



*Collection Field Function Procedures  
Were Not Always Followed When  
Assessing Taxes on Businesses That  
Have Not Filed Tax Returns*

**September 17, 2012**

**Reference Number: 2012-30-110**

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.

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Phone Number | 202-622-6500

E-mail Address | [TIGTACommunications@tigta.treas.gov](mailto:TIGTACommunications@tigta.treas.gov)

Website | <http://www.tigta.gov>



## HIGHLIGHTS

### **COLLECTION FIELD FUNCTION PROCEDURES WERE NOT ALWAYS FOLLOWED WHEN ASSESSING TAXES ON BUSINESSES THAT HAVE NOT FILED TAX RETURNS**

## Highlights

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

Highlights of Reference Number: 2012-30-110 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

### **IMPACT ON TAXPAYERS**

The IRS has the ability to prepare returns and assess taxes under the authority of Internal Revenue Code (I.R.C.) Section (§) 6020(b) when business taxpayers do not file required returns or file false or fraudulent returns. However, case histories of I.R.C. § 6020(b) business assessments made by Collection Field function revenue officers (RO) did not always contain the proper documentation to support the reason for the assessment, which increases the risk of an improper assessment. In addition, ROs did not always allow taxpayers 30 calendar days to respond to proposed assessments prior to processing the 6020(b) returns, which potentially violates the taxpayers' rights.

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

Collection Field function 6020(b) assessments have increased significantly in recent years. In Fiscal Year 2011, \$1.64 billion in 6020(b) assessments entered the collection stream. TIGTA initiated this audit to evaluate the impact of the Collection Field function's use of I.R.C. § 6020(b) authority on taxpayer compliance and to determine whether employees are using the proper procedures to assess tax liabilities.

### **WHAT TIGTA FOUND**

TIGTA reviewed a statistical sample of 96 6020(b) assessments and determined that ROs followed many of the required procedures. However, in 20 (21 percent) cases, there was no

evidence for the basis of assessments. In addition, in 10 (10 percent) cases, ROs did not allow, or there was no evidence to support the allowance of, the required 30 calendar days for taxpayers to respond to proposed assessments prior to the IRS processing the 6020(b) returns.

TIGTA also determined that during Calendar Year 2008, taxpayers with stand-alone 6020(b) assessments (assessments made in which the taxpayers had potential delinquent returns due but no outstanding tax liabilities) were less compliant in subsequent years than taxpayers without 6020(b) assessments. However, a more in-depth study of delinquent returns in which the use of I.R.C. § 6020(b) authority was considered but not used may be needed to better understand these results. The IRS does not track subsequent filing compliance when I.R.C. § 6020(b) authority is used.

### **WHAT TIGTA RECOMMENDED**

TIGTA recommended that the Director, Enterprise Collection Strategy, Small Business/Self-Employed Division: 1) develop an internal control to help ensure ROs properly document a complete explanation for the basis of 6020(b) assessments, 2) develop an internal control to allow taxpayers 30 calendar days to respond to proposed assessments before submitting returns for processing, and 3) establish a methodology to compare actual results with management's anticipated benefit of improving filing compliance when I.R.C. § 6020(b) authority is used for business taxpayers.

In their response to the report, IRS officials agreed with the recommendations and plan to: 1) initiate a change to the Integrated Collection System to help ensure ROs document the required basis for the 6020(b) assessment, 2) initiate a change to the Integrated Collection System to help ensure ROs allow taxpayers 30 calendar days to respond to the proposed assessment before submitting the prepared returns for processing, and 3) request a research project to measure the effectiveness of the Collection Field function I.R.C. § 6020(b) program on future filing compliance of business taxpayers and weigh the results against ultimate case resolution to determine if any program changes are warranted.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

September 17, 2012

**MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED  
DIVISION**

**FROM:** Michael E. McKenney  
Acting Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – Collection Field Function Procedures Were Not  
Always Followed When Assessing Taxes on Businesses That Have Not  
Filed Tax Returns (Audit # 201130017)

This report presents the results of our review to evaluate the impact of the Small Business/  
Self-Employed Division<sup>1</sup> Collection Field function's use of Internal Revenue Code Section  
6020(b)<sup>2</sup> authority on taxpayer compliance and to determine whether employees are using the  
proper procedures to assess tax liabilities. This audit is included in our Fiscal Year 2012 Annual  
Audit Plan and addresses the major management challenge of Tax Compliance Initiatives.

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

Copies of this report are also being sent to the Internal Revenue Service managers affected by the  
report recommendations. Please contact me at (202) 622-6510 if you have questions or  
Frank Dunleavy, Acting Assistant Inspector General for Audit (Compliance and Enforcement  
Operations), at (213) 894-4470 (Ext. 128).

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<sup>1</sup> See Appendix V for a glossary of terms.

<sup>2</sup> 26 U.S.C. § 6020(b)



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*Collection Field Function Procedures Were Not  
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## *Table of Contents*

<b>Background</b> .....	Page 1
<b>Results of Review</b> .....	Page 4
Collection Field Function 6020(b) Assessments Have Significantly Increased in Recent Years.....	Page 4
Revenue Officers Followed Many of the Required Procedures for Processing 6020(b) Assessments .....	Page 8
Evidence Was Not Always Available to Support the Basis of 6020(b) Assessments .....	Page 9
<u>Recommendation 1</u> :.....	Page 10
Revenue Officers Did Not Always Allow 30 Calendar Days for Taxpayers to Respond Prior to Processing 6020(b) Returns .....	Page 10
<u>Recommendation 2</u> :.....	Page 11
Many Taxpayers Remain Noncompliant After 6020(b) Assessments Have Been Made.....	Page 12
<u>Recommendation 3</u> :.....	Page 14
<b>Appendices</b>	
Appendix I – Detailed Objectives, Scope, and Methodology.....	Page 15
Appendix II – Major Contributors to This Report.....	Page 18
Appendix III – Report Distribution List .....	Page 19
Appendix IV – Outcome Measure .....	Page 20
Appendix V – Glossary of Terms .....	Page 21
Appendix VI – Management’s Response to the Draft Report .....	Page 24



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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## *Abbreviations*

CFf	Collection Field function
CNC	Currently Not Collectible
FY	Fiscal Year
ICS	Integrated Collection System
I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
RO	Revenue Officer



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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## *Background*

The Internal Revenue Service (IRS) has the authority to prepare returns and assess taxes under Internal Revenue Code (I.R.C.) Section (§) 6020(b)<sup>1</sup> when taxpayers do not file required returns or file false or fraudulent returns. This authority includes both individual and business taxpayers, and the IRS has specific programs for each of them.

The programs developed for individual taxpayers are the Substitute for Return Program and its automated version, the Automated Substitute for Return Program. Although assessments are proposed under the Substitute for Return Program by revenue officers (RO)<sup>2</sup> and various other compliance employees, the Automated Substitute for Return Program is the key compliance program for taxpayers who have not filed individual income tax returns but owe a significant income tax liability. The purpose of both programs is to assess the correct tax liability by either securing a voluntary income tax return from the taxpayer or by computing tax, interest, and penalties based upon the IRS's internal information.

