



*Fiscal Year 2008 Statutory Review of
Compliance With Lien Due Process
Procedures*

March 27, 2008

Reference Number: 2008-30-082

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

Redaction Legend:

1 = Tax Return/Return Information



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

March 27, 2008

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION

Michael R. Phillips

FROM:

Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT:

Final Audit Report – Fiscal Year 2008 Statutory Review of Compliance
With Lien Due Process Procedures (Audit # 200830001)

This report presents the results of our review of the Internal Revenue Service's (IRS) lien due process procedures. The overall objective of this review was to determine whether IRS Notice of Federal Tax Lien filings and notices of taxpayers' appeal rights complied with legal guidelines set forth in Internal Revenue Code Section (I.R.C. §) 6320.¹ The Treasury Inspector General for Tax Administration is required by law to determine annually whether lien notices sent by the IRS comply with the legal guidelines in I.R.C. § 6320.² This is our tenth annual audit to determine the IRS' compliance with the law and with its own related internal guidelines when sending lien notices.

Impact on the Taxpayer

After filing Notices of Federal Tax Lien, the IRS must notify the affected taxpayers in writing within 5 business days of the lien filings. However, it has not always complied with this statutory requirement and did not always follow its own internal guidelines for notifying taxpayer representatives of the filing of lien notices. Therefore, some taxpayers' rights to appeal the lien filings may have been jeopardized, and others may have had their rights violated when the IRS did not notify their representatives of lien filings, or provided information to individuals not authorized to represent the taxpayers.

¹ I.R.C. § 6320 (Supp. V 1999).

² I.R.C. § 7803(d)(1)(A)(iii) (Supp. V 1999).



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Synopsis

The IRS attempts to collect Federal taxes due from taxpayers by sending letters, making telephone calls, and meeting face to face with taxpayers. When its initial contacts do not result in the successful collection of an unpaid tax, the IRS has the authority to attach a claim (called a Federal Tax Lien) to the taxpayer's assets for the amount of the unpaid tax.³ It files a Notice of Federal Tax Lien, which notifies interested parties that a lien exists. Since January 19, 1999, I.R.C. § 6320 has required the IRS to notify taxpayers in writing within 5 business days of the filing of a Notice of Federal Tax Lien.

The IRS may not have complied with the law in all cases. Our review of a statistically valid sample of 150 Federal Tax Lien cases identified 145 cases (97 percent) for which the IRS did mail lien notices correctly and in a timely manner, as required by I.R.C. § 6320 and internal procedures. For the other 5 lien notices (3 percent), we could not determine if the law was complied with because the IRS could not provide proof of mailing.

In 145 of 150 Federal Tax Lien cases, the IRS maintained records supporting the timely issuance of lien notices.

When an initial lien notice is returned because it could not be delivered and a different address is available for the taxpayer, the IRS does not always meet its statutory requirement to send the lien notice to the taxpayer's last known address. For 29 (7 percent) of 400 cases, employees did not research IRS computer systems for different addresses. For 104 (26 percent) of the 400 cases, the research was not performed within 5 business days. We also identified two cases for which a new lien notice should have been sent to the taxpayer at the updated address because the IRS systems listed the address prior to the lien filing. These two cases could involve legal violations because the IRS did not meet its statutory requirement of sending lien notices to the taxpayer's last known address.

Also, the IRS did not always follow its own internal guidelines for notifying taxpayer representatives of the filing of lien notices. For 12 (40 percent) of the 30 cases in which the taxpayer had an authorized representative at the time of the lien actions, the IRS did not notify the taxpayer's representative of the lien filing. In addition, on two cases it sent notifications to representatives not authorized to receive such information.

³ I.R.C. § 6321 (1994).



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Recommendations

We recommended that the Director, Collection, 1) consult with the IRS Office of Chief Counsel to identify any actions necessary to correct the potential legal violations we identified in this audit; 2) provide better oversight to ensure IRS employees are properly controlling and processing returned mail as undelivered, researching computer systems for correct addresses, and resending lien notices; and 3) ensure that employees are notifying taxpayer representatives of lien filings and safeguarding taxpayer information from inadvertent disclosures, and computer enhancements are uploading power-of-attorney information as intended.

Response

IRS management agreed with the findings and recommendations. Management has consulted with their Office of Chief Counsel and will issue new Collection Due Process notices to the seven taxpayers and will review procedures for maintaining certified mailing lists. Further, management revised the Internal Revenue Manual requiring the requesting employee or function to conduct research for the correct addresses so appropriate actions can be taken on undelivered mail. Management will determine if the Inbound Return Receipt Notice Delivery System can include lien notice processing and if additional computer enhancements are required to ensure proper uploading of power-of-attorney information. Management's complete response to the draft report is included as Appendix VII.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Margaret E. Begg, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-5959.



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Abbreviations

ACS	Automated Collection System
ALS	Automated Lien System
ICS	Integrated Collection System
IDRS	Integrated Data Retrieval System
I.R.C.	Internal Revenue Code
IRS	Internal Revenue Service



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Background

The Internal Revenue Service (IRS) attempts to collect Federal taxes due from taxpayers by sending letters, making telephone calls, and meeting face to face with taxpayers. When initial contacts do not result in the successful collection of an unpaid tax, the IRS has the authority to attach a claim to the taxpayer's assets for the amount of unpaid tax.¹ This claim is referred to as a Federal Tax Lien. The IRS files in appropriate local government offices a Notice of Federal Tax Lien,² which notifies interested parties that a lien exists.

