A Concerted Effort Should Be Taken to Improve Federal Government Agency Tax Compliance

September 5, 2012

Reference Number: 2012-30-094

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

Redaction Legend:
1 = Tax Return/Return Information
2(f) = Risk Circumvention of Agency Regulation or Statute

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A CONCERTED EFFORT SHOULD BE TAKEN TO IMPROVE FEDERAL GOVERNMENT AGENCY TAX COMPLIANCE

Highlights

Final Report issued on September 5, 2012

Highlights of Reference Number: 2012-30-094 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

Federal agencies are exempt from paying Federal income taxes; however, they are not exempt from meeting their employment tax deposits and related reporting requirements. As of December 31, 2011, 70 Federal agencies with 126 delinquent tax accounts owed approximately $14 million in unpaid taxes. In addition, 18 Federal agencies had not filed or were delinquent in filing 39 employment tax returns. Federal agencies should be held to the same filing and paying standards as all American taxpayers.

WHY TIGTA DID THE AUDIT

In August 2007, TIGTA issued a report citing the need to expand the Federal Agency Delinquency Program's efforts to identify and address the causes for Federal agency delinquencies, strengthen controls over case processing, and develop strategies to resolve aged cases. Although the overall objective of the current review was to determine the effectiveness of the IRS's process to collect delinquent taxes and secure delinquent tax returns from Federal agencies, TIGTA also followed up on the effectiveness of the corrective actions taken in response to the prior TIGTA report.

WHAT TIGTA FOUND

The corrective actions the IRS took in response to the prior TIGTA report did not fully address previously identified internal control weaknesses. Specifically, a process to resolve aged Federal agency delinquent tax accounts has not been fully developed.

TIGTA analyzed 132 aged Federal agency delinquent tax accounts from the December 2008 Federal Agency Delinquency Listing. As of December 31, 2011, TIGTA identified 40 aged Federal agency delinquent tax accounts totaling approximately $2.6 million that were still open after three years. In addition, Federal Agency Delinquency Program employees suspended collection actions for 34 of the 40 aged delinquent tax accounts totaling approximately $2.4 million.

Management information reports do not provide sufficient details about the causes of Federal agency delinquencies in order to be effectively used to enhance outreach and educational efforts. A lack of control over processing Federal agency cases permitted the use of enforcement actions that violated IRS policies. In addition, limited procedures concerning the timeliness of case processing resulted in delayed case resolution.

WHAT TIGTA RECOMMENDED

To improve the administration of the Federal Agency Delinquency Program, TIGTA made several recommendations to the Commissioner, Small Business/Self-Employed Division, which include strengthening the procedures for resolving delinquent tax accounts and assisting Federal agencies with understanding and meeting their tax responsibilities.

IRS management agreed with the recommendations and the outcome measures in this report. In addition, IRS management responded that in October 2011 they had completed the corrective action for one of the recommendations. Prior to issuing the draft report, TIGTA requested the IRS provide confirmation that the updates to the management information reports were completed and that the information was useful. The IRS provided and TIGTA reviewed the updates, which addressed TIGTA's main concerns. However, the IRS did not confirm that it was making use of the updated report information.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

September 5, 2012

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION

FROM: Michael E. McKenney
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – A Concerted Effort Should Be Taken to Improve Federal Government Agency Tax Compliance (Audit # 201130035)

This report presents the results of our review to determine the effectiveness of the Internal Revenue Service's (IRS) Federal Agency Delinquency (FAD) Program to collect delinquent taxes and secure delinquent tax returns from Federal agencies. Specifically, we determined whether the corrective actions taken by the FAD Program effectively addressed the weaknesses identified in an August 2007 Treasury Inspector General for Tax Administration audit report[1] and whether resources were effectively used to maximize enforcement efforts to improve Federal agency compliance. This review was part of our Fiscal Year 2011 Annual Audit Plan and addresses the major management challenge of Tax Compliance Initiatives.

Management's complete response to the draft report is included as Appendix XI.

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 Frank Dunleavy, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations), at (213) 894-4470 (Ext. 128).

[1] Treasury Inspector General for Tax Administration, Ref. No. 2007-10-166, *Efforts to Collect Delinquent Employment Taxes Owed by Government Entities Could Be Improved* (Aug. 2007).

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Abbreviations

CFO	Chief Financial Officer
CY	Calendar Year
FAD	Federal Agency Delinquency
FSLG	Federal, State, and Local Government
FY	Fiscal Year
IDRS	Integrated Data Retrieval System
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
SB/SE	Small Business/Self-Employed
TDA	Taxpayer Delinquent Account
TDI	Taxpayer Delinquency Investigation
TIGTA	Treasury Inspector General for Tax Administration

Background

Federal Government agencies (hereafter referred to as Federal agencies) are exempt from paying Federal income taxes. However, Internal Revenue Code Sections (§§) 3121 (1984) and 3404 (1976) require Federal agencies to withhold and pay employment taxes[1] for their employees and report wages and taxes paid through the filing of the Forms 941, *Employer's Quarterly Federal Tax Return*, and the Forms W-2, *Wage and Tax Statement*. As of December 31, 2011, 70 Federal agencies with 126 delinquent tax accounts owed approximately $14 million in unpaid taxes.[2] In addition, 18 Federal agencies had not filed, or were delinquent in filing, 39 employment tax returns.[3]

The Internal Revenue Service (IRS) has two offices primarily responsible for ensuring that Federal agencies comply with the tax laws.

- The Federal, State, and Local Government (FSLG) Office of the Tax Exempt and Government Entities Division assists Federal agencies in complying with the tax laws and information return reporting through examinations, compliance checks, customer education, and outreach.
- The Federal Agency Delinquency (FAD) Program in the Small Business/Self-Employed (SB/SE) Division is responsible for collecting delinquent taxes and securing delinquent tax returns from Federal agencies.

The IRS Chief Financial Officer's (CFO) Office of Financial Management provides the FAD Program with a monthly listing of Federal agencies with delinquent tax liabilities and/or tax returns (hereafter referred to as the FAD Listing). The FAD Program uses this information to update the FAD Program database as well as to provide cases for assignment to its employees to pursue collection.

The IRS's mission is to "provide America's taxpayers top quality service to help them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all." While the IRS seeks to help Federal agencies understand their tax responsibilities, IRS employees are severely limited in what enforcement actions they can take against these delinquent agencies. Specifically:

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[1] See Appendix X for a glossary of terms.
[2] See Appendix V for a list of Federal agencies with delinquent tax accounts.
[3] See Appendix VI for a list of Federal agencies with delinquent employment tax returns.

- The Comptroller General Opinion B-161457, dated May 9, 1978, states that Federal agencies are not authorized to pay interest and penalties to the IRS for late filed or underpaid employment taxes.
- IRS Policy Statement 2-4,[4] which supports the Comptroller General Opinion, prevents the IRS from assessing interest and penalties against delinquent Federal agencies.
- Various IRS policies do not allow enforcement actions to be taken against Federal agencies with delinquent tax accounts.