The parallel program for business taxpayers is referred to as simply 6020(b). Business returns are prepared and assessed for entities when: 1) the business appears to be liable for a return, 2) the person required to file the business return does not file it, and 3) attempts to secure the return fail. The 6020(b) assessments on business returns are generally proposed in one of two ways:

***Business returns may be prepared and assessed under I.R.C. § 6020(b) authority when it appears the business is liable for a return, the return is not filed, and attempts to secure the return have failed.***

- Systemically through the Automated 6020(b) Program. This program uses information (such as wages and taxes) from the taxpayer's last return filed as the basis for the assessment.
- Manually by ROs and other compliance employees (such as revenue agents). ROs may secure additional information from the taxpayer or third parties to help determine a basis for the assessment.

The Automated 6020(b) Program is limited to employment tax returns with last return assessments and/or credits between \$250 and \$1,500, and extending back only three years from the current year. Despite this limitation, most assessments of business returns are made through the automated program. Figure 1 shows that in Fiscal Year (FY) 2011, 153,347 (71 percent) of 216,150 6020(b) business assessments were created through the Automated 6020(b) Program.

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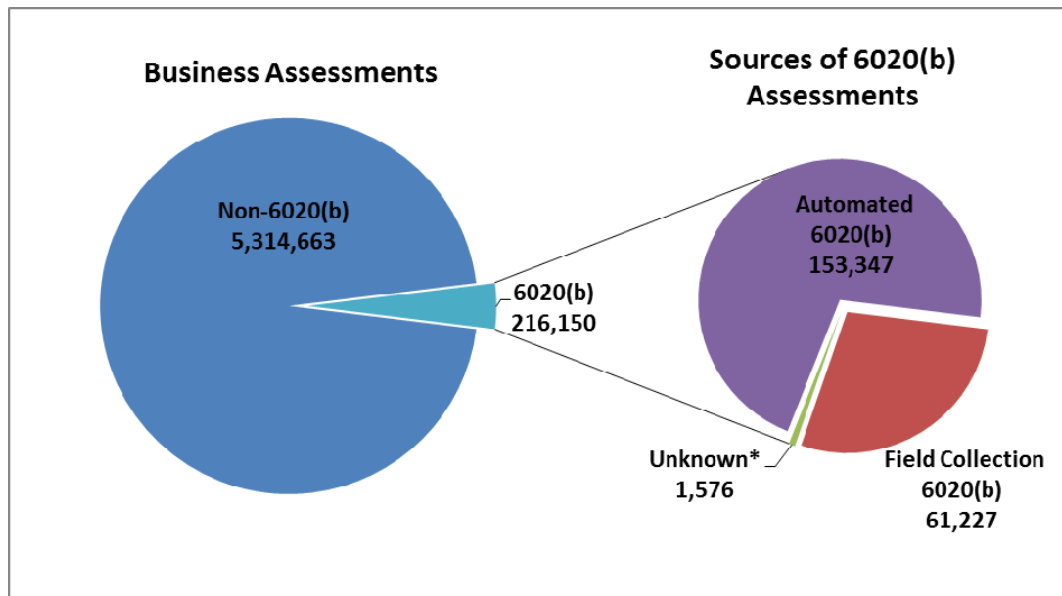
<sup>1</sup> 26 U.S.C. § 6020(b)

<sup>2</sup> See Appendix V for a glossary of terms.



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

**Figure 1: Business Assessments That Entered the Collection Stream**



Source: Our analysis of Collection Activity Report 5000-2/242.

\*Unknown source of assessment due to IRS case processing errors.

Employment tax returns that are not in the \$250 to \$1,500 range are assessed manually by the Collection Field function (CFf). The 6020(b) assessments made by the CFf account for the majority of dollars assessed. Specifically, in FY 2011, \$1.07 billion (65 percent) of \$1.64 billion in 6020(b) assessments that entered the collection stream<sup>3</sup> were manually created in the CFf by ROs. This review focused only on manually processed 6020(b) business assessments in the CFf (hereafter referred to as 6020(b)).

When the IRS pursues a case involving a business nonfiler, it will usually send the taxpayer one or two notices concerning the return in question. If the taxpayer fails to resolve the situation during the delinquency notice process, a Taxpayer Delinquency Investigation (hereafter referred to as a delinquent return investigation) is created. The delinquent return investigation is then assigned a case prioritization code that determines where it will be assigned to be worked. The case may be assigned to the CFf, where an RO will begin the investigation. Before using I.R.C. § 6020(b) authority to secure a return on a delinquent return investigation, ROs consider a number of factors, including:

- Prior history of noncompliance.
- Existence of income from illegal sources.

<sup>3</sup> Assessments that enter the collection stream receive a balance due notice. Some assessments never enter the collection stream because they may have credit balances or liabilities may be resolved prior to that point.



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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- Effect upon voluntary compliance.
- Anticipated revenue and collectability in relation to the time and effort required to determine tax due.

ROs close some delinquent return investigations without the use of I.R.C. § 6020(b) authority. For example, some cases may be closed because the nonfiling is not willful and:

- There would be no tax due on the delinquent return.
- There would be minimal net tax due on the return.
- The cost to the IRS to secure a return would exceed anticipated revenue.

After being assigned a delinquent return investigation, ROs conduct a field call to determine if the taxpayer's business is in operation and paying wages to its employees. These conditions are indications that the taxpayer is potentially liable for the delinquent return. ROs then establish a specific date for filing the delinquent return, and if the taxpayer fails to file any required employment, excise, and/or partnership tax returns by the specified date, ROs may prepare the returns under I.R.C. § 6020(b) authority using the Integrated Collection System (ICS).

This review was performed at the IRS Small Business/Self-Employed Division's Headquarters office in New Carrollton, Maryland, and the CFf office in Baltimore, Maryland, during the period August 2011 through April 2012. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Detailed information on our audit objectives, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.





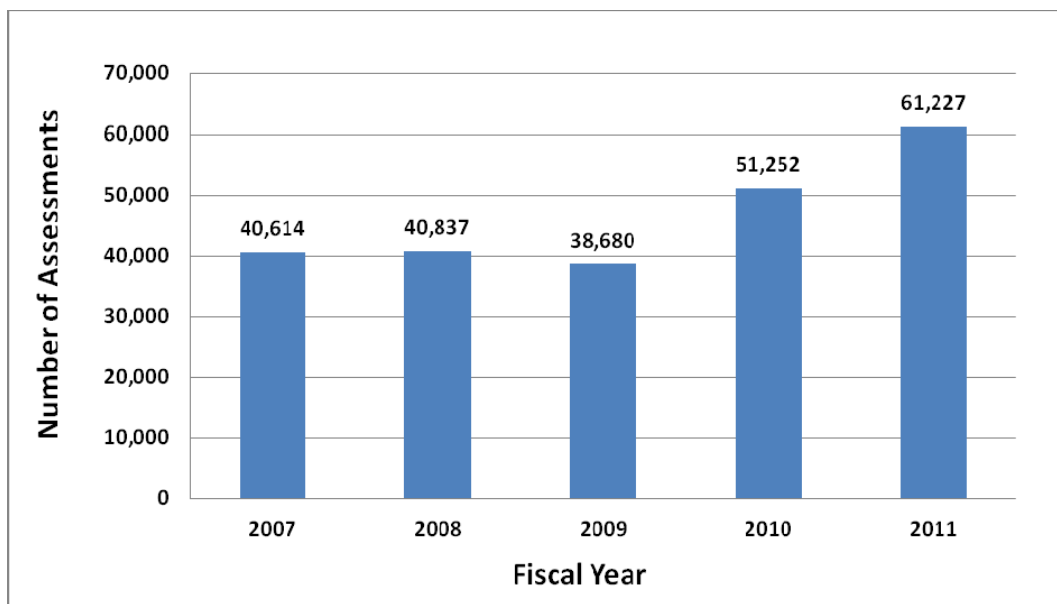
*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

*Results of Review*

**Collection Field Function 6020(b) Assessments Have Significantly Increased in Recent Years**

We reviewed IRS Collection Activity Reports for FY 2007 through FY 2011 to identify Cff trends for 6020(b) assessments. Figure 2 shows there has been a substantial increase in the number of 6020(b) assessments over the last few years.

