

**The Internal Revenue Service Can Further  
Reduce the Burden on Taxpayers Who Disagree With Proposed  
Assessments**

**February 2000**

**Reference Number: 200010033**

**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.**



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

February 29, 2000

MEMORANDUM FOR COMMISSIONER ROSSOTTI

FROM: Pamela J. Gardiner  
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Internal Revenue Service Can Further  
Reduce the Burden on Taxpayers Who Disagree With Proposed  
Assessments

The attached report presents the results of our follow-up review over the steps taken by the Internal Revenue Service (IRS) to reduce the number of taxpayers in three California District Offices who petitioned the U.S. Tax Court and who did not respond to the final notice of assessment. Our objective was to assess the effectiveness of the corrective actions taken by the IRS in response to our prior audit report titled, *Review of Docketed Office Audit Cases in Western Region* (Reference Number 980903, dated November 24, 1997).

In summary, we found the number of taxpayers petitioning the United States (U.S.) Tax Court has declined significantly since our prior review, which reduced taxpayer burden and the IRS' costs of resolving disagreements. However, the IRS did not complete certain corrective actions that could help it continue the trend of minimizing the burden on taxpayers who disagree with proposed assessments. The IRS should ensure that it has the most current address available so that its letters are sent to the taxpayers' proper address. This would enable the IRS to locate more taxpayers and resolve issues with less correspondence and through less formal procedures than petitioning the U.S. Tax Court. The IRS should also ensure that audit groups adhere to its correspondence procedures to avoid contributing to taxpayers' perceptions that they are not treated properly.

IRS management concurred with our findings and agreed to take corrective action based on our recommendations. Management's comments have been incorporated into the report where appropriate, and the full text of their comments is included in Appendix V.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions, or your staff may contact Maurice S. Moody, Associate Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

Attachment

**The Internal Revenue Service Can Further Reduce  
the Burden on Taxpayers Who Disagree  
With Proposed Assessments**

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## **Executive Summary**

Resolving unagreed tax examinations is a burdensome process for taxpayers and a costly one for the Internal Revenue Service (IRS). In 1997, the IRS Inspection Service (now the Treasury Inspector General for Tax Administration) issued a report titled, *Review of Docketed Office Audit Cases in Western Region* (Reference Number 980903, dated November 24, 1997). The review focused on actions the IRS could take to reduce the number of taxpayers who petition the United States (U.S.) Tax Court and who do not respond to the final notice of assessment.

Between 1994 and 1995, the Los Angeles, Northern California, and Southern California Districts accounted for a disproportionate number (about 43 percent) of the office audits that were petitioned to the U.S. Tax Court nationwide. This follow-up review was conducted in these three districts to determine whether or not the IRS took the corrective actions it planned and, when taken, whether or not the corrective actions were effective. The Regional Commissioner, Western Region, was responsible for completing corrective actions in response to the prior report.

## **Results**

The number of taxpayers petitioning the U.S. Tax Court from the Los Angeles, Northern California and Southern California Districts has declined significantly since the 1997 review. This decline in petitions reduced taxpayer burden and the IRS' costs of resolving disagreements. However, not all of the previously recommended corrective actions were taken. While the IRS has made considerable progress, we believe it should take additional actions to further reduce the number of taxpayers who petition the U.S. Tax Court and who do not respond to the final notice of assessment.

### **The Number of Taxpayers Petitioning the United States Tax Court Has Dropped Significantly**

During the period April through September 1998, the percentage of office audits petitioned to the U.S. Tax Court from the Los Angeles, Northern California, and Southern California Districts was 39 percent lower than for the same period in 1997. We estimate that this decline has reduced the time taxpayers from these districts spent dealing with the IRS by about 225,000 days. We also estimate that the IRS reduced its costs to resolve disagreements in office audits by almost \$800,000.

We attribute the decline in the number of taxpayers petitioning the U.S. Tax Court primarily to more group manager involvement. The initial step in IRS procedures for

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resolving disagreements with taxpayers about their assessments is for the group manager to discuss the issues with the taxpayer and attempt to settle the disagreement. Unlike the prior review, where only 22 percent of the sampled audits with disagreements showed evidence of managerial involvement, 82 percent of the audits with disagreements examined during this review showed evidence of group manager involvement.

