



*The Process for Individuals to  
Report Suspected Tax Law Violations  
Is Not Efficient or Effective*

**September 10, 2012**

**Reference Number: 2012-40-106**

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

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Phone Number | 202-622-6500

E-mail Address | [TIGTACommunications@tigta.treas.gov](mailto:TIGTACommunications@tigta.treas.gov)

Website | <http://www.tigta.gov>



## HIGHLIGHTS

### THE PROCESS FOR INDIVIDUALS TO REPORT SUSPECTED TAX LAW VIOLATIONS IS NOT EFFICIENT OR EFFECTIVE

## Highlights

Final Report issued on  
September 10, 2012

Highlights of Reference Number: 2012-40-106 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

### IMPACT ON TAXPAYERS

The IRS website for reporting fraud was visited 501,218 times in Fiscal Year 2011, and during that year 116,307 individuals submitted a Form 3949-A, *Information Referral*, to the IRS. The IRS is not efficiently or effectively processing these referrals. Reporting guidelines provided to taxpayers and employees are confusing and inconsistent and cause individuals to use Forms 3949-A for other than its intended purpose. This creates a burden on both the individuals and tax administration. Additionally, a lack of oversight and effective procedures has resulted in workable Forms 3949-A, including identity theft claims, being destroyed without any acknowledgement of receipt to the taxpayer.

### WHY TIGTA DID THE AUDIT

This audit was initiated based on a TIGTA Office of Investigations referral which reported that thousands of identity theft cases reported on Forms 3949-A were not being processed.

### WHAT TIGTA FOUND

Reporting guidelines provided to taxpayers and employees are confusing and inconsistent. Instructions on Form 3949-A do not explain what types of fraud and tax law violations to report using this form. As a result, individuals often use Form 3949-A for purposes other than reporting suspected tax fraud or tax law violations. Additionally, because Form 3949-A lacks specificity, taxpayers do not always provide the IRS with sufficient information for the

IRS to take action. Finally, the IRS routes identity theft referrals received on a Form 3949-A as regular correspondence, which delays actions from being taken on identity theft cases.

As a result, many referrals do not meet any criteria under which the IRS could or would be able to take action(s). A lack of quality review resulted in referrals being destroyed. Additionally, the forms are often used for other purposes (e.g., claims by victims of identity theft). About 3,000 Forms 3949-A used to report identity theft were destroyed due to a lack of procedures on how to process these claims. Victims were not notified.

Ineffective routing procedures and oversight have allowed Forms 3949-A to be misrouted to the wrong functions. Others are mistakenly considered unworkable and retained for 90 days and then destroyed.

### WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS: 1) revise IRS.gov to ensure taxpayers know the intended purpose of Form 3949-A; 2) improve internal and external guidance for reporting identity theft, including a revision of Form 3949-A and instructions; 3) ensure that an IRS-wide coordinated process is implemented, including expediting identity theft claims; 4) implement controls that include developing formal Internal Revenue Manual procedures, ensuring all employees have updated procedures for routing documents; 5) conduct a feasibility study for developing an online Form 3949-A that ensures sufficient information is collected; and 6) evaluate the clerical unit routing process to determine if it would be more efficient if technical employees assumed those responsibilities.

The IRS agreed with all recommendations and plans to revise IRS.gov, clarify the intent of Form 3949-A, review current procedures for necessary changes, and evaluate steps to ensure a more effective quality review process and tracking system. Finally, it plans to ascertain the feasibility of an online Form 3949-A and assess the level of technical expertise required for the needs of the process after considering the effects of the other corrective actions.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

September 10, 2012

**MEMORANDUM FOR** COMMISSIONER, WAGE AND INVESTMENT DIVISION

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

**SUBJECT:** Final Audit Report – The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective (Audit # 201240034)

This report presents the results of our review to evaluate whether the Internal Revenue Service is effectively processing Form 3949-A, *Information Referral*. This audit was added to our Fiscal Year<sup>1</sup> 2012 Annual Audit Plan and addresses the major management challenges of Fraudulent Claims and Improper Payments and Providing Quality Taxpayer Service Operations.

Management's complete response to the draft report is included in Appendix VI.

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Augusta R. Cook, Acting Assistant Inspector General for Audit (Returns Processing and Account Services), at (770) 617-6434.