**Figure 2: RO's 6020(b) Assessments That Entered the Collection Stream**



Source: Collection Activity Report 5000-2/242.

Since FY 2009, the number of Cff 6020(b) assessments entering the collection stream has increased by 58 percent. Specifically, there was a 33 percent increase in the number of 6020(b) assessments from FY 2009 to FY 2010 and a 19 percent increase from FY 2010 to FY 2011. IRS management indicated that the increase can be attributed to additional ROs hired in FY 2009 and FY 2010. A recent report<sup>4</sup> by the Treasury Inspector General for Tax Administration found that between June 2009 and February 2010, the IRS hired 1,515 ROs. As a result of the hiring initiative, and after accounting for normal attrition, the total number of ROs

<sup>4</sup> Treasury Inspector General for Tax Administration, Ref. No. 2011-30-039, *Challenges Remain to Balance Revenue Officer Staffing With Attrition and Workload Demands* (May 2011).



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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increased by 580. According to IRS management, new hires typically handle more delinquent return investigations than Taxpayer Delinquent Accounts (hereafter referred to as balance due accounts) during the training process. This policy may increase the number of 6020(b) assessments made because it is one of the primary enforcement tools available to ROs to address delinquent return investigations of business nonfilers.

Our analysis of IRS data also suggests that the increase in 6020(b) assessments by ROs may be related to increases in staffing. According to IRS Collection Activity Reports, there has been a 38 percent increase in the number of delinquent returns secured by the CFf between FY 2009 and FY 2011. However, the number of delinquent returns secured by all Collection functions decreased by one percent during the same time period. Therefore, the increase in delinquent returns secured by the CFf (the function with the increased staffing) corresponds to the increase in 6020(b) assessments.

**Many balance due accounts are closed as currently not collectible (CNC) or fully abated**

After a liability is assessed under I.R.C. § 6020(b) authority and a balance is due, the first of two balance due notices is issued to the taxpayer. Initially, a Master File notice is issued. If there is no response, a Computer Paragraph 504, *Final Notice – Balance Due*, is issued. The notice phase represents the beginning of the collection process. From a resources standpoint, resolving tax liabilities during the notice phase is cost effective because the process is highly automated, which helps contain administrative and personnel costs.

If a tax liability is not resolved during the balance due notice phase, the module becomes a balance due account. The Inventory Delivery System is an application that uses specific criteria and established business rules to select and route balance due accounts to either the Automated Collection System, the Queue, or to the CFf for further action. However, IRS management informed us that balance due accounts originating as 6020(b) assessments by ROs typically deviate from this process and are worked by the original RO until the case is closed. This deviation allows the taxpayer to work with only one IRS employee throughout the entire collection process. ROs may also be assigned to work balance due accounts that were originally assessed under I.R.C. § 6020(b) authority by other collection functions and employees, such as tax examiners or the Campus Compliance Services' Automated 6020(b) Program.

The Internal Revenue Manual (IRM)<sup>5</sup> describes the collection procedures that ROs should utilize when working balance due accounts. CFf employees informed us that the balance due accounts resulting from 6020(b) assessments are treated no differently procedurally during the collection process, nor are they given any particular priority over other balance due accounts, after being assigned to the RO. The IRM instructs ROs to contact the taxpayer and demand full payment when a return is received without full payment of tax, penalty, and interest.

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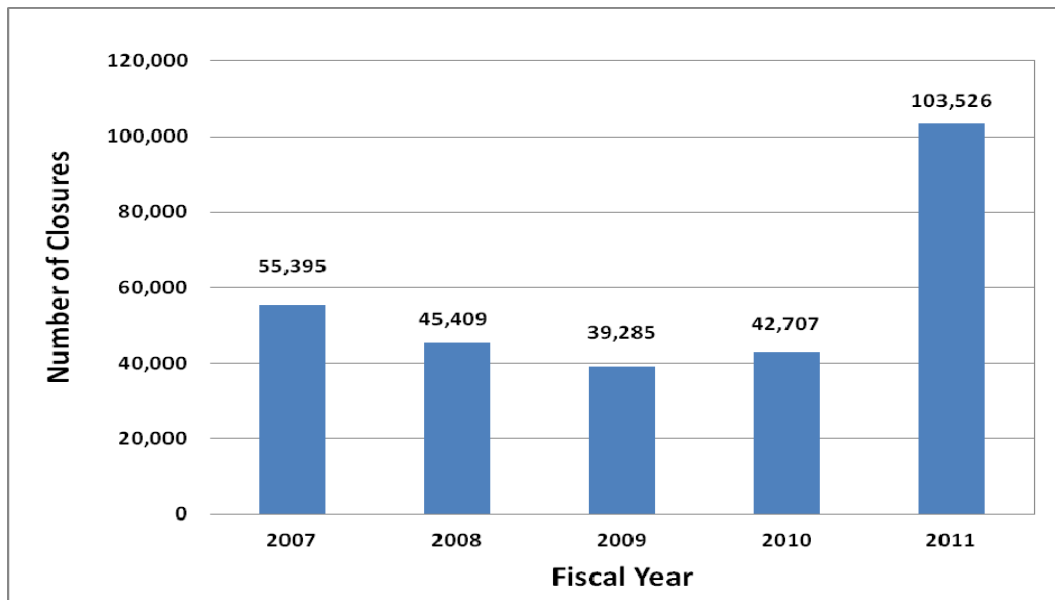
<sup>5</sup> IRM 5.1.1.1 and 5.1.1.2 (Nov. 29, 2011).



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

Figure 3 shows that during FY 2011, the CFf closed 103,526 balance due accounts that were assessed using I.R.C. § 6020(b) authority. This amount represents an increase of more than 163 percent since FY 2009.

**Figure 3: CFf 6020(b) Balance Due Accounts Closed by ROs**



Source: Collection Activity Report 5000-242.

CFf employees can close a balance due account in a variety of ways. From a financial and resources perspective, the best resolution for a case is the collection of the full amount of tax, penalty, and interest owed to the IRS. However, balance due accounts can also be closed in other ways, such as:

- CNC.
- Installment agreement.
- Offer in compromise.
- Full abatement.

Cases closed as either CNC or full abatement can potentially affect the number of accounts receivable reported by the IRS. A prior audit report<sup>6</sup> noted that closing balance due accounts as CNC is a high-risk collection activity because the balance due from the taxpayers are then at risk of never being collected.

