TD P 15-71

The Collection Inventory Replacement Initiative Was Generally Effective; However, Additional Attention Is Needed

June 2003

Reference Number: 2003-30-113

TD P 15-71

INSPECTOR GENERAL
for TAX
ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

June 6, 2003

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION

Gordon C. Milbourn III

FROM: Gordon C. Milbourn III
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report - The Collection Inventory Replacement Initiative Was Generally Effective; However, Additional Attention Is Needed (Audit # 200230020)

This report presents the results of our review of the Internal Revenue Service's (IRS) Collection revenue officer inventory replacement initiative. The overall objective of this review was to determine whether the Small Business/Self-Employed (SB/SE) Division's Compliance function has taken effective steps to implement the revenue officer inventory replacement phase of the Collection reengineering blueprint.[1]

In summary, the revenue officer inventory replacement initiative was generally effective. The IRS removed approximately 33,000 lower risk cases from active inventories. This should allow revenue officers to concentrate their efforts on cases with a higher likelihood of collection.

However, several changes and/or refinements would increase the effectiveness of the Collection revenue officer inventory replacement initiative. First, approximately 3,700 higher risk cases were also included in the shelved cases. This occurred because there was confusion about the criteria for shelving some higher risk cases. A judgmental sample[2] of 74 of these higher risk cases identified 22 cases (30 percent) that should not have been shelved. Second, an analysis of shelved cases in excess of

[1] The IRS initiated a study of how the Collection function operates and sought ways to improve its effectiveness.
[2] A judgmental sample does not allow any inference to the entire universe of cases.

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(b)(2),(b)(7)(E) identified 7 cases with various risk codes, which were also shelved. Finally, some lower risk cases were shelved that later met higher risk definitions due to timing issues and risk code definition changes; however, there was no systemic method to reclassify a case once assigned to a revenue officer.

We recommended that the Director, Compliance Policy, SB/SE Division, establish more effective procedures for communicating with field personnel. We also recommended that the Director, Workload and Selection Development, SB/SE Division, re-assign to revenue officers cases we identified that were inappropriately shelved, have the field review shelved cases in which the taxpayer requested assistance, and consider permitting systemic or procedural risk-code changes after case assignment to revenue officers to account for recent tax modules.[3]

Management's Response: IRS management generally agreed with our findings. They agreed to establish a single channel of communications to better convey directives involving large and complex initiatives and maintain communication and feedback. They also agreed to reactivate some cases and to initiate a systems change request to ensure that the compliance risk of an assigned case is updated to reflect new or changed data that increases its score. However, they did not agree to have their field staff review 1,739 shelved high risk code cases and apply their September 19, 2002 memorandum's procedures to their disposition because of existing problems with erroneous high risk code case assignments and the "labor-intensive requirement to research these cases." While we continue to believe our recommendation is worthwhile, we do not intend to elevate our disagreement concerning this issue to the Department of the Treasury for resolution. In addition, although management took issue with the measurable impact of our recommendations, they did not disagree with the gross amount of tax due from the identified erroneously shelved cases. They concurred with our assessment that the net amount collectable is in question due to a variety of reasons. Management's response to the draft report is included as Appendix VI.

IRS management has requested that this report be designated as "Limited Official Use", because they believe that public knowledge of their procedures for working certain cases, while shelving other cases, could negatively affect collection efforts.

The Treasury Inspector General for Tax Administration (TIGTA) has also designated this report as Limited Official Use (LOU) pursuant to Treasury Directive TD P-71-10, Chapter III, Section 2, "Limited Official Use Information and Other Legends" of the Department of Treasury Security Manual. Because this document has been designated LOU, it may only be made available to those officials who have a need to know the information contained within this report in the performance of their official duties. This report must be safeguarded and protected from unauthorized disclosure; therefore, all

[3] Part of a taxpayer's account, which reflects the tax data for one tax class and one tax period.

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requests for disclosure of this report must be referred to the Disclosure Unit within the TIGTA's Office of Chief Counsel.

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 Richard Dagliolo, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs), at (631) 654-6028.

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The Collection Inventory Replacement Initiative Was Generally Effective; However, Additional Attention Is Needed

Background

The Internal Revenue Service (IRS) has indicated that it has been dealing with a significant and on-going imbalance between the Compliance Collection inventory and the resources available to work that inventory. The IRS has also indicated that in some field offices, large hold files[1] existed and low-priority[2] work was assigned to revenue officers.

To help alleviate this imbalance and to concentrate the efforts of approximately 3,500 revenue officers on the most potentially productive casework, the IRS initiated a study of how the Collection function operates and sought ways to improve its effectiveness.