### **Additional Changes in Correspondence Procedures Can Lead to Further Improvements**

A significant number of taxpayers never respond to the IRS' correspondence regarding their examination. When this occurs, the IRS sends a final notice of assessment to the taxpayer, via certified mail, stating that he/she must pay the tax or petition the U.S. Tax Court within 90 days. If the taxpayer does not respond, the IRS assesses the tax. IRS data show that almost 54 percent of the dollars assessed in office audits from these three districts from January 1, 1998, through March 31, 1999, can be traced to taxpayers who did not respond to the final notice of assessment. Taxpayers assessed in this manner are not likely to pay the amounts assessed, which can cause the IRS to expend resources on collection efforts.

The lack of response may not be entirely the fault of the taxpayers. The previous audit report showed that almost 17 percent of letters notifying taxpayers of proposed changes contained addresses different from those on the U.S. Tax Court petitions, indicating the IRS might not have sent the notices to the proper address. Ideally, the IRS would be able to locate the taxpayer and resolve the issue with less correspondence and through less formal procedures than petitioning the U.S. Tax Court. In this regard, the previous audit report recommended that the IRS send letters of proposed changes to taxpayers, via certified mail and with return receipt requested, to help ensure the taxpayers received the notices or to identify incorrect addresses. Before committing to the extra cost of sending the letters by certified mail, the IRS wanted to test the impact certified letters had on reducing the number of taxpayers who ignore the final notice of assessment and who petition the U.S. Tax Court. Unfortunately, the IRS did not perform this test.

We also noted that, contrary to IRS guidelines, district offices did not always issue letters of proposed changes to taxpayers. In other instances, the letters of proposed changes were altered without permission from the National Office. The time given for some taxpayers to respond to the proposed changes was shortened from 30 days to 15 days. In other letters, taxpayers were threatened with a summons. Although the Regional Commissioner, Western Region, issued a memorandum instructing the districts to ensure letters of proposed changes are issued in all unagreed cases, no follow-up reviews were performed by regional officials to ensure the directive was followed. As a result, correspondence procedures were still not consistently followed, which could contribute to taxpayers' perceptions that they are not treated fairly.

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## **Summary of Recommendations**

We believe that sending letters of proposed changes by certified mail, with return receipt requested, will enable the IRS to identify cases for which it has incorrect taxpayer addresses. This information will help the IRS avoid mailing final notices of assessment that may not be received by the taxpayers. As a result of this action, the IRS should experience a reduction in the number of taxpayers who do not respond to the final notice of assessment and who petition the U.S. Tax Court. In addition, future management or quality reviews need to evaluate whether audit groups are adhering to correspondence procedures.

Management's Response: IRS management concurred with our findings and agreed to take corrective action based on our recommendations. With respect to our first recommendation, IRS management proposed an alternative solution that uses additional address research techniques to ensure letters are sent to the taxpayer's most current address. In response to the second recommendation, IRS management will provide additional guidance to IRS employees and managers in the Examination of Returns and the Compliance and Customer Service Managers' Handbooks. Management will also include correspondence procedures in its planned Special Conformance Reviews.

Management's comments are included in this report where appropriate, and the full text of management's response appears as Appendix V.

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*We evaluated the effectiveness of actions taken in response to a prior audit report.*

## Objective and Scope

Our objective was to assess the effectiveness of corrective actions taken in response to an Internal Revenue Service (IRS) Inspection Service (now the Treasury Inspector General for Tax Administration) report titled, *Review of Docketed Office Audit Cases in Western Region* (Reference Number 980903, dated November 24, 1997). The audit tests were focused on the following areas:

- Measuring reductions in taxpayer burden and the IRS' audit costs associated with declines in the number of taxpayers petitioning the United States (U.S.) Tax Court.
- Determining whether group managers increased their involvement with taxpayers who disagree with proposed assessments.
- Determining whether correspondence procedures were consistently followed.
- Measuring the impact of sending letters of proposed changes via certified mail.

