

**The Office of Appeals Should Strengthen and
Reinforce Procedures for Collection Due
Process Cases**

September 2005

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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

September 1, 2005

MEMORANDUM FOR CHIEF, APPEALS

A handwritten signature in cursive script, reading "Pamela J. Gardiner".

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - The Office of Appeals Should Strengthen
and Reinforce Procedures for Collection Due Process Cases
(Audit # 200410033)

This report presents the results of our statutory review of the Office of Appeals (Appeals) Collection Due Process (CDP) procedures. The overall objective of this review was to determine whether the Internal Revenue Service (IRS) complied with the provisions of 26 United States Code (U.S.C.) Sections (§§) 6320 and 6330 when taxpayers exercised their right to appeal the filing of a lien or a notice of intent to levy.¹ The Treasury Inspector General for Tax Administration is required to determine annually if the IRS complied with the legal guidelines and procedures for the filing of a notice of lien or a notice of intent to levy and the right of the taxpayer to appeal.²

In summary, we could not determine if the IRS complied with legal guidelines and required procedures to protect taxpayer rights because a significant portion of the Appeals CDP and Equivalent Hearing closed case files we requested could not be located or did not contain sufficient documentation. As such, we could not determine whether all Appeals actions were appropriate. In certain instances, the missing and incomplete files could affect taxpayers because if a taxpayer has a change in circumstances that affects the Appeals determination, or if the Collection function does not properly carry out an Appeals determination, the case can come back to Appeals. Because of the missing documentation, similar documentation would have to be gathered to effectively resolve the case.

In some instances, hearing officers did not comply with the procedural and legal requirement to document whether they had any prior involvement with the unpaid tax.³

¹ 26 U.S.C. §§ 6320 and 6330 (Supp. IV 1998).

² 26 U.S.C. § 7803(d)(1)(A)(iii) and (iv) (Supp. IV 1998).

³ Hearing officers are either Appeals Officers or Settlement Officers.

Moreover, some Appeals determination letters did not contain clear and detailed explanations of the basis for the hearing officers' decisions and did not adequately communicate the results of the hearings to the taxpayers. Some determination letters did not address the specific issues raised or tax periods discussed by the taxpayers in their hearing requests. Although Appeals provides guidance, including a Determination Letter Guide, to assist hearing officers in preparing determination letters, the guidance was not always followed.

Appeals case files did not always contain documentation that Appeals verified the timeliness of the hearing request or the date suspension of collection activity should begin. Specific computer codes are used to indicate the suspension of collection activity and to recalculate the expiration date for the collection statute. When these codes are missing, inappropriate collection activity may continue, and the expiration date for the collection statute will not be recalculated.

From our review of Equivalent Hearing cases, we concluded these cases were properly classified. All Equivalent Hearing cases in our sample were instances in which the taxpayers' hearing requests were not filed timely. As such, the taxpayers were not entitled to CDP hearings. For an Equivalent Hearing case, the IRS is not required to suspend collection action and the taxpayer does not have the right to a judicial review.

We recommended the Chief, Appeals, evaluate case control procedures to identify weaknesses in the system and remind personnel of the requirement to retain all necessary supporting documentation according to current procedures and guidance. We also recommended the Chief, Appeals, reiterate the requirement to include the impartiality statement in the determination letters and case files and remind Appeals managers to verify this during case reviews. The managers should ensure the determination letters adhere to current IRS guidance and procedures. We also recommended hearing officers and managers be reminded to verify hearing requests are properly screened for timeliness and correctness of the suspension of collection activity. In addition, a statement and supporting documentation should be included in the Appeals case file to indicate verification was conducted.

Management's Response: The Office of Appeals agreed with the findings and recommendations in this report. Appeals has begun the process of centralizing the closing and maintenance of office files for all CDP cases into two campus⁴ locations, which should minimize the instances of missing case files. Procedures will be updated and communicated to employees to reinforce the requirement to retain necessary documentation that supports the Appeals decision and the taxpayer's hearing request. In conjunction with this effort, Appeals is working on the Electronic Case File programming and equipment procurement for the creation of paperless files, which should minimize the instances of missing documents in case files. Appeals has added guidance for documenting "no prior involvement" when securing a CDP summary notice of determination and will make it mandatory to include a contact letter that incorporates

⁴ The campuses are the data processing arm of the IRS. They process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

the necessary wording to meet the impartiality documentation requirement. In addition, Appeals will emphasize the need for the impartiality statement through quarterly meetings and will monitor compliance through the Appeals Quality Measurement System.

Appeals has incorporated an example of how to prepare a determination letter in both the Determination Letter Guide and the latest revision of the Appeals procedures. The changes will be highlighted through meetings with the Area Collection Contact coordinators and shared at group meetings with employees working CDP cases. Lastly, to ensure timely and accurate suspension of collection activity, Appeals is planning to assume full responsibility for the initial input of the computer codes that signal the suspension of collection activity and recalculation of the expiration date for the collection statute. Until Appeals assumes this responsibility in late 2005, employees will be reminded through meetings and training methods of the verification and documentation requirements. Management's complete response to the draft report is included as Appendix V.

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.

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Background

When initial contacts by the Internal Revenue Service (IRS) do not result in the successful collection of unpaid tax, the IRS has the authority to attach a claim, commonly referred to as a lien, to the taxpayer's assets.¹ The IRS also has the authority to work directly with financial institutions and other parties to obtain funds owed by a taxpayer;² this is commonly referred to as a levy.