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<sup>1</sup> A 12-consecutive-month period ending on the last day of any month, except December. The Federal Government's Fiscal Year begins on October 1 and ends on September 30.



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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## *Table of Contents*

<b>Background</b> .....	Page 1
<b>Results of Review</b> .....	Page 3
Guidance for Individuals to Report Suspected Tax Law Violations Creates Burden for Taxpayers and Tax Administration .....	Page 3
<u>Recommendations 1 through 3:</u> .....	Page 8
The Process for Routing Information Referrals Is Not Effective and Needs Improved Oversight .....	Page 9
<u>Recommendations 4 and 5:</u> .....	Page 12
<u>Recommendation 6:</u> .....	Page 13
<b>Appendices</b>	
Appendix I – Detailed Objective, Scope, and Methodology .....	Page 14
Appendix II – Major Contributors to This Report .....	Page 16
Appendix III – Report Distribution List .....	Page 17
Appendix IV – Outcome Measures .....	Page 18
Appendix V – Form 3949-A, <i>Information Referral</i> .....	Page 19
Appendix VI – Management’s Response to the Draft Report .....	Page 21



*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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*Abbreviations*

IRS

Internal Revenue Service

TIGTA

Treasury Inspector General for Tax Administration



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## *Background*

When an individual wishes to report possible instances of Federal tax fraud by another individual, the Internal Revenue Service (IRS) instructs him or her to complete Form 3949-A, *Information Referral*, or to provide this information via a letter. Figure 1 is an excerpt from the IRS public Internet website, IRS.gov, which provides guidelines for reporting suspected fraud.

### **Figure 1: Guidelines for Reporting Suspected Tax Fraud Activity**

#### **How Do You Report Suspected Tax Fraud Activity?**

If you suspect or know of an individual or company that is not complying with the tax laws, you may report this activity by completing Form 3949-A. You may fill out Form 3949-A online, print it, and mail it to:

Internal Revenue Service  
Fresno, CA 93888

If you do not wish to use Form 3949-A, you may send a letter to the address above. Please include the following information, if available:

- Name and address of the person you are reporting.
- The Taxpayer Identification Number (Social Security Number for an individual or Employer Identification Number for a business).
- A brief description of the alleged violation, including how you became aware of or obtained the information.
- The years involved.
- The estimated dollar amount of any unreported income.
- Your name, address, and daytime telephone number.

Although you are not required to identify yourself, it is helpful to do so. Your identity can be kept confidential.

Frequently Asked Questions – 1.13 IRS Procedures: Reporting Fraud [link to web page entitled IRS Procedures].

How to Report:

- **Abusive Tax Promotions and/or Promoters:**  
Complete the referral form [link to Form 14242, *Report Suspected Abusive Tax Promotions or Preparers*] which documents the information necessary to report an abusive tax avoidance scheme. The form can be mailed or faxed to the IRS address and fax number on the form.
- **Fraudulent IRS e-Mails and Websites**  
Visit this page if you receive an e-mail claiming to be from the IRS. [*The IRS does not initiate contact with taxpayers by email or any social media tools to request personal or financial information.* Link to web page on how to Report Phishing.]

Source: IRS.gov web page “How Do You Report Suspected Tax Fraud Activity?”



*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

In Fiscal Year 2011,<sup>1</sup> the IRS website for reporting fraud was visited 501,218 times, and 116,307 Forms 3949-A were received by the Accounts Management function<sup>2</sup> clerical unit in Fresno, California. However, Forms 3949-A are not classified<sup>3</sup> or investigated in that function; the clerical unit is merely a conduit for the referrals. Figure 2 shows the volume of Forms 3949-A the IRS received in Fiscal Years 2010 through 2012.

**Figure 2: Forms 3949-A Inventory  
for Fiscal Years 2010 Through 2012<sup>4</sup>**

	Fiscal Year 2010	Fiscal Year 2011	Fiscal Year 2012 <sup>5</sup>
<b>Total Receipts</b>	89,944	116,307	54,842
<b>Receipts Routed for Further Review</b>	73,168	114,943	53,967
<b>Receipts Destroyed</b>	14,628	12,401	6,104
<b>Ending Inventory</b>	5,614	4,250	3,375

*Source: IRS management information reports.*

This review was performed in the Wage and Investment Division Customer Account Services Accounts Management function clerical unit in Fresno, California, and in the Accounts Management function and Accounts Management function Project Management Office and Support function in Oakland, California, during the period February through June 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

<sup>1</sup> A 12-consecutive-month period ending on the last day of any month, except December. The Federal Government's fiscal year begins on October 1 and ends on September 30.

