to review the language in Letter 2205 and revise the language, if needed, so it is clear that tax representatives can attend all audit appointments on behalf of taxpayers.

Recommendation 3: Needed to provide periodic refresher briefings for examiners on the importance of adhering to the processes designed to recognize taxpayer representation.

Management's Response: IRS officials did not concur with this recommendation. In April 2010, the SB/SE Division revised two IRM sections to provide additional directions to staff regarding the importance of adhering to the processes designed to recognize taxpayer representation. IRS officials indicated they believe the recent updates to the IRM, as well as any revisions made to the initial appointment letter as determined from Recommendation 2, will provide the appropriate guidance.

Office of Audit Comment: TIGTA believes this recommendation remains valid and is not alone in its position. As discussed in the report, the National Taxpayer Advocate has reported receiving practitioners concerns about IRS personnel bypassing representatives without reason and has similarly concluded there is a need for additional training. In their response to TIGTA's report, IRS officials indicated that they believe the report may overstate the number of occurrences of potential direct contact violations because we used unverified anecdotal accounts from taxpayer representatives to cite possible violations. They further stated that they believe these representatives may have misinterpreted IRS normal audit procedures to request to interview the taxpayer, when



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appropriate, and tour the taxpayer's business location as an attempt to bypass the representative's valid power of attorney which is not the case. As noted in the report, we did not attempt to verify the accuracy of the accounts the representatives provided due to the time constraints imposed upon us for completing this review. However, we did refer the written accounts provided by the representatives to TIGTA's Office of Investigations for appropriate action.



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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether the IRS complied with legal guidelines addressing the direct contact of taxpayers and their representatives as set forth in I.R.C. §§ 7521(b)(2) and (c). To accomplish this objective, we:

- I. Determined if an IRS system and/or process has been implemented since our last review to identify those cases where taxpayers have requested to consult with a representative or where IRS employees bypassed a representative and directly contacted the taxpayer.
 - A. Interviewed IRS management personnel in the SB/SE and LB&I Divisions.
 - B. Reviewed a judgmental sample of 20 of 2,168 LB&I Division open industry cases where the taxpayers had a power of attorney in the audit and the cases were open in the third and fourth quarters of FY 2010. This sample was taken to validate concerns raised by LB&I Division personnel who reached out to the TIGTA concerning examiners making first contacts with taxpayers. We also evaluated the cases to identify any indication of the following potential violations of I.R.C. §§ 7521(b)(2) or (c):
 - a. The examiner denied the taxpayer the opportunity to obtain representation.
 - b. The examiner bypassed the representative and contacted the taxpayer directly.
 - c. The examiner mandated the appearance of the taxpayer with an authorized representative.
- II. Determined if any systems or processes have been modified since our last review to track taxpayer complaints relating to IRS violations of I.R.C. §§ 7521(b)(2) and (c).
 - A. Interviewed IRS personnel responsible for the Taxpayer Advocate Management Information System¹ and the e-trak System² to determine if these two systems have been modified to track taxpayer complaints relating to IRS violations of I.R.C. §§ 7521(b)(2) and (c).
 - B. Reviewed the TIGTA Office of Investigations' complaint and investigation cases that were closed in FY 2010 and tracked on the Performance and Results Information

¹ The Taxpayer Advocate Management Information System is an electronic database and case inventory control system used by Taxpayer Advocate Service function employees.

² The e-trak application is a web-based data tracking system that enables meaningful data management, tracking, retrieval, and reporting.



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- System³ to determine the validity of these cases and what actions the IRS has taken as a result, as well as the potential number of taxpayers that may have had their rights and entitlements infringed upon.
- III. Evaluated the complaints received by the Deputy Inspector General for Audit to gain an understanding of the issues raised and determine if the IRS has proper controls to address the concerns identified.
- A. Interviewed two tax representatives about the concerns they had raised on IRS employees bypassing taxpayers' representatives and reviewed documentation they provided regarding direct contact complaints.
 - B. Contacted TIGTA Office of Investigations personnel to determine if there are investigations that have started as a result of forwarding these allegations to them and the current status of any related investigation.
 - C. Researched the pertaining IRMs and training materials to identify the LB&I Division audit process and determine if the LB&I Division has proper procedures/guidelines and trainings in response to I.R.C. §§ 7521(b)(2) and (c).
- IV. Reviewed information on the actions taken by the IRS in response to I.R.C. §§ 7521(b)(2) and (c) to determine the impact of these code sections on IRS programs.
- A. Reviewed prior TIGTA audit reports to identify recommendations and the IRS's planned corrective actions.
 - B. Evaluated the procedures in the IRM to determine whether the IRS has completed the corrective action in response to our FY 2009 report.⁴ The planned corrective action was to update IRM Section 1.4.40, Resource Guide for Managers - SB/SE Compliance Field Examination Group Manager, to include specific guidance for Examination function group managers to ensure that the requirements of I.R.C. §§ 7521(b)(2) and (c) are understood and followed.
 - C. Researched the IRS Intranet to identify additional guidance to IRS employees for meeting the direct contact provisions and determine the impact on IRS programs.
 - D. Reviewed www.irs.gov and the related IRS publications to identify how the IRS informs taxpayers of its prohibition against directly contacting taxpayers and evaluated whether they provide adequate guidance for taxpayers and their representatives.