The audit was performed in accordance with *Government Auditing Standards* from October 1998 through September 1999. On-site tests were performed in the Los Angeles, Northern California, and Southern California Districts.

Appendix I outlines the detailed objective, scope, and methodology of this review. Major contributors to this report are listed in Appendix II.

## Background

Resolving tax audit disagreements is a burdensome process for taxpayers and a costly one for the IRS. The



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*The Los Angeles, Northern California, and Southern California Districts accounted for a disproportionate number of taxpayers who petitioned the U.S. Tax Court.*

1997 audit report titled, *Review of Docketed Office Audit Cases in Western Region*, focused on actions the IRS could take to reduce the number of taxpayers who petitioned the U.S. Tax Court and who do not respond to the final notice of assessment.

Between 1994 and 1995, the Los Angeles, Northern California, and Southern California Districts accounted for a disproportionate number of taxpayers who petitioned the U.S. Tax Court nationwide.

In addition, a significant number of taxpayers never responded to IRS correspondence. When this occurs, the IRS sends a final notice to the taxpayer, via certified mail, stating that he/she must pay the tax or petition the U.S. Tax Court within 90 days. If taxpayers do not respond, the IRS ultimately assesses the tax and begins collection actions. Most of the taxpayers assessed in this manner are not likely to pay the deficiency within a reasonable period of time, if ever.

The 1997 report made the following observations:

- Significant resources were spent resolving petitioned office audits.
- Group managers were not sufficiently involved in the resolution of unagreed audits.
- Taxpayers were not always issued instructions for responding to notices of proposed changes when disagreements surfaced over proposed assessments.
- Letters of proposed changes were not always sent to taxpayers' current addresses.

### Results

*Group managers' involvement in audits contributed to the decline in taxpayers petitioning the U.S. Tax Court.*

The number of taxpayers petitioning the U.S. Tax Court has declined significantly since the prior review. This has reduced taxpayer burden and the IRS' costs of resolving disagreements. We attribute the decline in taxpayers petitioning the U.S. Tax Court primarily to

## **The Internal Revenue Service Can Further Reduce the Burden on Taxpayers Who Disagree With Proposed Assessments**

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more group manager involvement in audits with taxpayer disagreement.

However, not all of the previously recommended corrective actions were taken. In particular, the IRS needs to measure the impact of sending letters of proposed changes via certified mail and to ensure that correspondence procedures are followed.

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### **The Number of Taxpayers Petitioning the United States Tax Court Has Dropped Significantly**

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#### *Prior Condition*

Between 1994 and 1995, the Los Angeles, Northern California, and Southern California Districts accounted for approximately 43 percent of taxpayers nationwide who petitioned the U.S. Tax Court. The audit report attributed the relatively high number of petitions primarily to a lack of involvement by first-line managers in resolving the cases.

Resolving an audit that is petitioned to the U.S. Tax Court typically involves employees from several IRS functions, which can significantly increase the time taxpayers spend dealing with their audit as well as the IRS' audit costs. On average, during Fiscal Years 1994 through 1996, taxpayers spent about 361 days on audits they petitioned to the U.S. Tax Court. The IRS, on the other hand, incurred salary and benefits costs of roughly \$820 for each petitioned audit.

The latter costs occur when a taxpayer disagrees with the audit recommendation and chooses to bypass the IRS' administrative appeal process and take the issue directly to the U.S. Tax Court. Once a taxpayer takes this step, the IRS Offices of Appeals and District Counsel attempt to resolve the disagreement before it goes to trial.

*Both taxpayers and the IRS  
spend considerable resources  
to resolve these relatively  
small dollar audits.*

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### *Planned Corrective Actions*

To reduce the number of U.S. Tax Court petitions, the IRS planned actions to ensure that group managers increased their involvement in disputed audits so that more audits were closed as agreed to or referred to the Office of Appeals.