Since January 19, 1999, Internal Revenue Code Section (I.R.C. §) 6320³ has required the IRS to notify taxpayers in writing within 5 business days of the filing of a Notice of Federal Tax Lien. The IRS is required to notify taxpayers the first time a Notice of Federal Tax Lien is filed for each tax period. The lien notice, Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320⁴ (Letter 3172), is used for this purpose and advises taxpayers that they have 30 calendar days, after that 5-day period, to request a hearing with the IRS Appeals office. The lien notice indicates the date on which this 30-day period expires.

The IRS must notify taxpayers in writing of the filing of a Federal Tax Lien within 5 business days of the filing.

The law also requires that the lien notice explain, in simple terms, the amount of unpaid tax, administrative appeals available to the taxpayer, and provisions of the law and procedures relating to the release of liens on property. The lien notice must be given in person, left at the taxpayer's home or business, or sent by certified or registered mail to the taxpayer's last known address.

The lien processing operation has been centralized at the Cincinnati, Ohio, Campus,⁵ except for the printing and mailing of taxpayer lien notices. The centralization took most of Fiscal Year 2005 to be implemented. The Correspondence Production Services Sites in Detroit, Michigan, and Ogden, Utah, are responsible for the printing and mailing of taxpayer lien notices. They have a goal of reducing late filings of lien notices by using mail facilities located at their sites. IRS personnel take the mail lists and lien notices to the Mail unit, where they are metered and prepared daily for shipment to the main United States Postal Service. In the in-house mail

¹ Internal Revenue Code Section 6321 (1994).

² Notice of Federal Tax Lien (Form 668(Y) (c); (Rev. 10-1999)), Cat. No. 60025X.

³ I.R.C. § 6320 (Supp. V 1999).

⁴ Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320 (Letter 3172 (Rev. 9-2006)), Cat. No. 26767I.

⁵ A campus is the data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

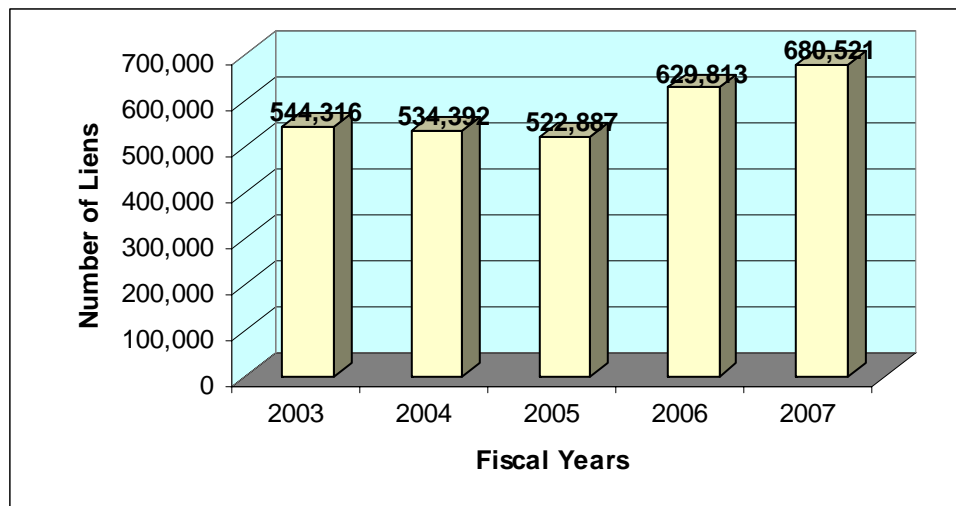


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facility, a United States Postal Service employee is responsible for date stamping the certified mail lists. After these mail lists are stamped, an IRS employee sends them to the Centralized Lien Unit via overnight mail. A synopsis of the IRS collection and lien filing processes is included in Appendix V. A description of IRS computer systems used in the filing of liens is included in Appendix VI.

The IRS has been relatively consistent in the number of Federal Tax Liens it has filed to protect the Federal Government's interest. As shown in Figure 1, the number of Federal Tax Liens filed decreased slightly in Fiscal Years 2004 and 2005, then increased in Fiscal Years 2006 and 2007.

Figure 1: Liens Filed



Source: IRS Data Book 2006 and IRS personnel.⁶

The Treasury Inspector General for Tax Administration is required to determine annually whether, when filing Notices of Federal Tax Lien, the IRS complied with the law regarding the notifications of affected taxpayers and their representatives.⁷ We performed our audit work in the Small Business/Self-Employed Division Office of Collection Policy in Washington, D.C., and the Centralized Lien Unit in Covington, Kentucky, during the period August 2007 through January 2008. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed

⁶ The IRS Data Book is published annually by the IRS and contains statistical tables and organizational information on a fiscal year basis.

⁷ I.R.C. § 7803(d)(1)(A)(iii) (Supp. V 1999).