As part of the reengineering blueprint – Phase I, the Deputy Director, Compliance Policy, issued guidelines on November 1, 2001, for replacing non-productive case inventory. This case inventory exchange is referred to as the revenue officer inventory replacement initiative. The objective of the revenue officer inventory replacement initiative was to exchange low-priority Collection cases in active inventory with more productive cases, thus putting available resources to their most productive use. As part of the overall reengineering effort, new risk codes were developed for Collection cases that refer to the likelihood of collection for each case if the taxpayer is not contacted quickly.

The revenue officer inventory replacement initiative instructions specify that any Collection case meeting the higher risk designations of b)(2),(b)(7)(E) [redacted] will remain in active inventory. The remainder of the inventory should be shelved.[3]

Implementation of the revenue officer inventory replacement initiative was originally scheduled to begin

[1] Hold files are for cases that cannot be assigned in less than 30 days.
[2] Low-Priority Cases: Cases that are deemed to have a low likelihood of collection.
[3] Shelved cases are cases closed and no longer in active inventory.

October 31, 2001, and conclude December 14, 2001, but was extended until January 31, 2002. However, as of September 19, 2002, the ability to shelve cases had not yet been systematically blocked on the Integrated Collection System (ICS).[4] Approximately 37,000 cases were shelved by June 17, 2002, with the majority of cases (approximately 90 percent) shelved by the end of January 2002. See Appendix V for more details.

We conducted this review at the Small Business/Self-Employed (SB/SE) Division Headquarters, New Carrollton, Maryland; and the Nashville, Tennessee, and Los Angeles, California, Area Offices from February through September 2002. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors are listed in Appendix II.

The Revenue Officer Inventory Replacement Initiative Reduced the Volume of Lower Risk Cases in the Active Collection Case Inventory

The revenue officer inventory replacement initiative resulted in the shelving of approximately 33,000 lower risk cases (b)(2),(b)(7)(E) [redacted] within revenue officers' and managers' hold file inventories between October 2001 and June 2002. As part of this process, Collection Field function (CFf) personnel were directed to review all cases coded as (b)(2),(b)(7)(E) [redacted] in active inventory and shelve those cases with low collection potential.

Procedures allowed the CFf to keep lower priority cases in their inventory if they met certain criteria. We reviewed a sample of 121 lower risk cases still in inventory within the 2 area offices and found that overall, they met 1 or more of the criteria for retaining lower risk cases within their assigned inventories. The criteria included reasons such as the case was: near resolution, affiliated with 1 or more higher risk cases (b)(2),(b)(7)(E) [redacted], or a high profile case.

[4] A computer system that is used for Collection case inventory processing.

Many Higher Risk and Large Dollar Cases Were Also Shelved

Although lower risk cases were removed from inventory when appropriate, higher risk and large dollar cases were sometimes inappropriately removed. As a result, the IRS may not be able to collect the taxes due on these accounts. We identified 3,749 higher risk cases (b)(2),(b)(7)(E) (b)(2),(b)(7)(E) that were shelved from October 2001 through June 2002. According to management's directives, these cases were to remain in active inventory, and the authority to shelve cases expired January 31, 2002. Inappropriate shelving mostly occurred in (b)(2),(b)(7)(E) (b)(2),(b)(7)(E) cases. Out of the 3,749 nationwide higher risk cases shelved, 1,739 (46 percent) cases, representing approximately $73.12 million, were (b)(2),(b)(7)(E)

Some CFf group managers believed the authorizing memorandum allowed them to use their individual judgment regarding the shelving of cases, while others followed its direction verbatim. CFf personnel stated that they were uncertain how to handle some unique situations and that the many methods of communication (memorandums, E-mails, Website, and voice messaging system) used throughout the process added to their confusion.

Collection management and CFf personnel acknowledged that communication was confusing during the revenue officer inventory replacement initiative, which apparently led to the inappropriate and inadvertent shelving of cases. As a result, Collection management issued several memoranda[5] near the conclusion of our fieldwork, providing more specific instructions to field personnel for handling Collection cases within their inventories. Because of this confusion, and as identified in separate analyses by the Treasury Inspector General for Tax Administration and the

[5] Memoranda dated July 31, 2002, August 2, 2002, and September 19, 2002, from the Deputy Director, Compliance Policy regarding: revenue officer inventory replacement, treatment of taxpayers requesting assistance, and Federal Employee/Retiree Delinquency Initiative (FERDI) cases.

IRS, a significant number of cases were inappropriately shelved.