### *Follow-up Results*

To determine if the number of taxpayers petitioning the U.S. Tax Court declined after IRS officials acted on the recommendations from the previous report, we compared two Audit Information Management Systems (AIMS) databases.<sup>1</sup> The first database contained audit results from examinations closed between April and September 1997. The second database contained audit results from closures between April and September 1998. The comparison showed that the percentage of office audits petitioned to the U.S. Tax Court fell by 39 percent.

*Typically, a petitioned audit takes roughly six months longer to resolve than a non-petitioned one.*

On average, a petitioned audit takes 181 more days to resolve than a non-petitioned audit. We estimate the 39 percent decline in the percentage of petitioned audits reduced the time taxpayers spent dealing with the IRS by about 225,000 days annually.

We analyzed data from the Examination, Appeals, and Counsel offices to determine the IRS' direct salary and benefits costs associated with office audits. We estimated there are about \$820 of salary and benefit costs associated with each audit that is petitioned to the U.S. Tax Court. Comparatively, other office audits have salary and benefit costs of roughly \$438. We estimate that the 39 percent drop in the percentage of petitioned audits reduced the amount the IRS spent to resolve disagreements by almost \$800,000 in the three districts. This does not include any potential savings that could

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<sup>1</sup> The Audit Information Management System (AIMS) contains results from examinations of tax returns.

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*Unlike the first review, group managers increased their efforts to close more cases as agreed or sent to Appeals.*

have been realized by reducing the impact on collection resources.

The initial step in IRS procedures for resolving an audit disagreement is for the group manager to discuss the issues with the taxpayer and try to resolve the disagreement. Unlike the prior review where only 22 percent of the audits with taxpayer disagreement showed evidence of managerial involvement, this follow-up review found a dramatic increase in managerial efforts to resolve issues at the group level. Eighty-two percent of the audits with taxpayer disagreement that we reviewed showed evidence of managerial involvement. Figure 1 graphically presents the differences between the amount of managerial involvement that we found in our previous and current case reviews.

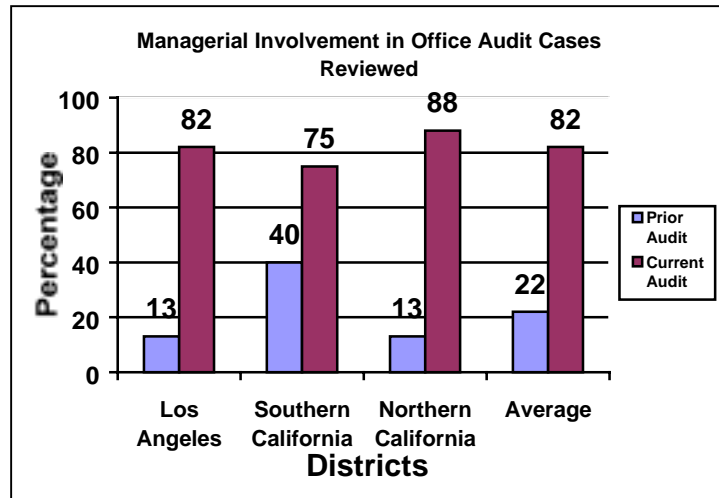


Figure 1

## The Internal Revenue Service Can Further Reduce the Burden on Taxpayers Who Disagree With Proposed Assessments

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### Additional Changes in Correspondence Procedures Can Lead to Further Improvements

#### *Prior Condition*

A significant number of taxpayers never respond to the IRS' initial audit contact letter. When this occurs, the IRS will send a letter of proposed tax changes before sending a final notice of assessment to the taxpayer. The letter of proposed tax changes encourages taxpayers to either reconsider their position or appeal the proposed changes to the IRS' Office of Appeals. The final notice of assessment is sent, via certified mail, stating that the taxpayer must pay the tax or petition the U.S. Tax Court within 90 days. If the IRS does not receive a response to the final notice of assessment, it assesses the tax and begins collection actions. However, taxpayers assessed in this manner are not likely to pay the deficiency within a reasonable period of time, if ever. For example, 84,956 taxpayers did not respond to the final notices of assessment between October 1993 and September 1996 and were assessed roughly \$641.8 million. As of April 1997, about \$423.7 million (66 percent) of the assessments were still unpaid.