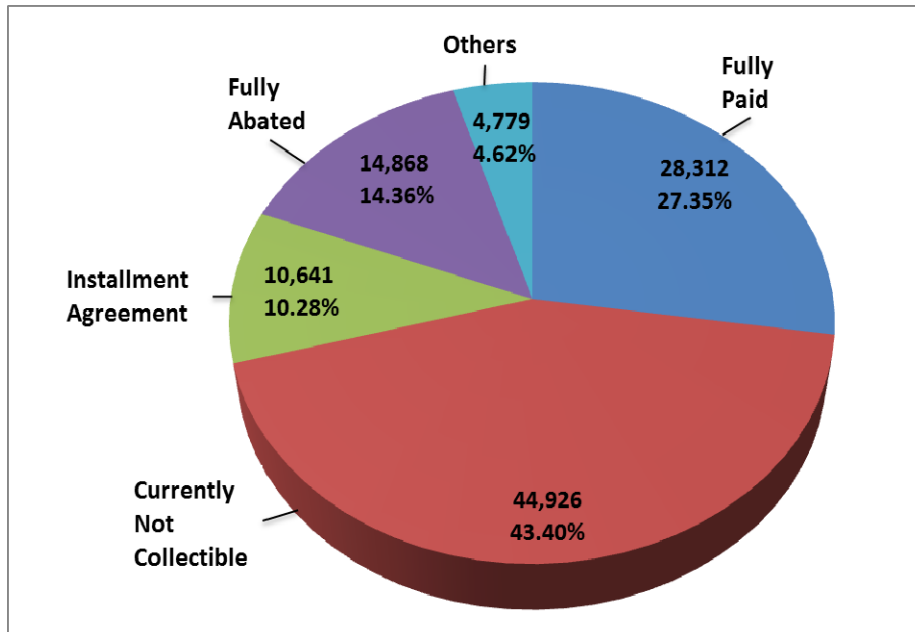
<sup>6</sup> Treasury Inspector General for Tax Administration, Ref. No. 2006-30-168, *Currently Not Collectible Decisions on Delinquent Accounts Were Appropriate; However, Closing Actions Need to Be Improved* (Sept. 2006).



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

Figure 4 shows that in FY 2011, 44,926 (43 percent) of the 103,526 balance due accounts originating from 6020(b) assessments were closed by ROs as CNC.

**Figure 4: Balance Due Accounts Closed by ROs in FY 2011 (by Disposition)**



Source: IRS Collection Activity Report 5000-242.

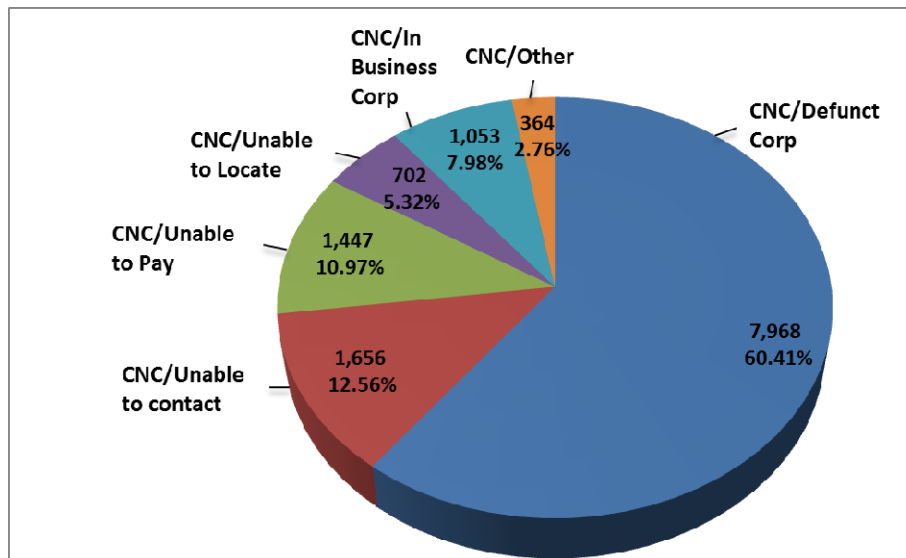
The IRS does not collect any revenue on taxpayer's accounts with liabilities originating from 6020(b) assessments that are fully abated. An additional 14,868 (14 percent) balance due accounts originating from 6020(b) assessments were fully abated. The combined figures of CNC and abated accounts indicate that the IRS did not collect any immediate payments for 59,794 (58 percent) closed balance due accounts originating from 6020(b) assessments. IRS management informed us that 6020(b) assessments may help encourage delinquent taxpayers to become filing compliant by submitting their own returns. IRS management also stated that many taxpayers may ignore the delinquency notices and then later, after the assessments have been processed, file their own return showing no tax liability. These assessments are likely to be fully abated. However, it is important to note that the full assessment amounts were included in the IRS's accounts receivable inventory.

Management also advised us that many CNC closures are likely to be defunct corporations. We analyzed a population of 6020(b) assessments made by ROs from April 1, 2010, to March 31, 2011, that were later worked by ROs when they became balance due accounts. Figure 5 shows that 7,968 (60 percent) of the 13,190 cases ROs closed as CNC were defunct corporations.



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

**Figure 5: RO's Balance Due Accounts Closed As CNC (by Disposition)**



Source: Our analysis of balance due accounts that originated as 6020(b) assessments and closed as CNC by ROs from April 1, 2010, to March 31, 2011.

IRS officials informed us that ROs may intentionally process some 6020(b) assessments on cases likely to be closed as CNC/Defunct Corporation when there is a good indication that the Trust Fund Recovery Penalty can be assessed and collected from the company's responsible officers.<sup>7</sup> Unless the return is filed and the tax is assessed, pursuit of this penalty is not possible.

### **Revenue Officers Followed Many of the Required Procedures for Processing 6020(b) Assessments**

The IRM<sup>8</sup> details the procedures that ROs use for processing 6020(b) assessments. There are specific tasks ROs must perform before and after deciding to use I.R.C. § 6020(b) authority to prepare and process the delinquent return for the taxpayer.

We reviewed a statistical sample of 96 closed taxpayer cases where ROs completed 6020(b) assessments from April 1, 2010, to March 31, 2011, to determine if proper procedures were being followed. Our analysis determined there were numerous instances in which ROs followed required procedures.

<sup>7</sup> We did not research subsequent Trust Fund Recovery Penalty assessment cases to determine outcomes during this review.

<sup>8</sup> IRM 5.1.11 (Nov. 29, 2011).



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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For example, ROs:

- Conducted investigations including field visits, when appropriate.
- Determined if taxpayers were still in business.
- Determined if taxpayers paid wages during the tax period(s) in question.
- Determined if taxpayers were liable for filing the return(s).
- Specified a date for taxpayers to submit their own return(s).

However, our review also determined that ROs did not always document the basis for 6020(b) assessments, as required, or allow taxpayers the required 30 calendar days to respond to proposed 6020(b) assessments.

***Evidence Was Not Always Available to Support the Basis of 6020(b) Assessments***

IRM procedures<sup>9</sup> require ROs to fully document a complete explanation for the basis of the 6020(b) assessment(s) in the ICS history. The explanation should include information such as wages paid, income tax withheld, tax deposits submitted, and calculations or other information used to establish the correct liability for each tax period. Form 5604, *Section 6020(b) Action Sheet*, is used to initiate and prepare 6020(b) returns. Procedures also state that a copy of the ICS history documentation that explains the basis for the assessment(s) should be attached to Form 5604. Attaching the ICS history to the form would eliminate the need to complete the Basis for Assessment section of Form 5604.