³ The Performance and Results Information System is a management information system that provides the TIGTA with the ability to manage complaints received and investigations initiated.

⁴ *Fiscal Year 2009 Statutory Review of Restrictions on Directly Contacting Taxpayers* (Reference Number 2009-30-054, dated March 24, 2009).



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Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective:

- The agency level internal control activities:
 - a. The IRS's mission statement and supporting policy statements along with the IRM guidelines provide guidance to IRS employees to ensure compliance with direct contact provisions.
 - b. Numerous publications keep taxpayers informed of their rights.
- The operational level internal control activities: the first line managers are responsible for ensuring the personnel they supervise follow procedures and that their work meets acceptable standards. They will need to review the work of the personnel they supervise, both while it is in process and after it is completed, which helps identify problems so prompt corrective actions, if needed, can be taken.



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Appendix II

Major Contributors to This Report

Margaret E. Begg, Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Frank Dunleavy, Director
Alan Lund, Audit Manager
Jean Kao, Lead Auditor
Stanley Pinkston, Senior Auditor



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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner (Operations), Large Business and International Division SE:LB
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Communications, Liaison, and Disclosure, Small Business/Self-Employed Division
SE:S:CLD
Director, Examination, Small Business/Self-Employed Division SE:S:E
Director, Pre-Filing and Technical Guidance, Large Business and International Division
SE:LB:PFTG
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
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Office of Internal Control OS:CFO:CPIC:IC
Audit Liaisons:
 Commissioner, Small Business/Self-Employed Division SE:S
 Commissioner, Large Business and International Division SE:LB



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Appendix IV

Previous Audit Reports Related to This Statutory Review

The Internal Revenue Service Needs to Enhance Guidance on and Monitoring of Compliance With Procedures for Directly Contacting Taxpayers and Their Representatives (Reference Number 1999-10-076, dated September 30, 1999).

Letter Report: Improvements Have Been Implemented for Directly Contacting Taxpayers and Their Representatives (Reference Number 2000-10-132, dated September 18, 2000).

Letter Report: The Internal Revenue Service Has Not Implemented a Process to Monitor Compliance With Direct Contact Provisions (Reference Number 2001-10-116, dated July 23, 2001).

The Internal Revenue Service Cannot Monitor Its Compliance With the Direct Contact Provisions (Reference Number 2002-40-177, dated September 11, 2002).

Fiscal Year 2003 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2003-40-131, dated June 16, 2003).

Fiscal Year 2004 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2004-40-059, dated February 24, 2004).

Fiscal Year 2005 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2005-40-040, dated February 22, 2005).

Fiscal Year 2006 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2006-40-136, dated August 28, 2006).

Fiscal Year 2007 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2007-40-118, dated July 13, 2007).

Fiscal Year 2008 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2008-40-090, dated March 27, 2008).

Fiscal Year 2009 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2009-30-054, dated March 24, 2009).

Fiscal Year 2010 Statutory Review of Restrictions on Directly Contacting Taxpayers (Reference Number 2010-30-060, dated June 3, 2010).



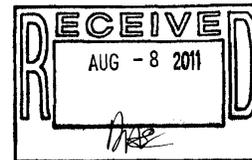
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Appendix V

Management's Response to the Draft Report



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



August 8, 2011

MEMORANDUM FOR MICHAEL R. PHILLIPS
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Faris R. Fink *Faris R. Fink*
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – Fiscal Year 2011 Statutory
Review of Directly Contacting Taxpayers (Audit # 201130004)

Thank you for the opportunity to review your draft report titled: "Fiscal Year 2011 Statutory Review of Directly Contacting Taxpayers." Preservation of taxpayer rights is of utmost importance to the IRS. We appreciate your acknowledgement that IRS has an array of policies, procedures, and techniques (internal controls) that are in line with the Government Accountability Office's *Standards for Internal Control in the Federal Government* to assist examiners and collectors in meeting their responsibilities to properly consider and protect taxpayer rights when conducting audits and taking collection actions.

At the operational level, first-line managers over IRS collectors and examiners are a key control as they are responsible for ensuring the personnel they supervise follow procedures and their work meets acceptable standards. To assist managers in ensuring procedures are followed and standards are met, the Internal Revenue Manual (IRM) requires managers to conduct reviews over the work of the personnel they supervise, both while it is in process and after it is completed. These control techniques help identify problems so prompt corrective actions, if needed, can be taken.