In contrast, enforcement actions that IRS employees can take against business taxpayers that do not timely file or pay their employment taxes include:

- Assessment of penalties and interest.
- Filing of a tax lien.
- Sending a final notice informing the taxpayer of the intent to levy.
- Assessment of a Trust Fund Recovery Penalty on the responsible officer for nonpayment of the trust fund portion of employment taxes.
- Seizure of property.

Federal agencies are not subject to the same enforcement actions taken against business taxpayers for not filing required tax returns or not paying delinquent taxes.

The FAD Program faces an additional obstacle in the collection of delinquent taxes. Generally, Federal appropriations law[5] authorizes Federal agencies to pay their current year's taxes only with current fiscal year funds. However, IRS examination and collection processes typically occur after the current year's appropriations have expired. If a Federal agency becomes delinquent in paying its taxes after the current year, the agency is generally limited in its ability to pay prior year's delinquent taxes.

This review was a follow-up to the Treasury Inspector General for Tax Administration's (TIGTA) August 2007 audit report in which we made three recommendations to improve Federal agency case processing,[6] as well as determined whether SB/SE Division officials ensured that resources were effectively used to maximize enforcement efforts to improve Federal agency tax compliance. The review was performed at the FSLG Offices in Washington, D.C., and Austin, Texas; the FAD Program Office at the Brookhaven Campus in Holtsville, New York;

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[4] Internal Revenue Manual 1.2.20.1.2 (Nov. 6, 1981).
[5] 31 U.S.C. § 1301(a) (1982).
[6] TIGTA, Ref. No. 2007-10-166, *Efforts to Collect Delinquent Employment Taxes Owed by Government Entities Could Be Improved* (Aug. 2007). The scope of the prior audit included Federal, State, and local government entities. This review addresses only Federal agencies.

and the CFO's Office of Financial Management in Washington, D.C., during the period December 2010 through January 2012.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Detailed information on our audit objectives, scope, and methodology are presented in Appendix I. Major contributors to the report are listed in Appendix II.

Results of Review

Corrective Actions on Previously Identified Internal Control Weaknesses Have Not Been Fully Implemented

As a result of our August 2007 audit report, SB/SE Division officials agreed to implement the following actions.

- Develop a process for resolving aged Federal agency delinquent tax accounts.
- Develop a methodology for recording and sharing information regarding the causes and resulting case resolution actions of Federal agency tax delinquencies to allow the FSLG Office to better focus its outreach and education efforts.
- Ensure comprehensive guidelines and procedures were developed for assigning, controlling, and resolving Federal agency tax delinquencies.

During this review, we followed up to assess the effectiveness of the IRS's corrective actions and found that previously identified weaknesses continue to exist.

The Government Accountability Office's *Standards for Internal Control in the Federal Government*[7] require that monitoring should assess the quality of performance over time and ensure that the findings of audits are promptly resolved. By not fully implementing the corrective actions to address the recommendations from our prior report, SB/SE Division officials have not been as effective in educating Federal agencies about their tax responsibilities, preventing the violation of IRS policies, and reducing the amount of time required to work and close FAD Program cases.

A process to adequately resolve aged Federal agency delinquent tax accounts has not been fully developed

In our August 2007 report, SB/SE Division officials responded that their analysts met with FAD Program employees to discuss and develop Internal Revenue Manual (IRM) procedures to resolve aged Federal agency delinquent tax accounts.[8] The analysts were to review current procedures, identify obstacles, and explore alternative processes. The analysts were then to provide their findings and recommendations to IRS executives for consideration.

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[7] Government Accountability Office (formerly known as the General Accounting Office), GAO/AIMD-00-21.3.1, *Standards for Internal Control in the Federal Government* p. 20 (November 1999).
[8] IRM 5.19.15 (Sep. 12, 2008).

During our current review, we did not identify any new IRM procedures[9] that specifically addressed the resolution of aged Federal agency delinquent tax accounts. For the FAD Program, delinquent tax accounts are resolved by the filing of the delinquent tax returns, paying of delinquent taxes, or suspension of collection actions against the delinquent Federal agencies. SB/SE Division officials confirmed that there are no specific instructions for resolving aged Federal agency delinquent tax accounts. However, an analyst told us that procedures were added for resolving tax accounts for which the Federal agency did not file the tax returns that were due or for which taxes were owed but not paid. These procedures included manually filing tax returns[10] for the delinquent Federal agencies and/or suspending the collection of taxes[11] owed by them. The analyst told us that these procedures were applied to the aged delinquent tax accounts referenced in our previous report.

We reviewed the IRM[12] and determined that the added procedures were general processing instructions applicable to all Federal agency delinquencies. These added procedures can be used to resolve the tax obligations for Federal agencies that have not filed their tax returns. However, the FAD Program is limited in the enforcement actions it can take against delinquent Federal agencies. For those agencies where collection actions were suspended, the age of their delinquent tax accounts will continue to increase even though the FAD Program considers them resolved.

To determine the impact of unresolved aged delinquent tax accounts on the FAD Program, we compared 132 aged delinquent tax accounts for 68 Federal agencies on the December 2008 FAD Listing to the December 2011 FAD Listing. Specifically, we identified the following IRS actions taken on the 132 aged delinquent tax accounts from the December 2008 FAD Listing:

- 43 (33 percent) were closed because the Federal agencies paid the delinquent taxes owed.
- 48 (36 percent) had their collection statutes expire and the IRS was unable to collect $175,954.
- 40 (30 percent) were still open and remain unresolved three years later.[13] In addition, 34 (85 percent) of the 40 open aged delinquent tax accounts had collection actions suspended by the IRS.

As of December 31, 2011, 40 aged Federal agency delinquent tax accounts still remain unresolved after three years.

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[9] IRM 5.19.15 (Dec. 3, 2010).
[10] If attempts to secure a delinquent return are unsuccessful, the IRS can file a substitute return for the Federal agency under Internal Revenue Code § 6020(b) (1984).
[11] When the IRS is unable to contact the taxpayer, collection of the delinquent tax account can be suspended and removed from active inventory. This may be reversed if certain conditions occur, such as the receipt of a payment or an overpayment credited from another tax period.
[12] IRM 5.19.5 (Dec. 3, 2010).
[13] See Appendix IX for a list of the 23 Federal agencies with 40 aged delinquent tax accounts.

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Figure 1 reflects our detailed analysis of the 132 aged delinquent tax accounts from the December 2008 FAD Listing.