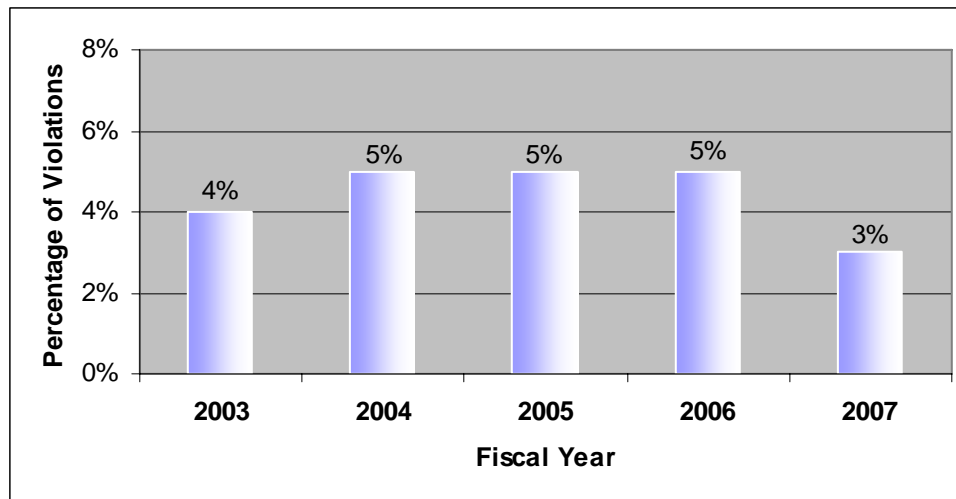
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information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Results of prior Treasury Inspector General for Tax Administration reviews

This is our tenth annual audit to determine if the IRS complied with the legal requirements of I.R.C. § 6320 and its own related internal guidelines for filing Notices of Federal Tax Lien. In prior years, we reported the IRS had not yet achieved full compliance with the law and its own internal guidelines. This year our statistically valid sample did not identify any Federal Tax Lien cases that were not mailed in a timely manner. However, for 5 of the lien notices (3 percent), we could not determine if the IRS complied with the law because the IRS could not provide proof of mailing. Figure 2 shows the percentages of potential violations of taxpayer rights we identified during our prior annual audits.

Figure 2: Potential Violations of Taxpayer Rights



Source: Treasury Inspector General for Tax Administration mandatory lien reports issued during Fiscal Years 2003-2007.

The IRS National Headquarters conducted a notice compliance review

In February 2007, the IRS performed a review of Centralized Lien Unit activities to ensure IRS procedures are being followed and taxpayers' rights are being protected. This was the second review performed since the lien operation was centralized at the Cincinnati Campus and was conducted by Headquarters Campus Compliance Service and Collection Policy staff.

For the IRS compliance review of the Centralized Lien Unit operations, Automated Lien System (ALS)⁸ programmers randomly selected 100 serial lien identification numbers from liens filed

⁸ See Appendix VI for descriptions of the IRS computer systems used in the filing of Notices of Federal Tax Lien.



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between July 2006 and January 2007. They selected a judgmental sample of 65 numbers and obtained the corresponding certified mail lists for review. The sample was extracted so cases were reviewed from all areas. The IRS review found that all lien notices were issued in a timely manner.

IRS personnel selected another random sample of 50 lien notices from January 2007 to evaluate the processing of undelivered lien notices. The Centralized Lien Unit appropriately researched all 50 lien notices and input the undelivered mail status to the ALS database for all 50 notices.



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Results of Review

Lien Notices Were Mailed Timely, but Proof of Mailing Could Not Always Be Located

A review of a statistically valid sample of 150 Federal Tax Lien cases identified 145 (97 percent) for which the IRS did mail correctly and in a timely manner the taxpayers' notices of a lien filing and appeal rights, as required by I.R.C. § 6320 and internal procedures. For the other 5 lien notices (3 percent), we could not determine if the law was complied with because the IRS could not provide proof of mailing.

I.R.C. § 6320 requires the IRS to notify taxpayers in writing within 5 business days of the filing of a Notice of Federal Tax Lien. Because of difficulties in obtaining and controlling the filing dates from numerous courthouses across the country, IRS procedures require that the notices be mailed within 5 business days after they have been printed for mailing to the courthouses. IRS procedures also require retention of the date-stamped copy of the certified mail lists for 10 years after the end of the processing year.

We did not identify any untimely notifications. This result is an improvement in the timeliness of mailing lien notices since completion of our prior audit, which had shown 3 percent of the lien notices were sent late (projected to a potential 15,847 late notices). However, the five lien notices without proof of mailing was a slight increase over the four lien notices identified in our prior audit. We project that 22,642 taxpayers might not have been provided with lien notices, causing potential legal violations of taxpayers' rights.

Management could not explain why the mail lists were not available. Without the dated proof of mailing, the IRS may be unable to protect itself against a taxpayer's claim that he or she did not receive timely notice of the lien and was unaware that a Federal Tax Lien existed against his or her assets.

Recommendation

Recommendation 1: The Director, Collection, should consult with the IRS Office of Chief Counsel to identify any actions necessary to correct the potential legal violations we identified in this audit and ensure that IRS employees are properly maintaining the Certified Mail Lists.

Management's Response: IRS management agreed with the recommendation. Management has consulted with the IRS Office of Chief Counsel and was advised to 1) send new Collection Due Process notices to the seven taxpayers identified in the report, 2) review procedures for maintaining certified mail lists including scanning the



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certified mail lists to a searchable file, and 3) ensure that procedures for maintaining certified mail lists include safeguards to verify that all date-stamped certified lists have been received from the print site and that all lists have been scanned.

Ineffective Working of Undelivered Lien Notices Resulted in Violations of Taxpayers' Rights

IRS procedures require that employees send another lien notice to a new address if 1) the originally mailed notice is returned as undelivered mail, 2) research confirms the original lien notice was not sent to the last known address, and 3) a different address is available for the taxpayer. Employees are responsible for certain actions when notices are returned as undeliverable. They should research the IRS computer system within 5 business days to ensure the address on the original lien notice is correct. If the employee cannot find a new address on the computer system, the undelivered lien notice will be destroyed and the case will be closed.