<sup>2</sup> The Accounts Management function in the Wage and Investment Division provides assistance to individual taxpayers with tax and account-related inquiries via telephone, correspondence, and e-mail.

<sup>3</sup> Once Forms 3949-A are routed to the IRS functions, the allegations are reviewed and classified by technical employees to determine if there are auditable issues.

<sup>4</sup> The IRS-reported categories of inventory do not equal total receipts, and the IRS stated that the information for Fiscal Year 2010 is incomplete.

<sup>5</sup> As of March 24, 2012.



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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## *Results of Review*

### ***Guidance for Individuals to Report Suspected Tax Law Violations Creates Burden for Taxpayers and Tax Administration***

Reporting guidelines provided to taxpayers and employees are confusing and inconsistent. Instructions on Form 3949-A do not explain what types of fraud and/or tax law violations may be reported on this form. As a result, individuals often use Form 3949-A for purposes other than reporting suspected tax fraud and/or tax law violations. Additionally, because Form 3949-A lacks specificity, taxpayers do not always provide the IRS with sufficient information for the IRS to take action. Finally, the IRS routes identity theft referrals received on Form 3949-A as regular correspondence, which delays actions from being taken on identity theft cases.

#### **Forms contain insufficient information or are used for purposes other than what the IRS intended**

A review of a statistical sample<sup>6</sup> of 530 Forms 3949-A screened on April 24, 2012, at the Accounts Management function clerical unit showed that 358 (68 percent) forms reviewed had insufficient information or information not related to tax administration, or were being used for purposes for which the form was not intended. An analysis of the 358 Forms 3949-A showed:<sup>7</sup>

- 143 (27 percent) forms were unworkable because the taxpayer did not provide sufficient information.
- 112 (21 percent) forms were used by individuals incorrectly to report that they were victims of identity theft.<sup>8</sup>
- 49 (9 percent) forms were used incorrectly by individuals to report allegations that were not related to tax administration and could not be acted upon by the IRS.
- 38 (7 percent) forms were incorrectly used by individuals to report that a known party (e.g., ex-spouse) is using the individual's or his or her dependent's Social Security Number on the known party's tax return.

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<sup>6</sup> The same statistical sample is referred to throughout the report.

<sup>7</sup> Percentages shown in the bullets do not add to 68 percent due to rounding.

<sup>8</sup> Identity theft is used to describe instances where the taxpayer reported that his or her Social Security Number or dependent's Social Security Number was used on another return either as primary or dependent and the person who is using the identity is unknown.





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*The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

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- 16 (3 percent) forms were used by individuals to incorrectly report alleged fraud by a tax preparer.

Taxpayers can obtain information about reporting suspected tax fraud by:

- Calling the IRS toll-free telephone number (1-800-829-1040). An assistor should advise the caller/taxpayer to complete a Form 3949-A or to submit the information via a letter and mail it to: IRS, Fresno, California, 93888. Form 3949-A can be obtained from IRS.gov or can be mailed to the taxpayer.
- Calling the Tax Fraud Referral Line (1-800-829-0433). This is an automated line that provides instructions for reporting tax fraud and abuse.
- Researching IRS.gov.
- Visiting a local IRS Taxpayer Assistance Center.<sup>9</sup>

However, in all cases, the individuals are instructed to complete Form 3949-A and mail it to the IRS in Fresno, California. IRS employees are instructed to not take the information from the taxpayer but should only offer to help the taxpayer obtain Form 3949-A by directing the taxpayer to IRS.gov or by having Form 3949-A mailed to the taxpayer.

**Form 3949-A guidance is unclear and inconsistent**

Neither Form 3949-A nor IRS.gov explains what is considered fraud activity to be reported on Form 3949-A. The only reference to fraud provided is a link to “Frequently Asked Questions – 1.13 IRS Procedures,” which links to the following:

**Reporting Fraud**

1. [What can I do if I think someone has filed a tax return using my Social Security Number?](#)

Additionally, even though the IRS.gov web page advises individuals to use Form 3949-A to report an individual or company that is not complying with the tax laws, nowhere on Form 3949-A is fraud mentioned. There are no instructions on the form itself as to what should be reported on it.