We reviewed a statistically valid sample of 96 taxpayer cases and identified 20 (21 percent) cases in which ROs did not document the basis of 6020(b) assessments as required. ROs did not properly follow 6020(b) procedures to fully document the ICS history or Form 5604 with a complete explanation for the basis of the assessment. IRS management informed us there is no specific review process for a 6020(b) assessment or an internal control to ensure ROs are following this procedure. If the steps taken to determine the basis of the assessment are not fully explained and documented, there is a greater risk of an improper assessment.

IRS management attempted to recreate the missing information in the 20 cases we identified. However, due to the lack of documentation, management was unable to recreate the basis of the assessments in 12 (60 percent) of the 20 cases. Management was able to identify the basis from other sources (such as Integrated Data Retrieval System research) for most of the assessments<sup>10</sup> on the remaining eight cases. However, IRS procedures state that fully documenting the basis is

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<sup>9</sup> IRM 5.1.11 (Nov. 29, 2011).

<sup>10</sup> Some of the 96 taxpayer cases in our sample had more than one assessment.



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## *Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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important because it could be used later if the taxpayer requests an appeal, files suit, or requests Taxpayer Advocate Service assistance. Also, if the assessment is not properly documented and completely explained as required, an employee would have to repeat steps originally completed by another employee if there is any reason to later determine the basis. This practice would result in a duplication of efforts by the IRS's limited resources.

Based on our sample results from a population of 14,746 taxpayer cases, we estimate there are 3,072 taxpayer cases in which ROs did not have proper documentation for the basis for the 6020(b) assessment. We are 95 percent confident that the range of improperly documented cases is between 1,872 and 4,272.

### ***Recommendation***

***Recommendation 1:*** The Director, Enterprise Collection Strategy, Small Business/Self-Employed Division, should develop an internal control to help ensure ROs properly document a complete explanation for the basis of the 6020(b) assessment.

***Management's Response:*** IRS management agreed with this recommendation and will initiate a change to the ICS to help ensure ROs document the required basis for the 6020(b) assessment.

### ***Revenue Officers Did Not Always Allow 30 Calendar Days for Taxpayers to Respond Prior to Processing 6020(b) Returns***

The Letter 1085, *30 Day Letter Proposed IRS 6020(b) Assessment*, package is sent to a taxpayer when all other efforts to secure a business return have failed. The package includes:

- A notice informing the taxpayer that there are tax periods he or she may be liable to file.
- Computer-generated returns with estimated wage and tax amounts.
- Taxpayer appeal rights.
- A return envelope.

ROs are required to mail either Letter 1085 or Letter 1616, *30 Day Letter, Proposed IRC 6020(b) Assessment Partnership Return*, along with all applicable enclosures, to the taxpayer. Procedures instruct IRS employees to keep a copy of the letter and tax returns in the case file. These letters inform the taxpayer that I.R.C. § 6020(b) gives the IRS authority to prepare and file tax returns on the taxpayer's behalf. They also advise that if the IRS does not hear from the taxpayer within 30 calendar days from the date of the letter, the IRS will process the enclosed tax returns that were prepared for the taxpayer.

ROs did not always follow 6020(b) procedures to allow taxpayers 30 calendar days to respond or did not include the necessary evidence in the case file or ICS history for us to determine whether





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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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taxpayers had been allowed the 30 calendar days. In our statistically valid sample of 96 taxpayer cases, we identified 10 (10 percent) cases in which ROs either did not allow 30 calendar days to pass before submitting the prepared return for processing or there was no evidence available to determine if taxpayers were allowed the 30 calendar days. In five of these cases, we confirmed that taxpayers were not provided the specified 30 calendar days to respond to proposed 6020(b) assessments before the prepared returns were submitted for processing. The remaining five cases did not contain evidence to determine whether 30 calendar days had expired before prepared returns were submitted for processing.

IRS management informed us that there is no specific review process for a 6020(b) assessment or an internal control to ensure ROs are following this procedure. However, if the IRS does not allow the taxpayer 30 calendar days to respond as indicated in Letters 1085 and 1616, the taxpayer's rights may be violated. For example, both letters state that within 30 calendar days from the date of the letter, if the taxpayer does not agree that the returns have been prepared correctly, they may request a conference discussion with the person whose name and number are given in the letter. If the taxpayer does not agree with any or all of the IRS findings presented, then they may request a meeting or telephone conference with the supervisor of the person who issued the findings. If the taxpayer still does not agree, they may appeal the case to the Area Director of General Appeals.

In addition, the taxpayer may be burdened by an additional requirement to contact the IRS about the situation. For example, if the taxpayer submitted a return prior to the expiration of the 30 calendar days and subsequently received a balance due notice as a result of the RO submitting an early 6020(b) return, the taxpayer will have to make an additional contact with the IRS. In addition, the IRS will have to expend additional resources to handle the contact and make the necessary account adjustments.

Based on our sample results, from a population of 14,746 taxpayer cases, we estimate there are approximately 1,536 taxpayers whose rights were potentially violated when ROs did not allow taxpayers 30 calendar days to respond or did not include the necessary evidence in the case file or ICS history to determine whether taxpayers had been allowed the 30 calendar days prior to processing 6020(b) returns. We are 95 percent confident that the range of errors is between 633 and 2,439.

## ***Recommendation***

**Recommendation 2:** The Director, Enterprise Collection Strategy, Small Business/Self-Employed Division, should develop an internal control to help ensure ROs allow taxpayers 30 calendar days to respond to the proposed assessment before submitting the prepared return(s) for processing.





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## *Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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***Management's Response:*** IRS management agreed with this recommendation and will initiate a change to the ICS to help ensure ROs allow taxpayers 30 calendar days to respond to the proposed assessment before submitting the prepared returns for processing.

### ***Many Taxpayers Remain Noncompliant After 6020(b) Assessments Have Been Made***

The Government Performance and Results Act of 1993<sup>11</sup> establishes that Federal Government agencies are expected to identify performance measures for program activities and compare results of activities with measures identified. Performance measures help managers by providing them information on how resources should be allocated to ensure effectiveness. They also help support development and justification of budget proposals by indicating how taxpayers and others benefit. Performance measures keep managers focused on the key goals of a program.

IRS management informed us that an important benefit of using I.R.C. § 6020(b) authority is to improve filing compliance among business nonfilers. The impact of using I.R.C. § 6020(b) authority to bring taxpayers into filing compliance is important for the IRS to know to help managers make strategic decisions about the best ways to address nonfiling taxpayers. However, management has not established a method for comparing 6020(b) business return results with anticipated benefits. Management also informed us there have been no special projects, research reports, or studies in the CFf to measure the impact 6020(b) assessments have had on taxpayer behavior in subsequent period filing compliance.

To determine if the CFf's use of I.R.C. § 6020(b) authority made an impact on subsequent filing compliance, we identified and compared subsequent delinquent return data on taxpayers with 6020(b) assessments to taxpayers without 6020(b) assessments in Calendar Year 2008. To avoid any bias from the impact of other enforcement actions that ROs typically use to bring taxpayers into compliance, such as liens and levies, we only analyzed those assessments that were stand-alone delinquent return investigations. According to IRS management, stand-alone delinquent return investigations are comprised of taxpayers that have potential delinquent returns due but no balance due accounts. In addition, management advised us that most taxpayer cases being worked in the CFf have combinations of both delinquent return investigations and balance due accounts.