Since February 1996, IRS procedures have allowed taxpayers to appeal the filing of liens and proposed or actual levies. However, this protection was not mandated by law. If the IRS did not follow its own procedures, there was no remedy available to the taxpayer. Based on concerns that taxpayers were not always provided adequate notice and that appeal rights were needed for liens and levies, the IRS Restructuring and Reform Act of 1998 codified this protection into law.³

Since January 19, 1999, the IRS has been required to notify taxpayers in writing that a lien has been filed or that it intends to levy.⁴ A taxpayer is allowed to appeal the lien or levy action through the Collection Due Process (CDP) by filing a hearing request.⁵ This hearing request must be received within 30 calendar days plus 5 business days of the filing of the lien or within 30 calendar days from the date of the levy notice.⁶ If a taxpayer's hearing request is submitted on time, the IRS will suspend all tax collection efforts and the Office of Appeals (Appeals) will provide the taxpayer a CDP hearing, after which the taxpayer has the right to a judicial review if he or she does not agree with the Appeals decision. If a taxpayer's hearing request is not submitted timely, Appeals will provide the taxpayer an Equivalent Hearing and consider the same issues as in a CDP hearing;

¹ 26 United States Code (U.S.C.) Section (§) 6321 (1994).

² 26 U.S.C. § 6331 (1994 & Supp. IV 1998).

³ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

⁴ 26 U.S.C. §§ 6320(a) and 6330(a) (Supp. IV 1998) and Code of Federal Regulations (C.F.R.) §§ 301.6320-1 and 301.6330-1 (2002).

⁵ Taxpayers can use Request for a Collection Due Process Hearing (Form 12153) or other similar written communication to request a CDP hearing.

⁶ 26 U.S.C. §§ 6320 and 6330 (Supp. IV 1998).

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however, collection action is not required to be suspended and the taxpayer does not have the right to a judicial review.

Taxpayers are entitled to one hearing per tax period for which a notice of lien or intent to levy has been issued. The hearing is conducted by an Appeals Officer or Settlement Officer (hearing officer) who had no prior involvement with the unpaid tax.⁷ During the hearing, the hearing officer must verify whether the requirements of all applicable laws or administrative procedures were met related to the lien or levy. The hearing officer must also address any issues the taxpayer may raise relevant to the unpaid tax or the proposed lien or levy, such as whether the taxpayer is an innocent spouse; determine if collection actions were appropriate; and decide if other collection alternatives would facilitate the payment of the tax. The hearing officer must determine whether the proposed collection action balances efficient tax collection with the taxpayer's legitimate concerns. The taxpayer may not raise an issue that was considered at a prior administrative or judicial hearing if the taxpayer participated meaningfully in the prior proceeding.

At the conclusion of a hearing, Appeals issues to the taxpayer a CDP determination letter,⁸ CDP summary notice of determination,⁹ or Equivalent Hearing decision letter.¹⁰ These letters present the hearing officer's findings, agreements reached with the taxpayer, any relief provided to the taxpayer, and any actions the taxpayer and the IRS are required to take. The CDP determination letter also provides an explanation of the right to judicial review by filing a petition or complaint in the appropriate Federal Tax Court or United States District Court within 30 calendar days. The CDP summary notice of determination is issued when the taxpayer confirms agreement with Appeals, waives the right to judicial review, and waives the suspension of levy action.

⁷ The taxpayer may waive this requirement.

⁸ Determination Letter (Form 3193 or Form 3194).

⁹ Summary Notice of Determination, Waiver of Right to Judicial Review of a Collection Due Process Determination, and Waiver of Suspension of Levy Action (Form 12257).

¹⁰ Decision Letter (Letter 3210).

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The CDP or Equivalent Hearing case is reviewed by the hearing officer's manager at the completion of the case to evaluate whether the hearing officer followed all requirements and procedures. In addition, the Appeals Quality Measurement System evaluates quality of casework nationwide by selecting a national sample. The Appeals Quality Measurement System reported an 80 percent overall compliance rate for CDP cases completed in Fiscal Year (FY) 2004. This is down from 88 percent and 82 percent for cases completed in FYs 2003 and 2002, respectively.

After Appeals has made a determination on a case, if the taxpayer has a change in circumstances which affects the Appeals determination or if the Collection function did not carry out the determination, the taxpayer has the right to return to Appeals. The taxpayer has this right as long as all administrative remedies have been exhausted and until the collection statute expires for the tax period. The Appeals office that made the original determination generally retains jurisdiction over the case.¹¹

The Treasury Inspector General for Tax Administration (TIGTA) is required to determine annually whether the IRS complied with legal guidelines and procedures for the filing of a notice of lien or a notice of intent to levy and the right of the taxpayer to appeal.¹² The TIGTA has divided this requirement into three statutory audits: one to review the filing of a notice of tax lien;¹³ one to review the intent to levy;¹⁴ and one to review the rights of taxpayers to appeal these issues,¹⁵ which is the focus of this report. This is the fifth annual audit of this area conducted by the TIGTA.

This audit was performed in the National Headquarters of the Chief, Appeals, in Washington, D.C., during the period September 2004 through May 2005. The scope of the audit covered CDP and Equivalent Hearing cases closed between April 1 and September 30, 2004. The audit was conducted

¹¹ C.F.R. §§ 301.6320-1(h) and 301.6330-1(h) (2002).

¹² 26 U.S.C. § 7803(d)(1)(A)(iii) and (iv) (Supp. IV 1998).

¹³ 26 U.S.C. § 6320(a) (Supp. IV 1998).

¹⁴ 26 U.S.C. § 6330(a) (Supp. IV 1998).

¹⁵ 26 U.S.C. §§ 6320(b) and (c) and 26 U.S.C. §§ 6330(b) and (c) (Supp. IV 1998).

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Some Office of Appeals Case Files Could Not Be Located or Were Incomplete

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.