Moreover, the IRS.gov web page “How Do You Report Suspected Tax Fraud Activity?” (see Figure 1) does not specify what should not be reported using Form 3949-A. IRS.gov does not state that fraud related to a preparer should be reported on Form 14157, *Complaint: Tax Return Preparer*. By way of the link to Frequently Asked Questions, taxpayers can find what to do if they believe they have been a victim of identity theft. However, if taxpayers choose not to use

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<sup>9</sup> An IRS office with employees who answer questions, provide assistance, and resolve account-related issues for taxpayers face to face.



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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the link, they may use Form 3949-A to report someone else has used their Social Security Number to file a tax return.

Form 14157, recently revised in May 2012, is two pages and could be used as a best practice when considering revisions to Form 3949-A. For example, Form 14157 clearly identifies the purpose of the form, the name of the preparer who is the subject of the complaint, and the contact information of the individual reporting the complaint.

Form 3949-A requests the taxpayer's name on Line 1 as well as "your information" on Line 6. Based on an analysis of completed Forms 3949-A, taxpayers are unsure where to put their name and/or the name of the individual they are referring. In some instances, taxpayers listed the same name in Line 1 and Line 6, and the IRS was unable to determine which individual was the subject of the referral.

**Guidance followed by Taxpayer Assistance Centers leads to incorrect use of Form 3949-A**

Individuals who visit Taxpayer Assistance Centers to report suspected identity theft were incorrectly advised to use Form 3949-A. Internal guidelines stated that the Taxpayer Assistance Center assistors should instruct taxpayers to prepare Form 3949-A when they have knowledge of another person filing a Federal tax return with a stolen Social Security Number. The taxpayer is then instructed to mail the Form 3949-A to the IRS in Fresno, California.

After bringing this to the IRS's attention, on April 25, 2012, IRS management alerted assistors in the Taxpayer Assistance Centers of the issue. When a taxpayer visits a Taxpayer Assistance Center to report that someone is filing a tax return using his or her Social Security Number, employees are now instructed to advise the taxpayer to complete Form 14039, *Identity Theft Affidavit*. Taxpayers will need to file a paper return and return to the Taxpayer Assistance Center with the documentation.

**Clarifying guidance would reduce the volume of Forms 3949-A received by the IRS**

Many Forms 3949-A reviewed did not meet any criteria under which the IRS could or would be able to take action(s). In addition, because of the lack of specificity on Form 3949-A, taxpayers are not providing the IRS with sufficient information on which it could take action. Therefore, the IRS most often takes no action on those Forms 3949-A.

The IRS's Accounts Management function clerical unit in Fresno, California, routes Forms 3949-A. However, the forms are not classified or investigated by that unit; it is merely a conduit for the complaints. Clerical unit clerks sort Forms 3949-A and forward them to other IRS functions<sup>10</sup> or, if not workable, are retained for 90 days and then destroyed. Forms 3949-A

