



*Additional Documentation Is  
Needed to Support Office of Appeals  
Penalty Abatement Decisions*

**July 30, 2015**

**Reference Number: 2015-10-059**

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

2 = Risk Circumvention of Agency Regulation or Statute

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## HIGHLIGHTS

### **ADDITIONAL DOCUMENTATION IS NEEDED TO SUPPORT OFFICE OF APPEALS PENALTY ABATEMENT DECISIONS**

## Highlights

**Final Report issued on July 30, 2015**

Highlights of Reference Number: 2015-10-059 to the Internal Revenue Service Chief of Appeals.

### **IMPACT ON TAXPAYERS**

The Office of Appeals (Appeals) is an independent function within the IRS whose mission is to resolve disputes on a fair and impartial basis without litigation. Appeals has the authority to abate certain taxpayer penalties when the abatement has been denied by other functions within the IRS. In Fiscal Year 2013, Appeals abated approximately \$127 million in penalties. It is important that Appeals personnel apply a consistent methodology when deciding whether or not to abate penalties to promote fair and impartial resolutions to taxpayers.

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

This audit was initiated to evaluate whether penalties assessed against taxpayers were fully or partially abated in accordance with Appeals criteria.

### **WHAT TIGTA FOUND**

TIGTA found that in most cases Appeals properly accepted cases in which the IRS operating divisions had previously denied the taxpayer's request for abatement and sufficiently documented the reasons for penalty abatements in case files. However, TIGTA found that 59 of 140 sampled penalty appeal cases were not abated in accordance with Appeals criteria because operating divisions had not denied the abatement or because case files did not support the abatement. Based on these results, TIGTA estimates that in Fiscal Year 2013, 1,411 penalty appeal cases and more than \$39 million in penalty abatements did not comply with Appeals criteria.

For 57 cases, TIGTA could not determine the justification Appeals personnel used to abate the penalties. For example, Appeals used its authority to abate penalties based on the hazards of litigation, which reflects the uncertainty of the court's decision if the taxpayer were to take his or her case to trial. However, for some cases, Appeals did not document how it arrived at its determination by outlining the hazards of litigation.

TIGTA also identified a small number of other processing errors and control weaknesses affecting taxpayer accounts. For example, Appeals managerial case review policy does not specify that high-dollar abatements by Appeals Officers and Settlement Officers must be reviewed by a manager. Specifically, in four cases, Appeals Officers abated a total of more than \$580,000 in penalties without managerial approval. Appeals Officers did not violate IRS policy because they have been delegated the authority to abate unlimited penalty amounts without managerial approval.

### **WHAT TIGTA RECOMMENDED**

TIGTA recommended that the Chief, Appeals, provide training to Appeals personnel on the requirements instructing them to clearly document the reasons for abatement decisions and review the delegated settlement authority of Appeals Officers to determine whether changes are needed to address the risk of allowing unlimited abatements without managerial approval.

The IRS agreed with the recommendations. The IRS plans to provide additional training to Appeals Technical Employees who work penalty abatement cases and to review the existing delegated settlement authority and evaluate any risk associated with the current delegation.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

July 30, 2015

**MEMORANDUM FOR CHIEF, APPEALS**

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

**SUBJECT:** Final Audit Report – Additional Documentation Is Needed to Support  
Office of Appeals Penalty Abatement Decisions (Audit # 201410018)

This report presents the results of our review to evaluate whether penalties assessed against taxpayers were fully or partially abated in accordance with Office of Appeals criteria. This audit is included in our Fiscal Year 2015 Annual Audit Plan and addresses the major management challenge of Providing Quality Taxpayer Service Operations.

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

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. If you have any questions, please contact me or Gregory D. Kutz, Assistant Inspector General for Audit (Management Services and Exempt Organizations).



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Office of Appeals Penalty Abatement Decisions*

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*Additional Documentation Is Needed to Support  
Office of Appeals Penalty Abatement Decisions*

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*Abbreviations*

FY	Fiscal Year
IRM	Internal Revenue Manual
IRS	Internal Revenue Service



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Office of Appeals Penalty Abatement Decisions*

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## *Background*

The Office of Appeals (hereafter referred to as Appeals) is an independent function within the Internal Revenue Service (IRS) whose mission is to settle tax disputes on a fair and impartial basis without litigation. As part of its mission, Appeals reviews cases in which the taxpayer is requesting an abatement of certain penalties that have already been assessed to the taxpayer's account. This type of case is what makes up the penalty appeal case work stream. Specifically, the types of penalties under the penalty appeal designation, although not inclusive, are:

- Bad Check.
- Daily Delinquency Penalty.
- Deposit Penalty.
- Estimated Tax Penalty.
- Failure to File.
- Failure to File Using Electronic Media.
- Failure to Pay.
- Information Return Penalties.
- Return Related Penalties.