Figure 1: Analysis of Aged Federal Agency Delinquent Tax Accounts Found on the December 2008 Federal Agency Delinquency Listing (as of December 31, 2011)

Description of Activity on Aged Tax Accounts	Number of Accounts	Tax Revenue Owed, Paid in Full, or Lost
Aged Delinquent Tax Accounts/Tax Revenue Owed (as of December 31, 2008)	132	$4,238,348
Status as of December 31, 2011:		
• Closed – Full Paid/Tax Revenue Collected	43	$1,439,632
• Closed – Statute Expired/Tax Revenue Lost	48	$175,954
• Open – Collection Actions Suspended/Tax Revenue Owed[14]	34	$2,376,691
• Open – Being Worked in the FAD Program/Tax Revenue Owed[15]	6	$233,829
• **************1*************	**1**	***1***

Source: Results of comparison of FAD Listings for Calendar Years (CY) 2008 and 2011 and research of the IRS's Integrated Data Retrieval System (IDRS) and Master File to identify the status of the aged Federal agency delinquent tax accounts.

FAD Program employees suspended collection for 34 of the 40 aged Federal agency delinquent tax accounts for various reasons that included being unable to contact agency personnel and that the amount owed was below the dollar collection threshold of **2(f)**. Because the IRS has suspended pursuing these aged delinquent tax accounts, the possibility that the delinquent

[14] Partial payments of $697 were made on three delinquent tax accounts. However, the accounts are still delinquent and are in suspended collection status. These payments are not included in the total of the revenue collected.
[15] Partial payments of $3,295 were made on two delinquent tax accounts. However, the accounts are still delinquent and are not in suspended collection status. These payments are not included in the total of the revenue collected. The remaining four tax accounts did not have any payment activity from CYs 2008 through 2011.

Federal agencies will now voluntarily pay their outstanding tax liabilities is very low. Figure 2 reflects our analyses of the 34 suspended aged delinquent tax accounts.

Figure 2: Analysis of the 34 Aged Federal Agency Delinquent Tax Accounts Found on the December 2008 Federal Agency Delinquency Listing With Suspended Collection Actions as of December 31, 2011

Description of Suspended Collection Action	Number of Aged Tax Accounts With Suspended Collection Actions	Percentage of Aged Tax Accounts With Suspended Collection Actions	Dollars Owed for Aged Tax Accounts With Suspended Collection Actions
Unable to Contact	14	41%	$94,432
****1****[16]	**1**	**1**	******1*****
Below**2(f)** Threshold	8	24%	$3,316
********1*********[17]	**1**	**1**	*****1*****
Total	34	100%	$2,376,691

Source: Results of the comparison of FAD Listings for CYs 2008 and 2011 and research of the IRS's IDRS and Master File to identify aged Federal agency delinquent tax accounts with suspended collection actions.

Figure 3 reflects the collection statute expiration for all 40 open aged Federal agency delinquent tax accounts from the December 2008 FAD Listing as of December 31, 2011. The collection statute for 10 of the 40 delinquent tax accounts will expire in CY 2012, with more than $220,000 that could no longer be collectible. As of April 30, 2012, six of the 10 delinquent tax accounts owed by five Federal agencies were already no longer collectible and have resulted in the loss of $193,078 in tax revenue.

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Figure 3: Analysis of the Collection Statute Expiration Dates for 40 Aged Federal Agency Delinquent Tax Accounts Found on the December 2008 Federal Agency Delinquency Listing (as of December 31, 2011)

Number of Aged Delinquent Tax Accounts	Dollars Owed for the Aged Delinquent Tax Accounts	CY Collection Statute Will Expire for Aged Delinquent Tax Accounts
10	$222,439	2012
6	$717,822	2013
9	$1,391,165	2014
5	$7,439	2015
4	$7,904	2016
5	$263,121	2017
1	***1***	***1***
Total **1**	*******1*******	

Source: Results of comparison of the FAD Listings for CYs 2008 through 2011 and research of the IRS's IDRS and Master File to identify the aged Federal agency delinquent tax accounts and the collection statute expiration dates.

At the onset of this review, we wanted to determine the impact that unresolved aged Federal agency delinquent tax accounts had on tax administration and whether additional procedures were needed. Our results show that the procedures FAD Program officials implemented, which include suspending collection action on aged delinquent tax accounts, negatively impact tax administration and result in the loss of tax revenue.

In addition, our results support the need to revisit the current procedures and develop ones that will improve the protection of tax revenue. More than 90 percent of the delinquent taxes owed are employment taxes, which include monies withheld from employees' wages that are required to be remitted to the IRS on the employees' behalf. These taxes are necessary to support Federal programs like Social Security and Medicare.

Limited enforcement actions impact the resolution of aged Federal agency delinquent tax accounts

Due to the IRS's limitations on enforcement actions that can be taken against Federal agencies, FAD Program employees work unresolved aged cases by making phone calls and sending e-mails or letters to the delinquent Federal agencies. For example, the IRM[18] requires employees to make as many as four telephone calls at different periods of time and send written correspondence to the delinquent Federal agencies before suspending collection actions on the delinquent tax accounts.

During this review, we learned that in May and June 2005, the IRS CFO issued two letters to the delinquent Federal agencies' CFOs in an effort to assist them with reducing their agency's tax delinquencies. The first letter stated that the IRS was committed to helping the delinquent Federal agencies comply with the tax laws. The second letter[19] was a final attempt to resolve the outstanding tax delinquencies.

We were advised by the IRS CFO that the letters were issued only during Fiscal Year (FY) 2005 and neither the CFO's Office nor the FAD Program measured the impact the letters had on reducing Federal agencies' tax delinquencies. In an attempt to assess the impact of the IRS CFO's letters, we reviewed IRS documentation that showed Federal agencies owed $406 million in tax delinquencies as of June 2005. By December 2006, these delinquent tax accounts had been reduced to $45 million. Based on these results, we believe that the reductions could have been attributed to the efforts of the FAD Program, as well as the issuance of the IRS CFO's letters to the delinquent Federal agencies.[20]

Several options are available for Federal agencies to pay delinquent tax debts

Funds appropriated to Federal agencies for their operations generally have to be spent within the year of the appropriation. However, during our review, we found that there may be options available for Federal agencies to pay prior year tax debts. These options include:

- Requesting a supplemental or deficiency appropriation.
- Using prior year unobligated expired funds.
- Using up to one percent of current year appropriated funds.

We believe that if the IRS CFO reinstituted issuing the letters to the CFOs of the delinquent Federal agencies and included the above payment options, the letters could assist in demonstrating the IRS's commitment to help the Federal agencies comply with the tax laws. It

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[18] IRM 5.19.5 (Dec. 3, 2010).
[19] See Appendix VIII for a sample of the IRS CFO's letter.
[20] In June 2006, the IRS centralized the collection of Federal agency delinquent tax accounts at the Brookhaven Campus to ensure employees consistently and timely processed the delinquent tax accounts.

is our opinion that a letter from the IRS CFO to the delinquent Federal agencies' CFOs raises awareness of and accountability for the outstanding tax debts.