Almost 30 percent of the cases reviewed were improperly shelved

We reviewed a judgmental sample[6] of 74 out of approximately 570 higher risk cases (b)(2),(b)(7)(E) [redacted] shelved within 2 area offices. The sample was comprised of a judgmental selection of cases that we selected and a sample that Collection management previously reviewed.

We determined that 22 (30 percent) of these 74 cases, representing approximately $1.25 million, should not have been shelved. For example, (b)(3):26 U.S.C. 6103,(b)(7)(C) [redacted] In addition, revenue officers did not always conduct sufficient research before shelving cases. CFf personnel re-opened 20 of the 22 cases during the course of our review, leaving [redacted] The remaining 52 cases from our sample either did not meet established exceptions to shelving criteria, or did not demonstrate reasonable collection potential.

(b)(3):26 U.S.C. 6103,(b)(7)(C)

Of the 74 higher risk cases (b)(2),(b)(7)(E) [redacted] shelved within 2 area offices, 50 (68 percent) were risk code (b)(2),(b)(7)(E) [redacted] 14 (28 percent) of the 50 should not have been shelved. CFf personnel regarded many (b)(2),(b)(7)(E) [redacted] not to be higher risk cases due to (b)(2),(b)(7)(E) [redacted] The Deputy Director, Compliance Policy, was aware that there were problems with cases being erroneously transferred from the

[6] A judgmental sample does not allow any inference to the entire universe of cases.

[7] An Offer-In-Compromise is an agreement between the IRS and the taxpayer to settle their tax liability for a lesser amount in return for payment or an agreed payment schedule.

Automated Collection System[8] to the field and issued a policy memorandum on September 19, 2002, that re-emphasized the importance of all taxpayer requests for assistance and gave the field specific instructions for the disposition of such cases.

A separate Internal Revenue Service analysis showed that 14 percent of higher risk cases were improperly shelved

Collection management also conducted a separate analysis during early 2002 and determined that 15 (14 percent) out of a sample of 111 higher risk cases were improperly shelved. CFf personnel re-opened 9 of the 15 cases, representing $576,869. Six of these cases, representing approximately $2.46 million, have not yet been re-opened.

One possible reason for the different percentages between our analysis (30 percent) and the IRS' analysis (14 percent) might have been because management's analysis only covered 1 month, while ours covered almost 8 months. However, both reviews indicated that some higher risk cases were inappropriately shelved.

Large dollar cases were shelved

In a separate judgmental sample from the 2 area offices, we reviewed 40 large dollar cases (aggregate balance due (b)(2),(b)(7)(E) [redacted] out of approximately 300 such cases. We determined that 10 (25 percent) of the 40 cases, representing approximately $4.6 million, should not have been shelved for various reasons, (b)(2),(b)(7)(E) [redacted] CFf personnel re-opened 5 of the 10 cases identified during our review, representing approximately $1.75 million. In an August 2, 2002, memorandum from the Deputy Director, Compliance

[8] A telephone contact system where telephone assistors collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.

Policy, all cases with a balance due over [redacted] that were in the Queue,[9] regardless of risk code, were to be assigned to revenue officers' active inventories.

Using computer analysis of nationwide data provided by the IRS of cases shelved during October 2001 to June 2002, we identified 7 large dollar cases with balances due greater than [redacted] that were shelved. [redacted] The 6 remaining shelved cases represented $104,710,301, as of April 15, 2003. We did not have case files to determine if these cases were inappropriately shelved, as we did during our case reviews in the area offices; therefore, we have included them to be re-assigned in our recommendation. The November 2001 authorizing memorandum did not preclude the shelving of large dollar cases. However, using only minimal resources, the IRS could assign the remaining 6 cases to revenue officers to ensure that cases over [redacted] do, in fact, have a low potential for collection.

In summary, 1,753 cases representing $180 million[10] are possibly at risk if the IRS does not take action to ensure that potentially collectible revenues are pursued. However, we realize that not all of the balances due will likely be collected because some taxpayers may not be able to pay the full amount due. Twenty-six cases, representing $8.9 million, have already been re-opened. Finally, cases that were inadvertently closed, although the taxpayer may have requested contact, can result in negative taxpayer relations, which is inconsistent with the IRS' goal of improved customer service.

Recommendations

1. The Director, Compliance, SB/SE Division, who is responsible for formulating short-range and long-

[9] An automated holding file of unresolved cases.
[10] See Recommendations 2 (14 cases, $107.2 million) and 3 (1,739 cases, $73.1 million), as well as Appendix IV, for more detail.

range program strategies, policies, and objectives, should establish procedures for more effectively communicating directives when implementing large and complex initiatives such as the inventory replacement initiative. The Director should also establish more effective procedures to maintain communication and feedback throughout the implementation process with field personnel.

