

**Information on the Centralized Authorization
File Is Often Not Accurate or Complete**

August 2004

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



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

August 25, 2004

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION
DIRECTOR, OFFICE OF PROFESSIONAL RESPONSIBILITY

FROM:

(for) Gordon C. Milbourn III
Acting Deputy Inspector General for Audit

David R. Dwyer

SUBJECT:

Final Audit Report - Information on the Centralized Authorization
File Is Often Not Accurate or Complete (Audit # 200310037)

This report presents the results of our review of the Internal Revenue Service's (IRS) Centralized Authorization File (CAF). The overall objective of this review was to determine whether the processes and procedures established for the CAF were effective to maintain the accuracy of the database and to prevent unauthorized disclosure of taxpayer information. Because the information on the CAF is used by the IRS to communicate with taxpayers' representatives about confidential tax matters, it is important that the information on the CAF is accurate and complete to prevent disclosure of tax information to unauthorized individuals and to ensure timely communication with taxpayers or representatives.

In summary, we determined that the records on the CAF often contained incomplete or incorrect information. In a statistical sample of 500 records, there were 202 with discrepancies between information submitted on the authorization forms and information on the CAF. The factors that caused these discrepancies included representatives submitting new contact information on the authorization forms without indicating whether the information on the CAF should be updated, recent changes to IRS procedures and to the CAF database, and transcription errors on the part of IRS employees. In addition, the process to ensure authorization forms are transmitted timely to the CAF units was not adequate.

In the same sample of 500 records, there were 27 representatives who did not appear to be authorized to practice before the IRS under the designation or jurisdiction listed on their authorization forms.

Finally, there were 308 disciplinary actions taken against practitioners during the period January 15, 1999, through December 31, 2003; 228 (74 percent) were not properly or accurately recorded on the CAF.

We recommended the Director, Customer Account Services, Small Business/Self-Employed (SB/SE) Division, alert CAF processing unit managers that the units are not always following the most recent procedures for adding secondary taxpayer (spouse) information to the CAF and provide training to ensure employees understand and follow the most current procedures for processing taxpayer authorization forms.

We also recommended the Deputy Commissioner for Services and Enforcement ensure timely processing of taxpayer authorization forms by establishing procedures that require all IRS functions to forward these authorization forms to the appropriate CAF processing unit within 24 hours of receipt. The Director, Customer Account Services, SB/SE Division, should also consistently use date stamping and process work within established guidelines in the CAF processing units. In addition, the Deputy Commissioner for Services and Enforcement should consider developing a review process to identify whether representatives listed on the Power of Attorney and Declaration of Representative (Form 2848) are authorized to practice before the IRS.

Further, the Director, Customer Account Services, SB/SE Division, should assign responsibility to a national coordinator to update the CAF based on notices from the Office of Professional Responsibility. The Director, Office of Professional Responsibility, should ensure the accuracy and consistency of practitioner actions within the Office's database and web site, Internal Revenue Bulletins, and the CAF by periodically verifying the information.

Management's Response: IRS management agreed with our recommendations and has initiated or is planning to implement corrective actions. Specifically, the IRS plans to alert CAF unit managers to ensure employees are following current procedures and plans to provide training material with current procedures to be delivered during annual training presentations. The IRS also plans to contact Internal Revenue Manual coordinators and functional leadership to request inclusion of a requirement to forward authorization forms to the appropriate CAF processing unit within 24 hours after validation of the information on the form.

Additionally, the IRS has initiated corrective actions for implementation of specific guidelines for capturing the received dates of faxed submissions and date stamping requirements for mail and routed submissions, drafted an interim guidance memorandum outlining procedures for verification of a representative's eligibility, and is in the process of upgrading electronic systems that will compare information on the eligibility of practitioners. The IRS has established a national coordinator who will be responsible for updating the CAF based on notices from the Office of Professional Responsibility. In addition, the Office of Professional Responsibility has updated its web site and is implementing procedures to improve its computer control systems and provide better communication of its disciplinary actions.

Management did not agree with the magnitude of our assessment of the issues regarding different, inaccurate, or incomplete information recorded on the CAF. Management believes it would have been difficult for us to make a conclusive determination on the accuracy of each record because the CAF cannot provide an audit trail to identify all changes that have been made to each CAF record. As such, management believes some discrepancies could have been caused by subsequent updates provided by the taxpayers or their representatives. Accordingly, management did not agree with the estimate we provided in Appendix IV of the total number of taxpayer records affected over a 5-year period. Management's complete response to the draft report is included as Appendix V.

Office of Audit Comment: The errors and inaccuracies identified from our statistical samples were evaluated based on the signed date of the authorization form. Our sample errors or inaccuracies involved an authorization form with a signed date that was more current than the last recorded signed date on the CAF. Therefore, the discrepancies we identified were not caused by subsequent updates by taxpayers or their representatives. Moreover, the IRS quality review system¹ as well as an internal independent review² established that there are problems with the accuracy of information on the CAF. Based on the methodology of our analysis and the results of the IRS' own internal review processes, we believe our estimate of the number of taxpayer records affected is valid.

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 Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

¹ SB/SE Accounts Management Program Analysis System.

² IRS SB/SE Division, "Power of Attorney Independent Review," dated February 6, 2004.