Overall, we could not determine if the IRS complied with the legal guidelines and required procedures to protect taxpayer rights when taxpayers appealed lien and levy actions because a significant portion of the Appeals closed case files we requested as part of our samples could not be located or did not contain sufficient documentation.

We selected statistical samples of 80 cases each from the 12,270 CDP cases and the 4,286 Equivalent Hearing cases closed by Appeals between April 1 and September 30, 2004. Appeals was unable to locate eight of the CDP and Equivalent Hearing case files requested for our samples. Consequently, we could not verify if all actions were appropriate and met the requirements of the law for the missing case files.

In addition, 60 of the Appeals case files we received were incomplete—missing key documents needed to support and present Appeals' findings. For example, the taxpayer's hearing request (including any applicable attachments), which shows when and why the taxpayer was seeking assistance from Appeals, was not always in the case file. The CDP summary notice of determination was also missing from some CDP case files. This document is issued by Appeals when the taxpayer confirms agreement with the determination, waives the right to judicial review, and waives the suspension of levy action.

Table 1 summarizes the number of Appeals CDP and Equivalent Hearing case files in our sample that could not be located or were incomplete, as well as the projected estimates for the 6-month period of our review.

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Table 1: Unable to Locate or Incomplete Appeals Case Files

| Reason Case Could Not Be Reviewed for All Guidelines and Procedures | Number of Sample Cases | Estimate of Total Cases ¹⁶ |
|---|---------------------------|--|
| <i>CDP cases</i> | | |
| Unable to locate case file | 5 | 767 |
| Case file received did not include taxpayer hearing request | 24 | 3,681 |
| Case file received did not include summary notice of determination | 2 | 307 |
| Case file received did not include taxpayer hearing request and did not include summary notice of determination | 1 | 154 |
| Total unable to locate or incomplete CDP case files | 32 | 4,908¹⁷ |
| <i>Equivalent Hearing cases</i> | | |
| Unable to locate case file | 3 | 161 |
| Case file received did not include taxpayer hearing request | 33 | 1,768 |
| Total unable to locate or incomplete Equivalent Hearing case files | 36 | 1,929 |

Source: TIGTA sample of 80 CDP and 80 Equivalent Hearing cases closed by Appeals between April 1 and September 30, 2004.

Appeals procedures and guidelines include a list of documentation that should be retained in the closed case file, which should include the taxpayer's hearing request and the Appeals determination provided to the taxpayer. Because Appeals was unable to locate the case file or the required documentation was not maintained, we could not confirm the hearing officers' actions and the appropriateness of the Appeals determinations.

Despite internal guidance requiring Appeals to retain pertinent documentation in a closed case file until the collection statute date expires for the protested tax period (generally 10 years from the date the tax was assessed), Appeals officials stated, in practice, closed case files are

¹⁶ See Appendix IV for the statistical sample and estimate information.

¹⁷ The column does not add due to rounding.

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typically reduced to a minimum of documentation after the judicial protest period has expired (90 calendar days).

Missing and incomplete files could affect taxpayers because if a taxpayer has a change in circumstances that affects the Appeals determination, or if the Collection function does not properly carry out an Appeals determination, the case can come back to Appeals. Because of the missing documentation, similar documentation would have to be gathered to effectively resolve the case.

Recommendations

The Chief, Appeals, should:

1. Evaluate case control procedures and identify weaknesses in the system to determine what further actions are needed to properly locate and retain completed CDP and Equivalent Hearing cases until the appropriate collection statute date expires.

Management's Response: Appeals agreed with this recommendation and has begun the process of centralizing the closing and maintenance of office files for all CDP cases into two campus¹⁸ locations, which should minimize instances of missing files.

2. Remind personnel of the requirement to retain all necessary documents supporting the Appeals decision, including the taxpayer's hearing request and, when applicable, the CDP summary notice of determination, as required in Appeals guidance and procedures. This could be accomplished through nationwide correspondence, local office meetings, and training sessions.

Management's Response: Appeals agreed with this recommendation and will update its procedures accordingly. Appeals will inform employees of document retention requirements during monthly conference calls, post an article on its webpage, and discuss the requirements at local

¹⁸ The campuses are the data processing arm of the IRS. They 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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Impartiality Statements Were Not Documented As Required for Collection Due Process Determinations

training sessions. Appeals is also working on the Electronic Case File programming and equipment procurement for the creation of paperless files, which should minimize the instances of missing documents in closed case files.

The CDP hearing should be conducted by a hearing officer who had no prior involvement with respect to the unpaid tax; however, the taxpayer may waive this requirement. To comply with this requirement, Appeals procedures require CDP determination letters to include an impartiality statement. An impartiality statement is also required to be documented in the case file when a CDP summary notice of determination is issued (this is a different type of letter issued by Appeals in cases for which the taxpayer confirms agreement with the determination, waives the right to judicial review, and waives the suspension of levy action).

We found the impartiality statement, or a waiver from the taxpayer, was not always mentioned in the letters or notices provided to the taxpayers. Based on the documentation in the case files, we could not determine if the hearing officers had prior involvement with the unpaid tax. In our statistical sample of 80 CDP cases, there were 49 cases in which Appeals issued a CDP determination letter and 18 cases in which Appeals issued a CDP summary notice of determination. However, five of the cases with a CDP determination letter and two of the cases with a CDP summary notice of determination did not contain an impartiality statement or supporting documentation in the case file. Based on our sample, we estimate 1,074 CDP cases did not contain impartiality statements.¹⁹

While the lack of impartiality statements in the letters or documentation in the Appeals case files appears to be an oversight and does not necessarily indicate a lack of impartiality, hearing officers are required to certify and document their impartiality. Appeals officials stated the impartiality statement should be contained in either the determination letter or the Appeals case file documentation; however, it appears hearing officers are not consistently following the procedures.