Management's Response: The Deputy Director, Compliance Policy, will establish a single channel of communications to better convey directives involving large and complex initiatives and maintain communication and feedback.

2. The Director, Centralized Workload and Selection Development, SB/SE Division, who is responsible for the routing of Collection work, should ensure that the 14 cases,[11] representing $107.2 million, are re-assigned to revenue officers to fully assess their collection potential.

Management's Response: The Director, Centralized Workload Selection and Delivery, has reviewed and will reactivate cases with assessed values consistent with their current policy that have not already been re-activated.

3. The Director, Centralized Workload and Selection Development, SB/SE Division, who is responsible for the routing of collection work, should have the field review the 1,739 shelved cases designated as (b)(2),(b)(7)(E) and apply the September 19, 2002, memorandum's prescribed procedures regarding their disposition.

Management's Response: IRS management disagreed with this recommendation to re-open these cases.

[11] The 14 cases are identified as follows: (b)(3):26 U.S.C. 6103,(b)(7)(C) 6 IRS analysis cases (page 5), and 6 large dollar cases (page 5).

Management believes the risk that the taxpayer actually requested assistance may be "relativity low" due to existing problems of erroneous (b)(2),(b)(7)(E) [redacted] case assignments, that many taxpayers would have already reestablished contact with the IRS, and that the effort to research these cases would be labor-intensive.

Office of Audit Comment: While we agree that researching these cases would be time consuming, these are cases in which IRS records indicated that the taxpayer needs assistance. Not attempting to contact them is inconsistent with the IRS' goal of improved customer service.

Some Shelved Lower Risk Cases Now Meet Higher Risk Definitions Due to Timing Issues and Risk Code Definition Changes

Using computer analysis, we reviewed nationwide data provided by the IRS of cases shelved during the period October 2001 to June 2002. We identified 75 out of approximately 3,500 (b)(2),(b)(7)(E) [redacted] cases shelved that later met the higher risk (b)(2),(b)(7)(E) [redacted] definitions. These 75 cases represented approximately $4.6 million. The revenue officer inventory replacement initiative instructions specify that any Collection case meeting the higher risk designations of (b)(2),(b)(7)(E) [redacted] will remain in active inventory. The shelving criteria allowed cases designated as (b)(2),(b)(7)(E) [redacted] to be shelved.

This problem exists because Entity risk codes could not be changed either systemically or manually once cases were assigned to revenue officers. Cases were locked at the lower risk code numbers, although other tax modules posted afterward. For example, if a case was assigned to a revenue officer during October 2001, that case may have appropriately been assigned a (b)(2),(b)(7)(E) [redacted] at that time. However, (b)(2),(b)(7)(E) [redacted] will not change even if another tax module[12] was subsequently issued that would have otherwise increased this case's (b)(2),(b)(7)(E) [redacted]

[12] Part of a taxpayer's account, which reflects the tax data for one tax class and one tax period.

(b)(2),(b)(7)(E)

We also determined that 106 of approximately 2,600 [redacted] shelved[13] later met the [redacted] which were to be retained in inventory according to management's directives. These cases represent approximately $34 million. Collection management indicated that the [redacted] had changed during the shelving period. This change may have contributed to the inconsistency in risk classification. However, we did not independently verify this as a cause of the misclassification.

(b)(2),(b)(7)(E)

When higher risk cases are not properly identified and assigned to revenue officers, the CFf is not working the accounts that they have determined to be the most in need of collection action and is inadvertently shelving cases with collection potential.

Recommendation

4. The Director, Centralized Workload and Selection Development, SB/SE Division, who is responsible for the routing of Collection work, should consider permitting risk codes to be systematically or manually upgraded after having been assigned to a revenue officer to prevent higher risk cases from being improperly shelved.

Management's Response: The Director, Centralized Workload Selection and Delivery, will initiate a systems change request to ensure that the compliance risk of an assigned case is updated to reflect new or changed data that would increase its score.

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[13] Source: Nationwide Entity data provided by the IRS.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether the Small Business/Self-Employed (SB/SE) Division's Compliance function has taken effective steps to implement the revenue officer inventory replacement phase of the Collection reengineering blueprint.[1]

Scope and Limitations of Case Reviews:

A portion of our audit involved taxpayer case reviews. Due to the length of time initially required by the Internal Revenue Service (IRS) to gather data of cases shelved nationwide and our desire to provide results to the IRS as quickly as possible, we elected to use judgmental samples of cases shelved and cases remaining in active inventory from the Nashville, Tennessee, and Los Angeles, California, Area Offices. These offices were selected because they represented an office with few higher risk cases shelved proportionate to the number of cases shelved, and an office with many higher risk cases shelved proportionate to the number of cases shelved. Once gathered, Collection function management provided a database of all cases shelved. Appendix IV includes additional information regarding our case reviews and database analysis.