The lack of response may not be entirely the taxpayers' fault. The prior report noted that almost 17 percent of letters of proposed changes contained addresses different from those on the U.S. Tax Court petition, indicating the IRS might not have sent the notices to the proper address. In addition, district offices did not always send letters of proposed changes to taxpayers if they, or their representative, were present at the audit. As a result, this left some taxpayers little choice but to petition the U.S. Tax Court or let the IRS assess the deficiency.

#### *Planned Corrective Actions*

In response to the previous report, the IRS agreed to test sending letters of proposed changes via certified mail.

*Letters of proposed changes encourage taxpayers to exercise their appeal rights within the IRS when disagreements cannot be resolved at the audit group level.*

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The planned test was to focus on taxpayers who had not responded to the IRS' initial audit contact letters. The test was expected to show the impact certified letters of proposed changes have on reducing the number of taxpayers who petition the U.S. Tax Court and who do not respond to the final notice of assessment.

To further ensure district offices followed correspondence procedures, the IRS also planned to issue an instructive memorandum to all Western Region district offices requiring them to follow the Internal Revenue Manual (IRM) guidelines. The IRM requires issuance of a letter of proposed changes on every audit where adjustments are proposed, regardless of whether the taxpayer or the representative is present. The IRS also planned to provide instructions in the memorandum for the districts to maintain a copy of the letter in the case file for future review purposes.

### *Follow-up Results*

There is no evidence that the planned test to send letters of proposed changes, via certified mail, was performed. Our analysis of IRS data from January 1, 1998, through March 31, 1999, indicates that many taxpayers are still not responding to IRS correspondence, including the final notice of assessment. Almost 54 percent of the dollars assessed on office audits by these three districts during this time frame can be traced to taxpayers who did not respond to the final notice of assessment.

The Regional Commissioner, Western Region, issued a memorandum to the districts directing audit groups to issue the letter of proposed changes in all cases with taxpayer disagreements. However, no follow-up reviews were performed by regional officials to verify that audit groups were adhering to the directive. As a result, correspondence procedures were still not consistently followed, which could contribute to taxpayers' perceptions that they are not treated fairly.

We randomly selected 180 audits for review (60 from each district) awaiting taxpayer responses to the final notices of assessment, and identified problems in

*Official IRS correspondence that is altered locally may contribute to taxpayers' perceptions that they are not treated fairly.*

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50 (27.8 percent) of the audits. Sixteen of the audits we reviewed showed no evidence that the taxpayers were issued a letter of proposed changes. In the remaining 34 audits, the letters were altered, which is contrary to the IRS' correspondence procedures. Some of the altered letters omitted the taxpayers' appeal rights. In other instances, letters reduced the time the taxpayer could respond to the proposed changes from 30 to 15 days. In others, taxpayers were threatened with a summons if they did not timely provide the information requested.

### **Recommendations**

The Assistant Commissioner (Examination) should take steps to complete the following corrective actions.

1. Send letters of proposed changes via certified mail, with return receipt requested, when taxpayers do not respond to the initial contact letter.

Management's Response: IRS management proposed an alternative solution to ensure all taxpayers are receiving its correspondence. The proposed strategy involves selecting three to four districts with a demonstrated higher than average no response rate, and using advanced address research techniques to ensure IRS has the best available address.

Office of Audit Comment: We concur with the proposed test and recommend that the successful techniques identified during this test be implemented at all processing sites as soon as possible.

2. Ensure future management or quality reviews include evaluating whether office audit groups are adhering to correspondence procedures.

Management's Response: IRS management committed to providing additional guidance to IRS employees and managers in the Examination of Returns and the Compliance and Customer Service Managers' Handbooks.

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**Conclusion**

The number of taxpayers petitioning the U.S. Tax Court has declined since the previous review. This decline has reduced the time taxpayers spent dealing with IRS audits and the IRS' audit costs. This trend can be continued by taking actions to identify proper taxpayer addresses and to improve correspondence procedures.