¹⁹ See Appendix IV for the statistical sample and estimate information.

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Because the impartiality of the hearing officer is a legal requirement, the documentation of no prior involvement should always be included in letters provided to taxpayers and supporting documentation in the case file. Without that documentation, there is no evidence to inform the taxpayer and any reviewing court that the hearing officer had no prior involvement with the unpaid tax liability under review and, therefore, could provide an impartial hearing.

We reported this same concern in a prior TIGTA report.²⁰ Appeals management responded to that report by stating they would reiterate procedures for documenting the impartiality statement to hearing officers. The Appeals Quality Measurement System also found that hearing officers did not properly document the impartiality statement in 31 percent of the FY 2003 CDP cases reported in its FY 2004 Annual Report. Appeals management uses the Appeals Quality Measurement System's annual results to identify areas needing improvement, yet lack of documentation of impartiality statements continues to be a significant problem.

Recommendation

3. The Chief, Appeals, should emphasize that hearing officers must provide impartiality statements in determination letters and include clear documentation supporting the statements in the Appeals case files. Managers should verify whether this requirement has been met during their reviews of completed cases.

Management's Response: Appeals agreed with this recommendation. Appeals has added guidance for documenting "no prior involvement" when securing a CDP summary notice of determination and will make it mandatory to include a contact letter that incorporates the necessary wording to meet the impartiality documentation requirement. Additionally, Appeals will emphasize to employees the need for the impartiality statement through quarterly meetings with the Area Collection coordinators

²⁰ *Appeals Complied With the Legal Requirements for Collection Due Process and Equivalent Hearings* (Reference Number 2003-10-156, dated July 2003).

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Determination Letters Were Not Clear or Did Not Address All Issues Raised by the Taxpayers

and will monitor compliance through the Appeals Quality Measurement System.

Appeals procedures state the determination letter should contain a clear and detailed explanation of the basis for the hearing officer's decision. This should, at a minimum, include three required elements:

- Verification that the requirements of applicable laws and administrative procedures have been met.
- Issues raised by the taxpayer.
- Whether any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the taxpayer that any collection action be no more intrusive than necessary.

In the 49 cases in our sample in which Appeals issued a CDP determination letter, we found 2 cases in which the hearing officers did not clearly explain the Appeals decision and did not follow guidance, such as in the Determination Letter Guide, for preparation of the determination letters.

- One case involved both a lien and a levy on various tax periods. The determination letter did not use the suggested table format in its background section to clearly identify the tax periods involved. As a result, the Appeals decision was not clear about which tax periods were covered and how they were resolved.
- The other case involved a levy action that was not sustained because the balance was paid in full. The hearing officer's conclusion stated "levy is denied." The determination letter should have explained the levy action was appropriate; however, the balance was paid in full and the levy was no longer needed and therefore not sustained.

In addition to the determination letters not having clear explanations, we found three other cases in our sample in which the hearing officers failed to discuss in the determination letters specific issues stated by the taxpayers in the hearing requests.

- In the first case, the taxpayer asked for an installment agreement; however, there was no mention of this request in the determination letter.

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- In the second case, the taxpayer asked for additional time to submit an Offer in Compromise that was not mentioned in the determination letter.
- In the third case, the taxpayer asked for a hearing involving three tax periods, but the determination letter addressed only two tax periods without explaining why the remaining tax period was not eligible for a hearing.

We estimate 307 CDP cases in our review period did not include determination letters with clear explanations of the hearing officers' decisions. We also estimate an additional 461 CDP cases in our review period did not include determination letters that addressed all specific issues raised in the taxpayers' hearing requests.²¹

Determination letters that do not clearly explain the hearing officers' decisions or do not include all issues raised by the taxpayers may cause confusion and increase taxpayer burden. Taxpayers and any courts reviewing the cases may be unable to determine whether applicable laws and administrative procedures were followed and whether relevant issues presented by the taxpayers were considered. Moreover, a determination letter that does not include the three required elements may not adequately communicate to the taxpayer that the proposed collection action balances the need for efficient collection of taxes with the concerns of the taxpayer. Appeals needs to continue to emphasize compliance with procedures that address the content of the CDP determination letter.

Recommendation

4. The Chief, Appeals, should remind hearing officers, and managers conducting case reviews, of the procedure to provide a clear and complete explanation in determination letters and to adhere to guidance such as that contained in the Determination Letter Guide. These reminders could be accomplished through nationwide correspondence, local office meetings, and training sessions.

²¹ See Appendix IV for the statistical sample and estimate information.

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Management's Response: Appeals agreed with this recommendation and has incorporated an example of how to prepare the determination letter in both the Determination Letter Guide and the latest revision of Appeals procedures. The changes will be highlighted through meetings with Area Collection Contact coordinators and shared at group meetings with employees working CDP cases.

The Office of Appeals Is Not Consistently Verifying the Suspension of Collection Activity

When a CDP hearing request is received timely, collection activity is suspended from the hearing request received date until either the date the Appeals determination becomes final or the date of withdrawal by the taxpayer.²²

Suspension of collection activity is initiated by the entry of a code into the taxpayer's account on the IRS computer system. Another code is later entered to remove the suspension.²³ These codes are generally entered by Collection function employees before and after the Appeals hearing. The codes are used to communicate to other IRS employees when suspension of collection activity is in effect and to recalculate the expiration date for the collection statute.

In 10 of the 80 cases we sampled, the Appeals case files did not contain documentation to indicate verification of the timeliness of the hearing request and the date suspension of collection activity should begin. In 2 of the 10 sample cases, the computer codes were not entered into the taxpayers' accounts when Appeals received the hearing requests.