Because current IRS enforcement actions against delinquent Federal agencies are limited, SB/SE Division officials should discuss the results of this report with IRS Chief Counsel to determine what, if any, regulatory or legislative remedies might be appropriate to better assist the IRS in resolving aged Federal agency delinquent tax accounts. We believe that the IRS CFO's letters combined with FAD Program employees' communication efforts, as well as the implementation of favorable regulatory or legislative remedies could assist in resolving many of the aged Federal agencies delinquent tax accounts.

Limited information on FAD Program reports hinders outreach and educational efforts

In our August 2007 report, we recommended that SB/SE Division officials develop a methodology for recording and sharing information with the FSLG Office about the causes of Federal agency delinquencies and the resulting case resolution actions. We believed that this information would help the FSLG Office to better focus its outreach and education efforts. The IRS responded that the FAD Program database had been developed to capture the causes and the resulting case resolution actions. In addition, analysts had planned to create a process to share this information with the FSLG Office. This process included the production of quarterly Federal Agency Delinquency Program reports (hereafter referred to as Cause and Cure Reports).

We reviewed the first quarter FY 2011 Cause and Cure Report and determined that the primary causes of Federal agency delinquencies, taken from the FAD Program database and listed in the report, were vague. Examples of the causes for delinquencies shown in the Cause and Cure Report were:

- Agency.
- IRS Processing.
- Dead End.

We reviewed information recorded in the FAD Program database and identified that the Secondary Issues field[21] had more descriptive delinquency causes. However, these descriptions were not captured on the Cause and Cure Report. Some examples included:

- Agency did not file.
- Payment misapplied to other tax period.
- Unable to locate payment.

[21] See Appendix VII for examples of primary causes and secondary issues.

FSLG Office management advised us that, historically, the Cause and Cure Reports have not provided an explanation for the causes of the Federal agencies' delinquencies; instead, they have only shown that there was a delinquency and it was resolved. If the Cause and Cure Reports provided more information, the FSLG Office could use the reports to identify issues that need to be reviewed during their examinations of Federal agencies, as well as identify general topics to address at their annual Federal agency seminars.[22] In addition, the FSLG Office could use these reports to help focus its overall Federal agency outreach and education efforts.

We believe opportunities exist for SB/SE Division officials to improve the administration of the FAD Program by providing FSLG Office management with information that can be used to help Federal agencies understand and meet their tax responsibilities. Adding the Secondary Issues field information from the FAD Program database to the Cause and Cure Reports would allow the FSLG Office to use the reports to tailor educational topics for the annual seminars. In addition, FSLG Office management can use the reports to identify delinquent Federal agencies that should be invited to its seminars to educate them about their tax compliance obligations.

During this review, we asked FLSG and FAD Program officials whether they discussed and identified improvements for the Cause and Cure Reports. We were told that they had not discussed the reports; however, as a result of our audit, FSLG Office management advised us that there was an option they would consider. In August 2011, FAD Program and FSLG Office management began developing proposed updates to the FAD Program database, which included capturing additional fields on the Cause and Cure Reports. We did not review the proposed updates, but FSLG management agreed the additional information could better assist them with identifying specific topics to share with Federal agencies experiencing tax compliance issues.

Procedures for processing FAD Program cases were not followed

In response to our August 2007 report, SB/SE Division officials developed new procedures[23] for FAD Program case processing.[24] To determine whether the new procedures improved case processing and whether resources were efficiently used, we judgmentally selected and reviewed a total of 70 open and closed FAD Program cases.[25] We selected:

- 50 cases from a population of 1,834 taxpayer delinquent accounts (TDA) and taxpayer delinquency investigations (TDI) closed during FYs 2009 and 2010.
- 10 unresolved cases from a population of 27 open TDAs in which collection actions were suspended in either FY 2009 or FY 2010.

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[22] The FSLG Office conducts annual seminars to provide education and outreach for Federal agencies regarding tax law updates that include filing and paying requirements and changes in withholding rates and forms.
[23] IRM 5.19.5 (Dec. 3, 2010).
[24] A case represents either a delinquent tax return and/or a delinquent tax account that has not been filed or paid, as with quarterly employment taxes and/or annual unemployment taxes.
[25] A judgmental sample is a nonstatistical sample, the results of which cannot be used to project to the population.

- 10 cases from a population of 92 unresolved TDAs open for more than 360 days from the November 2010 CFO's FAD Listing.[26]

Our results showed internal controls need strengthening to ensure employees follow procedures when processing FAD Program cases. For example, 54 (77 percent) of the 70 open or closed cases had one or more of the following errors:

- For 25 (36 percent) of 70 cases, FAD Program employees did not refer Federal agencies with repeat tax delinquencies to the FSLG Office for education. The IRM[27] states that many Federal agency tax delinquencies are due to a lack of understanding of the tax requirements. When employees determine this to be the case, they should refer the delinquent Federal agency to the FSLG Office to address the agency's educational needs through outreach.

- For 17 (24 percent) of 70 cases, FAD Program employees did not take follow-up actions[28] within the required 60-calendar-day time period. They took an average of 95 calendar days (ranging from 63 to 282 calendar days). Because FAD Program employees are limited in the enforcement actions that they can take, SB/SE Division officials developed the 60-calendar-day time standard as part of a series of actions to help demonstrate continuous and consistent efforts to resolve Federal agency tax delinquencies.

- For 25 (36 percent) of 70 cases, a final notice was issued; this is an enforcement action against a Federal agency and is a violation of IRS policy.

- For 17 (24 percent) of 70 cases, IRS employees not assigned to the FAD Program manually assessed $335,957 in penalties and interest; this is an enforcement action against a Federal agency and is a violation of IRS policy. While FAD Program employees identified and reversed the incorrect assessments, all of the actions (from the initial assessment of the penalties and interest to their reversal) unnecessarily wasted IRS resources that could have been put to better use.

- For 17 (24 percent) of 70 cases, FAD Program employees took an average of 686 calendar days (ranging from 396 to 995 calendar days) to close Federal agency delinquent tax cases. While there is no case closure time standard in the IRM for Federal agency delinquent tax cases, FAD Program officials stated that each agency's circumstances are considered unique and that FAD Program employees have to use their own judgment as to when to contact and ultimately close their cases. However, we

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[27] IRM 5.19.15.1.1 (3) (Dec. 3, 2010).

[28] Follow-up actions include contacting the Federal agency by telephone, e-mail, or letter.

believe that any case closure taking longer than 360 calendar days should be considered excessive.

We discussed the above results with SB/SE Division officials who agreed that FAD Program employees did not always follow procedures when processing Federal agency delinquency cases. In October 2011, an SB/SE Division analyst advised us that a programming request was submitted to the Office of the Chief Technology Officer to suppress the issuance of final notices to Federal agencies. The programming change is scheduled for implementation later in FY 2012. In the interim, SB/SE Division officials implemented temporary guidance to manually place holds on delinquent Federal agency accounts to prevent the issuance of notices. We were also advised that a programming request is being created to prevent the assessment of penalties and interest against Federal agencies. SB/SE Division officials issued an alert in September 2011 to non-FAD Program employees stating that they are not to assess penalties and interest against Federal agencies. If these programming changes do not occur as planned, the IRS continues to run the risk of violating its own policies by taking enforcement actions against Federal agencies with delinquent tax liabilities.