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**Appendix I**

**Detailed Objective, Scope, and Methodology**

Our objective was to assess the effectiveness of the Internal Revenue Service's (IRS) corrective actions taken in response to the IRS Inspection Service (now Treasury Inspector General for Tax Administration) report titled, *Review of Docketed Office Audit Cases in Western Region* (Reference Number 980903, Dated November 24, 1997). Our audit tests were performed in the Los Angeles, Northern California, and Southern California Districts. The specific audit tests included:

- I. Reviewing Treasury's Inventory Tracking and Closure system to determine the implementation dates of planned corrective actions for the recommendations in the prior report.
- II. Reviewing memoranda and other supporting documentation to determine if planned corrective actions for the recommendations in the prior report were completed.
- III. Evaluating new procedures, objectives, and action plans established by the Los Angeles, Northern California, and Southern California Districts to increase the resolution of disputes at the audit group level.
- IV. Analyzing notices of proposed changes and the extent of managerial involvement in a judgmental random sample of 180 unagreed office audits (60 audits per district) that were waiting for a taxpayer response to a final notice of assessment.
- V. Comparing examination closures between the Fiscal Years 1997 and 1998 Audit Information Management System (AIMS) databases to measure the decline in the number of petitioned office audits.
- VI. Computing reductions in cycle time (length of audit) associated with the decline in the number of taxpayers petitioning the United States (U.S.) Tax Court.
- VII. Measuring reductions in the IRS' audit costs associated with the decline in the number of taxpayers petitioning the U.S. Tax Court.

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**Appendix II**

**Major Contributors to This Report**

Maurice S. Moody, Associate Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)

Stephen Mullins, Director

Frank Dunleavy, Audit Manager

Earl Charles Burney, Senior Auditor

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**Appendix III**

**Report Distribution List**

Chief Operations Officer OP  
Assistant Commissioner (Examination) OP:EX  
National Director for Legislative Affairs CL:LA  
Office of Management Controls M:CFO:A:M  
Office of Chief Counsel CC  
Assistant Commissioner (Program Evaluation and Risk Analysis) M:OP  
Regional Commissioner, Western Region RC  
District Director, Los Angeles District D  
District Director, Northern California District D  
District Director, Southern California District D  
Audit Liaisons:  
    Chief Operations Officer OP  
    Assistant Commissioner (Examination) OP:EX

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**Appendix IV**

**Outcome Measures**

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

Finding and recommendation:

The percentage of office audits petitioned to the United States (U.S.) Tax Court from the Los Angeles, Northern California, and Southern California Districts fell by 39 percent between comparable periods in Fiscal Years (FY) 1997 and 1998. We attribute the decline primarily to more group manager involvement. Unlike our prior audit report, *Review of Docketed Office Audit Cases in Western Region* (Reference Number 980903, Dated November 24, 1997) where only 22 percent of unagreed audits reviewed showed evidence of managerial involvement, this follow-up review found a dramatic increase in managerial efforts to resolve issues at the group level. Eighty-two percent of the unagreed audits reviewed showed evidence of managerial involvement.

Type of Outcome Measure:

Cost Savings - Actual

Taxpayer Burden - Actual

Value of the Benefit:

We estimate that the decline in the number of taxpayers petitioning the U.S. Tax Court reduced the costs the IRS incurs to resolve disagreements by almost \$800,000 in comparable periods for FYs 1997 and 1998. We also estimate that the decline reduced the time taxpayers spent dealing with the IRS by about 225,000 days annually.

Methodology Used to Measure the Reported Benefit:

To determine if the number of taxpayers petitioning the U.S. Tax Court declined after IRS officials acted on the recommendations from the previous audit report, we compared two Audit Information Management Systems (AIMS) databases. The first database contained audit results from examinations closed between April and September 1997 showing 4.0 percent of the examinations were petitioned (2,474 of 61,853 total examinations). The second database contained audit results from closures between April and September 1998 showing 2.41 percent of the examinations were petitioned (845 of 35,081 total examinations). The comparison showed that the percentage of petitioned audits to total office audits in these three districts fell from 4.0 percent to 2.41 percent (39 percent decline) between the two periods.