Our review determined that during Calendar Year 2008, taxpayers with stand-alone 6020(b) assessments were less compliant in subsequent years than taxpayers without 6020(b) assessments. Figure 6 shows that 40 percent of taxpayers with 6020(b) assessments in Calendar Year 2008 were compliant in the eight quarters (or two years) following the tax period of the

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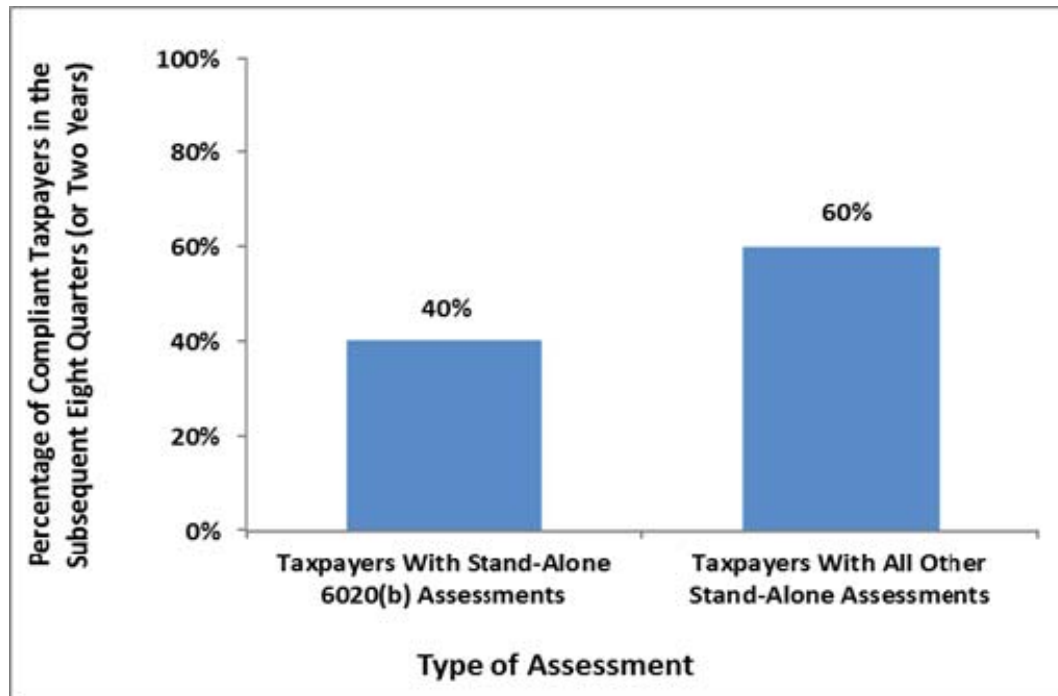
<sup>11</sup> Pub. L. No. 103-62, 107 Stat. 285 (codified as amended in scattered sections of 5 U.S.C., 31 U.S.C., and 39 U.S.C.).



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

6020(b) assessment. In comparison, 60 percent of taxpayers with assessments where I.R.C. § 6020(b) authority was not used were compliant.

**Figure 6: Subsequent Filing Compliance for Stand-Alone 6020(b) Assessments Compared With All Other Stand-Alone Assessments**



*Source: Our analysis of Calendar Year 2008 stand-alone delinquent return investigations and subsequent delinquencies.*

These results indicate the use of I.R.C. § 6020(b) authority to secure delinquent returns may not have influenced the taxpayers to remain compliant with filing subsequent returns. IRS management indicated that taxpayers with assessments where I.R.C. § 6020(b) authority was not used may be more compliant with filing subsequent returns because they were more responsive to IRS communications (RO field visits, correspondence, *etc.*) and voluntarily filed their own return in a shorter time period, prior to ROs using I.R.C. § 6020(b) authority on these taxpayers. However, to gain a better understanding of the data results, a more in-depth study may be needed. For example, a review of closed taxpayer delinquent investigations where the use of I.R.C. § 6020(b) authority was considered, but not used, may provide valuable information.

Furthermore, without performance measures or a method to help determine whether 6020(b) assessments are improving taxpayer filing compliance as expected, IRS management may be losing an opportunity to improve the program and achieve better results. Management does not know if the use of I.R.C. § 6020(b) authority is meeting anticipated benefits or is an effective tool.



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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***Recommendation***

***Recommendation 3:*** The Director, Enterprise Collection Strategy, Small Business/Self-Employed Division, should establish a methodology to compare actual results with management's anticipated benefit of improving filing compliance when I.R.C. § 6020(b) authority is used for business taxpayers.

***Management's Response:*** IRS management agreed with this recommendation and will request a research project to measure the effectiveness of the Collection Field function I.R.C. 6020(b) program on future filing compliance of business taxpayers and weigh the results against the ultimate case resolution to determine if any program changes are warranted.



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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## **Appendix I**

### *Detailed Objectives, Scope, and Methodology*

The overall objectives were to evaluate the impact of the Small Business/Self-Employed Division<sup>1</sup> Cff's use of I.R.C. § 6020(b) authority on taxpayer compliance and to determine whether Collection function employees are using the proper procedures to assess tax liabilities. To accomplish these objectives, we:

- I. Identified the Cff's policies and procedures and the management strategies and measures for using I.R.C. § 6020(b) authority for business taxpayers.
  - A. Researched and reviewed applicable IRM sections, internal guidance, management directives, and prior audit reports.
  - B. Discussed the 6020(b) process with Cff management from the Small Business/Self-Employed Division's Headquarters Office in New Carrollton, Maryland.
    1. Determined how management measures the performance of the program and evaluates the measures for reasonableness.
    2. Obtained management's feedback about any positive or negative issues affecting the program and possible suggestions for improvements.
  - C. Conducted a field visit to a Cff Area Office to talk with Territory and group managers and ROs about the 6020(b) process.
    1. Performed a walk-through of the procedures for using the 6020(b) process with ROs.
    2. Obtained any desk procedures and ROs' feedback about any positive or negative issues affecting the program and possible suggestions for improvements.
- II. Evaluated the impact that 6020(b) assessments had on subsequent year filing compliance in the Cff.
  - A. Determined the extent to which 6020(b) assessments promoted taxpayer filing compliance in subsequent tax periods.
    1. Obtained from the Treasury Inspector General for Tax Administration Data Center Warehouse an extract of 6020(b) assessments made by ROs in Calendar Year 2008 that were stand-alone Taxpayer Delinquency Investigation modules

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<sup>1</sup> See Appendix V for a glossary of terms.



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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and identified those taxpayers that had subsequent Taxpayer Delinquency Investigation modules over the next eight quarters (two years). We validated the data by verifying various data fields with the Integrated Data Retrieval System.