In order to accomplish our overall objective, we completed the following sub-objectives and performed the following tests:

I. Determined whether Collection function management took effective steps to ensure that non-priority cases within the active inventory were identified and closed, and that priority cases were retained.

   A. Interviewed selected field office personnel to determine how the inventory replacement was implemented.

   B. Evaluated the population of shelved cases during October 2001 through June 2002 and determined whether they met the criteria for this closing action. We accepted the data provided by the IRS as the entire universe of cases shelved in accordance with this initiative. We used computer analysis to review the 37,141 cases that were shelved from October 27, 2001, to June 17, 2002. We also performed case analysis on judgmental samples[2] of 74 of 569 higher risk cases and 40 of 296 large dollar (aggregate balance due (b)(2),(b)(7)(E) [redacted] cases from the 2 area offices.

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[1] The Internal Revenue Service initiated a study of how the Collection function operates and sought ways to improve its effectiveness.

[2] A judgmental sample does not allow any inference to the entire universe of cases.

C. Determined whether lower risk cases remained in active inventory and the reasons they were retained. We reviewed a judgmental sample of 121 lower risk cases still in inventory.

D. Interviewed the management review team assigned to review Collection inventory levels beginning February 2002.

II. Ascertained whether Collection function management had effective controls to ensure that work assigned to the SB/SE Division's Collection function, during and subsequent to the inventory replacement, met the higher risk definitions as set forth in Compliance Policy's memorandum dated November 1, 2001, regarding revenue officer inventory replacement.

A. Interviewed appropriate Collection personnel at all levels to ascertain management's appraisal of the overall effectiveness of the inventory replacement effort.

B. Determined whether work assigned to the SB/SE Division's Collection function, subsequent to the inventory replacement, met the higher risk definitions and whether cases were being closed using Transaction Code (TC) 530, Closing Code (cc) 39 or TC 598, cc 57.

Appendix II

Major Contributors to This Report

Richard J. Dagliolo, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs)
Parker F. Pearson, Director
Gary Swilley, Audit Manager
Joseph Cooney, Senior Auditor
Cynthia Dozier, Senior Auditor
Philip A. Smith, Senior Auditor
Rashme Sawhney, Auditor
Jeffrey Williams, Computer Specialist

Appendix III

Report Distribution List

Commissioner N:C
Deputy Commissioner N:DC
Acting Deputy Commissioner, Small Business/Self-Employed Division S
Director, Compliance, Small Business/Self-Employed Division S:C
Deputy Director, Compliance Policy, Small Business/Self-Employed Division S:CP
Director, Centralized Workload and Selection Development, Small Business/Self-Employed Division S:C:CS
Deputy Chief Financial Officer, Department of the Treasury
Audit Liaison:
Commissioner, Small Business/Self-Employed Division S

Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. We realize that not all of the balances due will likely be collected because some taxpayers may be unable to pay the full amount due. These benefits will be incorporated into our Semiannual Report to the Congress.

Type and Value of Outcome Measure:

- Rights and Entitlements – Potential; $73,123,555;[1] 1,739 taxpayer accounts (see page 3).

Methodology Used to Measure the Reported Benefit:

Using a database program, we sorted national Entity[2] data provided by the Internal Revenue Service (IRS) of cases shelved during the period October 2001 to June 2002, by risk codes, to isolate the (b)(2),(b)(7)(E) [redacted] cases shelved with their balances due. Out of the 3,749 nationwide higher risk cases shelved, 1,739 cases representing $73,123,555 were (b)(2),(b)(7)(E) [redacted]

Type and Value of Outcome Measure:

- Increased Revenue – Potential; $1,248,148; 22 taxpayer accounts (see page 3).

(b)(2),(b)(7)(E)

Methodology Used to Measure the Reported Benefit:

We reviewed a combined judgmental sample of 74 higher risk cases shelved (b)(2),(b)(7)(E) [redacted] [redacted] of approximately 570 higher risk cases shelved from the Nashville, Tennessee, and Los Angeles, California, Area Offices. We chose 30 of 62 cases shelved by 1 group manager whom we interviewed during the week of April 8, 2002, from a list provided by an IRS analyst in Nashville. We also reviewed 44 higher risk cases from a sample of 50 (higher and lower risk) shelved cases that had been previously selected and reviewed by a Los Angeles IRS analyst.