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The FY 1998 AIMS database shows that a petitioned audit takes, on average, 181 more days to resolve than a non-petitioned audit. In other words, we estimate that the 39 percent decline in the percentage of petitioned audits reduced the time taxpayers spent dealing with the IRS by about 225,000 days. Using cost information developed in the prior report, we estimate that the 39 percent drop in the percentage of petitioned office audits reduced the amount the IRS spent to resolve disagreements by almost \$800,000.

The prior report estimated that there are \$820 of salary and benefit costs associated with a petitioned audit. Non-petitioned office audits in the same three districts cost approximately \$438, and agreed or no-change audits cost \$86.

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Appendix V

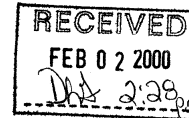
Management's Response to the Draft Report



COMMISSIONER

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

January 21, 2000



MEMORANDUM FOR TREASURY INSPECTOR GENERAL FOR  
TAX ADMINISTRATION

FROM: Charles O. Rossotti *COR*  
Commissioner of Internal Revenue

SUBJECT: Draft Audit Report - The Internal Revenue Service (IRS) Can  
Further Reduce the Burden on Taxpayers Who Disagree With  
Proposed Assessments (IGAMIS #199902)

Thank you for the opportunity to review and comment on your recent draft report entitled "The Internal Revenue Service (IRS) Can Further Reduce the Burden on Taxpayers Who Disagree with Proposed Assessments." This report is based on a followup of a previous review conducted in Western Region (Reference Number 980903, dated November 24, 1997). While the original report was limited to an investigation of the three districts in California, you have raised issues that require guidance on a national level.

We were pleased to note that your followup report found a significant decline in the number of taxpayers in the three California districts who did not respond to the final notice of deficiency but instead petitioned the U. S. Tax Court. This reduced the time taxpayers spent dealing with the IRS by about 225,000 days during the same time periods. You attribute this decline to more group manager involvement as required by IRS procedures. We agree that this is a critical step in resolving cases at the lowest level with the least burden to the taxpayers and the least cost to the IRS. We also agree with your concerns about the lack of consistency in correspondence procedures and regret that the certified mail test agreed to by the Western Region has not been conducted.

As we discussed with you in our closeout conference, we are hesitant to agree to using certified mail (with return receipts) for all no response cases, due to the cost involved and the burden for taxpayers who work during the normal mail delivery hours. We are proposing an alternative option that would require office audit groups in selected districts to test the use of additional address research on all no response cases to

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ensure that we have the most current address available. We would ask your support for this test as a means of identifying a less costly and burdensome option for improving taxpayer response to our contacts.

We would like to take this opportunity to share with you some of the steps we have taken to communicate and reinforce examination procedures for taxpayer correspondence relating to contacting taxpayers and issuing audit reports. Since your first review, we have taken the following actions at a national level:

- In January 1998, we issued a memorandum to all IRS employees regarding the protection of taxpayers' rights. It stated in part that all IRS employees are obligated to ensure that taxpayers receive all rights guaranteed to them by the Internal Revenue Code, including the two Taxpayer Bill of Rights, and the additional internal procedures and policies we have adopted for their protection.
- A redesigned Internal Revenue Manual (IRM) was issued for Examination in May 1999 (IRM 4.2, Examination of Returns Handbook) which includes specific requirements for correspondence and issuance of reports, as well as specific guidelines for ensuring taxpayers' rights.
- During 1999, several memoranda were issued from the Assistant Commissioner (Examination) to the field offices reemphasizing taxpayer notification requirements related to initial contacts and the issuance of first notices of proposed deficiencies. These memoranda further reinforced the requirements for issuing Publications 1, 5, and 594 in all cases to ensure that taxpayers were fully aware of all their rights, including appeal rights. These memoranda were also posted to the National Resource Center Website to maximize the communication of this information.
- A memorandum is currently in clearance that will provide expanded address research requirements based on a recent multifunctional study of unlocatable taxpayers.