If the address on the notice is not the last known address and a different address was in effect prior to issuance of the original lien notice, employees should issue a new notice to the better address. A new notice (Letter 3172) is created by using an option in the ALS.

For the period July 23 through August 3, 2007, we selected a judgmental sample of 400 undelivered lien notices from the Cincinnati Campus. The sample included only returned mail identified as undelivered. It did not include returned mail identified as refused or unclaimed. For these 400 cases, we reviewed computer system audit trails to determine whether IRS employees performed any research on IRS computer systems to determine whether the addresses were correct on the originally mailed notices. Employees were not always researching IRS computer systems to determine whether taxpayer addresses on undelivered lien notices were correct. The 400 cases were handled by requesting employees as follows:

- For 29 cases (7 percent), employees did not research IRS computer systems for a different address.
- For 104 cases (26 percent), employees performed the required research but not within 5 business days of receipt of the returned notice (average was 8.6 business days, ranging from 6 days to 31 days).
- For 267 cases (67 percent), employees performed the required research within 5 days of receipt of the returned notice.

Our research also identified 39 cases for which the address on IRS computer systems and the original lien notice did not agree. The ALS was properly documented for 35 cases to show that the original lien notice was returned as undelivered. For 20 of the 39 cases, the address on the IRS computer system was updated after the original lien notice was sent to the taxpayer. Therefore, no additional action was required. For the remaining 19 cases (49 percent), the address was updated prior to the mailing of the original lien notice, and a new lien notice should



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have been sent to the taxpayer at the updated address. In 17 of the 19 cases, the IRS sent a new lien notice to the taxpayer at the updated address. The two cases for which a new lien notice was not sent could involve potential legal violations because the IRS did not meet its statutory requirement of sending each lien notice to the taxpayer's last known address.

Management oversight was not adequate to ensure that returned mail is properly controlled and worked in a timely manner. In addition, the routing of the returned mail to the lien unit could have caused the untimely research of the undelivered mail (i.e., not within the required 5 business days).

Recommendation

Recommendation 2: The Director, Collection, should provide better oversight to ensure that employees are properly controlling and processing returned mail as undelivered, researching computer systems for correct addresses, and resending lien notices.

Management's Response: IRS management agreed with the recommendation. Management plans to 1) complete research on undelivered mail identified as not having research performed and 2) determine the feasibility of reviewing undelivered mail returned to the requesting employee or function and continue to pursue Inbound Return Receipt Notice Delivery System programming. In addition, the Internal Revenue Manual was revised to require undelivered mail be returned to the employee or function requesting the Notice of Federal Tax Lien for proper control and processing. The requesting employee or function is required to research computer systems for a correct address and send the notice to a new address, if appropriate. An ALS programming change currently returns undelivered mail to the requesting employee or function.

Internal Guidelines for Notifying Taxpayer Representatives Were Not Always Followed

Taxpayer representative information is contained on the Centralized Authorization File⁹ that is located on the Integrated Data Retrieval System (IDRS), a system that enables employees to access taxpayer accounts. Using the IDRS, employees can research the Centralized Authorization File to identify the types of authorization given to taxpayer representatives.

Employees responsible for making the lien filing determination are to ensure that all appropriate persons, such as those with a taxpayer's power of attorney, receive a notice of the lien filing and the taxpayer's appeal rights. Specifically, IRS procedures require that a copy of the notice be

⁹ The Centralized Authorization File contains information regarding the types of authorization that taxpayers have given representatives for various modules within their accounts.



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sent to the taxpayer's representative no later than 5 business days after the notice is sent to the taxpayer, when a Notice of Federal Tax Lien is filed.

Revenue officers are also required to document in the case history when they request a lien filing and a lien notice for a taxpayer's representative. Revenue officers' managers are required to examine case files for this documentation during their regular review process.

In August 2006, the IRS implemented the Automated Collection System (ACS) and Integrated Collection System (ICS) interfaces with the ALS. The ACS uploads the taxpayer representative information to ALS, which generates the lien notice. Likewise, the ICS sends taxpayer representative information to the ALS when liens are requested. For these enhancements to work, revenue officers need to keep current data on the ICS and IDRS.

Our review of the statistically valid sample of 150 liens determined 30 involved taxpayers with representatives authorized on the Centralized Authorization File to receive notifications at the time the liens were filed. In 12 (40 percent) of the 30 cases, the ALS records did not indicate that the IRS had sent copies of the lien notices to the representatives. In seven cases, revenue officers did not document that they had requested lien notices be sent to the taxpayer representatives. In the other five cases, the ACS function did not electronically forward the taxpayer representatives' information to the ALS. In addition, on two cases, it sent notifications to representatives not authorized to receive such information. We project that 54,342 taxpayer representatives may not have been provided lien notices, resulting in potential legal violations of taxpayers' rights. We also project that 9,057 taxpayer representatives may have been provided unauthorized lien notices, resulting in potential legal violations of taxpayers' rights.

Although improvements have been made, the systemic changes have had little impact on improving performance. In last year's report, we found 25 cases had taxpayer representatives listed on the Centralized Authorization File. In 15 (60 percent) of the 25 cases, the IRS had no record of sending copies of lien notices to the representatives.

IRS management indicated that lien notices may not have been issued to taxpayer representatives because systemic problems may exist that were not uncovered. Another explanation is that the power-of-attorney information was not input. To obtain more information, the IRS Headquarters Operations function plans to evaluate the effectiveness of the ICS and ACS interface during its annual review of the Centralized Lien Unit operation, which is scheduled to be completed in March 2008.