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Background

By law, the Internal Revenue Service (IRS) can disclose tax information to the taxpayer or to a designee or attorney-in-fact of the taxpayer.¹ Individual or business taxpayers can authorize one or more individuals to represent them on tax returns or other tax-related issues including Appeals function, tax court, examination, and collection activity. A taxpayer can also authorize a designee or attorney-in-fact to receive confidential tax information.²

A taxpayer may authorize someone to represent him or her by submitting a Power of Attorney and Declaration of Representative (Form 2848) or a United States Estate (and Generation-Skipping Transfer) Tax Return (Form 706) to the IRS. A taxpayer may authorize the IRS to disclose tax information to a designee by submitting a Tax Information Authorization (Form 8821). Taxpayers also may orally communicate their authorizations to disclose tax information to a designee.

These taxpayer authorization forms are sent directly by the taxpayer or forwarded by an IRS employee to one of three centralized processing units.³ Information from the taxpayer authorization forms is then recorded on a national IRS computer file called the Centralized Authorization File (CAF). The three CAF processing units are part of the Small Business/Self-Employed (SB/SE) Division.

Once information from a taxpayer authorization form is recorded on the CAF, IRS employees are able to determine the scope of authority granted by the taxpayer. It also enables the IRS to direct copies of tax notices and correspondence to a representative using the address on file. In addition, the CAF provides important contact information (telephone and fax numbers) that IRS employees can use to communicate with representatives. If the CAF information is not reliable, the IRS can inadvertently disclose sensitive tax information to individual(s) that are not authorized by the taxpayer.

¹ Internal Revenue Code (I.R.C.) § 6103 (2002).

² I.R.C. § 6103 (c) (2002).

³ The Centralized Authorization File processing units are located in Memphis, Tennessee; Ogden, Utah; and Philadelphia, Pennsylvania.

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Guidelines governing practice before the IRS have been revised for individuals or practitioners representing taxpayers. The Office of Professional Responsibility has the duty of administering and enforcing the regulations governing practice before the IRS. Complaints about practitioners are investigated and can result in censure, suspension, and disbarment if a practitioner is incompetent; is disreputable; violates Department of the Treasury Circular Number 230; or, with intent to defraud, willfully and knowingly misleads or threatens the taxpayer being represented. The Office of Professional Responsibility reports to the Deputy Commissioner for Services and Enforcement.

This review was performed at the Memphis, Ogden, and Philadelphia Accounts Management Centers, the CAF Section of the Detroit Computing Center, the Office of Professional Responsibility in Washington, D.C., and the SB/SE Division in New Carrollton, Maryland, during the period September 2003 through May 2004. 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 to the report are listed in Appendix II.

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Because the information on the CAF is used by the IRS to communicate with taxpayers' representatives about confidential tax matters, it is important that the information on the CAF is accurate and complete to prevent disclosure of tax information to unauthorized individuals and to ensure timely communication with taxpayers or representatives. However, 41 percent of a statistical sample of CAF records contained discrepancies between information on the authorization forms and information on the CAF.

Approximately 1.1 million taxpayer authorization forms were recorded on the CAF during Fiscal Year (FY) 2003. We selected a statistical sample of 500 records and found 202 records with discrepancies between the authorization forms and the CAF. The discrepancies included different, inaccurate, or incomplete information for such items as telephone numbers, fax numbers, addresses, and secondary

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taxpayer (spouse) information. Table 1 provides a summary of the types of discrepancies we identified in the sample.

Table 1: Discrepancies Between Authorization Forms and the CAF

Type of Discrepancy	Count ⁴
Representative's address was different, inaccurate, or incomplete.	85
Representative's telephone number or fax number was different, inaccurate, or incomplete.	70
Secondary taxpayer's (spouse) information was not included or was incomplete on the CAF.	40
Enrollment numbers for Enrolled Agents ⁵ were not included on the CAF.	23
Taxpayer's or representative's name on the authorization form did not match that on the CAF.	20
Other (e.g., certain tax periods were not recorded on the CAF, signature dates were missing).	20

Source: Treasury Inspector General for Tax Administration (TIGTA) review of 500 taxpayer authorization forms submitted during FY 2003 compared to information on the CAF.

Based on our sample results, we estimate approximately 456,000 of the records recorded on the CAF in FY 2003 have discrepancies that could lead to delays in providing information to representatives or inadvertent disclosure of confidential tax information to unauthorized third parties.

There are a number of factors which caused discrepancies between authorization forms and the CAF. These factors included representatives submitting new contact information on the authorization forms without indicating whether the information on the CAF should be updated, recent changes to IRS procedures and to the CAF database, and transcription errors on the part of IRS employees.

Internal Revenue Manual (IRM) procedures for processing taxpayer authorization forms were significantly revised in FYs 2002, 2003, and 2004. The newest revision of the IRM

⁴ There were 202 CAF records identified with 258 inaccuracies. Some of these records contained multiple inaccuracies or incomplete fields.

⁵ An enrolled agent is a tax professional who has demonstrated special competence in tax matters, has applied for enrollment, and has been issued an enrollment card by the IRS.

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should help improve the accuracy of representative contact information recorded on the CAF. It requires CAF processing unit employees to take further action to verify the information provided on an authorization form when the information appears outdated, in error, or incomplete. Those actions will include comparing the date the form was received in the CAF processing unit with the date(s) of the signatures on the form and contacting the representative via telephone, fax, or correspondence.

In March 2003, the CAF database was redesigned and reprogrammed. The database was changed to accommodate secondary taxpayer (spouse) information separately on the CAF. This caused confusion for the CAF processing unit employees as to what action was necessary to correctly input the secondary Power of Attorney requestor to the CAF. In addition, the CAF database was expanded in early 2003 to allow a representative's fax number to be input; however, employees did not always record this fax number on the CAF.