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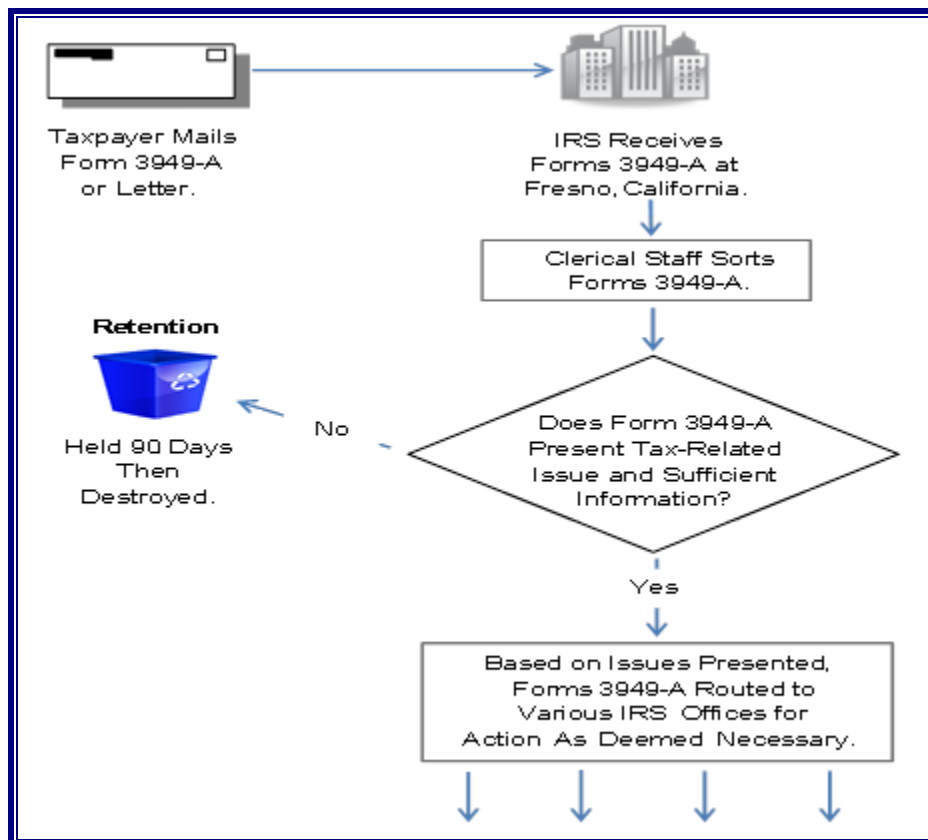
<sup>10</sup> After Forms 3949-A are received by the IRS functions, the forms are classified to determine whether there are auditable issues based on the allegations presented on the Forms 3949-A.



*The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

in the Retention category are not workable and are destroyed after 90 days. Figure 3 represents the Form 3949-A process in the Accounts Management function clerical unit.

**Figure 3: Forms 3949-A Processing**



Source: Observation and interviews with IRS officials.

Our statistical sample of 530 Forms 3949-A identified that 192 (36 percent)<sup>11</sup> were not tax related or lacked needed information. Based on the 116,307 Forms 3949-A received in Fiscal Year 2011, the IRS could potentially process 41,871 Forms 3949-A that are not routable. Taxpayers sent these Forms 3949-A to the IRS only for the forms to be ultimately destroyed. The sender was not notified of the destruction.

**Forms 3949-A used to report identity theft were mishandled**

The Accounts Management function clerical unit does not have adequate procedures in place to process Forms 3949-A that taxpayers submitted to report that they have been victims of identity

<sup>11</sup> These 192 forms are the 143 + 49 forms discussed in the bullets on page 3 of this report. The remaining forms discussed in those bullets (112 + 38 + 16 = 166), while reported on the incorrect form, are issues for which the IRS can take action.



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## *The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

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theft. As a result, the forms were not forwarded for appropriate actions, and most were destroyed.

Prior to Fiscal Year 2009, Forms 3949-A were generally destroyed if identity theft was reported on them. In Fiscal Year 2009, clerical unit staff became concerned about the growing emphasis on identity theft and attempted to establish procedures for processing identity theft reported on Forms 3949-A. However, the Identity Protection Specialized Unit<sup>12</sup> refused to accept the Forms 3949-A, and procedures were never developed. The inventory of these Forms 3949-A began to build and in December 2010 approximately 3,000 Forms 3949-A were destroyed, in part because there were no procedures and no letters existed for contacting the identity theft victims.

In March 2012, temporary procedures were established to handle another buildup of Forms 3949-A inventory. On May 2, 2012, the IRS implemented guidelines instructing employees to treat Form 3949-A used to report identity theft as a Form 14039, *Identity Theft Affidavit*. The Form 3949-A, accepted as a Form 14039, must have an attached police report and State/Federal identification. However, this is inconsistent with IRS identity theft procedures that state a Form 14039 may be accepted as a claim of identity theft without a police report.