We also identified two cases in which the IRS sent lien notices to representatives who were not authorized to receive such information. The two liens may have been issued prior to a programming change that matched at least one tax period on the lien to one tax period for the power of attorney. Although the liens were manually input to the ALS, the requesting employee may not have verified that the power-of-attorney information was current.



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For a lien not requested through the ICS, revenue officers should send to the Centralized Lien Unit a request to mail a lien notice to the taxpayer representative. An ICS procedure, created on February 13, 2006, enables revenue officers to request a copy of the Letter 3172 for the taxpayer representative and to send to the Centralized Lien Unit a “secure” email with the taxpayer representative information. The procedures had not changed since the last review.

Inadvertent, improper disclosures include an invalid or incomplete written or oral authorization. While still unauthorized, those disclosures cover cases in which no willfulness of intent is involved. However, public confidence in the ability of the IRS to protect the confidentiality of tax information influences taxpayer compliance. As indicated in IRS guidance, a perception that the IRS is careless in preserving privacy rights could have serious compliance ramifications.

Management oversight did not ensure that revenue officers documented their work or kept Centralized Authorization File data current or that system improvements uploaded these data as planned.

Recommendation

Recommendation 3: The Director, Collection, should provide better oversight to ensure that 1) employees are notifying taxpayer representatives of lien filings and safeguarding taxpayer information from inadvertent disclosures and 2) computer enhancements are uploading power-of-attorney information as intended.

Management’s Response: IRS management agreed with the recommendation. Management plans to 1) establish power of attorney Collection Due Process notice issuance verification procedures for employees requesting Notices of Federal Tax Lien, 2) determine if IRS computer systems have programming that matches Notice of Federal Tax Lien and power-of-attorney tax period authorizations prior to sending notifications to the ALS, 3) request programming enhancements to eliminate potential disclosure issues, if necessary, and 4) determine if additional computer enhancements are required to ensure proper uploading of power-of-attorney information.



Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether IRS Notice of Federal Tax Lien¹ filings and notices of taxpayers' appeal rights complied with legal guidelines set forth in I.R.C. § 6320.² To accomplish the objective, we:

- I. Determined whether taxpayer lien notices related to 150 Notices of Federal Tax Lien filed by the IRS complied with legal requirements set forth in I.R.C. § 6320 (a) and related internal guidelines.
 - A. Selected a statistically valid sample of 150 Federal Tax Lien cases from an ALS³ extract of the 679,273 liens filed by the IRS nationwide between July 1, 2006, and June 30, 2007. We used a statistical sample because we wanted to project the number of cases with errors. We used attribute sampling to calculate the minimum sample size (n),⁴ which we rounded to 150:
$$n = (Z^2 p(1-p))/(A^2)$$

Z = Confidence Level: 90 percent (expressed as 1.65 standard deviation)
p = Expected Rate of Occurrence: 5 percent⁵
A = Precision Rate: ±3 percent
 - B. Validated the ALS extract by comparing the sampled records to online data from the IDRS and by reviewing management system evaluations that covered reliability, completeness, and accuracy.
 - C. Determined whether the sampled liens adhered to legal guidelines regarding timely notifications of lien filings to the taxpayer, the taxpayer's spouse, and/or business partners by reviewing data from the ALS and certified mail lists.
 - D. Assessed the controls and procedures established for transferring, storing, and safeguarding certified mail lists at the Centralized Lien Unit to determine whether enhancements had been implemented since the completion of our prior audit.

¹ Notice of Federal Tax Lien (Form 668(Y) (c); (Rev. 10-1999)), Cat. No. 60025X.

² I.R.C. § 6320 (Supp. V 1999).

³ See Appendix VI for descriptions of IRS computer systems used in the filing of Notices of Federal Tax Lien.

⁴ The formula $n = (Z^2 p(1-p))/(A^2)$ is from *Sawyer's Internal Auditing - The Practice of Modern Internal Auditing*, 4th Edition, pp. 462-464.

⁵ The actual error rate in our prior report was 4.67 percent.



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- E. Determined whether the taxpayer representatives were provided a copy of the lien notices by reviewing data from the ALS, ICS, ACS, and IDRS.
 - 1. Reviewed IDRS screens and Master File⁶ extracts for Centralized Authorization File⁷ indicators (Transaction Code 960) for the sampled cases.
 - 2. Reviewed the ALS history screens for all sampled accounts to determine whether notices were mailed to taxpayer representatives.
 - 3. Reviewed ICS case histories for documentation that taxpayer representatives' name/address information was sent to the Centralized Lien Unit or that the revenue officers had mailed the notices directly to the taxpayer representatives for the sampled cases that did not have a taxpayer representative notification on the ALS histories.
 - 4. Reviewed the ACS case history for documentation that taxpayer representatives' name/address information was electronically transmitted to the Centralized Lien Unit.
- F. Provided all exception cases to Office of Collection Policy for agreement to potential violations and corrective actions if appropriate.
- II. Evaluated the procedures for processing lien notices⁸ that are returned as undelivered.
 - A. Selected a judgmental sample of 400 undelivered lien notices from a total of 1,417 received during the 2-week period of July 23 through August 3, 2007, and recorded the taxpayer's name, address, Social Security Number, and serial lien identification number. The judgmental sample included only returned mail identified as undelivered. It did not include returned mail identified as refused or unclaimed. A judgmental sample was used because the IRS did not control the receipt of undelivered mail and the test was conducted to show control weaknesses for which management needed to take corrective action.
 - B. Researched the Master File using the IDRS command code INOLES and determined whether the address on the Master File matched the address on the undelivered lien notice for each sampled case.
 - C. Reviewed taxpayer audit trails and determined whether IRS employees performed the required Master File research using the IDRS for each sampled case.