2. Analyzed the data to determine subsequent filing compliance trends.
- B. Discussed analysis results and conclusions with IRS management to obtain concurrence.
- III. Analyzed the Cff assessment, abatement, and collection trends on cases for which the source of the assessment was I.R.C. § 6020(b) authority and determined if and how the information was being reported and used to measure the program.
  - A. Identified data trends from the IRS Collection Activity Reports for FYs 2007 through 2011.
  - B. Determined the potential impact of the 6020(b) data trends on accounts receivables.
  - C. Discussed conclusions with IRS management.
- IV. Determined if ROs are following proper procedures on cases selected for 6020(b) processing.
  - A. Performed case reviews to determine if ROs are following the proper procedures and guidelines to prepare 6020(b) assessments on business nonfilers.
    1. Through the Treasury Inspector General for Tax Administration Data Center Warehouse, obtained a population of 14,746 closed taxpayer cases, of 6020(b) assessments made by ROs between April 1, 2010, and March 31, 2011. We validated the data by verifying various data fields with the Integrated Data Retrieval System.
    2. Reviewed a statistically valid random sample of 96 taxpayer cases from the population identified in Step 1. We requested from the IRS and the Federal Records Center 200 cases to ensure we were provided enough cases. Cases were reviewed in the order in which they were received from the IRS and the Federal Records Center. While we planned to review a random sample of 100 taxpayer cases, we later eliminated four cases because they did not meet the sample criteria.
    3. Reviewed cases and searched documentation to determine if ROs are following all proper procedures including:
      - a. Conducting required field calls to determine if the taxpayer is still in business, insolvent, or deceased.



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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- b. Establishing a specific date with the taxpayer to have all delinquent returns submitted.
  - c. Allowing 30 calendar days after the issuance of a Letter 1085, *30 Day Letter Proposed IRS 6020(b) Assessment*, or Letter 1616, *30 Day Letter, Proposed IRC 6020(b) Assessment Partnership Return*, before assessing the taxpayer's account.
  - d. Using all available data sources and third-party information when calculating and documenting 6020(b) assessments, including taxpayer records, State wage information, information return data to help determine wages paid to employees, income and Federal Insurance Contribution Act tax withheld, and inflation factors if appropriate.
4. Reviewed cases to identify any indications of fraud and the risk of fraud.
- B. Discussed case review exceptions with IRS management for concurrence.
- C. Projected the number of errors in each finding to the entire population based on the actual error rate, actual precision, and a 95 percent confidence level.
1. Based on our sample results, we used the population of 14,746 taxpayer cases, an actual error rate of 20.83 percent, a precision of 8.14 percent, and a confidence level of 95 percent for the projection of cases for which ROs did not have the proper documentation for the basis for the 6020(b) assessment.
  2. Based on our sample results, we used the population of 14,746 taxpayer cases, an actual error rate of 10.42 percent, a precision of 6.12 percent, and a confidence level of 95 percent for the projection of cases for which ROs failed to allow the taxpayer 30 calendar days to respond to proposed 6020(b) assessments or for which no evidence was available in the case file or ICS history for us (or the IRS) to determine whether the taxpayer had been allowed the 30 calendar days.

**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 objectives: IRS policies, procedures, and practices for ensuring that ROs in the Cff are following proper procedures on cases selected for 6020(b) processing as well as for measuring the overall performance of the program. We evaluated these controls by reviewing source materials, interviewing management, reviewing delinquent return case files, and researching taxpayer accounts.



*Collection Field Function Procedures Were Not  
Always Followed When Assessing Taxes on  
Businesses That Have Not Filed Tax Returns*

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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, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations)  
Carl L. Aley, Director  
Phyllis Heald London, Audit Manager  
Julian E. O'Neal, Lead Auditor  
Janis Zuika, Senior Auditor  
Matthew J. Schimmel, Senior Audit Evaluator  
Rebecca A. Arendosh, Auditor  
Joseph L. Katz, Ph.D., Contractor, Statistical Sampling Consultant



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*Collection Field Function Procedures Were Not  
Always Followed When Assessing Taxes on  
Businesses That Have Not Filed Tax Returns*

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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, Small Business/Self-Employed Division SE:S  
Director, Communications, Liaison, and Disclosure, Small Business/Self-Employed Division  
SE:S:CLD  
Director, Enterprise Collection Strategy, Small Business/Self-Employed Division SE:S:ESC  
Director, Field Collection, Small Business/Self-Employed Division SE:S:FC  
Director, Collection Policy, Small Business/Self-Employed Division SE:S:ESC:CP  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Office of Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis RAS:O  
Office of Internal Control OS:CFO:CPIC:IC  
Audit Liaison: Commissioner, Small Business/Self-Employed Division SE:S





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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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## Appendix IV

### *Outcome Measure*

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. This benefit will be incorporated into our Semiannual Report to Congress.

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

- Taxpayer Rights and Entitlements – Potential; 1,536 taxpayers for whom ROs failed to allow 30 calendar days to respond to proposed 6020(b) assessments (or no evidence was available in the case file or ICS history to determine whether the taxpayer had been allowed the 30 calendar days), resulting in a potential violation of taxpayers' rights (see page 10).

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

In our review of a statistically valid sample of 96 taxpayer cases for which ROs completed 6020(b) assessments during the period April 1, 2010, to March 31, 2011, we identified 10 (10 percent) taxpayer cases for which the RO did not allow 30 calendar days to expire prior to submitting the prepared return for processing or there was no evidence available to determine if the taxpayers were actually allowed the 30 calendar days. We initially oversampled by selecting a random sample of 200 cases to ensure we would receive enough case files from the IRS. Cases were reviewed in the order in which they were received from the IRS.

We projected the finding to the total population of 14,746 taxpayer cases with 6020(b) assessments between April 1, 2010, and March 31, 2011. Based on the actual error rate of 10.42 percent, actual precision of 6.12 percent, and a 95 percent confidence level, we estimate there are approximately 1,536 taxpayer cases for which ROs failed to allow 30 calendar days for taxpayers to respond or evidence was not available in the case file or ICS history to determine whether taxpayers had been allowed the 30 calendar days as required by Letter 1085, *30 Day Letter Proposed IRS 6020(b) Assessment*. We are 95 percent confident that the range of errors is between 633 and 2,439.



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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## Appendix V

### *Glossary of Terms*

**Abatement** – A reduction in value or amount. The IRS may make an abatement of certain taxes, interest, penalties, fees, or additions to tax, and a taxpayer may request this using Form 843, *Claim for Refund and Request for Abatement*.

**Appeal** – A way for a taxpayer to resolve tax controversies, without litigation, on a basis which is fair and impartial to both the Government and the taxpayer.

**Assessment** – A determination by the IRS that an amount of tax (including penalty, interest, *etc.*) is owed by the taxpayer.

**Automated 6020(b) Program** – The Automated 6020(b) Program is a business nonfiler program that handles employment tax returns with proposed tax liabilities between \$250 and \$1,500.

**Automated Collection System** – 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.

**Calendar Year** – The 12-consecutive-month period ending on December 31.

**Campus Compliance Services** – The organization that manages and implements strategies pertaining to the Collection and Examination programs for the IRS.

**Collection Field function** – The function in the Area Offices consisting of ROs who handle personal contacts with taxpayers to collect delinquent accounts or secure unfiled returns.

**Currently Not Collectible** – If, after taking all steps in the collection process, it is determined that an account receivable is CNC, it should be so reported in order to remove it from active inventory.

**Data Center Warehouse** – A centralized storage and administration of files that provides data and data access services of IRS data.

