Letter Report: Collection Was Suspended Indefinitely for Some Accounts Because of Control Weaknesses in Processing Taxpayer Claims

August 2000

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INSPECTOR GENERAL
for TAX
ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

August 31, 2000

MEMORANDUM FOR COMMISSIONER ROSSOTTI

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Letter Report – Collection Was Suspended Indefinitely for Some Accounts Because of Control Weaknesses in Processing Taxpayer Claims

This report presents the results of our review of the Internal Revenue Service's (IRS) balance due accounts where billing had been suspended. Our objective was to determine the adequacy of controls to ensure that taxpayer claims were monitored pending adjustment action and that collection activity was promptly resumed on accounts in which a balance remained.

In summary, the IRS suspended collection indefinitely on some accounts with no evidence of subsequent action being taken to adjust the taxpayers' accounts or to resume collection.

We recommended that billing suspensions be limited to 26 weeks for accounts in billing status. We also recommended implementing a computer-generated inventory control to provide management with the means to monitor accounts with billing suspended. Our final recommendation requested that management determine the reasons why transcripts designed to identify unresolved conditions were not effective.

Management's response was due on August 23, 2000. As of August 24, 2000, management has not responded to the draft report.

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 call Gordon C. Milbourn III, Associate Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-3837.

Objective and Scope

The objective of this review was to determine whether controls over taxpayers' claims ensured that collection activity was resumed when warranted.

The objective of this review was to determine whether Internal Revenue Service (IRS) controls over taxpayers' claims[1] ensured that collection activity was resumed when warranted.

We focused on balance due accounts for which collection notices were suspended for 6 months or more during the processing of taxpayers' claims. We identified open accounts with suspended collection activity by using a computer program to analyze the IRS' delinquent accounts.

We determined the validity of the collection delays by reviewing:

- IRS criteria for suspending collection.
- Controls designed to monitor case inventories and unresolved accounts.

We conducted the review at the Brookhaven IRS Center from January through April 2000 in accordance with *Government Auditing Standards.* The scope included nationwide data from all 10 IRS Centers through June 1999.

Major contributors to this report are listed in Appendix I. Appendix II contains the Report Distribution List.

Background

When the IRS processes a taxpayer claim to adjust taxes and/or locate payments on a delinquent account, a code is entered on an IRS computer system to temporarily suspend collection while the IRS conducts research.

[1] Most taxpayer claims are requests for the IRS to adjust their taxes and/or locate taxpayer payments.

The recommended length of suspension is generally up to 15 weeks and is not intended to exceed 26 weeks. The code suppresses billing while the IRS processes the taxpayer claim and allows billing to resume when specified, unless the IRS employee suspends collection again. Collection activity should be suspended as briefly as possible during the billing process because collection potential decreases rapidly as delinquent accounts age.

Taxpayer claims must be controlled in inventory when they cannot be readily resolved. Management receives inventory listings that allow them to monitor aged cases. Further, an IRS computer system periodically produces transcripts of unresolved taxpayer claims to provide for independent follow-up by IRS Center employees.

As of June 1999, there were 3,004 accounts for which collection notices were suspended for 6 months or more pending the resolution of the taxpayers' claims. This figure does not include an unknown number of delinquent accounts in which the collection statute expired while billing remained indefinitely suspended.

Results

In 1,237 of the 3,004 accounts reviewed, totaling $16.7 million, the IRS suspended collection indefinitely[2] during taxpayer claim processing. Revenue remained uncollected in the 1,237 accounts when the taxpayers' claims did not result in either the resolution of the tax liability or the resumption of billing. In the remaining 1,767 accounts, the suspension was reversed because IRS employees took subsequent actions or because the taxpayers fully paid their balances due.

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[2] Billing was suspended using a code that can be released only through full payment of the balance due or through employee intervention. These accounts were not controlled in the inventory of the employee responsible for suspending collection, and the code used does not systemically release.

Several factors caused collection activity to be suspended indefinitely on these accounts:

- Employees were not using the proper codes to suspend collection.
- Accounts suspended from collection were not maintained in employee inventories.
- The IRS' controls were not always effective in identifying and correcting unresolved accounts.

Collection Was Suspended Indefinitely for Some Accounts

The IRS suspended collection indefinitely in 1,237 (41 percent) of the 3,004 accounts reviewed, totaling $16.7 million, with no evidence of action being taken to resolve the cases.

The IRS suspended collection indefinitely in 1,237 (41 percent) of the 3,004 accounts reviewed, totaling $16.7 million, with no evidence of action being taken to resolve the cases. The reasons for suspending collection activity on these accounts were not always apparent. We estimate that systemically limiting the billing suspensions to 26 weeks for taxpayer claim processing would prevent collection delays and increase revenue by $6.5 million over the next 5 years.

In 815 (66 percent) of the 1,237 accounts, collection had been suspended for 1 to 9 years at the time of our review. The majority of these suspended accounts represented delinquent employment taxes.

We referred these 1,237 accounts to the Treasury Inspector General for Tax Administration Strategic Enforcement Division (SED) to evaluate the potential for employee misconduct in the handling of these cases. As of June 2000, the SED had not made any determinations regarding these cases.

Some IRS employees used codes that were mentioned in reference material but were not specifically described in the IRS' written instructions.

Employees were not using the proper codes to suspend collection

IRS written instructions were not adequate to ensure that the proper codes were used to suspend billing for up to 26 weeks. Some IRS employees used codes that were mentioned in reference material but were not specifically described in the IRS' written instructions.