As noted in your report, our quality measurement staffs annually review hundreds of closed enforcement cases to measure and evaluate the quality of audits and collection actions, communicate areas of concern to upper management, identify potential training needs, and improve work processes. These reviews assess the degree to which enforcement personnel are complying with procedures for protecting taxpayer rights.

In addition to reviews by first-line managers and the quality measurement staffs, mid-level managers evaluate ongoing work in open audits and collection cases during their operational reviews. Operational reviews are required to be performed at least annually to ensure work is being done in conformance with procedures. These



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processes serve as a quality control by identifying managerial, technical, and procedural problems and providing a basis for corrective actions.

We appreciate the recognition in your report that the evidence obtained from TIGTA's Office of Investigations over the years suggests potential direct contact violations are small considering that thousands of IRS enforcement personnel routinely interact with millions of taxpayers and their representatives each year. We take seriously every potential direct contact violation and while the potential number of direct contacts is small, we believe that your report may overstate the number of potential occurrences. During your annual audit for this year, you utilized unverified anecdotal accounts from taxpayer representatives to cite possible indications of violations of taxpayer rights. We believe these representatives may have misinterpreted our normal audit procedures to request to interview the taxpayer, when appropriate, and tour the taxpayer's business location as an attempt on our part to bypass the representative's valid power of attorney which is not the case.

As discussed, preservation of taxpayer rights is of utmost importance to the IRS and we continue to take steps to ensure our employees are aware of direct contact provisions. We concur with recommendations one and two and partially concur with recommendation three. Attached is a detailed response outlining our corrective actions.

If you have any questions, please contact me, or a member of your staff may contact Shenita Hicks, Director, Examination, at (859) 669-5526.

Attachment



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Attachment

RECOMMENDATION 1:

The Deputy Commissioner (Operations), LB&I Division, should ensure examiners and their frontline managers take advantage of IRS's automated information systems to identify and involve tax representatives during the initial stages of audits.

CORRECTIVE ACTION:

We concur with this recommendation. The Deputy Commissioner (Operations), Large Business and International (LB&I Division), will ensure that examiners and their frontline managers follow current procedures regarding the direct taxpayer contact provisions of the Internal Revenue Code (I.R.C.) §§ 7521(b) (2) and (c). The LB&I Division will provide written guidance to examiners and frontline managers on their responsibility to take proper steps to review the power of attorney information from the IRS automated systems prior to contacting taxpayers.

IMPLEMENTATION DATE:

September 15, 2012

RESPONSIBLE OFFICIAL(S):

Director, Pre-Filing and Technical Guidance (PFTG), LB&I Division

CORRECTIVE ACTION MONITORING PLAN:

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

RECOMMENDATION 2:

The Deputy Commissioner (Operations), LB&I Division, and the Director, Examination, SB/SE Division, should coordinate in initiating actions to review the language in the audit contact letter (Letter 2205) and use the review results to revise the language, as needed, so it is clear that tax representatives can attend all audit appointments on behalf of taxpayers.

CORRECTIVE ACTION:

We concur with this recommendation. The Director, Examination, Small Business/Self-Employed (SB/SE) Division, will coordinate with the Deputy Commissioner (Operations), LB&I Division, to review the language in the Initial Contact Letter (Letter 2205) and revise the language, if needed, so it is clear that tax representatives can attend all audit appointments on behalf of taxpayers.

IMPLEMENTATION DATE:

September 15, 2012

RESPONSIBLE OFFICIAL(S):

Director, Examination Policy, SB/SE Division
Director, PFTG, LB&I Division



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CORRECTIVE ACTION MONITORING PLAN:

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

RECOMMENDATION 3:

The Deputy Commissioner (Operations), LB&I Division, and the Director, Examination, SB/SE Division, should coordinate in initiating actions needed to provide periodic refresher briefings for examiners on the importance of adhering to the processes designed to recognize taxpayer representation.

CORRECTIVE ACTION:

We agree that it is important that examiners and managers have the appropriate guidance. In April 2010, SB/SE revised the Internal Revenue Manual (IRM) 4.10.2 and 4.11.55 to provide additional directions to staff regarding the importance of adhering to the processes designed to recognize taxpayer representation. We believe the recent updates to the IRM, as well as any revisions made to the initial appointment letter as determined from recommendation 2 above, will provide the appropriate guidance.

IMPLEMENTATION DATE:

September 15, 2012

RESPONSIBLE OFFICIAL(S):

Director, Examination Policy, SB/SE Division
Director, PFTG, LB&I Division

CORRECTIVE ACTION MONITORING PLAN:

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