The IRS recently completed its own review of the Power of Attorney process.⁶ Its findings indicated that taxpayers and their representatives are experiencing a high number of problems with the process and the loading of information on to the CAF. The IRS internal review team identified potential actions, such as updating training materials and publishing a desk reference to guide employees, which could help improve the reliability of information on the CAF. The SB/SE Division Customer Account Services function is also planning to develop a communication package with its Taxpayer Education and Communication function, as well as to send brochures explaining the rejection process to taxpayers and their representatives.

Further, the IRS is planning to allow these authorization forms to be filed electronically through its Disclosure Authorization Program. This may help to reduce the percentage of incomplete or inaccurate CAF records, especially those related to incomplete submissions or transcription errors. However, this Program is not available

⁶ IRS SB/SE Division, "Power of Attorney Independent Review," dated February 6, 2004.

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to the general public. Only approved IRS business partners, such as electronic filing tax professionals and payers, are eligible to participate. At the time of this report, the IRS had begun the implementation phase of this Program.

Overall, while the IRS has taken a number of actions to improve the process for validating and inputting the authorization forms, additional action is needed to ensure employees understand and follow the process.

Recommendations

The Director, Customer Account Services, SB/SE Division, should:

1. Alert CAF processing unit managers that the units are not always following the most recent procedures for adding secondary taxpayer (spouse) information to the CAF.

Management's Response: IRS management agreed to remind managers to ensure employees are following the current guidelines for adding secondary taxpayer (spouse) information to the CAF.

IRS management did not agree with the magnitude of our assessment of the issues regarding different, inaccurate, or incomplete information recorded on the CAF. Management believes it would have been difficult for us to make a conclusive determination on the accuracy of each record because the CAF cannot provide an audit trail to identify all changes that have been made to each CAF record. Management stated that the 202 of 500 sample records identified with different, inaccurate, or incomplete information probably overstated the magnitude of the issues because there is currently no audit trail and discrepancies could have been caused by subsequent changes submitted by the originators of the requests. Accordingly, management did not agree with the estimate we provided in Appendix IV of the total number of taxpayer records affected over a 5-year period.

Office of Audit Comment: The errors and inaccuracies identified from our statistical samples were evaluated based on the signed date of the authorization form. Our sample

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errors or inaccuracies involved an authorization form with a signed date that was more current than the last recorded signed date on the CAF. Therefore, the discrepancies we identified were not caused by subsequent updates by taxpayers or their representatives. Moreover, the IRS quality review system⁷ as well as an internal independent review⁸ established that there are problems with the accuracy of information on the CAF. Based on the methodology of our analysis and the results of the IRS' own internal review processes, we believe our estimate of the number of taxpayer records affected is valid.

2. Provide training to ensure employees understand and follow the most current procedures for processing taxpayer authorization forms. Specific training modules should be devoted to adding secondary taxpayer (spouse) information to the CAF and performing further research when information on authorization forms appears outdated, in error, or incomplete to ensure the information is accurate before it is input to the CAF.

Management's Response: IRS management agreed to provide training material to address secondary taxpayer (spouse) information and procedures for researching outdated, erroneous, or incomplete information identified on authorization forms. This material will be provided during annual training. In addition, the IRM is being revised to provide more detailed instructions on these areas.

Based on our statistical sample of 500 taxpayer authorization forms submitted in FY 2003, there was generally not enough information available to determine whether the forms were received and processed timely.

The CAF processing units have established guidelines for time standards but have inconsistent date stamping procedures. Only one CAF processing unit adequately date stamped the taxpayer authorization forms when they arrived in the unit and when the employees completed recording the information to the CAF.

Procedures for Transmitting Forms to the Centralized Authorization File Units Are Not Adequate

⁷ SB/SE Division Accounts Management Program Analysis System.

⁸ IRS SB/SE Division, "Power of Attorney Independent Review," dated February 6, 2004.

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In the one CAF processing unit that did date stamp the forms, employees generally input the form information timely to the CAF. However, some of the other IRS functions that received the authorization forms often took long periods of time to transmit the forms to this CAF processing unit. For example, we found that it took longer than 5 workdays for the functions to forward 38 (21 percent) of the 182 forms in our sample to this CAF processing unit; the average time to forward these 38 forms was 19 days. If forms are not timely sent to a CAF processing unit, representatives may be delayed in receiving taxpayer information and discussing the information with IRS employees.

CAF processing unit managers and personnel stated that the delays in receiving forms from other IRS functions are usually caused by inconsistent procedures and practices in those functions. The IRS internal review team recommended IRS functions implement procedures to forward taxpayer authorization forms to the CAF processing units within 24 hours of receipt. We agree that the IRS should implement this recommendation.

The timely processing of taxpayer authorization forms is important for IRS customer service and helps prevent taxpayer problems. Without consistent procedures and practices to timely process the forms and a means to monitor timeliness, the IRS will not know if its processes are adequate.

Recommendations

3. The Deputy Commissioner for Services and Enforcement should ensure timely processing of taxpayer authorization forms by establishing procedures that require all IRS functions to forward these authorization forms to the appropriate CAF processing unit within 24 hours of receipt.