According to the IRS, penalties exist to encourage compliance with the Internal Revenue Code. For most taxpayers, compliance consists of preparing an accurate return, filing it timely, and paying any tax due. Efforts made to fulfill these obligations constitute compliant behavior. Most penalties apply to behavior that fails to meet any or all of these obligations. Penalties help to encourage voluntary compliance by:

- Defining standards of compliant behavior.
- Defining consequences for noncompliance.
- Providing monetary sanctions against taxpayers who do not meet the standard.

IRS customer service and compliance personnel located in other operating divisions and functions have the authority to abate certain types of penalties under certain circumstances:

- **Statutory Exception** – In certain cases, tax legislation may provide relief for the penalty. For example, taxpayers in a Presidentially declared combat zone or disaster area may receive relief from certain penalties.



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- **Administrative Waiver**<sup>1</sup> – An administrative waiver may be necessary when there is a delay by the IRS in printing or mailing forms, publishing guidance, or other conditions. Another aspect of the administrative waiver is the first-time abate policy, in which Failure to File, Failure to Pay, and Failure to Deposit penalties can be abated when certain conditions exist.
- **Correction of Service Error** – A service error can be any error made by the IRS in computing or assessing tax, crediting accounts, *etc.* For example, a computer programming application could have caused a penalty to be assessed in error.
- **Reasonable Cause** – A reasonable cause abatement is generally granted when the taxpayer exercised ordinary business care and prudence in determining his or her tax obligations but nevertheless failed to comply with those obligations. Reasonable cause **does not exist** if, after the facts and circumstances that explain the taxpayer's noncompliant behavior cease to exist, the taxpayer fails to comply with the tax obligation within a reasonable period of time.

In addition to the authorities to abate penalties available to IRS compliance personnel, Appeals can also consider hazards of litigation.<sup>2</sup> Appeals is the only administrative function in the IRS with authority to consider settlements of tax controversies, and the proper use of this settlement authority is critical to Appeals in fulfilling its mission of resolving disputes without litigation.

When operating division personnel either fully or partially deny a taxpayer's request for penalty abatement, they are required to give the taxpayer written notification of his or her appeal rights. If the taxpayer chooses to appeal the full or partial denial of the penalty, he or she sends the appeal to the office that denied the request. The taxpayer's request is then sent to Appeals for consideration.

Appeals criteria include two key elements when processing penalty appeal cases. Internal Revenue Manual (IRM) 20.1.1.3.5.1(4) requires that a taxpayer's request for a penalty abatement must have been previously considered and denied by an IRS operating division before Appeals can accept the case. After acceptance, Appeals can abate penalties based on the previously mentioned authorities. IRM 8.11.4.1.7(3) requires that Appeals personnel working penalty appeal cases prepare an Appeals Case Memo that should outline the facts and circumstances supporting the sustention or abatement of the penalty. These two key elements establish that Appeals had the authority to review the case and establish the justification for Appeals' decision to abate or sustain the penalty.

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<sup>1</sup> The IRS may formally interpret or clarify a provision to provide administrative relief from a penalty that would otherwise be assessed. An administrative waiver may be addressed in either a policy statement, news release, or other formal communication stating that the policy of the IRS is to provide relief from a penalty under specific conditions.

<sup>2</sup> Hazards of litigation are the uncertainties of the outcome of the court's decision in the event of a trial.



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If the taxpayer disagrees with Appeals’ decision, he or she must first pay the tax and penalty and then file a Form 843, *Claim for Refund and Request for Abatement*. If the IRS denies the taxpayer’s claim, he or she has the right to petition the U.S. District Court or the U.S. Court of Federal Claims. Taxpayers do not have the right to petition the U.S. Tax Court on penalty appeal cases.

In September 2004, Appeals centralized the processing of most penalty appeal cases in its Ogden Campus<sup>3</sup> Appeals office. While the Ogden Campus works the majority of penalty appeal cases, it sometimes transfers cases to Appeals Officers in the field, such as when the taxpayer requests a face-to-face conference or if the issue involves an international penalty.