⁶ The Master File is the IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

⁷ The Centralized Authorization File contains information regarding the types of authorization that taxpayers have given representatives for various modules within their accounts.

⁸ Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320 (Letter 3172 (Rev. 9-2006)), Cat. No. 26767I.



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- D. Researched the ALS database and determined whether the lien notice was mailed to the updated address and was identified as undelivered on the ALS, and whether a new lien notice was sent to the taxpayer's updated address for each sampled case.
- III. Determined whether internal guidelines had been implemented or modified since completion of our last audit by discussing procedures and controls with appropriate IRS personnel in the Office of Collection Policy.
- IV. Determined the status of planned ICS and ACS system enhancements and any problems encountered.



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Appendix II

Major Contributors to This Report

Margaret E. Begg, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs)

Carl Aley, Director

Edward Gorman, Audit Manager

Darryl Roth, Senior Auditor

Lawrence R. Smith, Senior Auditor

Stephen Elix, Student Trainee



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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Acting Chief of Staff
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Director, Campus Compliance Services, Small Business/Self-Employed Division SE:S:CCS
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Collection Policy, Small Business/Self-Employed Division SE:S:C:CP
Chief Counsel CC
National Taxpayer Advocate NTA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Commissioner, Small Business/Self-Employed Division SE:S



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 Congress.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 22,642 taxpayers may not have been provided Notices of Federal Tax Lien and Your Right to a Hearing Under IRC 6320 (Letter 3172),¹ resulting in potential legal violations of taxpayers' rights (see page 5).

Methodology Used to Measure the Reported Benefit:

From a statistically valid sample of 150 Federal Tax Lien cases, we identified 5 cases (3 percent) for which IRS employees could not provide proof of mailing of the Letters 3172, resulting in potential legal violations of taxpayers' rights (see page 5). The sample was selected based on a confidence level of 90 percent, a precision rate of ± 3 percent, and an expected rate of occurrence of 5 percent. We projected the findings to the total population provided by the IRS of 679,273 Notices of Federal Tax Lien generated by the ALS between July 1, 2006, and June 30, 2007. We estimated that similar taxpayer rights could have been affected in 22,642 lien notices ($5/150 \times 679,273$). We are 90 percent confident that the range of notices with similar problems is between 6,213 and 39,072.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; two taxpayers were not provided Letters 3172, resulting in potential legal violations of taxpayers' rights (see page 6).

Methodology Used to Measure the Reported Benefit:

In a judgmental sample of 400 undelivered lien notices, we determined that the IRS did not send notices to the updated addresses of 2 taxpayers.

Taxpayer rights could be affected because a taxpayer not receiving a notice or receiving a late notice might be unaware of the right to appeal or might receive less than the 30-calendar day

¹ Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320 (Letter 3172 (Rev. 9-2006)), Cat. No. 26767I.



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period allowed by the law to request a hearing. In addition, taxpayer rights could be affected when the taxpayer appeals the filing of the lien and the IRS denies the request for the appeal.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 54,342 taxpayer representatives may not have been provided Notices of Federal Tax Lien and Your Right to a Hearing Under IRC 6320 (Letter 3172),² resulting in potential legal violations of taxpayers' rights (see page 7).

Methodology Used to Measure the Reported Benefit:

From a statistically valid sample of 150 Federal Tax Lien cases, we identified 30 cases (20 percent) that involved taxpayers with representatives authorized to receive notifications at the time the ALS actions filed the liens. In 12 (40 percent) of the 30 cases (see page 7), the ALS record did not indicate that the IRS had sent copies of the lien notices to the representatives. The sample was selected based on a confidence level of 90 percent, a precision rate of ± 3 percent, and an expected rate of occurrence of 5 percent. We projected the findings to the total population provided by the IRS of 679,273 Notices of Federal Tax Lien generated by the ALS between July 1, 2006, and June 30, 2007. We estimated that similar taxpayer rights could have been affected in 54,342 lien notices ($12/150 \times 679,273$). We are 90 percent confident that the range of notices with similar omissions is between 29,512 and 79,172.

Type and Value of Outcome Measure:

- Taxpayer Privacy and Security – Potential; 9,057 taxpayer representatives may have been provided unauthorized Notices of Federal Tax Lien and Your Right to a Hearing Under IRC 6320 (Letter 3172),³ resulting in potential violations of taxpayers' privacy (see page 7).

Methodology Used to Measure the Reported Benefit:

From a statistically valid sample of 150 Federal Tax Lien cases, we identified 30 cases (20 percent) that involved taxpayers with representatives authorized to receive notifications at the time the ALS actions filed the liens. In 2 (7 percent) of the 30 cases (see page 7), the ALS records indicate that the IRS had sent copies of the lien notices to unauthorized representatives.

² Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320 (Letter 3172 (Rev. 9-2006)), Cat. No. 26767I.

³ Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320 (Letter 3172 (Rev. 9-2006)), Cat. No. 26767I.



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The sample was selected based on a confidence level of 90 percent, a precision rate of ± 3 percent, and an expected rate of occurrence of 5 percent. We projected the findings to the total population provided by the IRS of 679,273 Notices of Federal Tax Lien generated by the ALS between July 1, 2006, and June 30, 2007. We estimated that similar taxpayer privacy rights could have been affected in 9,057 lien notices ($2/150 \times 679,273$). We are 90 percent confident that the range of notices with similar errors is between 0 and 19,555.