Management's Response: The Director, Customer Account Services, SB/SE Division, will contact IRM coordinators and functional leadership to establish that authorization forms be forwarded to the appropriate CAF processing units within a specific time frame. The Director will encourage

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the receiving functions to first verify the information on the forms before forwarding them to the CAF units. As the verification process may take more than 1 day, corrective actions will include a requirement to forward each authorization form to the appropriate CAF unit within 24 hours after verification of information on the form.

4. The Director, Customer Account Services, SB/SE Division, should consistently use date stamping and process work within established guidelines in the CAF processing units.

Management's Response: IRS management has revised the IRM guidelines for capturing the received date of faxed submissions and date stamping mail and routed submissions.

Some Representatives on the Centralized Authorization File May Not Be Authorized to Practice Before the IRS

On Form 2848, the IRS instructs taxpayers that the individual they authorize to represent them must be a person eligible to practice before the IRS. The representative named by the taxpayer must sign and date the declaration, enter the designation under which he or she is authorized to practice before the IRS, and provide the state of his or her jurisdiction if he or she is an attorney or Certified Public Accountant. The designations a representative may enter are as follows:

- Attorney.
- Certified Public Accountant.
- Enrolled Agent.
- Officer (of the business represented).
- Full-Time Employee (of the business represented).
- Family Member.
- Enrolled Actuary.
- Unenrolled Return Preparer (with limitations).⁹

The approximately 1.1 million taxpayer authorization forms that were recorded on the CAF during FY 2003 provided authorization for 1.6 million representatives (more than

⁹ An unenrolled return preparer is permitted to represent taxpayers only before customer service representatives, revenue agents, and examination officers, with respect to an examination regarding the return he or she prepared.

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1 representative can be included on the form). Of these representatives, over 1.2 million were listed as Attorneys, Certified Public Accountants, and Enrolled Agents. Our review of the Power of Attorney forms recorded on the CAF indicated that some of these individuals did not accurately record their jurisdiction, authorization level, or status of professional license and may not be authorized to represent taxpayers before the IRS.

In our statistical sample of 500 taxpayer authorization forms submitted in FY 2003, there were 487 representatives who provided their designations as either Attorneys, Certified Public Accountants, or Enrolled Agents authorized to practice before the IRS. Based on our search of public records and an IRS database,¹⁰ there were 27 representatives who did not appear to be authorized to practice before the IRS under the designation or jurisdiction listed on their authorization forms. These 27 representatives recorded inaccurate information or had lapsed professional licenses or certifications; they are representing approximately 25,000 taxpayers before the IRS.

The status of these representatives may cause problems if the taxpayers need to rely on these individuals for representation during the IRS examination or collection process or in the Appeals function or tax court. The IRS currently has no process to verify the accuracy of the professional designations before accepting the Forms 2848. Although the IRS Office of Professional Responsibility will investigate matters such as potential misrepresentation, it relies heavily on IRS employees to review the accuracy of a taxpayer representative declaration and forward identified irregularities for the appropriate disciplinary action(s).

Recommendation

5. The Deputy Commissioner for Services and Enforcement should consider developing a review process to identify whether representatives listed on

¹⁰ Public records include State Bar Associations and State Boards of Accountancy on the Internet. The IRS Office of Professional Responsibility has a database of Enrolled Agents.

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Forms 2848 are authorized to practice before the IRS.
This could include a review of a sample of Forms 2848.

Management's Response: The Director, Payment Compliance, SB/SE Division, has drafted an interim guidance memorandum outlining procedures for verification of a representative's eligibility and status to practice before the IRS prior to forwarding a form to a CAF processing unit. In addition, electronic systems are being upgraded to compare database information on the eligibility and status of practitioners.

Disciplinary Actions Against Practitioners Are Often Not Properly Recorded

The IRS Office of Professional Responsibility administers the laws and regulations governing the practice of tax professionals before the IRS. In FY 2003, it operated with a staff of 27 and a budget of \$2.8 million to carry out its responsibilities.¹¹ One of its key responsibilities is to enforce the regulations governing practice before the IRS, including censure, suspension, and disbarment if a practitioner is incompetent; is disreputable; violates Department of the Treasury Circular Number 230; or, with intent to defraud, willfully and knowingly misleads or threatens the taxpayer being represented.

When the Office of Professional Responsibility takes disciplinary actions, such as censure, suspension, or disbarment, on representatives who practice before the IRS, its policy is to maintain the actions on its own databases, record the information on its web site, and inform the public through Internal Revenue Bulletins. However, our review of the disciplinary actions taken by the Office of Professional Responsibility indicates the IRS did not always record the actions in each of these locations, nor did the CAF units always accurately or timely record these actions on the CAF.

We reviewed 308 disciplinary actions taken between January 1999 and December 2003.¹² Of these 308 actions,

¹¹ The IRS has increased its emphasis on the oversight of tax professionals. In FY 2004, the Office of Professional Responsibility has a staff of 49 and a budget of approximately \$5 million.

¹² The IRS does not have a comprehensive list of these actions. We compiled the list of 308 actions by analyzing the databases, the IRS web site, and the 2003 Internal Revenue Bulletins.

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66 were not recorded in the IRS databases and 95 were not published on the IRS web site. Furthermore, 228 (74 percent) of the 308 actions were not properly or accurately recorded on the CAF. Table 2 shows a comparison of the disciplinary actions with the information recorded on the CAF.