When Appeals works a taxpayer’s appeal of a denied request for abatement of penalties, there are three possible resolutions: 1) sustained,<sup>4</sup> 2) abated,<sup>5</sup> or 3) partially abated.<sup>6</sup> Figure 1 shows penalty appeal case closure results for Fiscal Years<sup>7</sup> (FY) 2010 through 2013.

**Figure 1:** \*\*\*\*\*2\*\*\*\*\*

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This review was performed with information obtained from the Office of Appeals located in Washington, D.C.; Pittsburgh, Pennsylvania; and Ogden, Utah, during the period July 2014 through March 2015. 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.

<sup>3</sup> The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

<sup>4</sup> Sustained means none of the penalties are removed.

<sup>5</sup> Abated means the penalties are fully removed.

<sup>6</sup> Partially abated means only a part of the penalties are removed.

<sup>7</sup> Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government’s fiscal year begins on October 1 and ends on September 30.





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Office of Appeals Penalty Abatement Decisions*

*Results of Review*

***A Majority of Penalty Abatement Decisions Were Made in Accordance With Appeals Criteria, but Some Cases Lacked Support Justifying Abatements***

We found that for the majority of cases sampled, Appeals accepted cases and supported abatement decisions according to its criteria. Specifically, Appeals accepted cases and supported its decisions in 81 of the 140 sampled cases. However, in 59 cases,<sup>8</sup> abatements did not follow Appeals criteria because the cases had not been denied by operating division personnel or because Appeals case files did not support its decision to abate penalties. Based on our sample projection, we estimate that 1,411<sup>9</sup> penalty appeal cases and more than \$39,000,000<sup>10</sup> in penalty abatements did not comply with Appeals criteria.

***The majority of penalty appeal cases had been appropriately referred by IRS operating divisions and accepted by Appeals***

IRM 20.1.1.3.5.1(4) requires that the taxpayer's request for a penalty abatement must have been previously considered and denied by an IRS operating division before being accepted by Appeals. We found that the majority of sampled cases (135 of 140) were accepted appropriately by Appeals because an IRS operating division had previously denied the taxpayer's request to abate the penalties. In the remaining five cases, the operating division had not issued a denial letter for all tax periods on the case. Based on our sample findings, it appears that the penalty appeal case acceptance criteria is being properly applied by Appeals in most instances.

***Case files did not always support the decision to abate penalties***

We determined that 57 of the 140 penalty appeal case files sampled did not support Appeals' decisions to abate the penalties as required by Appeals criteria.<sup>11</sup> Based on our sample

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<sup>8</sup> \*\*\*\*\*1 \*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\* , 54 cases did not meet abatement justification criteria because Appeals Case Memos did not support its decision to abate some or all penalties, and three cases involved both acceptance and support criteria problems.

<sup>9</sup> The estimate is based on 140 stratified randomly selected cases closed in FY 2013 with a 45.07 percent point estimate error rate, ± 9.66 percent precision rate, and a 95 percent confidence level.

<sup>10</sup> The point estimate projection is based on a two-sided 95 percent confidence interval. We are 95 percent confident that the point estimate is between \$28,999,422 and \$49,741,723

<sup>11</sup> Appeals agreed with our determination in 54 of the 57 penalty appeal cases with support issues.



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projection, we estimate that 1,403<sup>12</sup> penalty appeal cases and more than \$34,000,000<sup>13</sup> in penalty abatements were not fully supported. As previously stated, IRM 8.11.4.1.7(3) requires that Appeals personnel working penalty appeal cases prepare an Appeals Case Memo that should outline the facts and circumstances supporting the sustention or abatement of the penalty. The 57 errors included cases in which Appeals did not clearly identify the hazards of litigation associated with the abatement, cases in which Appeals misinterpreted IRS guidance, and cases in which Appeals did not adequately document the reason for accepting verbal and written testimony to justify the abatement. During our discussions with Appeals management, they explained that the lack of documentation in the case files could be attributable to inattention to details when using existing guidance. In addition, we found that, while IRS guidance did instruct Appeals personnel to outline the facts and circumstances supporting a decision, more specific documentation requirements would help to ensure that a clear record is maintained of the evidence used to justify the abatement or sustention of a penalty. Without clear and sufficient evidence in a case file justifying an Appeals decision to abate a penalty, the IRS cannot verify that abatements are being made in accordance with applicable IRS guidance.