Appendix V

Synopsis of the Internal Revenue Service Collection and Lien Filing Processes

The collection of unpaid tax begins with a series of letters (notices) sent to the taxpayer advising of the debt and asking for payment of the delinquent tax. The IRS computer systems are programmed to mail these notices when certain criteria are met. If the taxpayer does not respond to these notices, the account is transferred for either personal or telephone contact.

- IRS employees who make personal (face-to-face) contact with taxpayers are called revenue officers and work in various locations. The ICS¹ is used in most of these locations to track collection actions taken on taxpayer accounts.
- IRS employees who make only telephone contact with taxpayers work in call sites in Customer Service offices. The ACS is used in the call sites to track collection actions taken on taxpayer accounts.

When these efforts have been taken and the taxpayer has not paid the tax liability, designated IRS employees are authorized to file a lien by sending a Notice of Federal Tax Lien² to appropriate local government offices. Liens protect the Federal Government's interest by attaching a claim to the taxpayer's assets for the amount of unpaid tax. The right to file a Notice of Federal Tax Lien is created by I.R.C. § 6321 (1994) when:

- The IRS has made an assessment and given the taxpayer notice of the assessment, stating the amount of the tax liability and demanding payment.
- The taxpayer has neglected or refused to pay the amount within 10 calendar days after the notice and demand for payment.

When designated employees request the filing of a Notice of Federal Tax Lien using either the ICS or the ACS, the ALS processes the lien filing requests from both Systems. In an expedited situation, employees can manually prepare the Notice of Federal Tax Lien. Even for manually prepared liens, the ALS controls and tracks the liens and initiates subsequent lien notices³ to notify responsible parties of the lien filings and of their appeal rights. The ALS maintains an

¹ See Appendix VI for detailed descriptions of IRS computer systems used in the filing of Notices of Federal Tax Lien.

² Notice of Federal Tax Lien (Form 668(Y) (c); (Rev. 10-1999)), Cat. No. 60025X.

³ Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320 (Letter 3172 (Rev. 9-2006)), Cat. No. 26767I.



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electronic database of all open Notices of Federal Tax Lien and updates the IRS' primary computer records to indicate that a Notice of Federal Tax Lien has been filed.

Most lien notices are mailed to taxpayers by certified or registered mail, rather than delivered in person. To maintain a record of the notices, the IRS prepares a certified mail list (United States Postal Service Form 3877), which identifies each notice that is to be mailed. The notices and a copy of the certified mail list are delivered to the United States Postal Service. A United States Postal Service employee ensures that all notices are accounted for, date stamps the list, and returns a copy to the IRS. The stamped certified mail list is the only documentation the IRS has that certifies the date on which the notices were mailed. IRS guidelines require that the stamped certified mail list be retained for 10 years after the end of the processing year.



Appendix VI

Internal Revenue Service Computer Systems Used in the Filing of Notices of Federal Tax Lien

The Automated Collection System (ACS) is a computerized call site inventory system that maintains balance-due accounts and return delinquency investigations. ACS function employees enter all of their case file information (online) on the ACS. Lien notices requested using the ACS are uploaded to the ALS, which generates the Notices of Federal Tax Lien¹ and related lien notices and updates the IRS' primary computer files to indicate that Notices of Federal Tax Lien have been filed.

The Automated Lien System (ALS) is a comprehensive database that prints Notices of Federal Tax Lien and lien notices, stores taxpayer information, and documents all lien activity. Lien activities on both ACS and the ICS cases are controlled on the ALS by Technical Support or Case Processing functions at the Cincinnati, Ohio, Campus.² Employees at the Cincinnati Campus process Notices of Federal Tax Lien and lien notices and respond to taxpayer inquiries using the ALS.

The Integrated Collection System (ICS) is an IRS computer system with applications designed around each of the main collection tasks such as opening a case, assigning a case, building a case, performing collection activity, and closing a case. The ICS is designed to provide management information, create and maintain case histories, generate documents, and allow online approval of case actions. Lien requests made using the ICS are uploaded to the ALS. The ALS generates the Notices of Federal Tax Lien and related lien notices and updates the IRS' primary computer files to indicate Notices of Federal Tax Lien have been filed.

The Integrated Data Retrieval System (IDRS) is an online data retrieval and data entry system that processes transactions entered from terminals located in campuses and other IRS locations. It enables employees to perform such tasks as researching account information, requesting tax returns, entering collection information, and generating collection documents. The IDRS serves as a link from campuses and other IRS locations to the Master File³ for the IRS to maintain accurate records of activity on taxpayers' accounts.

¹ Notice of Federal Tax Lien (Form 668(Y) (c); (Rev. 10-1999)), Cat. No. 60025X.

² A campus is the data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

³ The Master File is the IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.



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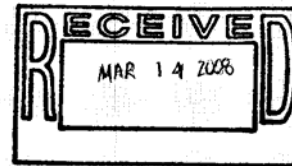
Appendix VII

Management's Response to the Draft Report



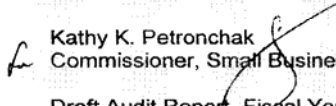
COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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



March 14, 2008

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR ADUIT

FROM:  Kathy K. Petronchak
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report- Fiscal Year 2008 Statutory Review of
Compliance with Lien Due Process Procedures
(Audit No. 200830001)

We have reviewed the draft report titled, "Fiscal Year 2008 Statutory Review of Compliance with Lien Due Process Procedures." We are pleased the report recognizes that the IRS has maintained a decrease in potential legal violations.