Recommendations

The Commissioner, SB/SE Division, should:

Recommendation 1: Coordinate with the IRS CFO's Office to develop a process to send formal letters to the delinquent Federal agencies' CFOs, including those agencies for which collection of the delinquent tax accounts has been suspended and collection statutes are in jeopardy. The letters should also provide information on the options available to Federal agencies to pay prior year tax debts.

> ***Management's Response:*** IRS management agreed with this recommendation. They agree there should be a mechanism for ensuring delinquent Federal agencies' CFOs are aware of the tax debts that have not been resolved after FAD program processing as well as the payment options available. SB/SE Division officials will discuss with the IRS CFO and the Tax Exempt and Government Entities Division the most feasible options for communicating a message concerning these cases.

Recommendation 2: Discuss the results of this report with the IRS Chief Counsel to determine what, if any, regulatory or legislative changes need to be pursued that will allow the IRS to collect taxes from current year appropriations of Federal agencies that have not fulfilled their tax obligations.

> ***Management's Response:*** IRS management agreed with this recommendation. They will discuss with Counsel any regulatory or legislative changes that can be pursued that will allow the IRS to collect taxes from the current year appropriations of Federal agencies that have not fulfilled their tax obligations.

Recommendation 3: Coordinate with the Commissioner, Tax Exempt and Government Entities Division, to ensure that the FAD Program completes the development of proposed updates to the FAD Program database, which include capturing the Secondary Issues field on the Cause and Cure Reports to meet the FSLG Office's needs.

> ***Management's Response:*** IRS management agreed with this recommendation. The database was updated in October 2011 with changes to the Cause and Cure Report to capture the secondary issues. The IRS will continue to update the FAD Program database when applicable to capture data that will assist the FSLG Office. In addition, the IRS will continue quarterly calls between the FAD Program, SB/SE Division Collection Policy, FSLG Office, and IRS CFO to discuss and share identified trends, issues, and potential program changes.
>
> ***Office of Audit Comment:*** Although the IRS commented that the updates to the FAD Program database were completed in October 2011, prior to issuing the draft report, we requested the IRS provide confirmation that the updates to the Cause and Cure Reports were completed and that they were useful to the FSLG Office. The IRS provided the updates, which we reviewed and did not have any continued concerns. However, the IRS did not confirm that it was making use of the updated report information.

Recommendation 4: Ensure FAD Program employees adhere to procedures when processing delinquent Federal agency cases.

> ***Management's Response:*** IRS management agreed with this recommendation. They will update IRM 5.19.15 to provide specific guidance on when employees need to make referrals to the FSLG Office and take the appropriate actions, when required. The updated IRM will be used for training and program reviews.

Recommendation 5: Establish timeliness standards for FAD Program employees to follow when processing Federal agency delinquency cases.

> ***Management's Response:*** IRS management agreed with this recommendation. Specific timeline guidelines will be discussed with Collection Policy, SB/SE Division, and the FSLG Office and based on the results of these discussions, the IRM will be updated.

Performance Measures Need to Be Developed to Assess the Federal Agency Delinquency Program's Effectiveness and Impact on Tax Administration

Based on our analysis of information provided by FAD Program officials, for FYs 2008 through 2011, the FAD Program resolved nearly $197 million in delinquent taxes owed and closed out of its inventory approximately 2,900 delinquent tax returns due from Federal agencies. However, these and other business results are not readily captured or reported by the SB/SE Division to demonstrate the FAD Program's effectiveness and its impact on tax administration. In addition, SB/SE Division officials stated that performance measures, such as timeliness and accuracy, have not been established for the FAD Program. As a result, National Quality Review System reviewers[29] do not evaluate FAD Program cases or capture program data in order to report business quality results.

The IRS established a balanced performance measurement system to measure whether its programs achieve established performance goals. Balanced measures emphasize accountability for achieving results and reflect the IRS's priorities, which are provided in its mission and two strategic goals. The IRS's balanced measures are comprised of three key components: Customer Satisfaction, Employee Satisfaction, and Business Results. These measures should be considered when setting organizational objectives, establishing goals, and assessing progress and results.

In September 2006, SB/SE Division officials signed a Memorandum of Understanding with Tax Exempt and Government Entities Division officials providing collection services for TDAs and TDIs through September 2011. In the document, SB/SE Division officials listed performance measures they would use to evaluate the effectiveness of the Collection Program. The measures included capturing the number of Tax Exempt and Government Entities Division taxpayer cases received in the Collection inventory, the number of TDAs and TDIs that were resolved, and the ending TDA and TDI inventories. We asked whether these performance measures were captured by the SB/SE Division and used to report the business results for the FAD Program. SB/SE Division officials informed us that the current Memorandum of Understanding, signed in January 2012, continues to provide the collection services but no longer includes measures because they are captured on Collection Activity Reports. We reviewed the Collection Activity Reports and found that there are no specific measures listed that can be used to evaluate FAD Program effectiveness.

During this review, SB/SE Division officials asked the TIGTA to evaluate whether allocating resources to (and centralizing) the FAD Program was cost effective. SB/SE Division officials were very interested in the results because the FAD Program was centralized in response to a prior TIGTA recommendation. We completed cost-benefit analyses of the FAD Program's operating costs and performance data for FYs 2008 through 2011, which included an attempt to determine its return on investment. However, we were unable to determine an accurate return on investment because FAD Program officials include suspended collection actions and expired collection statute tax accounts in the tax revenue resolved from closed Federal agency delinquent tax accounts. Return on investment should be based on the revenue the IRS actually collected less the costs it incurred to pursue and obtain that revenue. Currently, FAD Program officials do not track this information, and time constraints during this review did not permit us to separate

[29] The National Quality Review System reviewers capture national program data obtained through case reviews and reports of official organizational business quality results.

the dollars actually collected from the dollars with suspended collection actions and the dollars lost due to the collection statute expirations on the various tax accounts.

Recommendation

Recommendation 6: The Commissioner, SB/SE Division, should identify and separate the tax revenues actually collected from the suspended collection actions and the delinquent tax accounts with expired collection statutes to determine the FAD Program's true return on investment.

> ***Management's Response:*** IRS management agreed with the recommendation and will work with Information Technology, Tax Exempt and Government Entities Division, and the CFO to determine if the data can be captured and if it would be cost effective to capture.