**Hazards of litigation support**

In a number of cases, Appeals personnel abated penalties based on the hazards of litigation; however, the case files did not always clearly identify the hazards or explain the decision to abate a certain percentage of penalties. \*\*\*\*\*1\*\*\*\*\*

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<sup>12</sup> The estimate is based on 140 stratified randomly selected cases closed in FY 2013 with a 44.80 percent point estimate error rate, ± 9.65 percent precision rate, and a 95 percent confidence level. See Appendix IV for more information. The point estimate projection is based on a two-sided 95 percent confidence interval. We are 95 percent confident that the point estimate is between 1,100 and 1,705.

<sup>13</sup> The point estimate projection is based on a two-sided 95 percent confidence interval. We are 95 percent confident that the point estimate is between \$25,605,102 and \$42,795,716.



## *Additional Documentation Is Needed to Support Office of Appeals Penalty Abatement Decisions*

### **Misinterpretation of IRS guidance**

Appeals also abated some penalties because it misinterpreted the applicable IRS guidance.

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### **Inadequate documentation when accepting verbal and written testimony**

There were also several cases in which Appeals personnel abated penalties, but the case files did not adequately document or support the acceptance of verbal testimony or letters from taxpayers or the taxpayer’s representative to abate penalties. \*\*\*\*\*1\*\*\*\*\*

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### **Recommendation**

The Chief, Appeals, should:

**Recommendation 1:** Provide training to Appeals personnel on the requirements instructing them to clearly document the reasons for abatement decisions, including justification for partial abatement percentages and specific hazards of litigation associated with an abatement case.



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**Management's Response:** Appeals management agreed with this recommendation. They stated that they have already taken steps in this area and will provide additional training to Appeals Technical Employees who work penalty abatement cases. However, Appeals management believes that the outcome measure is overstated and incorrectly assumes that all penalty abatement determinations lacking proper documentation should be rejected.

**Office of Audit Comment:** We maintain that our outcome measure is reasonable. The projected outcome measure discloses the potential revenue protection estimate based on a lack of adequate support for abated penalties. If adequate support was provided by Appeals, some of the abated penalties may be justifiable. However, adequate support was not included in the case files. Based on the information in the case files, the abatement of penalties were not supported, and Appeals management has no assurance the abatements were appropriate.

***Sampled Cases Had a Small Number of Other Processing Errors and Inconsistencies***

While most sample cases were processed according to Appeals policy, we identified errors and inconsistencies in our sampled cases. Specifically, we found \*\*\*\*\*1\*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\*and three instances in which adjustments to taxpayer accounts were not accurate. We also identified inconsistencies in managerial review in four cases.

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**Some adjustments to taxpayer accounts were not correct**

In three cases in our sample, adjustments proposed by Appeals were incorrectly input on the Integrated Data Retrieval System.<sup>14</sup> \*\*\*\*\*1\*\*\*\*\*  
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**Case files were not consistently reviewed by managers**

In our statistical sample of 140 cases, 70 involved the appeal of penalties in excess of \$25,000. In four of those 70 cases, Appeals Officers abated more than \$25,000 per case, and a management official did not sign as reviewing and approving the case actions.<sup>15</sup> The remaining 66 cases showed evidence of managerial review. The IRM allows Appeals Tax Specialists to abate penalty cases of less than \$25,000 without managerial review but requires managerial approval of cases involving penalties over \$25,000.<sup>16</sup> However, a separate delegation order states that other Appeals staff, Appeals Officers and Settlement Officers, are not required to obtain managerial approval on penalty abatements regardless of the penalty amount considered and abated. With this policy, there is a significant control weakness in that there is no limit to the amount that can be abated by Appeals Officers and Settlement Officers without any review.

When we questioned Appeals management about the policy, they explained that the delegation authority was established in 1992 and may have been a result of staffing levels at the time and also may have been implemented to reduce the burden on management to review cases. In the four cases identified, Appeals Officers abated more than \$580,000 in total without managerial approval. Appeals Officers did not violate IRS policy since they were not required to obtain managerial approval to abate the penalties. However, this policy creates a high level of risk for improper abatements of substantial dollar amounts.

<sup>14</sup> IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.

<sup>15</sup> Form 5402-c, *Appeals Transmittal and Case Memo*.

<sup>16</sup> Appeals Tax Specialists are campus employees who work campus-generated penalty appeal cases.



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***Recommendations***

The Chief, Appeals, should:

**Recommendation 2:** \*\*\*\*\*1\*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\*  
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**Management's Response:** \*\*\*\*\*1\*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\*.