In addition, it was not until March 2012 that the first procedures were established for dependent-related identity theft issues,<sup>13</sup> even though the Accounts Management function clerical unit did not consider dependent-related identity theft issues to be identity theft. However, employees are instructed to send Forms 3949-A reporting dependent-related identity theft to the Accounts Management function for assignment and resolution, classified as regular taxpayer correspondence. These forms should receive priority and be classified as identity theft cases. Taxpayers will experience delays until Forms 3949-A are classified as identity theft and subsequently sent to an Identity Theft unit to be worked and resolved. In a prior Treasury Inspector General for Tax Administration (TIGTA) report,<sup>14</sup> an analysis of correspondence identified that the average time to work a correspondence case was approximately 60 days. The 60 days will be in addition to the time it already takes to work an identity theft case. Another prior TIGTA report stated that it can take up to a year to resolve an identity theft case.<sup>15</sup>

Tax returns submitted by identity theft victims with Forms 3949-A are not processed timely. The IRS has developed IRS-wide identity theft procedures to ensure effective victim assistance

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<sup>12</sup> The intent of this unit is to enable victims of identity theft to have their questions answered and issues resolved quickly and effectively. This unit does not actually resolve identity issues but monitors the status of cases worked in designated identity theft units.

<sup>13</sup> Dependent-related identity theft issues are claims by the taxpayer that his or her Social Security Number or his or her dependent's Social Security Number has been used on another tax return of an unknown person.

<sup>14</sup> TIGTA, Ref. No. 2011-40-058, *Taxpayers Do Not Always Receive Quality Responses When Corresponding About Tax Issues* (Jul. 2011).

<sup>15</sup> TIGTA, Ref. No. 2012-40-050, *Most Taxpayers Whose Identities Have Been Stolen to Commit Refund Fraud Do Not Receive Quality Customer Service* (May 2012).



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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and processing of claims, including tax returns. However, the Accounts Management function clerical unit has not incorporated procedures for routing tax returns submitted with Forms 3949-A reporting identity theft. Tax returns identified in the sample of 530 Forms 3949-A were still not posted by the IRS as of June 21, 2012.

The IRS's mission is to provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all. Clear and consistent guidelines are essential to ensure that taxpayers who submit Forms 3949-A receive top-quality service.

### ***Recommendations***

The Commissioner, Wage and Investment Division, should:

**Recommendation 1:** Revise IRS.gov to ensure taxpayers know the intended purpose of Form 3949-A. It should state that the Form 3949-A is not to be used to report identity theft or complaints against tax return preparers and provide instruction and/or links for how to report those issues.

**Management's Response:** IRS management agreed with this recommendation. The IRS will revise IRS.gov content to more clearly explain the purpose of Form 3949-A and clarify instructions on reporting issues for which specialized forms have been developed.

**Recommendation 2:** Improve both internal and external guidance for reporting identity theft, including a revision of Form 3949-A and instructions, specifically stating the Form 3949-A should not be used for reporting claims of identity theft. In addition, ensure the language and information is consistent with internal and external guidelines and the intended purpose is fraud and/or tax law violations.

**Management's Response:** IRS management agreed with this recommendation and is revising the wording on Form 3949-A to indicate it should not be used for reporting identity theft and certain other issues. The IRS has also recently developed a desk guide for clerical staff and began training on July 16, 2012, for its use.

**Recommendation 3:** Ensure that an IRS-wide coordinated process is implemented to provide guidance for timely and effective processing of Forms 3949-A. This should include ensuring that Forms 3949-A reporting claims of identity theft are expedited to the appropriate Identity Theft unit for processing and not forwarded as regular correspondence in the Accounts Management function.

**Management's Response:** IRS management agreed with this recommendation and will review current procedures for necessary changes, including the expedited routing of forms reporting claims of identity theft.



*The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

***The Process for Routing Information Referrals Is Not Effective and Needs Improved Oversight***

The IRS's current method for processing Forms 3949-A is ineffective and needs improved oversight. Of 530 Forms 3949-A reviewed:

- 372 (70 percent) of the Forms 3949-A were correctly routed.
- 46 (9 percent) of the Forms 3949-A were scheduled to be destroyed even though sufficient information was available to identify the appropriate IRS function.
- 112 (21 percent) of the Forms 3949-A were routed to the incorrect IRS function.

Once Forms 3949-A reach a function, technical employees in the function screen and classify them. If the function receives a misrouted Form 3949-A, it returns the form to the Accounts Management function clerical unit responsible for initial screening to be rescreened and rerouted to the correct function. Returned forms are placed in the daily receipts and are not processed separately. If the Accounts Management function clerical unit cannot determine which IRS function should receive a Form 3949-A, that form is sent to Retention. Misrouting delays processing and results in workable Forms 3949-A being sent to Retention.