Appendix I

Detailed Objectives, Scope, and Methodology

Our overall objective was to determine the effectiveness of the IRS's FAD Program to collect delinquent taxes and secure delinquent tax returns from Federal agencies. Specifically, we determined whether the corrective actions taken by the IRS effectively addressed the weaknesses identified in an August 2007 TIGTA audit report[1] and whether SB/SE Division officials ensured that resources were effectively used to maximize enforcement efforts to improve Federal agency tax compliance. To accomplish these objectives, we:

I. Determined whether corrective actions to address recommendations from the previous audit report were implemented and were effectively working.

A. Determined whether the FAD Program database generates reports for the FSLG Office that list the causes of deficiencies and the actions that resolved these cases.

B. Determined whether comprehensive guidelines and procedures were developed for assigning, controlling, and resolving Federal agency delinquency cases.

C. Identified the process implemented for the FAD Program to resolve aged Federal agency delinquent tax accounts. Assessed whether the process is effective and has demonstrated improvement.

II. Determined whether the IRS has established goals and measures to monitor the FAD Program's progress toward achieving its purpose. This included assessing whether IRS resources are being effectively and efficiently used to improve Federal agency compliance.

A. Reviewed performance reports for FYs 2009 and 2010 to identify measures being used to monitor FAD Program performance. We discussed reasons why measures have not been established. In addition, we identified performance measures used by other Collection functions that could be used for the FAD Program.

B. Conducted cost-benefit analyses of the FAD Program to evaluate its return on investment for FYs 2008 through 2011.

III. Determined whether the FAD Program followed procedures to process cases and whether they efficiently used resources to improve Federal agency compliance.

[1] TIGTA, Ref. No. 2007-10-166, *Efforts to Collect Delinquent Employment Taxes Owed by Government Entities Could Be Improved* (Aug. 2007).

A. Determined whether the new procedures improved the processing of FAD Program cases:

   1. Identified the populations of closed TDIs and TDAs for FYs 2009 and 2010 as 1,211 TDIs and 623 TDAs, respectively.

   2. Selected a judgmental sample[2] of 50 closed FAD Program cases (25 TDIs and 25 TDAs). We used the judgmental samples in this Step and in Step B. after validating the computer-processed data by randomly selecting a total of 15 cases from the identified population of closed TDIs and TDAs. We requested the hard copy documents for the 15 cases from FAD Program management and compared them to entity and tax accounts data on the IDRS. All data matched for the 15 cases.

   3. Determined whether employees followed internal control procedures when processing cases.

      a) Identified indications of inefficient use of resources (*e.g.*, long delays, phone calls, or correspondence in excess of IRM requirements).

      b) Recorded the results for each case.

      c) Calculated the total number of errors and error rates for each attribute for processing TDAs and TDIs.

B. Determined whether resources were used efficiently to process unresolved FAD Program cases. We selected a judgmental sample of 20 unresolved cases (10 open – unresolved for more than a year and 10 closed – closed as currently not collectible or unable to contact). We determined the amount of time FAD Program employees expended to contact Federal agencies to secure tax returns and delinquent payments. In addition, we determined the potential causes of any identified inefficient use of resources. Specifically, we determined whether:

   1. The FAD Program referred Federal agencies to the FSLG Office to conduct education and outreach visits.

   2. The IRS CFO Office issued letters to Federal agency CFOs to address delinquencies.

   3. The other IRS program processing procedures resulted in inefficiencies or wasted resources.

[2] We determined that judgmental samples would be the most cost-effective way to identify noncompliance and prompt management to take corrective action. A judgmental sample is a nonstatistical sample, the results of which cannot be used to project to the population.

C. Determined whether Federal agencies with unresolved cases have newer tax modules with little or no activity that indicate they continually do not comply or is a repeat condition with their filing and payment requirements.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective: a Comptroller General Opinion; guidance from the Office of Management and Budget; and IRS policies, procedures, and practices for resolving Federal agency delinquent cases. We evaluated the controls by reviewing source material, interviewing management, reviewing open and closed cases, and researching taxpayer accounts.

Appendix II

Major Contributors to This Report

Margaret E. Begg, Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Frank Jones, Director
Bryce Kisler, Director
Deborah Smallwood, Audit Manager
Lynn Ross, Lead Auditor
Andrea Barnes, Senior Auditor
Margaret Filippelli, Senior Auditor

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 Financial Officer OS:CFO
Commissioner, Tax Exempt and Government Entities Division SE:T
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Deputy Commissioner, Tax Exempt and Government Entities Division SE:T
Director, Campus Compliance Services, Small Business/Self-Employed Division SE:S:CCS
Director, Enterprise Collection Strategy, Small Business/Self-Employed Division SE:S:ESC
Director, Government Entities, Tax Exempt and Government Entities Division SE:T:GE
Director, Campus Compliance Operations, Brookhaven, Small Business/Self-Employed Division SE:S:CCS:CCO:BR
Director, Collection Policy, Small Business/Self-Employed Division SE:S:ESC:CP
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaisons:

Commissioner, Small Business/Self-Employed Division SE:S
Commissioner, Tax Exempt and Government Entities Division SE:T

Appendix IV

Outcome Measures

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

Type and Value of Outcome Measure:

- Increased Revenue – Potential; approximately $2.4 million in delinquent taxes that may be collected if the 34 aged tax accounts[1] are resolved (see page 4).

Methodology Used to Measure the Reported Benefit:

We compared 132 aged delinquent tax accounts on the December 2008 FAD Listing generated by the IRS CFO's Office of Financial Management to the aged tax accounts on the December 2011 FAD Listing to determine whether any of the aged tax accounts from CY 2008 were still unresolved. Our comparison revealed that 40 aged tax accounts on the December 2008 listing were still reflected on the December 2011 listing, three years later. The 40 delinquent tax accounts represent approximately $2.6 million in total delinquent taxes owed by Federal agencies. However, $193,078 of the $2.6 million was lost due to the expired collection statutes for six of the 40 delinquent tax accounts as of April 30, 2012. Therefore, only $2.4 million still remains collectible.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Actual; 25 Federal agencies' delinquent accounts were erroneously issued final notices, which are enforcement actions that are a violation of IRS policy (see page 4).

Methodology Used to Measure the Reported Benefit:

- Our analysis of the judgmental sample of 50 closed cases (25 TDAs and 25 TDIs) and a second sample of 20 unresolved TDA cases indicated that 25 of the 70 Federal agencies had been sent final notices.
- We used the IDRS to verify that the notices were issued.

[1] See Appendix X for a glossary of terms.

Type and Value of Outcome Measure:

- Taxpayer Burden – Actual; 17 Federal agencies' delinquent accounts showed that FAD Program employees did not take follow-up actions within the required 60-calendar-day time period (see page 4).

Methodology Used to Measure the Reported Benefit:

Because FAD Program employees are limited in the enforcement actions that they can take, SB/SE Division officials developed the 60-calendar-day time standard as part of a series of actions to help demonstrate continuous and consistent efforts to resolve Federal agency tax delinquencies. As a result, FAD Program employees did not demonstrate consistent efforts for the 17 as was shown for the remaining 53 delinquent tax cases that received timely follow-up actions.