- One case was in Appeals for approximately 4 months before the hearing request was withdrawn by the taxpayer. This taxpayer's account did not include the code necessary to indicate suspension of collection activity; consequently, the expiration date for the collection statute was not recalculated.
- The second case did not have the appropriate computer codes input to the taxpayer's account until the case was completed by Appeals. Approximately 14 months passed from when the hearing request was received by

²² C.F.R. §§ 301.6320-1(g) and 301.6330-1(g) (2002).

²³ Transaction Code (TC) 520 is used for beginning and TC 521 is used for concluding the collection activity suspension period.

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the IRS to when Appeals completed the hearing. During this time, the taxpayer's account could have been subject to ongoing collection activity. Although the collection statute was recalculated at the conclusion of the Appeals hearing, IRS employees using information on the taxpayer's account could have inappropriately taken collection action while the Appeals hearing was in process.

Although the codes are generally entered by other IRS employees, one of the first tasks of the hearing officer is to verify the timeliness of the hearing request and the date the suspension of collection activity began. According to Appeals procedures, this verification must be documented in the Appeals case file and included in the determination letter if one is issued. Without this verification, a taxpayer may be denied his or her right to suspension of collection activity while the hearing request is in Appeals. IRS employees using information on the taxpayer's account could inappropriately attempt a collection action. In addition, the expiration date for the collection statute may not be recalculated after the Appeals hearing, which could affect the collection of tax revenue.

We estimate 1,534 CDP cases in our review period did not contain the verification statement and supporting documentation. Of these, we estimate 307 did not have collection activity suspended for the duration of the Appeals hearing. In addition, we estimate 154 CDP cases in our review period did not have the expiration date for the collection statute recalculated.²⁴

This appears to be an ongoing problem. In its FY 2004 results, the Appeals Quality Measurement System reported hearing officers either did not verify or did not adequately document the collection activity suspension date for 29 percent of the CDP cases completed in FY 2003. Appeals needs to ensure hearing officers confirm and document the suspension of collection activity is correct at the start of a CDP hearing, to protect taxpayer rights and tax revenue.

²⁴ See Appendix IV for the statistical sample and estimate information.

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Recommendation

5. The Chief, Appeals, should remind hearing officers, and managers conducting case reviews, of the procedure to verify hearing requests are properly screened for timeliness and correctness of the collection activity suspension. In addition, a statement and supporting documentation should be included in the Appeals case file to indicate verification was conducted.

Management's Response: Appeals agreed with the recommendation and is planning to assume full responsibility for the initial input of the computer codes that signal the suspension of collection activity and the recalculation of the expiration date for the collection statute. Until Appeals assumes this responsibility in late 2005, employees will be reminded of the verification and documentation requirements through meetings and training.

Equivalent Hearing Cases Were Properly Classified

If a taxpayer's CDP hearing request is filed more than 30 calendar days plus 5 business days after the filing of the lien or more than 30 calendar days after the date of the levy notice, Appeals will provide the taxpayer an Equivalent Hearing. This is similar to a CDP hearing, but the IRS is not required to suspend collection activity and the taxpayer does not have the right to a judicial review.

We selected a statistical sample of 80 Equivalent Hearing cases closed between April 1 and September 30, 2004, to evaluate whether any of these taxpayers were entitled to CDP hearings. For the 80 cases we sampled, Appeals provided 77 of the case files; however, only 44 contained the taxpayer hearing requests. Based on the timing of the hearing requests, other information in the Appeals case files, tax account information, and discussions with Appeals officials, we concluded these 44 cases were properly classified as Equivalent Hearing cases.

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Appendix I

Detailed Objective, Scope, and Methodology

The objective of this audit was to determine whether the Internal Revenue Service (IRS) complied with the provisions of 26 United States Code (U.S.C.) Sections (§§) 6320 and 6330 when taxpayers exercised their right to appeal the filing of a lien or a notice of intent to levy.¹ To accomplish our objective, we:

- I. Determined the status of corrective actions resulting from prior Treasury Inspector General for Tax Administration (TIGTA) audit reports by conducting interviews with Office of Appeals (Appeals) officials, as well as obtaining documentation supporting the implementation of the proposed IRS corrective actions and other procedural changes.
- II. Determined whether the IRS is in compliance with 26 U.S.C. §§ 6320 and 6330 when handling Collection Due Process (CDP) Appeals hearing requests.
 - A. Obtained a computer extract of CDP cases closed between April 1 and September 30, 2004, from the Appeals Centralized Database System (ACDS) file maintained at the TIGTA Data Center Warehouse.² We validated the computer extract using information from the TIGTA Data Center Warehouse, reviewed appropriate data within fields requested, compared extract data to source documents (using the sample in Step II.B.), and compared population totals to information obtained from Appeals officials.
 - B. Selected a statistical sample of 80 cases from the population of 12,270 CDP cases closed by Appeals between April 1 and September 30, 2004, based on a confidence level of 90 percent, a precision rate of ± 6 percent, and an expected error rate of 12 percent.
 - C. For the CDP sample, obtained the Appeals case files including the Case Activity Records, Case Summary Cards, Requests for a Collection Due Process Hearing (Form 12153), Determination Letters, Appeals Case Memoranda, and Integrated Collection System³ or Automated Collection System histories.⁴

¹ 26 U.S.C. §§ 6320 and 6330 (Supp. IV 1998).

² The ACDS is a computerized case control system used to control and track cases throughout the appeal process.

³ The Integrated Collection System provides workload management, case assignment/tracking, inventory control, electronic mail, case analysis tools, and management information capabilities to support tax collection fieldwork.