Table 2: Comparison of Disciplinary Actions and CAF Records

Result of Comparison	Count
Practitioner was suspended or disbarred, but the CAF did not indicate any type of action.	61
Practitioner was suspended or disbarred, but the CAF had no active record.	48
Practitioner action was completed, but the CAF indicated action was still in effect.	31
Practitioner died or resigned, but the CAF indicated an active record.	4
Practitioner was suspended, but the CAF indicated disbarment.	69
Practitioner was disbarred, but the CAF indicated suspension or resignation.	15
Practitioner action matched the CAF.	80
Total	308

Source: TIGTA comparison of disciplinary actions and CAF records.

These discrepancies can cause confusion and inappropriate action by IRS employees and increase burden for taxpayers and tax practitioners. Employees relying on information on the CAF could provide confidential taxpayer information to a suspended or disbarred practitioner. Conversely, employees may refuse to disclose taxpayer information to a practitioner who has completed the period of suspension.

Since its recent reorganization, the Office of Professional Responsibility has assigned an employee the responsibility of updating and maintaining the practitioner disciplinary actions on its web site to prevent further inconsistencies. However, the overall responsibility has not been established by CAF management to make sure the sanction actions are updated to the CAF timely and accurately.

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Recommendations

6. The Director, Customer Account Services, SB/SE Division, should assign responsibility to a national coordinator to update the CAF based on notices from the Office of Professional Responsibility.

Management's Response: IRS management established a national coordinator position in the Memphis CAF unit to be responsible for updating the CAF based on notices received from the Office of Professional Responsibility.

7. The Director, Office of Professional Responsibility, should ensure the accuracy and consistency of practitioner actions within the Office's database and web site, Internal Revenue Bulletins, and the CAF by periodically verifying the information.

Management's Response: The Office of Professional Responsibility is in the process of replacing its management information system and has recently updated its Intranet web site to allow for employee searches of practitioner disciplinary actions. The Office of Professional Responsibility will also obtain access to the Integrated Data Retrieval System¹³ for verifying that its disciplinary actions are input to the CAF.

¹³ IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.

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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective was to determine whether the processes and procedures established for the Centralized Authorization File (CAF) were effective to maintain the accuracy of the database and to prevent unauthorized disclosure of taxpayer information. To accomplish this objective, we:

- I. Determined what guidance has been provided to Internal Revenue Service (IRS) employees, taxpayers, and their designated Powers of Attorney regarding the disclosure, processing, and maintenance of taxpayer and representative information on the CAF.
 - A. Reviewed the Internal Revenue Code, Treasury Regulations, Internal Revenue Manual, IRS publications and instructions available to taxpayers and tax practitioners, IRS directives issued to IRS employees, and desk guides relating to the processing and maintenance of taxpayer authorizations and third-party practitioners.
 - B. Reviewed the National or local IRS Office of Chief Counsel opinions relating to the CAF or third-party practitioners.
- II. Obtained an extract of the CAF database to determine the number of Powers of Attorney and representatives it contained. We then selected a sample to be used during our testing.
 - A. Contacted the IRS Detroit Computing Center and the CAF Programming Group and obtained an extract of the CAF. We analyzed and validated the extract database values for accuracy and completeness.
 - B. Analyzed the CAF extract and identified approximately 1.1 million Power of Attorney authorization forms¹ recorded on the CAF during the period October 1, 2002, through September 30, 2003.
 - C. Discussed possible sampling methodologies with an expert statistician. Based on an attribute sampling methodology with a 95 percent confidence interval, an expected error rate between 40-60 percent, and a precision rate of +/- 5 percent, we selected a stratified sample of 500 Power of Attorney authorization forms for review. This one sample was used for all objectives and tests in this review. The first stratum was composed of Forms 2848, and the second and third strata were composed of Forms 8821 and 706, respectively. Based on the proportional number of authorization forms recorded on the CAF during Fiscal Year 2003, we selected a

¹ Power of Attorney authorization forms are Power of Attorney and Declaration of Representative (Form 2848), United States Estate (and Generation-Skipping Transfer) Tax Return (Form 706), and Tax Information Authorization (Form 8821).

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statistical sample of 409 Forms 2848 (82 percent), 46 Forms 8821 (9 percent), and 45 Forms 706 (9 percent) for review.

- III. Determined whether current procedures are adequate to identify possible misrepresentation when Power of Attorney designations are incorrectly stated on the authorization forms.
 - A. Reviewed the sample of authorization forms, compared each form to current CAF data, and validated by researching the Internet web sites (for State Bar Associations and State Boards of Accountancy) and the IRS Enrolled Practitioner System (EPS)² database for their current status.
 - B. Reviewed the accuracy of the Office of Professional Responsibility's censured, suspended, or disbarred practitioner information on the CAF by researching the Office of Professional Responsibility's database, the IRS web site, and Internal Revenue Bulletins for sanctioned actions taken during the period January 15, 1999, through December 31, 2003. We then researched the CAF to validate whether these practitioners were identified as censured, suspended, or disbarred.
- IV. Determined whether the data stored on the CAF were accurate and adequate to prevent unauthorized disclosure to third parties that contact or receive taxpayer information from the IRS. We compared our sample of original authorization forms to the current CAF database. We then determined the inaccuracies caused by transcription error, procedures, taxpayers and representatives, and database constraints.
- V. Determined whether the IRS is timely processing the Power of Attorney authorization forms and whether error rates have been reduced by the modernization of the CAF database. From our sample, we reviewed the original authorization forms for preprocessing dates, dates received in the CAF processing units, and dates authorization information was input to the CAF.
- VI. Determined what actions the IRS has taken or plans to initiate to modernize processing and increase the accuracy of the CAF.
 - A. Contacted the Small Business/Self-Employed Division Program Management Office, the Information Technology Services organization, and the IRS Office of Electronic Tax Administration to discuss IRS plans for the electronic filing of Power of Attorney authorizations. We learned of an e-service program called Disclosure Authorization.
 - B. Interviewed Disclosure Authorization Program personnel to determine the scope of the Disclosure Authorization Program.