- Our analysis of the judgmental sample of 50 closed cases (25 TDAs and 25 TDIs) and the second sample of 20 unresolved TDAs indicated 17 had untimely follow-up actions.
- We determined the timeliness errors by counting the number of days where no activity occurred between the last action and the next action taken by FAD Program employees.
- The average number of calendar days was 95, and the range was from 63 to 282 calendar days.

Appendix V

Federal Agencies With Delinquent Tax Accounts (as of December 31, 2011)

Count	Federal Agency Name[1]	Number of Delinquent Tax Accounts	Total Delinquent Taxes Owed
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
*1**	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****

[1] Federal agencies may have more than one Taxpayer Identification Number for various programs, locations, functions, or offices. In addition, the acronyms shown in the "Federal Agency Name" columns in Appendices V, VI, and IX were established by their respective agency and used by the IRS. The Federal agencies did not provide definitions for the acronyms.

Count	Federal Agency Name	Number of Delinquent Tax Accounts	Total Delinquent Taxes Owed
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****

Count	Federal Agency Name	Number of Delinquent Tax Accounts	Total Delinquent Taxes Owed
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
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1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****
1	****************1**************	**1**	****1*****

Count	Federal Agency Name	Number of Delinquent Tax Accounts	Total Delinquent Taxes Owed
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
1	***************1**************	**1**	****1*****
	TOTAL	**126**	**$13,867,144**

Source: The IRS's December 2011 FAD Listing.

Appendix VI

Federal Agencies With Delinquent Employment Tax Returns (as of December 31, 2011)

Count	Federal Agency Name	Number of Delinquent Employment Tax Returns
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
1	********************1******************	**1**
	Total	**39**

Source: The IRS's December 2011 FAD Listing.

Appendix VII

Primary Causes and Secondary Issues for Closed Federal Agency Delinquent Tax Accounts

Primary Causes Listed on Cause and Cure Reports	Top Five Secondary Issues in the FAD Program Database for the Primary Causes
Agency	Agency Did Not Timely File
	Balance Due Return Filed
	Did Not File or Close Filing Requirement
	Miscellaneous Assessment by Examination
	Tax Return Math Error
IRS Processing	Payment Misapplied to Other Tax Period
	Did Not File
	Other
	Account F Coded[1] – Error Penalty and Interest Assessment
	Did Not File Return Or Close Filing Requirement
Electronic Federal Tax Payment System	Systemic Federal Tax Error
	Did Not File
	Unprocessable Electronically Filed/Paper Tax Return Filed
	Miscellaneous Assessment by Examination
	Tax Return Math Error
Dead End	Did Not File
	Unable to Research/Locate/Determine Information (TDIs)
	Did Not File Final Return or Close Filing Requirement
	Unable to Research/Locate/Determine Information (TDAs)
	Unable to Locate Payment
Other/Not Selected	Other

Source: TIGTA analysis of the closed cases in the FAD Program database for FYs 2009 and 2010.

[1] The coding is for Federal agencies on the IRS's IDRS and Master File.

Appendix VIII

Sample Letter Sent to a Federal Agency's Chief Financial Officer Regarding a Delinquent Tax Account

********************************1**
********************************1**
********************************1**
********************************1**
********************************1**
********************************1**

Source: IRS CFO's Office of Financial Management.

Appendix IX

Aged Federal Agency Delinquent Tax Accounts Unresolved for More Than Three Years

Count	Federal Agency Name[1]	Number of Delinquent Tax Accounts	Delinquent Taxes Owed
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****
1	********************1*****************	**1**	*****1****

[1] Federal agencies may have more than one Taxpayer Identification Number for various programs, locations, functions, or offices.

Count	Federal Agency Name	Number of Delinquent Tax Accounts	Delinquent Taxes Owed
1	*******************1************	**1**	*****1***
1	*******************1************	**1**	*****1***
1	*******************1************	**1**	*****1***
1	*******************1************	**1**	*****1***
1	*******************1************	**1**	*****1***
1	*******************1************	**1**	*****1***
	Total	**40**	**$2,610,520**

Source: Results of comparison of the FAD Listings for CYs 2008 through 2011 and research of the IRS's IDRS and Master File to identify the aged Federal agency delinquent tax accounts.

Appendix X

Glossary of Terms

Aged Cases/Tax Accounts – Aged cases/tax accounts are assigned to and unresolved by a program for an extended period of time. For purposes of this audit, we defined an aged case/tax account as open and unresolved for 360 calendar days or longer (the FAD Program does not have aged case/tax account criteria).

Anti-Deficiency Act – This law prohibits making or authorizing an expenditure from, or creating or authorizing an obligation under, any appropriation or fund in excess of the amount available in the appropriation or fund unless authorized by law.

Calendar Year – A 12-consecutive-month period ending on December 31.

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

Cause and Cure Reports – Reports developed by the FAD Program from its review of Federal agencies' noncompliance with tax laws that are sent quarterly to assist the FSLG Office with education, outreach, and workload selection for examinations.

Collection Statute Expiration Date – Collection Statute Expiration Date established by law provides that the IRS has 10 years from the date it receives a tax return or assesses tax to collect any amount due from a taxpayer for a given tax period.

Currently Not Collectible – Tax accounts are reported as currently uncollectible when the taxpayer has no income or assets which are, by law, typically subject to levy.

Current Year Appropriated Funds – Funds authorized by Congress designated for a specific purpose to be used for expenses properly incurred for the fiscal year for which the appropriation was made.

Delinquent Tax Accounts – A tax account for which part or all of the amount owed to the IRS is overdue. These amounts can represent quarterly taxes such as employment taxes or annual taxes for unemployment taxes that are due once per year.

Employment Taxes – The payment of trust fund payroll deposits for Federal, Social Security, and Medicare withholding, reported on Form 941, *Employer's Quarterly Federal Tax Return*.

Final Notice – A final balance due notice advises the taxpayer of the intent to levy his or her assets and informs him or her on how to prevent collection action.

Fiscal Year – A 12-consecutive-month period that ends on the last day of any month, except December. The Federal Government's fiscal year begins on October 1 and ends on September 30.

Integrated Data Retrieval System – IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.

Levy – For tax debts, it is the legal process by which the IRS orders a third party to turn over property in its possession (*e.g.*, the Federal Government payment) that belongs to the tax debtor.

Lien – By filing a Notice of Federal Tax Lien, the Federal Government establishes its interest in your property as a creditor in competition with other creditors in certain situations, such as bankruptcy proceedings or sales of real estate.

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

Memorandum of Understanding – A formal written agreement between two IRS operating divisions that outlines the purpose, scope, responsibilities, specific services (*e.g.*, collection of taxes.), and information to be reported that one division will provide to the other division that may also include a set time period (*e.g.*, five years).