**Defunct Corporation** – The IRS defines a corporation as defunct when it is no longer in operation and all assets have been dispersed, or when it has been dissolved under State receivership proceedings or other State dissolution proceedings, or when it is a limited partnership where the partnership agreement limits the liability of the limited partners under local law and the trust fund recovery penalty is considered.

**Delinquent Return** – A tax return that a taxpayer does not file with the IRS by the due date (including extensions) for any year in which a filing requirement exists.



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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**Employment Tax Returns** – Various Form 940 return series (primarily Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, and Form 941, *Employer's QUARTERLY Federal Tax Return*) filed by businesses to report things such as employer's Federal unemployment taxes and Federal taxes withheld.

**Excise Tax Return** – Form 720, *Quarterly Federal Excise Tax Return*, is used to report and pay certain taxes, such as those on transportation and fuel.

**Federal Insurance Contribution Act Taxes** – Taxes on earned income paid into Social Security and Medicare.

**Installment Agreement** – An agreement between the IRS and a taxpayer for the taxpayer to make monthly payments to the IRS when the taxpayer is unable to fully pay his or her tax debt in one payment.

**Integrated Collection System** – An information management system designed to improve revenue collections by providing ROs access to the most current taxpayer information, while in the field, using laptop computers for quicker case resolution and improved customer service.

**Integrated Data Retrieval System** – An IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.

**Internal Revenue Manual** – Contains the policies, procedures, instructions, guidelines, and delegations of authority which direct the operation and administration of the IRS.

**Inventory Delivery System** – An application that uses specific criteria and established business rules to select and route balance due accounts to either the Automated Collection System, the Queue, or to the CFf for further action

**Levy** – A legal seizure of property to satisfy a tax debt. The IRS may collect outstanding taxes from sources such as bank accounts and wages, as well as other sources.

**Lien** – An encumbrance on property or rights to property as security for outstanding taxes.

**Master File** – The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

**Module** – Part of a taxpayer's account that reflects tax data for one tax class, *e.g.*, individual or business, and one tax period. For example, a taxpayer filed 12 Forms 941 and three Forms 940 within a three-year period. The taxpayer has only one account on the Master File but 15 modules.

**Nonfilers** – Individual and business taxpayers that have been identified as liable to file a tax return but have not filed a tax return by the return due date or extended due date.

**Offer in Compromise** – An agreement between a taxpayer and the Government that settles a tax liability for payment of less than the full amount owed.



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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**Partnership Tax Return** – Form 1065, *U.S. Return of Partnership Income*, is used to report the income and expenses of domestic partnerships and the share distributed to each partner.

**Queue** – An automated holding file for unassigned inventory of delinquent cases for which the Collection function does not have enough resources to immediately assign for contact.

**Revenue Agent** – Employees in the Examination function who conduct face-to-face examinations of more complex tax returns such as businesses, partnerships, corporations, and specialty taxes, *e.g.*, excise tax returns.

**Revenue Officer** – Employees in the Cff who attempt to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses or the Automated Collection System.

**Small Business/Self-Employed Division** – The IRS organization that services self-employed taxpayers and small businesses by educating and informing them of their tax obligations, developing educational products and services, and helping them understand and comply with applicable tax laws.

**Tax Period** – The period of time for which a return is filed. The IRS uses a six-digit code to indicate the end of the tax period for a given return. The first four digits represent the year and the next two digits represent the month.

**Taxpayer Advocate Service** – An independent organization within the IRS whose employees assist taxpayers that are experiencing economic harm, are seeking help in resolving tax problems that have not been resolved through normal channels, or believe that an IRS system or procedure is not working as it should.

**Taxpayer Delinquency Investigation** – An unfiled tax return for a taxpayer. One Taxpayer Delinquency Investigation exists for all tax periods.

**Taxpayer Delinquent Account** – A balance due account of a taxpayer. A separate Taxpayer Delinquent Account exists for each tax period.

**Trust Fund Recovery Penalty** – Assessments made against responsible business officers of a company that has not paid the taxes it withholds from employees' wages, such as Social Security or individual income tax withholding to the IRS.



*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

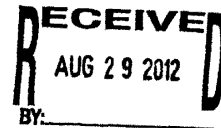
**Appendix VI**

*Management's Response to the Draft Report*



COMMISSIONER  
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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



AUG 29 2012

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

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

SUBJECT: Draft Audit Report – Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns (Audit # 201130017)

Thank you for the opportunity to review your draft report titled: "Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns." We agree with the findings of the report and the recommendations.

Internal Revenue Code Section 6020(b) processing is an important tool used by revenue officers when working cases involving business taxpayers who are liable to file but refuse to do so. We appreciate your acknowledgement that revenue officers followed many of the procedures required by the Internal Revenue Manual when processing Section 6020(b) assessments. We are looking into changes to the Integrated Collection System used by revenue officers to improve processing. In addition, we are preparing a Continuing Professional Education refresher course on Section 6020(b) procedures and are consulting with SB/SE Research on a project to look at the effect of Section 6020(b) processing on future taxpayer compliance.

We also concur with the potential outcome measure included in the report.

Attached is a detailed response outlining our corrective actions to address your recommendations.

If you have any questions, please contact me, or a member of your staff may contact Lois Burns, acting Director, Enterprise Collection Planning and Governance, at (502) 558-4616.

Attachment



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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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Attachment

**RECOMMENDATION 1:**

The Director, Enterprise Collection Strategy, Small Business/Self-Employed Division, should develop an internal control to help ensure ROs properly document a complete explanation for the basis of the 6020(b) assessment.

**CORRECTIVE ACTION:**

We will initiate a change to ICS to help ensure revenue officers document the required basis for the 6020(b) assessment.

**IMPLEMENTATION DATE:**

February 15, 2014

**RESPONSIBLE OFFICIAL:**

Acting Director, Enterprise Collection Planning and Governance, Small Business/Self-Employed Division

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 2:**

The Director, Enterprise Collection Strategy, Small Business/ Self-Employed Division, should develop an internal control to help ensure ROs allow taxpayers 30 calendar days to respond to the proposed assessment before submitting the prepared return(s) for processing.

**CORRECTIVE ACTION:**

We will initiate a change to ICS to help ensure revenue officers allow taxpayers 30 days to respond to the proposed assessment before submitting the prepared returns for processing.

**IMPLEMENTATION DATE:**

February 15, 2014

**RESPONSIBLE OFFICIAL(S):**

Acting Director, Enterprise Collection Planning and Governance, Small Business/Self-Employed Division

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.





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*Collection Field Function Procedures Were Not Always Followed When Assessing Taxes on Businesses That Have Not Filed Tax Returns*

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**RECOMMENDATION 3:**

The Director, Enterprise Collection Strategy, Small Business/ Self-Employed Division, should establish a methodology to compare actual results with management's anticipated benefit of improving filing compliance when I.R.C. § 6020(b) authority is used for business taxpayers.

**CORRECTIVE ACTION:**

We will request a research project to measure the effectiveness of the Field Collection IRC 6020(b) program on future filing compliance of business taxpayers and weigh the results against the ultimate case resolution to determine if any program changes are warranted.

**IMPLEMENTATION DATE:**

January 15, 2014

**RESPONSIBLE OFFICIAL(S):**

Acting Director, Enterprise Collection Planning and Governance, Small Business/Self-Employed Division

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.