² The EPS is a database that provides automated support to the Office of Professional Responsibility legal examiners who process practitioner records.

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Appendix II

Major Contributors to This Report

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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Operations Support OS
Deputy Commissioner for Services and Enforcement SE
Chief Information Officer OS:CIO
Associate Chief Information Officer, Business Systems Modernization OS:CIO:B
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
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 Chief Information Officer OS:CIO

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Appendix IV

Outcome Measures

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

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; approximately 2.3 million taxpayer records over a 5-year period could have discrepancies between information provided on the taxpayer authorization forms and information recorded on the Centralized Authorization File (CAF) (see page 2).

Methodology Used to Measure the Reported Benefit:

We obtained a computer extract of approximately 1.1 million taxpayer authorization forms recorded on the CAF during Fiscal Year (FY) 2003 (October 1, 2002, through September 30, 2003). We selected a statistical sample of 500 records that was stratified among the 3 types of authorization forms: Power of Attorney and Declaration of Representative (Form 2848), United States Estate (and Generation-Skipping Transfer) Tax Return (Form 706), and Tax Information Authorization (Form 8821). In this sample, we found 202 records with discrepancies between the authorization forms and the CAF. Using a 95 percent confidence level and applying the error rates for each stratum in our sample, we estimated 456,000 records (+/- 4.3 percent) have discrepancies between information on the authorization form and information recorded on the CAF. Over a 5-year period, this projects to approximately 2.3 million records. Discrepancies could lead to delays in providing information to representatives or to inadvertent disclosure of confidential tax information to unauthorized third parties.

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; approximately 25,000 taxpayers represented by 27 individuals who may not be authorized to practice before the IRS (see page 8).

Methodology Used to Measure the Reported Benefit:

We used the same statistical sample identified above of 500 authorization forms recorded on the CAF during FY 2003. In this sample, we identified 487 individuals who were listed on the authorization forms as Attorneys, Certified Public Accountants, or Enrolled Agents.¹ A review of Internet web site information indicated 27 individuals had an inaccurate authorization or a

¹ An enrolled agent is a tax professional who has demonstrated special competence in tax matters, has applied for enrollment, and has been issued an enrollment card.

Information on the Centralized Authorization File Is Often Not Accurate or Complete

lapsed certification. With assistance from the CAF Programming Group, we determined that these 27 individuals are representing approximately 25,000 taxpayers. The status of these representatives may cause problems if the taxpayers need to rely on these individuals for representation during the IRS examination or collection process or in the Appeals function or tax court.

Type and Value of Outcome Measure:

- Taxpayer Privacy and Security – Actual; 197 taxpayers whose representatives have been disbarred, censured, or suspended by the Office of Professional Responsibility, but the sanctions have not been properly or accurately recorded on the CAF (see page 10).
- Taxpayer Burden – Actual; 31 taxpayers whose representatives are listed on the CAF as currently under Office of Professional Responsibility sanction, when in fact the sanctions have been completed (see page 10).

Methodology Used to Measure the Reported Benefit:

We obtained databases of censured, suspended, and disbarred practitioners, evaluated the Office of Professional Responsibility's Internet web site, and reviewed the practitioner disciplinary actions listed in the Internal Revenue Bulletins during the period October 1, 2002, through September 30, 2003. We selected all actions applied by the Office of Professional Responsibility during the period January 15, 1999, through December 31, 2003 (5 years), and identified 308 individual sanctions. We reviewed the 308 individual disciplinary actions and found 66 were not recorded in the IRS databases and 95 were not published on the IRS web site. Furthermore, 228 (74 percent) of the 308 actions were not properly or accurately recorded on the CAF.

Of the 228 actions not properly or accurately recorded on the CAF, 197 involved taxpayers whose representatives have been disbarred, censured, or suspended by the Office of Professional Responsibility, but the sanctions were not properly or accurately recorded. The remaining 31 actions involved taxpayers whose representatives are listed on the CAF as currently under Office of Professional Responsibility sanction, when in fact the sanctions have been completed. Employees relying on information on the CAF could provide confidential taxpayer information to a suspended or disbarred practitioner. Conversely, employees may refuse to disclose taxpayer information to a practitioner who has completed the period of suspension.

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Appendix V

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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

July 29, 2004

RECEIVED
JUL 30 2004

MEMORANDUM FOR ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Kevin M. Brown *KMB*
Commissioner Small Business/Self-Employed Division

SUBJECT: Draft Audit Report - Information on the Centralized
Authorization File is Often Not Accurate or Complete
(Audit # 200310037)

Thank you for the opportunity to respond to the subject Draft Audit Report. I fully agree that it is very important that the information on the CAF is accurate and complete, to prevent disclosure of tax information to unauthorized individuals and to ensure timely communication with taxpayers and their representatives. The Internal Revenue Service places great value on the accuracy of the information reflected on the CAF and I appreciate your recognition of that in the report. We continuously seek to improve our services to the taxpaying public and tax professional communities.