**Recommendation 3:** Review the delegated settlement authority to Appeals Officers and Settlement Officers to address the risk associated with allowing unlimited abatements without managerial review for some Appeals staff.

**Management's Response:** Appeals management agreed with this recommendation and stated that they would review the existing delegated settlement authority and evaluate any risk associated with the current delegation.



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*Additional Documentation Is Needed to Support  
Office of Appeals Penalty Abatement Decisions*

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## **Appendix I**

### *Detailed Objective, Scope, and Methodology*

The overall objective of this review was to evaluate whether penalties assessed against taxpayers were fully or partially abated in accordance with Appeals criteria. To accomplish this objective, we:

- I. Determined what guidance has been provided to Appeals employees regarding the processing of penalty cases.
- II. Determined if the processing of penalty appeal cases was effective. Specifically, we selected a sample of penalty appeal cases closed in FY<sup>1</sup> 2013 and determined whether Appeals' acceptance of the case was appropriate and whether case files supported the decision to abate the penalties.
  - A. In order to project to the population, we selected a statistical random, stratified, variable sample of 140 penalty appeal cases closed with abatements greater than or equal to \$2,500 in FY 2013 from a population of 3,131 (we selected 90 cases with abatements greater than or equal to \$2,500 and less than \$100,000; another 38 cases with abatements greater than or equal to \$100,000 and less than \$1,000,000; and all 12 cases with abatements greater than \$1,000,000). A contracted statistician assisted with developing and reviewing our sampling plan and projections.
  - B. We queried the Appeals Centralized Database System to secure the 11,061 penalty appeal cases closed in FY 2013 and validated the reliability of the data by comparing the field descriptions to source data to ensure that the data matched, reviewed the appropriateness of data within fields, and compared population totals to information obtained from Appeals reports and management. We found the data to be sufficiently reliable for our purposes. For each sampled case, we:
    1. Determined if the taxpayer's case should have been accepted by Appeals by determining whether an IRS operating division had previously denied the request.
    2. Determined if the abatement action taken by Appeals was adequately documented and supported in the case files.
    3. Determined if abatements greater than \$25,000 were approved by management.

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<sup>1</sup> Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.



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4. Determined if the penalty adjustments were properly posted to taxpayer accounts on the Integrated Data Retrieval System.<sup>2</sup>
  5. Determined if Appeals made unauthorized disclosures to third parties.
- C. Discussed potential exceptions with Appeals management.

**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 that the following internal controls were relevant to our audit objective: Appeals and IRS policies, procedures, and practices for processing penalty appeal cases. We evaluated these controls by reviewing a random, stratified, variable sample of 140 penalty appeal cases closed in FY 2013 and interviewing Appeals management.

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<sup>2</sup> IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.





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**Appendix II**

*Major Contributors to This Report*

Gregory D. Kutz, Assistant Inspector General for Audit (Management Services and Exempt Organizations)  
Jonathan T. Meyer, Director  
Janice M. Pryor, Audit Manager  
Joseph P. Smith, Lead Auditor  
Lauren W. Bourg, Senior Auditor  
Mark A. Judson, Senior Auditor  
Ahmed M. Tobaa, Senior Auditor



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**Appendix III**

*Report Distribution List*

Commissioner C  
Office of the Commissioner – Attn: Chief of Staff C  
Deputy Chief, Appeals AP  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Office of Audit Coordination OS:PPAC:AC  
Director, Office of Program Evaluation and Risk Analysis RAS:O  
Office of Internal Control OS:CFO:CPIC:IC  
Audit Liaison: Chief, Appeals AP



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## Appendix IV

### *Outcome 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:**

- Revenue Protection – Potential; 1,403 cases and \$34,200,409 in penalties abated in which the Appeals case file did not adequately support the decision to abate penalties (see page 4). As a result, the IRS abated penalties that could have resulted in as much as \$34,200,409 of future tax revenue.<sup>1</sup>

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

In 57 of the 140 sampled FY 2013 closed penalty appeal cases reviewed, the Appeals case files did not support the decision to abate the penalties. We selected a statistical stratified, random sample of 140 cases from a population of 3,131 penalty appeal cases closed in FY 2013.<sup>2</sup>

We estimate that potentially 1,403 (3,131 x 44.80 percent error rate) cases were not fully supported for the abatement action taken.<sup>3</sup> Further, we estimate that potentially \$34,200,409 of penalties were abated in FY 2013 that were not fully supported by the case files.<sup>4</sup>

Figure 2 shows the sampling parameters for our stratified variable sample.