Using Taxpayer Identification Numbers (TIN), we researched each case's history on the Integrated Collection System (ICS)[3] and each case's balance due on the Integrated Data Retrieval System (IDRS).[4] We reviewed the revenue officer comments on the ICS for indicators about each case, such as [redacted] (b)(2),(b)(3):26 U.S.C. 6103

We reviewed the command codes on the IDRS that indicated when cases were shelved, when (b)(2),(b)(3):26 U.S.C. 6103 [redacted]

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[1] Dollars associated with taxpayer rights and entitlements outcome measures are not included in the total potential increased tax revenue estimate of $116,068,946. Also see the schedule on page 16 for more detail.

[2] The Entity management system is a computer system that is used for managing the Collection case inventory.

[3] A computer system that is used for Collection case inventory processing.

[4] IRS computer system capable of retrieving or updating stored information; works in conjunction with a taxpayer's account records.

(b)(2),(b)(3):26 U.S.C. 6103 [redacted] We determined that 22 of these 74 cases, representing $1,248,148, should not have been shelved.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; $2,460,618; 6 taxpayer accounts (see page 3).

Methodology Used to Measure the Reported Benefit:

Collection function management determined that 15 case shelvings were inappropriate or without explanation (and therefore improper). Management already re-opened 9 of these 15 cases, leaving 6 cases needing to be re-opened. We reviewed these cases August 22, 2002, on IDRS for their balances due and for their status as re-opened or not.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; $1,750,680; 5 taxpayer accounts (see page 3).

Methodology Used to Measure the Reported Benefit:

We reviewed a combined sample of 40 of 296 large dollar cases shelved from the Nashville and Los Angeles Area Offices. We chose 20 of 48 cases shelved by 4 group managers whom we interviewed during the week of April 15, 2002, from a list provided by Collection function personnel in Los Angeles. We also reviewed a sample of 20 of approximately 90 large dollar cases shelved from the Nashville Area Office. Nine of these 20 cases were shelved by a group manager whom we interviewed during the week of April 8, 2002. The other 11 cases were selected from an ICS database of large dollar cases that was provided by Collection function management. No estate cases were selected.

Using TINs, we researched each case's history on ICS and each case's balance due on IDRS. We reviewed the revenue officer comments on ICS for indicators about each case. [redacted] (b)(2),(b)(3):26 U.S.C. 6103

We reviewed the command codes on IDRS that indicate when cases were shelved, when (b)(2),(b)(3):26 U.S.C. 6103 [redacted] Collection Field function personnel re-opened 5 (representing $1,750,680) of the 10 cases identified during our review.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; $110,609,500; 7 taxpayer accounts (see page 3).

Methodology Used to Measure the Reported Benefit:

Using a database program, we sorted national Entity data provided by Collection function management of cases shelved during the period October 2001 to June 2002 by balances due. We identified 7 large dollar cases with balances due (b)(2),(b)(7)(E) [redacted] that were shelved representing $110,609,500. We reviewed the command codes on IDRS that indicate when [redacted] (b)(2),(b)(3):26 U.S.C. 6103 (b)(2),(b)(3):26 U.S.C. 6103 [redacted] The 6 remaining shelved cases represented $104,710,301, as of April 15, 2003.

The following schedule provides a reconciliation of the number of taxpayer accounts and balances due included within the outcome measures and contained within the report.

Summary of Taxpayer Accounts and Balances Due

	Cases Still To Be Re-Assigned (Recommendation #2)		Cases Already Re-Assigned		Total Outcome Measures	
Finding # 2	**# of Cases**	**$ Amount**	**# of Cases**	**$ Amount**	**# of Cases**	**$ Amount**
(b)(2),(b)(7)(E) [redacted]	1,739	$ 73,123,555			1,739	N/A
Higher Risk Sample of 74: IRS Analysis: Large Dollar Sample of 40: Large Dollar National Analysis: (04/15/03)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Totals:	14	$ 107,203,568	26 (Report, page 6)	$ 8,805,378	40 (Transmittal, page 2)	$ 110,008,946
Cases Possibly at Risk - Totals:	1,753 (Report, page 6)	$ 180,327,123				

Source: Auditors' workpapers.