The report addresses findings and recommendations regarding IRS processes for mailing Collection Due Process (CDP) notices, maintaining proof of mailings to taxpayers, and resolving undelivered mail. The report also states that issuing copies of CDP notices to the Powers of Attorney (POAs) continues to pose concerns after implemented systemic enhancements. We will continue to review and enhance our system and manual processes to eliminate errors.

We agree with the findings and recommendations and concur with your calculation and presentation methodology of the benefits to tax administration described in Appendix IV of your report.

Attached is a detailed response outlining our planned corrective actions. If you have any questions, please call me at (202) 622-0600 or Fred Schindler, Director, Collection Policy, Small Business/Self-Employed Division, at (202) 283-7650.

Attachment



Fiscal Year 2008 Statutory Review of Compliance With Lien Due Process Procedures

Attachment

RECOMMENDATION 1:

The Director, Collection, Small Business/Self-Employed Division, should consult with the IRS Office of Chief Counsel to identify any actions necessary to correct the potential legal violations we identified in this audit and ensure IRS employees are properly maintaining the Certified Mail Listings.

CORRECTIVE ACTIONS:

The report stated that, in a sample of 150 cases, five lien notices (3%) had no proof of mailing and two notices were not mailed to the last known address. We consulted with IRS Office of Chief Counsel and were advised to:

1. Send new Collection Due Process (CDP) notices to the seven taxpayers identified in the report.
2. Review procedures for maintaining certified mail lists including scanning the certified mail lists to a searchable file.
3. Ensure that procedures for maintaining certified mail listings include safeguards to verify that all date-stamped certified listings have been received from the print site and that all listings have been scanned.

IMPLEMENTATION DATES:

1. New CDP notices were issued February 4, 2008, for six of the identified cases; [REDACTED]
2. By August 15, 2008, conduct Continued Professional Education training to address procedures for maintaining certified mail lists.
3. By August 15, 2008, ensure procedures are in place that include use of Control D to verify receipt of date-stamped listings and accuracy and completeness of scanned listings.

RESPONSIBLE OFFICIAL

Director, Campus Compliance Services, Small Business/Self Employed Division

CORRECTIVE ACTION MONITORING PLAN

The SB/SE Director, Filing and Payment Compliance will monitor the corrective actions as part of our internal management control system.

RECOMMENDATION 2:

The Director, Collection, Small Business/Self-Employed Division, should provide better oversight to ensure employees are properly controlling and processing returned mail as undelivered, researching computer systems for correct addresses, and resending lien notices.



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CORRECTIVE ACTIONS:

1. Complete research on undelivered mail identified as not having research performed.
2. The Internal Revenue Manual was revised to require undelivered mail be returned to the employee or function requesting the Notice of Federal Tax Lien (NFTL) for proper control and processing. The requesting employee or function is required to research computer systems for a correct address and send a new address, if appropriate. An Automated Lien System (ALS) programming change currently returns undelivered mail to the requesting employee or function.
3. Determine the feasibility of reviewing undelivered mail returned to the requesting employee or function and continue to pursue Inbound Return Receipt Notice Delivery System (IRRNDS) programming.

IMPLEMENTATION DATES:

1. On February 9, 2008, we completed research on the 29 cases identified. In all instances, a new address was not on the Integrated Data Retrieval System and, therefore, a new CDP was not required.
2. On November 30, 2007, the Internal Revenue Manual was revised. As a result, the employee or function requesting the NFTL is currently responsible for resolving undelivered mail, including documenting the notice status on master file, researching systems for a correct address, and resending the notice, if appropriate. Further, on August 6, 2007, an ALS programming enhancement changed the Centralized Lien Unit return address for undelivered CDP notices to the Post of Duty address of the requesting employee or function.
3. By January 15, 2009, if feasible, establish procedures for reviewing undelivered mail returned to employees or functions. In addition, determine if the IRRNDS programming can be revised for ALS use.

RESPONSIBLE OFFICIAL

Director, Collection, Small Business/Self Employed Division

CORRECTIVE ACTION MONITORING PLAN

The SB/SE Director, Collection Policy will monitor the status and advise the SB/SE Director Collection of any delays in implementing the corrective actions.

RECOMMENDATION 3:

The Director, Collection, Small Business/Self-Employed Division, should provide better oversight to ensure (1) employees are notifying taxpayer representatives of lien filings and safeguarding taxpayer information from inadvertent disclosures and (2) computer enhancements are uploading power-of-attorney information as intended.

CORRECTIVE ACTIONS:

1. Establish Power of Attorney (POA) CDP notice issuance verification procedures for employees requesting NFTLs, determine if IRS systems have programming that matches NFTL and POA tax period authorizations prior to sending



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notifications to the ALS and request programming enhancements to eliminate potential disclosure issues, if necessary.

2. Determine if additional computer enhancements are required to ensure proper uploading of POA information.

IMPLEMENTATION DATES

1. By January 15, 2009, identify verification method; determine if the Automated Collection System has a NFTL and POA tax period matching process, request computer enhancements, if necessary.
2. By January 15, 2009, if required, identify computer programming enhancements.

RESPONSIBLE OFFICIAL

Director, Collection, Small Business/Self Employed Division

CORRECTIVE ACTION MONITORING PLAN

The SB/SE Director, Collection Policy will monitor the status and advise the SB/SE Director, Collection of any delays in implementing the corrective actions.