National Quality Review System – The National Quality Review System reviewers capture national program data obtained through case reviews. The National Quality Review System reports official organizational business quality results. Officials can assess program performance to identify training and educational needs that will improve work processes.

Prior Year Unobligated Expired Funds – Unobligated funds are the portion of the funds authorized for the Federal agency that have not been obligated from a previous budget period.

Seizure – The IRS can seize personal and business assets to satisfy tax debts. Among the items that can be seized are real estate, vehicles, business equipment, personal property, bank accounts, retirement funds, Social Security, and accounts receivable. After the assets are seized, they are sold at a public auction.

Substitute for Return 6020(b) Program – The IRS prepares a tax return and proposes a tax assessment for business taxpayers that have not filed based on information return data reported to the IRS combined with other internal data.

Supplemental or Deficiency Appropriation – A supplemental appropriation provides increased dollars to cover additional obligations (expenses) to meet the needs identified by the Executive Branch and concurred by Congress *in advance of* the expense. A deficiency appropriation is made to pay expenses for which sufficient funds were not available *at the time* the expenses were incurred. The need for deficiency appropriations often results from violations of the Anti-Deficiency Act, and they can be made in the same fiscal year as the over-obligated appropriation or in a later year.

Taxpayer Delinquency Investigation – Represents an unfiled tax return for taxpayers. One TDI exists for all delinquent tax periods of a taxpayer.

Taxpayer Delinquent Account – Represents a balance due tax account for taxpayers. A separate TDA exists for each delinquent tax period of a taxpayer.

Trust Fund Recovery Penalty – A penalty applied against 100 percent of the employment taxes an employer willfully failed to remit. The penalty is also imposed if the employer willfully attempted to evade or defeat payment of the tax.

Appendix XI

Management's Response to the Draft Report

DEPUTY COMMISSIONER

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

JUL 31 2012

RECEIVED
JUL 31 2012

MEMORANDUM FOR MICHAEL E. MCKENNEY, ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Faris R. Fink *Faris R. Fink*
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – A Concerted Effort Should Be Taken to Improve Federal Government Agency Tax Compliance (Audit # 201130035)

Thank you for the opportunity to review your draft report titled: "A Concerted Effort Should Be Taken to Improve Federal Government Agency Tax Compliance" (Audit # 201130035.) We appreciate your acknowledging the significant obstacles the Federal Agency Delinquency (FAD) program faces in collecting taxes and our accomplishments. We agree with your recommendations.

The FAD Compliance team has a unique role in assisting their assigned agencies with various issues that caused their tax liabilities. The team educates their contacts at the agencies in addition to collecting overdue taxes and returns. In addition, they take corrective actions on erroneous assessments, when applicable.

We concur with your reported outcome measures. However, with respect to the measure indicating that there are potential funds not obligated of $2.4 million from the 34 suspended delinquent accounts, as you mention in your report, Federal appropriations law and IRS policies make it difficult to collect delinquent taxes from federal agencies.

Attached is a detailed response outlining our corrective actions.

If you have any questions, please contact me, or a member of your staff may contact Denice Vaughan, Director of Campus Compliance Services at (404) 338-8977.

Attachment

Attachment

RECOMMENDATION 1:
Coordinate with the IRS CFO's Office to develop a process to send formal letters to the delinquent Federal agencies' CFOs, including those agencies where collection of the delinquent tax accounts has been suspended and collection statutes are in jeopardy. The letters should also provide information on the options available to Federal agencies to pay prior year tax debts.

CORRECTIVE ACTION:
We agree there should be a mechanism for insuring delinquent Federal agencies' Chief Financial Officers (CFO) are aware of the tax debts that have not been resolved after FAD program processing as well as the payment options available. We will discuss with the IRS CFO and the Tax Exempt and Government Entities Division (TE/GE) the most feasible options for communicating a message concerning this small volume of cases.

IMPLEMENTATION DATE:
March 15, 2013

RESPONSIBLE OFFICIAL(S):
Director, Campus Compliance Services, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 2:
Discuss the results of this report with the IRS Chief Counsel to determine what, if any, regulatory or legislative changes need to be pursued that will allow the IRS to collect taxes from current year appropriations of Federal agencies that have not fulfilled their tax obligations.

CORRECTIVE ACTION:
We agree with this recommendation and will discuss with Counsel any regulatory or legislative changes that can be pursued that will allow the IRS to collect taxes from the current year appropriations of Federal Agencies that have not fulfilled their tax obligations.

IMPLEMENTATION DATE:
January 15, 2013

RESPONSIBLE OFFICIAL(S):
Director, Campus Compliance Services, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 3:
Coordinate with the Commissioner, Tax Exempt and Government Entities Division, to ensure that the FAD Program completes the development of proposed updates to the FAD Program database, which include capturing the Secondary Issues field on the Cause and Cure Reports to meet the FSLG Office's needs.

CORRECTIVE ACTION:
The database was updated October 2011 with changes to the Cause and Cure reporting to capture the secondary issues. We will continue to update the FAD database when applicable to capture data that will assist Federal, State, & Local Governments (FSLG). In addition, we will continue quarterly calls between FAD, Small Business/Self-Employed Division (SB/SE) Collection Policy, FSLG and IRS CFO to discuss and share identified trends, issues and potential program changes.

IMPLEMENTATION DATE:
Completed – October 2011

RESPONSIBLE OFFICIAL(S):
N/A

CORRECTIVE ACTION MONITORING PLAN:
N/A

RECOMMENDATION 4:
Ensure FAD Program employees adhere to procedures when processing delinquent Federal agency cases.

CORRECTIVE ACTION:
We agree with this recommendation, and will update IRM 5.19.15 Federal Agencies to provide specific guidance on when employees need to make referrals to FSLG and take the appropriate actions, when required. The updated IRM will be used for training and program reviews.

IMPLEMENTATION DATE:
January 15, 2013

RESPONSIBLE OFFICIAL(S):
Director, Campus Compliance Services, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 5:
Establish timeliness standards for FAD Program employees to follow when processing Federal agency delinquency cases.

CORRECTIVE ACTION:
We agree with this recommendation. Specific timeline guidelines will be discussed with SB/SE Collection Policy and FSLG and updated in the IRM. Timely actions include when to refer cases to FSLG to request a compliance visit.

IMPLEMENTATION DATE:
April 15, 2013

RESPONSIBLE OFFICIAL(S):
Director, Campus Compliance Services, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 6:
The Commissioner, SB/SE Division, should identify and separate the tax revenues actually collected from the suspended collection actions and the delinquent tax accounts with expired collection statutes to determine the FAD Program's true return on investment.

CORRECTIVE ACTION:
We will work with Information Technology (IT), TE/GE and the CFO to determine if the data can be captured and if it would be cost effective to capture.

IMPLEMENTATION DATE:
April 15, 2013

RESPONSIBLE OFFICIAL(S):
Director, Collection Strategy & Organizational Performance, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.