(b)(3):26 U.S.C. 6103
(b)(3):26 U.S.C. 6103
(b)(3):26 U.S.C. 6103
(b)(3):26 U.S.C. 6103
(b)(3):26 U.S.C. 6103
(b)(3):26 U.S.C. 6103

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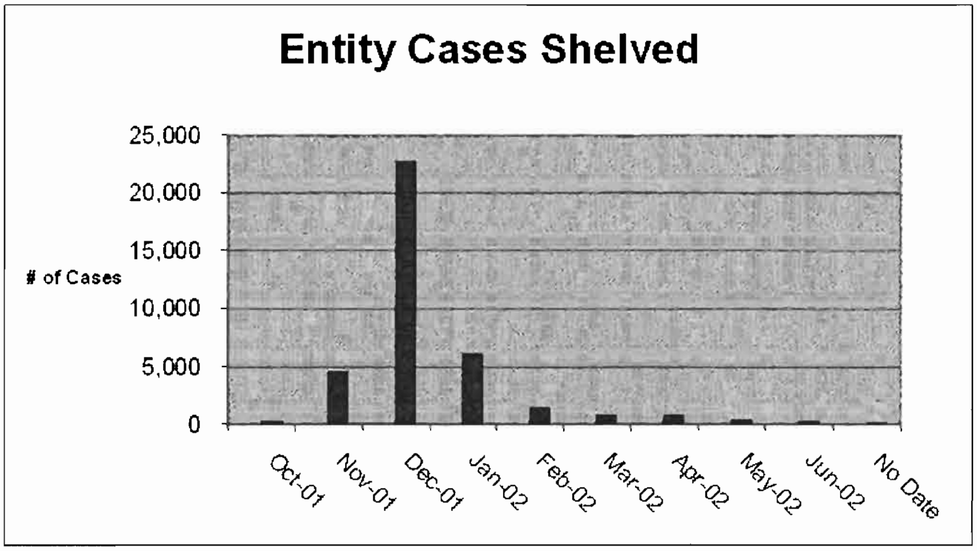
Appendix V

Cases Shelved Data By Month



Source: Nationwide Entity[1] data provided by the Internal Revenue Service.

	Number of Cases	Percent of Total
Cases Shelved from **October** 27, 2001, to end of month:	189	.5%
Cases Shelved During **November** 2001:	4,485	12.1%
Cases Shelved During **December** 2001:	22,759	61.3%
Cases Shelved During **January** 2002:	6,056	16.3%
Cases Shelved During **February** 2002:	1,414	3.8%
Cases Shelved During **March** 2002:	766	2.1%
Cases Shelved During **April** 2002:	759	2.0%
Cases Shelved During **May** 2002:	368	1.0%
Cases Shelved during **June**, to June 17, 2002:	243	.7%
No shelving date provided:	102	.3%
Totals	37,141	100%

[1] The Entity management system is a computer system that is used for managing the Collection case inventory.

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Appendix VI

Management's Response to the Draft Report

COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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

RECEIVED
MAY 15 2003

MAY 12 2003

MEMORANDUM FOR TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

FROM: Dale F. Hart *Dale F. Hart*
Acting Commissioner
Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – The Collection Inventory Replacement Initiative Was Generally Effective; However, Additional Attention Is Needed (Audit # 200230020)

I have reviewed your report of the Collection Inventory Replacement Initiative. We implemented this initiative to put the most potentially productive casework in field collection inventory and concentrate our limited resources on those taxpayers with the highest compliance risk. We generally agree with your findings, however, we believe the report requires a "Limited Official Use" designation under Treasury Directive (TD) P-171-10. Public knowledge of our procedures for working certain cases, while shelving other cases, could negatively affect collection efforts. Therefore, the entire report should not be available to the public, as is your usual practice when a report contains this type of information.

If you disagree, we request the opportunity to provide a line-by-line redaction for portions covered under the Treasury Directive.

We agree to the following points in your recommendations:

- Establish procedures to better communicate directives involving large and complex initiatives such as the inventory replacement process. Additionally, establish a better process to maintain communication and feedback throughout the implementation process with field personnel.
- When accounts contain unresolved collection issues, review and reactivate cases with assessed values consistent with our current policy that was not in place when the exchange of inventory began. We have safeguards incorporated into our systems that automatically reactivate shelved cases under certain conditions. These safeguards can also apply to many cases cited in your revised report. They address recidivism by looking for a new balance due or failure to file

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a return circumstance. They also contain a systemic (annual) match on internal documents that looks for new sources we can levy.

For both safeguards, we apply a new compliance risk determination based on the updated conditions and assign or work the case accordingly. The total value of the six cases recently added to your report that we agreed to reactivate, and the six cases that our safeguards have already reactivated, represent about 99 percent of the adjusted outcome measures.

- Systemically reclassify assigned revenue officer inventory when the compliance risk score of the case has been raised using new or updated elements not present when we determined the current score.

We disagree with your recommendation to have our field staff review 1,739 shelved cases and apply our September 19, 2002 memorandum's procedures to their disposition. As stated in your report, we initiated our own review on the adherence to the exchange process, which included many of these case types. This review, along with on-going studies and feedback from the frontline field resources, drove the decision to update our policy.