I agree with your conclusion that the information on the CAF is often not accurate or complete; however, we believe that the results from your statistical sample overstate the magnitude of the issues. The discrepancies found include differences between the representatives' addresses and telephone numbers shown on the taxpayer authorization forms and the CAF records. While some of these discrepancies may have been due to transcription errors, the report does not take into account the possibility that a representative may have updated this information with the IRS without submitting a new taxpayer authorization form for each taxpayer he or she represents. Taxpayers and their representatives are not required to provide a new taxpayer authorization form every time their representatives change their address or telephone number. When a representative indicates a change of address, the CAF Unit updates the representative's record on the CAF. Thus, while this address or telephone number no longer matches the address or telephone number provided on the taxpayer authorization form previously filed, the information is nonetheless accurate.

Continual efforts are being made to ensure the CAF database is maintained at a high level of accuracy. The following steps are being taken to make this happen:

- Direct single point coordination with the Office of Professional Responsibility to ensure current third party status.

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- Pursue electronic methods of validating and updating CAF records from other IRS databases, which will provide information regarding the current status of enrollment and licenses.
- Continue education efforts with the professional community through various outreach programs on the submission of authorizations that can be processed.
- Enhance training programs for employees.
- Monitor employees to ensure a high level of accuracy for document inputs.

We agree with your recommendations; however, we disagree, in part, with the outcome measures. Our response to each of your recommendations and comments on the outcome measures follow.

RECOMMENDATION 1

The Director, Customer Accounts Services, SB/SE Division should alert CAF processing unit managers that the units are not always following the most recent procedures for adding secondary TIN (spouse) information to the CAF.

CORRECTIVE ACTION

Current procedures in IRM 21.3.7.6 provide specific guidelines to work secondary spouse TINs when present on a third party authorization. Managers will be reminded to ensure employees are following current procedures.

IMPLEMENTATION DATE

September 1, 2004

RESPONSIBLE OFFICIAL

Deputy Director, Accounts Management, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 2

The SB/SE Director, Customer Account Services, Accounts Management should provide training to ensure employees understand and follow its most current procedures for processing taxpayer authorization forms. Specific training modules should be devoted to adding secondary taxpayer (spouse) information to the CAF and performing further research when information on authorization forms appear outdated, in error, or incomplete to ensure that the information is accurate before it is input to the CAF.

CORRECTIVE ACTION

SB/SE CAS will provide training material with current procedures which will be delivered during up-date training.

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On-going actions include:

CAF Units annually conduct training during the first quarter of the fiscal year to coincide with the issuance of revised IRM 21.3.7, and as program trends are identified updated Alerts are issued. New comprehensive training material was developed during FY2003, and the FY2004 update includes a module on secondary taxpayer processing; direction on how to research and attempt contact with the taxpayer or third party to perfect submissions with missing or incomplete information; and, instructions for thorough research and accurate input.

IRM 21.3.7, revision October 1, 2004 is focused on CAF processing and is significantly more detailed, providing step-by-step instruction for thorough research and accurate input, including the input of secondary taxpayer information and updating third party records. The revision is currently in the clearance process. Further, during FY2003, CAS revised Document 9909, *Third Party Awareness Training*, and developed Documents 12204 and 12205, *POA Desk Reference Guides*, to provide guidance to IRS personnel in identifying complete and processable authorizations and where to route such documents.

In an effort to further assist taxpayers and the tax professional communities in submitting completed and correct authorizations, CAS developed Publication 4245, *Power of Attorney*; Publication 4270, *The Unenrolled Return Preparer - Changes Effective January 1, 2004*; Publication 4271, *Terminating Third Party Authorizations - Revoking or Withdrawing Third Party Authorizations Recorded on the CAF*; Publication 4273, *Changes to Third Party Authorizations - Oral Consents and Third Party Designee Authorization*; and Publication 4272, *A Taxpayer's Guide to Third Party Authorization Products*. These publications were widely distributed at the 2004 IRS Nationwide Tax Forum and Exhibition, through the IRS website, and in various practitioner meetings.

IMPLEMENTATION DATE

December 1, 2004

RESPONSIBLE OFFICIAL

Deputy Director, Accounts Management, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 3

The Deputy Commissioner for Services and Enforcement should ensure timely processing of taxpayer authorization forms by establishing procedures that require all IRS functions to forward these authorization forms to the appropriate CAF processing unit within 24 hours of receipt.

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CORRECTIVE ACTION

We recognize that this recommendation mirrors a recommendation made by an internal review team. However, the Service function that receives the taxpayer authorization form is responsible for verifying the validity of the information on the form, not the CAF Unit. Verifying the validity of this information may take more than one business day. Thus, after further studying the feasibility of implementing such a recommendation, we have determined that a more appropriate period for forwarding these forms to the CAF Unit is within 24 hours from the time that the receiving function has validated the information contained on the form. We will encourage the receiving functions to verify the information within 24 hours of receipt of the taxpayer authorization form whenever possible. These actions are consistent with Recommendation 5, suggesting that the Service establish a process to verify the information on taxpayer authorization forms, and the Service's Power of Attorney Independent Review, p. III-3, February 6, 2004, recommending that all areas that receive a valid Form 2848/8821 forward it to the CAF Unit within 24 hours.

The Director, Customer Account Services, SB/SE Division will contact IRM coordinators and functional leadership to request inclusion of a requirement to forward authorization forms to the appropriate CAF processing unit within the specific timeframe.

IMPLEMENTATION DATE

July 15, 2005

Full implementation of this recommendation is projected for June 2005 to allow for concurrence of IRS functions and the Offices of Chief Counsel, OPR and Disclosure. Procedures may be issued through IRM updates prior to the 2005 revisions of the IRM.

