



Treasury Inspector General for Tax Administration Office of Audit

ADDITIONAL ACTIONS ARE NEEDED TO PROTECT TAXPAYERS' RIGHTS AND THE GOVERNMENT'S INTEREST DURING BANKRUPTCY PROCEEDINGS

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Highlights

Highlights of Report Number: 2009-30-036 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

The United States Bankruptcy Code's automatic stay provision is designed to protect taxpayers from collection activities while they are in bankruptcy. Nonetheless, an estimated 495 potential taxpayer rights violations occurred between October 2005 and December 2007 because the IRS filed liens while taxpayers were in bankruptcy. There were also 27,838 taxpayers at risk of having their rights violated because a bankruptcy freeze code was not posted to their accounts in a timely manner. The bankruptcy freeze code designates that the account is in bankruptcy status. The code is an important control component for protecting taxpayer rights during bankruptcy proceedings by helping the Internal Revenue Service (IRS) and its Centralized Insolvency Operation function identify and address potential automatic stay violations.

WHY TIGTA DID THE AUDIT

This audit was initiated because in October 2005 the IRS consolidated many of its bankruptcy processing activities performed throughout the country to a new unit called the Centralized Insolvency Operation function. By consolidating work, the IRS envisioned it would reduce operation costs, increase efficiency, and improve customer service. TIGTA's review evaluated the controls used in the Centralized Insolvency Operation function to ensure that taxpayers' rights and the Government's interest are protected during bankruptcy proceedings.

WHAT TIGTA FOUND

TIGTA found controls need to be strengthened in two areas during the opening and closing of bankruptcy cases to ensure that taxpayers' rights and the Government's interests are protected during bankruptcy proceedings. First, the Centralized Insolvency Operation function could take better

advantage of reports generated from IRS automated systems to identify and resolve potential stay violations. TIGTA identified cases in which taxpayers' rights were violated because the IRS filed liens on taxpayers' accounts while the taxpayers were in bankruptcy. TIGTA also identified taxpayers' accounts that were at risk of having their rights violated because a bankruptcy freeze code was not posted to their accounts in a timely manner. One factor that might have contributed to delays is the untimely resolution of mismatches on the Potentially Invalid Taxpayer Identification Number report. This report is generated daily and identifies cases where the bankruptcy freeze code failed to post to the taxpayer's account because Master File information (e.g., identification numbers and names) did not match the Bankruptcy Court data received and input to the Automated Insolvency System.

The second area where improvements are necessary involved holding managers more accountable for initiating bankruptcy closing actions in a timely manner. Failure to initiate bankruptcy closing actions in a timely manner affects the IRS' ability to collect taxes and also can place undue hardship and burden on taxpayers by withholding refunds. As of June 28, 2008, TIGTA identified 2,442 taxpayers' accounts in which closing actions had not been initiated within 30 calendar days of the Bankruptcy Courts' closing determination.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Operation Manager, Centralized Insolvency Operation, 1) develop and implement guidance for the identification and correction of potential lien stay violations when establishing bankruptcy cases on the Automated Insolvency System, 2) improve the Centralized Insolvency Operation function Weekly Inventory Reports to include aging information on taxpayers accounts, 3) enhance efforts to resolve freeze codes that do not post to accounts by ensuring that managers consistently work Potentially Invalid Taxpayer Identification Number reports, and 4) evaluate the frequency, consistency, and effectiveness of team manager reviews of the quality and timeliness of bankruptcy closing actions in future operational reviews.

In their response to the report, IRS officials agreed with the recommendations and have taken or plan to take appropriate corrective actions.

READ THE FULL REPORT

To view the report, including the scope, methodology, and full IRS response, go to:

<http://www.treas.gov/tigta/auditreports/2009reports/200930036fr.pdf>.

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