We believe the risk is relatively low to leave these cases in place when you factor in the labor-intensive requirement to research these cases using three separate data systems. If the taxpayer actually requested revenue officer assistance, we are reasonably confident that many of these taxpayers would have already reestablished contact with IRS. For erroneous assignments, our new policy allows the front-line manager to move the case to the queue for later assignment based on its true compliance risk score and available resources. We believe that our safeguards to reactivate shelved cases should mitigate some of the concerns associated with this recommendation.

We also disagree with the measurable impact of your recommended corrective actions. As your report states, not all the balance due accounts will be collected because some taxpayers will not be able to pay the full amount due. We can track results of the 12 out of 14 cases cited in your report, the six that we agreed to reactivate, and the six that our safeguards have already reactivated. However, from a measurable standpoint, when we actually select and work these cases, we are also not selecting or working others. As a result, we measure the narrow focused outcome of choosing that particular case and how much we did or did not collect, not whether another case would have been a better choice.

We would like to clarify a statement in the report to ensure the reader does not reach conclusions inconsistent with the facts. In the opening summary paragraph, the report states our belief that we face an ongoing imbalance between the collection workload and resources available to work that inventory. In the Collection Field function, that resource is our revenue officers. The next sentence says, "To alleviate this imbalance,

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the IRS recently implemented the Collection Reengineering Phase I revenue officer inventory replacement, which is a component of the overall Collection Reengineering blueprint." We did not expect the exchange process to cure this imbalance. As with

most process improvements, we expected efficiency and taxpayer and employee satisfaction gains, thus enabling us to narrow the gap.

Our comments on your recommendations follow:

RECOMMENDATION 1
The Director, Compliance, Small Business/Self-Employed Division, should establish procedures for more effectively communicating directives when implementing large and complex initiatives such as the inventory replacement initiative. Additionally, establish a better process to maintain communication and feedback through any implementation process with field personnel.

CORRECTIVE ACTIONS
We will develop and initiate procedures to establish a single channel of communications working in conjunction with the Deputy Director Field Operations.

IMPLEMENTATION DATE
Proposed: September 15, 2003

RESPONSIBLE OFFICIALS
Deputy Director, Compliance Policy

CORRECTIVE ACTION MONITORING PLAN
The Director, Centralized Workload Selection and Delivery, with the assistance of the Director, Payment Compliance will advise the Deputy Director Compliance Policy of any delays in completing the corrective action.

RECOMMENDATION 2
The Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division, who is responsible for the routing of Collection work, should ensure that the 14 cases, representing $107.2 million, are reassigned to revenue officers to fully assess their collection potential.

CORRECTIVE ACTIONS
We reviewed and will reactivate six of the 14 cases identified. These cases meet our current criteria. Our safeguards already have reactivated six additional cases. These 12 cases represent 99 percent of your total outcome measures.

(b)(2),(b)(3):26 U.S.C. 6103,(b)(7)(C),(b)(7)(E)

(b)(2),(b)(3):26 U.S.C. 6103,(b)(7)(C),(b)(7)(E)

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IMPLEMENTATION DATE
Proposed: September 15, 2003

RESPONSIBLE OFFICIAL
Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN
The Program Manager, Collection Case Selection, will advise the Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division, of any delays in completing the corrective action.

The Program Manager will also track these 12 cases and report on their outcome to the Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division.

RECOMMENDATION 3
The Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division, who is responsible for the routing of collection work, should have the field review the 1,739 shelved cases designated as (b)(2),(b)(7)(E) and apply the September 19, 2002, memorandum's prescribed procedures regarding their disposition.

CORRECTIVE ACTIONS
We disagree with this recommendation.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
N/A

CORRECTIVE ACTION MONITORING PLAN
N/A

RECOMMENDATION 4
The Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division, who is responsible for the routing of Collection work, should consider permitting risk codes to be systematically or manually upgraded after having been assigned to a revenue officer to prevent higher risk cases from being improperly shelved.

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CORRECTIVE ACTIONS
We will initiate a systems change request to ensure we update the compliance risk of an assigned case to reflect new or changed data that increases its score.

IMPLEMENTATION DATE
Proposed: January 15, 2004

RESPONSIBLE OFFICIAL
Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN
The Program Manager, Collection Case Selection will advise the Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division of any delays in completing the corrective action.

If you have any questions, please contact me at (202) 622-0600 or Joseph R. Brimacombe, Deputy Director, Compliance Policy, Small Business/Self-Employed Division at (202) 283-2200.