⁴ The Automated Collection System is a telephone contact system through which telephone assistants collect unpaid taxes and secure tax returns from delinquent taxpayers that have not complied with previous notices.

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- D. Reviewed the CDP sample case files and determined whether the following requirements of 26 U.S.C. §§ 6320 (b) and (c) and 6330 (b) and (c) had been addressed in the hearings by the hearing officers:⁵
 - 1. Verification that the requirements of applicable laws and administrative procedures had been met.
 - 2. Whether any proposed collection actions balanced the need for the efficient collection of taxes with the legitimate concerns of the taxpayers that any collection action be no more intrusive than necessary.
 - 3. The taxpayers were provided with impartial hearing officers or waived this requirement.
 - 4. The taxpayers were allowed to raise issues at the hearings relating to the unpaid tax or the proposed lien or levy actions, including appropriate spousal defenses, challenges to the appropriateness of collection activities, offers of collection alternatives, or the underlying liabilities.
 - E. Determined whether Appeals complied with current Internal Revenue Manual guidelines for documenting CDP case actions.
 - F. Discussed potential CDP exception cases with Appeals officials and identified and confirmed causes.
- III. Determined whether CDP cases were misclassified as Equivalent Hearing cases.
- A. Obtained a computer extract of Equivalent Hearing cases closed between April 1 and September 30, 2004, from the ACDS file maintained at the TIGTA Data Center Warehouse. We validated the computer extract using information from the TIGTA Data Center Warehouse, reviewed appropriate data within fields requested, compared extracted data to source documents (using the sample in Step III.B.), and compared population totals to information obtained from Appeals officials.
 - B. Selected a statistical sample of 80 cases from the population of 4,286 Equivalent Hearing cases closed by Appeals between April 1 and September 30, 2004, based on a confidence level of 90 percent, a precision rate of ± 3.9 percent, and an expected error rate of 4 percent.
 - C. For the Equivalent Hearing sample, obtained the Appeals case files including the Case Activity Records, Case Summary Cards, Forms 12153, Determination Letters, Appeals Case Memoranda, and Integrated Collection System or Automated Collection System histories.
 - D. Reviewed the Equivalent Hearing sample case files and determined whether any CDP cases were misclassified as Equivalent Hearing cases as follows:

⁵ Hearing officers are either Appeals Officers or Settlement Officers.

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1. Reviewed the case files to obtain the taxpayers' written hearing requests and determined whether the files contained the envelopes in which the requests were sent. From these documents, we extracted the dates the taxpayers signed the requests, the IRS date stamps showing when the cases were received by the IRS, and the postmark dates on the envelopes.
2. Reviewed Integrated Data Retrieval System (IDRS)⁶ transcripts for Equivalent Hearing cases and determined, based on the dates that certain computer codes were entered on the account, the dates of the notices of lien or proposed levy action. We reviewed the ACDS Case Summary Cards and identified the dates recorded by Appeals as the dates hearings were requested by the taxpayers. We then compared the dates recorded in the ACDS Case Summary Cards to the dates indicated on the hearing requests and the IDRS transcripts to identify discrepancies.
3. Reviewed the recorded hearing request dates with Appeals procedures to determine whether the guidance was followed.
4. Discussed Equivalent Hearing cases with Appeals officials.

⁶ The 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 II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)

Michael E. McKenney, Director

Aaron R. Foote, Audit Manager

Yasmin B. Ryan, Lead Auditor

Daniel M. Quinn, Senior Auditor

Stephanie K. Foster, Auditor

Frank I. Maletta, Auditor

Carolyn D. Miller, Auditor

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Appendix III

Report Distribution List

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 Chief, Appeals AP

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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 Rights and Entitlements – Potential; 6,749 closed Collection Due Process (CDP) cases either could not be located by the Office of Appeals (Appeals) or did not contain 1 or more of the following: sufficient documentation, sufficient determination letter, and/or verification of the suspension of collection activity (see page 4).

Methodology Used to Measure the Reported Benefit:

Using a computer extract from the Appeals Centralized Database System (ACDS),¹ we identified a population of 12,270 CDP cases closed between April 1 and September 30, 2004. We selected a statistical sample of 80 CDP cases and found 44 (55 percent) either could not be located by Appeals or did not contain 1 or more of the following: sufficient documentation, sufficient determination letter, and/or verification of the suspension of collection activity. Using a 90 percent confidence level and a precision of ± 9.12 percent, we estimate 6,749 CDP cases could affect taxpayer rights and entitlements. The 44 CDP cases are comprised of the following:

- There were 32 CDP case files which either could not be located by Appeals or did not contain documentation sufficient to determine if the IRS complied with the guidelines and procedures to protect taxpayer rights when appealing lien and levy actions (see page 5). Using a 90 percent confidence level, we estimate:

| Reason CDP Case Could Not Be Reviewed for All Guidelines and Procedures | Number of Sample Cases | Error Rate | Estimate of Total Cases | Precision of Estimate |
|---|-------------------------------|-------------------|--------------------------------|--------------------------------|
| Unable to locate case file | 5 | 6.25% | 767 | $\pm 4.44\%$ |
| Case file received did not include taxpayer hearing request | 24 | 30% | 3,681 | $\pm 8.40\%$ |
| Case file received did not include summary notice of determination | 2 | 2.5% | 307 | $\pm 2.86\%$ |
| Case file received did not include taxpayer hearing request and did not include summary notice of determination | 1 | 1.25% | 154 | $\pm 2.04\%$ |
| Totals | 32 | 40% | 4,908² | $\pm 8.98\%$ |

¹ The ACDS is a computerized case control system used to control and track cases throughout the appeal process.

² The column does not add due to rounding.