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<sup>1</sup> This figure assumes that taxpayer requests to abate penalties on all Appeals case files that did not adequately support the decision to abate would have been rejected and that the IRS would have been able to collect all penalties from taxpayers involved in the projected 1,403 cases.

<sup>2</sup> In FY 2013, Appeals closed a total of 11,061 penalty appeal cases; however, only 3,131 had abatement of penalties greater than or equal to \$2,500. We selected our sample of 140 cases from the 3,131 cases closed in FY 2013 that had abatements greater than or equal to \$2,500.

<sup>3</sup> The point estimate projection is based on a two-sided 95 percent confidence interval. We are 95 percent confident that the point estimate is between 1,100 and 1,705.

<sup>4</sup> The point estimate projection is based on a two-sided 95 percent confidence interval. We are 95 percent confident that the point estimate is between \$25,605,102 and \$42,795,716.



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**Figure 2: Sampling Parameters**

<b>Sampling Element</b>	<b>Stratum 1</b>	<b>Stratum 2</b>	<b>Stratum 3</b>	<b>Total</b>
Dollar Range of Abatements	\$2,500 - \$100,000	\$100,000 - \$1 Million	\$1 Million and Greater	--
Stratum Population	2,960	159	12	3,131
Population Percent to Total	0.945	0.051	0.004	1.000
Cases Reviewed	90	38	12	140
Number of Errors	41	12	4	59
Error Rate <sup>5</sup>	45.56%	31.58%	33.33%	--

*Source: Our analysis of 140 penalty appeals cases.*

<sup>5</sup> The stratified variable sample error rate of 44.80 percent is based on a computation of the data in this table.



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**Appendix V**

*Management's Response to the Draft Report*



CHIEF, APPEALS

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

July 14, 2015

MEMORANDUM FOR Michael E. McKenney  
Deputy Inspector General for Audit

FROM:

Kirsten B. Wielobob /s/ *Kirsten Wielobob*  
Chief, Appeals

SUBJECT:

Draft Audit Report – Additional Documentation Is Needed to  
Support Office of Appeals Penalty Abatement Decisions (Audit #  
201410018)

Thank you for the opportunity to review your draft audit report on Appeals' post-assessment penalty appeal decisions. We agree with your recommendations as described below and in our detailed response.

As a general matter, Appeals employees endeavor to handle all cases appropriately. To a couple of specific points in your report, we agree that we should document adequately our reasons for decisions. We believe, however, that weighing the value of taxpayer testimony is crucial to resolving cases without litigation and is consistent with Appeals approach to analyzing hazards of litigation.

We believe the outcome measure is overstated. It incorrectly assumes that all penalty abatement determinations lacking proper documentation should be rejected. Inadequate documentation does not necessarily equate to an improper abatement determination.

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

If you have any questions, please have a member of your staff contact John V. Cardone, Director, Appeals, Policy, Quality and Case Support, at 202-317-8830.

Attachment



*Additional Documentation Is Needed to Support  
Office of Appeals Penalty Abatement Decisions*

Attachment

**Recommendation 1:**

Provide training to Appeals personnel on the requirements instructing them to clearly document the reasons for abatement decisions, including justification for partial abatement percentages and specific hazards of litigation associated with an abatement case.

**Proposed Corrective Action:**

Appeals agrees with this recommendation. We have already taken steps in this area and will provide additional training to Appeals Technical Employees who work penalty abatement cases.

**Implementation Date:** July 15, 2016

**Responsible Official:** Director, Appeals Policy, Quality and Case Support

**Recommendation 2:**

\*\*\*\*\*1\*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\*.

**Proposed Corrective Action:**

\*\*\*\*\*1\*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\*.

**Implementation Date:** \*\*\*\*\*1\*\*\*\*\*

**Responsible Official:** \*\*\*\*\*1\*\*\*\*\*



*Additional Documentation Is Needed to Support  
Office of Appeals Penalty Abatement Decisions*

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**Recommendation 3:** Review the delegated settlement authority to Appeals Officers and Settlement Officers to address the risk associated with allowing unlimited abatements without managerial review for some Appeals staff.

**Proposed Corrective Action:**

Appeals agrees with this recommendation. We will review the existing delegated settlement authority and evaluate any risk associated with the current delegation.

**Implementation Date:** September 15, 2016

**Responsible Official:** Director, Appeals Policy, Quality and Case Support