RESPONSIBLE OFFICIAL

Director, Customer Account Services, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN

The Director, Customer Account Services, Small Business/Self-Employed Division will ensure all functions are in agreement with the new requirement by March 2005, which will allow for a mandate to include the requirement in all applicable 2005 revisions of the IRM.

RECOMMENDATION 4

The Director, Customer Account Services, SB/SE Division should consistently use date stamping and process work within established guidelines in the CAF processing units.

CORRECTIVE ACTION

We agree with this recommendation. IRM 21.3.7 (October 1, 2004 revision), which has already been completed, contains specific guidelines for capturing the received date of faxed submissions and date stamping requirements for mail and routed submissions. This procedure has also been put into place at campuses with the fax machine date

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recorded for receipt and a date stamp on the mail received as a result of the sharing of the draft report on May 28, 2004.

IMPLEMENTATION DATE

Completed

Date Stamping - Implemented in May 2004

RESPONSIBLE OFFICIAL

Deputy Director, Accounts Management, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 5

The Deputy Commissioner, Services and Enforcement, should consider developing a review process to identify whether representatives listed on Forms 2848 are authorized to practice before the IRS. This could include a review of a sample of Forms 2848.

CORRECTIVE ACTION

The Director, Payment Compliance, Small Business/Self-Employed Division, has drafted an interim guidance memorandum for compliance employees, outlining procedures for verification of a representative's eligibility. The status of the representative's professional license and standing before the IRS will be verified prior to being forwarded to a CAF processing unit. The memorandum is currently being reviewed by Chief Counsel.

The OPR and SB/SE databases, which track the eligibility status of practitioners, are currently in the process of being upgraded and/or have programming changes pending. These changes will provide mismatch reports, which can be utilized in the review process.

IMPLEMENTATION DATE

October 15, 2004 - Payment Compliance memorandum

July 15, 2005 - Electronic updates

RESPONSIBLE OFFICIALS

Director, Customer Account Services, Small Business/Self-Employed Division and
Director, Office of Professional Responsibility

CORRECTIVE ACTION MONITORING PLAN

The Director, Customer Account Services, SB/SE Division will monitor RIS activity and monthly briefing documents to ensure progress toward the electronic sharing of information which will ultimately serve to enhance the validity of the information recorded on the CAF.

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RECOMMENDATION 6

The Director, Customer Account Services, SB/SE Division should assign responsibility to a national coordinator to update the CAF based on notices from the Office of Professional Responsibility.

CORRECTIVE ACTION

We agree with this recommendation. Upon the sharing of the draft report on May 28, 2004, a national coordinator position was established in the Memphis CAF Unit. The coordinator is responsible for updating the CAF based on notice from the OPR. The October 2004 revision of IRM 21.3.7.20(2) details responsibilities and actions required of the coordinator for ensuring accurate and timely input, as well as requiring maintenance of a record of notice receipts. This practice will continue in force until systemic updates from the OPR database can be effectively programmed to update the CAF.

IMPLEMENTATION DATE

Completed

RESPONSIBLE OFFICIAL

Deputy Director, Accounts Management, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 7

The Director, Office of Professional Responsibility should ensure the accuracy and consistency of practitioner actions within its database, web site, Internal Revenue Bulletins, and the CAF by periodically verifying the information.

CORRECTIVE ACTION

The Office of Professional Responsibility (OPR) has recently updated its Intranet website to allow employees to search for practitioner disciplinary actions. OPR validates the information during the update process. The website is now current and is updated within 48 hours of a final disciplinary action. The site contains the effective date and end date for each disciplinary action. In addition, OPR has implemented procedures to ensure that practitioner disciplinary actions involving Enrolled Agents (EAs) are accurately reflected in the Enrolled Practitioner System (EPS) in Detroit. Information is provided to EPS upon a disciplinary action taking place, to include the name, address, EA Number, and social security number. EA enforcement actions and EA Enrollment Lists are validated monthly. The OPR is also in the process of replacing its management information system, and will include procedures to ensure the accuracy and consistency of data as part of the system replacement. OPR has published all practitioner sanctions in the Internal Revenue Bulletin quarterly since the office was established in 2003.

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With respect to the CAF, OPR notifies the appropriate CAF Unit Directors when disciplinary actions occur. OPR is receiving access to the Integrated Data Retrieval System (IDRS) in July 2004, which will provide a means of verifying that OPR actions are input to the CAF.

COMPLETION DATE

Completed

RESPONSIBLE OFFICIAL

Director, Office of Professional Responsibility

CORRECTIVE ACTION MONITORING PLAN

N/A

OUTCOME MEASURES

As stated above, the determination that forty percent of the records sampled include "different, inaccurate or incomplete" information probably overstates the magnitude of the issues. The CAF information may actually be accurate, because there is currently no audit trail and discrepancies could have been caused by subsequent changes submitted by the originator of the request. Thus, we do not agree with the measure of taxpayer burden, as shown below.

Type and Value of Outcome Measure:

- **Taxpayer Burden** – Potential; approximately 2.3 million taxpayer records over a 5-year period could have discrepancies between information provided on the taxpayer authorization forms and information recorded on the Centralized Authorization File (CAF) (see Page 2).

If you have questions or concerns about this matter, please call me or have a member of your staff contact John Crawford, Director, Customer Account Services, Small Business/Self-Employed Division at (859) 669-5344.