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- There were 7 CDP case files (8.75 percent) which did not contain an impartiality statement in the determination letters or in the case files (see page 7). Using a 90 percent confidence level and a precision of ± 5.18 percent, we estimate 1,074 cases did not include an impartiality statement in the determination letters or documentation in the case files.
- There were 5 CDP case files which did not contain clear and detailed descriptions in the determination letters or did not address all issues raised by the taxpayers in the determination letters (see page 9). Using a 90 percent confidence level, we estimate:

| Reason Determination Letter Was Not Adequate | Number of Sample Cases | Error Rate | Estimate of Total Cases | Precision of Estimate |
|---|------------------------|--------------|-------------------------|--------------------------------|
| Hearing officer did not provide a clear and detailed description | 2 | 2.5% | 307 | $\pm 2.86\%$ |
| Hearing officer did not address all issues raised by the taxpayer | 3 | 3.75% | 461 | $\pm 3.48\%$ |
| Totals | 5 | 6.25% | 767³ | $\pm 4.44\%$ |

- There were 10 CDP cases which did not contain documentation to indicate verification of the timeliness of the hearing request and the date suspension of collection activity should begin. In 2 of the 10 cases, the computer codes were not entered into the taxpayers' accounts when Appeals received the hearing requests (see page 11). Using a 90 percent confidence level, we estimate:

| Reason Suspension of Collection Activity Was Not Adequate | Number of Sample Cases | Error Rate | Estimate of Total Cases | Precision of Estimate |
|---|------------------------|------------|-------------------------|-----------------------|
| Case file did not contain documentation to indicate verification of the timeliness of the hearing request and the date suspension of collection activity should begin | 10 | 12.5% | 1,534 | $\pm 6.06\%$ |
| Computer code was not entered into the taxpayer's account when Appeals received the hearing request | 2 | 2.5% | 307 | $\pm 2.86\%$ |

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 1,929 closed Equivalent Hearing cases could not be located by Appeals or did not contain documentation sufficient to determine if these were properly classified as Equivalent Hearing cases (see page 4).

Methodology Used to Measure the Reported Benefit:

Using a computer extract from the ACDS, we identified a population of 4,286 Equivalent Hearing cases closed between April 1 and September 30, 2004. We selected a statistical sample of 80 Equivalent Hearing cases and found 36 that Appeals was unable to locate or that did not

³ The column does not add due to rounding.

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contain documentation sufficient to determine if they were properly classified as Equivalent Hearing cases (see page 5). Using a 90 percent confidence level, we estimate:

| Reason Equivalent Hearing Case Could Not Be Reviewed | Number of Sample Cases | Error Rate | Estimate of Total Cases | Precision of Estimate |
|---|-----------------------------------|-----------------------|------------------------------------|----------------------------------|
| Unable to locate case file | 3 | 3.75% | 161 | ±3.46% |
| Case file received did not include taxpayer hearing request | 33 | 41.25% | 1,768 | ±8.97% |
| Totals | 36 | 45% | 1,929 | ±9.06% |

Type and Value of Outcome Measure:

- Revenue Protection – Potential; 154 closed CDP cases did not have the expiration date for the collection statute recalculated (see page 11).

Methodology Used to Measure the Reported Benefit:

Using a computer extract from the ACDS, we identified a total population of 12,270 CDP cases closed between April 1 and September 30, 2004. We selected a statistical sample of 80 CDP cases and found 1 case (1.25 percent) that did not have the expiration date for the collection statute recalculated, which could affect the collection of tax revenue. Using a 90 percent confidence level and a precision of ±2.04 percent, we estimate 154 cases did not have the expiration date for the collection statute recalculated.

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Appendix V

Management's Response to the Draft Report



CHIEF, APPEALS

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

AUG 15 2005

MEMORANDUM FOR TREASURY INSPECTOR FOR TAX ADMINISTRATION

FROM:

David B. Robison
Chief, Appeals

Handwritten signature of David B. Robison in black ink.

SUBJECT:

Discussion Draft Audit Report – The Office of Appeals Should Strengthen and Reinforce Procedures for Collection Due Process Cases (Audit #200410033)

I have reviewed the draft report, and I appreciate your efforts to help us improve the processing of Collection Due Process (CDP) cases. Since the inception of CDP, Appeals has been working aggressively and diligently to improve our processes and work product, and your recommendations will further both efforts.

The two major issues you identified were that certain closed case files you requested during your review could either not be located or did not contain sufficient documentation to determine if all Appeals' actions were appropriate.

Appeals understands your concern over missing closed office files and is working on a plan to maintain electronic closed office files on all closed Appeals cases which should eliminate this problem. Also, after a final determination is made, Appeals returns the complete administrative file to Collection with all the information that was available to the Appeals employee when the determination was made. Collection is another source for information and should be able to provide you with the administrative file upon request.

Appeals also understands your concern regarding missing documentation in its closed office files and the impact on Retained Jurisdiction (RJ) cases. The electronic file mentioned above, and in greater detail later in this response, should also resolve this issue. However, we do not believe the missing documentation would have significant, if any, impact on the resolution on RJ cases. Appeals only retains jurisdiction on determinations made on timely protested cases in two circumstances:

- a. If a taxpayer perceives that the Collection function did not carry out Appeals' determination as it was stated, and
- b. If a taxpayer has a change in circumstances, which affects Appeals' determination

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The only issue(s) that will be considered in a RJ hearing are those that pertain to the resolution of the CDP Notice of Determination. In the event of a RJ request, the taxpayer would first attempt to resolve the issue with Collection before being referred to Appeals. In most instances, Collection would need to secure the original file and new information from the taxpayer. It is rare that Appeals would rely solely on the contents of our closed case file for a RJ determination and seldom that taxpayers request to return to Appeals on retained jurisdiction.