The following responses are provided to the recommendations contained in the draft report:

### IDENTITY OF RECOMMENDATION/FINDING # 1

Send letters of proposed changes via certified mail, with return receipt requested, when taxpayers do not respond to the initial contact letter.

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**ASSESSMENT OF CAUSE(S)**

The previous audit report showed that almost 17 percent of letters notifying taxpayers of proposed changes contained addresses different from those on the U.S. Tax Court petitions, indicating the IRS might not have sent the notices to the proper address. Ideally, the IRS would be able to locate the taxpayer and resolve the issue with less correspondence and through less formal procedures than petitioning the U.S. Tax Court. In this regard, the previous audit report recommended that the IRS send letters of proposed changes to taxpayers, via certified mail and with return receipt requested, to help ensure the taxpayers received the notices or to identify incorrect addresses. Before committing to the extra cost of sending the letters by certified mail, the IRS wanted to test the impact certified letters had on reducing the number of taxpayers who ignore the final notice of assessment and who petition the U.S. Tax Court.

**CORRECTIVE ACTIONS**

We believe that sending all proposed adjustments by certified mail would create a potential burden to taxpayers who work during normal mail delivery hours. Since our primary goal is to ensure that all taxpayers are receiving our correspondence (as another way of minimizing the number of taxpayers ultimately petitioning Tax Court), we propose testing an alternative strategy to achieve this goal. This strategy would involve selecting three to four districts with a demonstrated higher than average no response rate and using expanded address research techniques to ensure we are using the best address available. By attempting to perfect the address on all no response cases prior to issuing the 30-Day Report and reissuing initial correspondence as needed, we hope to minimize instances of taxpayer nonresponse due to the use of an address that is not current.

**IMPLEMENTATION DATE:**

June 1, 2000

**RESPONSIBLE OFFICIAL(S)**

Assistant Commissioner (Examination)

**CORRECTIVE ACTION MONITORING PLAN**

Using available management information systems, monitor the trends in no show and petitioning cases using historical data as a baseline. In addition, we plan to collect as much data as possible on the number of taxpayers who respond as a result of the additional address research.

**IDENTITY OF RECOMMENDATION/FINDING # 2**

Ensure future management or quality reviews include evaluating whether office audit groups are adhering to correspondence procedures.



**The Internal Revenue Service Can Further Reduce  
the Burden on Taxpayers Who Disagree  
With Proposed Assessments**

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**ASSESSMENT OF CAUSE(S)**

Based on your findings, the district offices included in your reviews did not always issue letters of proposed changes to taxpayers that included a full explanation of their rights. In addition, national letters were altered inappropriately to shorten the response times, to omit appeal language, and to include information on the possible issuance of summons. Even though IRM procedures are in place to cover the requirements for making taxpayer contacts and additional emphasis has been provided in several memoranda, additional management oversight and review are needed to ensure that these procedures are consistently followed.

**CORRECTIVE ACTIONS**

We concur with this recommendation. We will:

1. Provide additional clarifying guidance in IRM 4.2, Examination of Returns Handbook covering :
  - Required response times for 30-Day Letters;
  - Modification of national letters and forms; and
  - Notification of taxpayer rights, including appeal rights.
2. Provide additional guidance for group managers requiring review of correspondence procedures when conducting case reviews and workload reviews. This guidance will be provided in the form of memorandum and revisions to IRM 114.1, Compliance and Customer Service Managers Handbook.
3. Include correspondence procedures as a review area in future Special Conformance Reviews.

**IMPLEMENTATION DATE:**

June 1, 2000

**RESPONSIBLE OFFICIAL(S)**

Assistant Commissioner (Examination)

**CORRECTIVE ACTION(S) MONITORING PLAN**

The results of Special Conformance Reviews will be used to monitor the level of adherence to the appropriate correspondence procedures.

If you have any questions or need additional information, please call Tom Wilson at 202-622-4400.