In addition, the IRS' code designers and employees using the codes misunderstood how certain codes actually functioned. Some codes that suspend collection automatically allow billing to resume after 26 weeks, while others do not. The reference material describing the codes that are not automatically released contains only an obscure footnote that implies that billing will not resume. IRS manual instructions contain no reference to the fact that billing will not resume without full payment or employee intervention.

Accounts suspended from collection were not maintained in employee inventories

IRS employees are required to establish an inventory control when a taxpayer claim cannot be readily resolved. Inventory controls provide listings that allow management to monitor the timeliness and accuracy of processing. They also assist employees in coordinating their work and in preventing duplication of effort.

IRS employees did not maintain suspended accounts in their inventories, as required.

However, IRS management has no way to ensure that employees establish inventory control when a taxpayer claim cannot be readily resolved. In fact, none of the 1,237 suspended accounts we identified were maintained in the inventories of the employees responsible for suspending collection.

Controls were not always effective in identifying and correcting unresolved accounts

An IRS computer system produces two kinds of transcripts to assist IRS employees in analyzing unresolved taxpayer claims. Accounts Maintenance Transcripts are generated for analysis after billing has been suspended for 28 weeks. Diagnostic Transcripts are generated for analysis after billing has been suspended for more than 1 year.

For the accounts reviewed, one type of computer transcript was not always generated to help IRS employees analyze taxpayer claims and another type, if generated, was not reviewed.

However, of the 1,237 accounts we reviewed, Accounts Maintenance Transcripts were not generated for 541 accounts (44 percent). Further, there was no evidence of Diagnostic Transcript activity in 809 (99 percent) of the 815 accounts suspended for more than 1 year.

The IRS re-implemented two other types of Accounts Maintenance Transcripts as the result of our findings cited in a memorandum issued March 21, 2000.

Recommendations

The Assistant Commissioner (Customer Service) should:

1. Systemically limit the suspension of billing to a maximum of 26 weeks for taxpayer claim processing and clarify corresponding written instructions.
2. Have the computer generate an inventory control whenever an employee suspends collection for a taxpayer claim on an account in billing status.
3. Determine the reasons why transcripts were not produced for all of the suspended accounts we identified to ensure the future effectiveness of these controls.

<u>Management's Response</u>: Management's response was due on August 23, 2000. As of August 24, 2000, management has not responded to the draft report.

Conclusion

Collection activity for some delinquent accounts was suspended indefinitely because of control weaknesses in the processing of taxpayer claims. These cases need to be more effectively controlled to ensure that collection is suspended for the minimum duration necessary for taxpayer claim processing.

Appendix I

Major Contributors to This Report

Gordon C. Milbourn III, Associate Inspector General for Audit (Small Business and Corporate Programs)
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Appendix II

Report Distribution List

Deputy Commissioner Operations C:DO
Commissioner, Small Business/Self-Employed Division S
Chief Operations Officer OP
Assistant Commissioner (Collection) OP:CO
Assistant Commissioner (Customer Service) OP:C
Executive Officer for Service Center Operations OP:SC
Director, Collection Field Operations OP:CO:C
National Director, Customer Service Compliance, Accounts and Quality OP:C:A
Director, Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis M:O
Office of Management Controls CFO:A:M
Office of the Chief Counsel CC
National Taxpayer Advocate C:TA
Audit Liaisons:

Assistant Commissioner (Collection) OP:CO
Assistant Commissioner (Customer Service) OP:C

Appendix III

Outcome Measures

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 the Congress.

Finding and recommendation:
Collection was suspended indefinitely[1] for some accounts during taxpayer claim processing. Internal Revenue Service (IRS) controls were not adequate to ensure that employees were using the proper codes to suspend collection, suspended accounts were maintained in employee inventory, and unresolved accounts were identified for correction (see page 3).

We recommend:
- Systemically limiting the suspension of billing to a maximum of 26 weeks and clarifying corresponding written instructions.
- Automatically generating inventory case controls when collection suspension codes are used on an account in billing status.
- Determining the reasons why Accounts Maintenance Transcripts and Diagnostic Transcripts were not always produced.

Type of Outcome Measure:
- Increased Revenue - Potential

Value of the Benefit:
Correction of the condition cited will ensure the timely resumption of billing for 1,172 accounts and generate an increase in revenue of $6.5 million over the next 5 years.

Methodology Used to Measure the Reported Benefit:
Of the 1,237 total accounts identified totaling $16.7 million, 1,172 accounts totaling $16.0 million were incorrectly suspended during the 5-year period ending June 30, 1999. Using 5 years for projection purposes, we referred to the IRS Accounts Receivable Dollar Inventory report that contains projected collections per year based upon an account's status. For accounts in Notice status (actively billed), an estimated 48.7 percent would be

[1] Billing was suspended using a code that can be released only through full payment of the balance due or through employee intervention. These accounts were not controlled in the inventory of the employee responsible for suspending collection, and the code used does not systemically release.

collected for individual taxpayers and 38.1 percent for business taxpayers cumulatively for the first 5 years of collection. Based upon the dollar amount of balances due for accounts identified as incorrectly suspended during the past 5 years and the IRS' projected collections for the subsequent 5 years, we estimate that $6.5 million would be collected as a result of preventing indefinite collection suspensions.