We concur with the benefits recommended and the outcome measures you have used to assess such benefits. Appeals already has a number of initiatives underway which will address your recommendations.

Recommendation 1

The Chief, Appeals should evaluate case control procedures and identify weaknesses in the system to determine what further actions are needed to properly retain and locate completed CDP and Equivalent Hearing cases until the appropriate collection statute expires.

Corrective Action:

As a result of Appeals continuing efforts to create efficiencies to improve case processing and productivity, we have already begun the process of centralizing the closing of all CDP cases in two campus locations, Memphis and Fresno. The CDP case will be closed and the office file will be maintained in the centralized campus Appeals Processing Service (APS) office. This new procedure should minimize, if not eliminate, instances of missing files.

Implementation Date: December 31, 2005

Responsible Official: Director, Technical Services

Recommendation 2

Remind personnel of the requirement to retain all necessary documents supporting the Appeals decision including the taxpayer hearing request and when applicable the CDP Summary Notice of Determination, as required in Appeals' guidance and procedures. This could be accomplished through nationwide correspondence, local office meetings, and training.

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Corrective Action #1:

Appeals Processing Services (APS) has a published Desk Guide with instructions for closing CDP and Equivalent Hearing (EH) cases. The instructions include the requirements for retaining the necessary documentation that supports the Appeals decision and the taxpayer's hearing request. APS is in the process of updating IRM 8.20.7.9 with this guidance. Until the IRM is updated, APS will inform its employees of the change during monthly APS manager's conference call, post an article on the APS webpage and during discussions at local APS CPEs.

Implementation Date: December 31, 2005

Responsible Official: Director, Technical Services

Corrective Action #2:

Appeals is also working on the Electronic Case File programming and equipment procurement for the creation of paperless files. This means all important documents in all Appeals closed case files will be retained electronically which should further mitigate, if not eliminate, the incidences of missing documents in CDP cases.

As each phase of the Electronic Case File project is rolled out, and prior to full implementation, procedures will be drafted, results tested, and training held for all impacted employees. This corrective action is part of a major Appeals systems re-engineering project and must also be coordinated with our plans to have our Appeals Centralized Database System (ACDS) interact with other IRS systems.

Implementation Date: December 31, 2007

Responsible Official: Director, Technical Services

Recommendation 3

The Chief, Appeals, should emphasize that hearing officers must provide an impartiality statement in determination letters and include clear documentation supporting the statement in the Appeals case file. Managers should verify whether this requirement has been met during their reviews of completed cases.

Corrective Action:

Appeals has added guidance for documenting "no prior involvement" when securing a Form 12257 to IRM 8.7.2, the Special Collection Appeals Program manual. This documentation requirement is already in Appeals IRM 8.12.1 which provides guidance

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on Appeals Case Memorandum preparation. Adding this guidance to IRM 8.7.2, the section Appeals employees refer to when working CDP cases, will reduce, if not eliminate, the instances where the impartiality statement is missing in Form 12257 cases.

Appeals is also making the Substantive Contact Letter (L3855) mandatory. The following wording in this letter should further comply with our impartiality documentation requirement:

"You are entitled to have your conference with an Appeals employee who has had no prior involvement with the tax periods at issue, either in Appeals or in the Compliance division. I do not recall any previous involvement with these tax periods, however, if you believe I have, please notify me immediately. If I have been involved but you would still like me to conduct your hearing, you may waive this right."

Appeals will continue to emphasize to the Field the need for the impartially statement through quarterly meetings with the Area Collection coordinators, and with the assistance of the Appeals Quality Measurement System (AQMS) will continue to review cases to ensure this requirement is being met.

Implementation Date: December 31, 2005

Responsible Official: Director, Technical Services

Recommendation 4

The Chief, Appeals should remind hearing officers and managers conducting case review of the procedure to provide a clear and complete explanation in determination letters and to adhere to guidance such as that contained in the Determination Letter Guide. These reminders could be accomplished through nationwide correspondence; local office meetings, and future training session.

Corrective Action:

Appeals has incorporated an example on how to prepare the Determination Letter "Attachment" in both the Determination Letter Guide and in the latest revision of the Appeals IRM 8.7.2 - Special Collection Appeals Programs. We will highlight these changes through meetings with our Area Collection Contact coordinators, and prepare and share a summary of the revisions at group meetings with employees working CDP cases.

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Implementation Date: December 31, 2005

Responsible Official: Director, Technical Services

Recommendation 5

The Chief, Appeals should remind hearing officers and managers conducting case reviews of the procedure to verify hearing requests are properly screened for timeliness and correctness of the collection activity suspension. In addition, a statement and support documentation should be included in the Appeals case file to indicate verification was conducted.

Corrective Action:

Appeals is working with Collection to assume full responsibility for the initial input of the TC 520 on field sourced cases. By taking over this process we will ensure timely and accurate suspension of collection activity and eliminate the need to follow up with SBSE to have corrections made.

Since Appeals responsibility for the input of TC520 is not expected until late in 2005, Appeals will remind employees through the Area Collection Coordinator meetings and other training modes, of the verification and documentation requirement. Appeals headquarters staff and AQMS will review this requirement during Area Operation Reviews.

NOTE: Appeals believes the centralization of SB/SE's Collection Case Processing (CCP) units in the Philadelphia campus, which was completed in October 2004, has resulted in more timely and accurate inputs of the TC520. CCP significantly reduced the timeframe for processing the field-sourced collection work, which includes input of TC520.

Implementation Date: December 31, 2005.

Responsible Official: Director, Technical Services

If you have any questions, please have a member of your staff contact our GAO/TIGTA liaison Nancy Talajkowski at 415-744-9276.