**Forms 3949-A routed to Retention are not effectively reviewed before being destroyed**

On March 12, 2012, TIGTA auditors expressed concerns about the lack of quality review of Forms 3949-A routed to Retention. Subsequently, the IRS conducted a review of all Forms 3949-A processed over one day and sent to Retention. Twenty-two (50 percent) of the 44 Forms 3949-A in Retention were workable. Of the 22 workable forms:

- 10 Forms 3949-A (45 percent) implicated a business and should have been forwarded to the Small Business/Self-Employed Division.
- 7 Forms 3949-A (32 percent) did not contain a Social Security Number. However, with required research, the Social Security Numbers were identified.
- 4 Forms 3949-A (18 percent) had a valid Social Security Number and should have been forwarded to an IRS function.
- \*\*\*\*\*1\*\*\*\*\*  
\*\*\*\*\*1\*\*\*\*\*

Based on this review, IRS management stated that the Accounts Management function clerical unit had been informed of the procedure to better handle Forms 3949-A. Interim guidance was distributed to all responsible clerical unit employees to help ensure all employees who process Forms 3949-A have the correct guidance for screening. A new job function in the unit was





## *The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

created—one clerk on a daily basis screens the prior day’s Retention Forms 3949-A to identify any claims of identity theft.

However, our review of 210 Forms 3949-A routed to Retention and reviewed by IRS management identified 44 (21 percent) that were workable. Of these 44 referrals:

- 15 (34 percent) involved instances where the employees needed to associate the issue presented in the Form 3949-A with one of seven categories on the routing sheet.<sup>16</sup> For example, if the Form 3949-A indicates that the tax violation involves a tax return preparer, then per the routing sheet and interim procedures, the referral should be automatically routed to a designated function with no further research needed.
- 29 (66 percent) involved instances where information was missing on the Forms 3949-A, but the clerks had not adequately researched to identify the missing information.

Figure 4 presents the total Forms 3949-A that were destroyed for Fiscal Years 2010 through 2012 because of either a lack of procedures or lack of needed information or because they did not relate to tax administration.

**Figure 4: Volume of Forms 3949-A Destroyed for Fiscal Years 2010 Through 2012**

Destination	Fiscal Year 2010	Fiscal Year 2011	Fiscal Year 2012 <sup>17</sup>
Retention	19,842	16,122	6,104

*Source: Accounts Management function management information reports.*

### **Referrals are often routed to incorrect locations**

In Fiscal Year 2011, the volume of Forms 3949-A received and routed to other functions totaled 90,632. Based on our sample review results, an estimated 31,721 (35 percent) Forms 3949-A are misrouted per year. Accounts Management function clerical unit employees reprocess these at a cost of \$6.53 each, totaling \$207,138 spent for rework each year. This happened because there are insufficient and inconsistent procedures providing guidance to employees on the correct process for routing Forms 3949-A.

- No formal Internal Revenue Manual procedures exist. Draft procedures were sent to IRS National Headquarters in February 2012 for approval, but as of June 29, 2012, the procedures have not been issued to the Accounts Management function clerical unit. Currently, interim procedures are being used. However, clerks are using different

<sup>16</sup> The routing sheet lists seven categories that identify the routing locations.

<sup>17</sup> Through March 24, 2012.



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## *The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

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versions. Some employees are using the incorrect procedures and routing sheets. At least five different revisions of the routing sheet are used, which often prevents the Form 3949-A from being routed to the correct location. For example, one sheet incorrectly results in certain identity theft claims being destroyed.

- Clerks who route Forms 3949-A are located in 27 different clerical units and under as many managers.<sup>18</sup> IRS management could not immediately identify all employees who have participated in the routing process.
- No current training exists. The current program manager, in response to concerns raised by the TIGTA, stated that once formal Internal Revenue Manual procedures are established, a training class will be organized for the clerks and managers who screen Forms 3949-A.
- Clerks are not expected to conduct extensive research; it is not included in their training or position description. Technical employees would be better able to assess the allegations reflected on the forms to determine if the forms contain auditable issues.
- There is inadequate quality review of the Form 3949-A process. IRS management does not have effective oversight over the Form 3949-A routing process. In addition to the lack of quality reviews, management information reports are neither complete nor accurate, thereby hindering monitoring. IRS management stated that reports were missing weeks of information because of the management changes to the program.
- There is little coordination and communication between the Accounts Management function clerical unit and the functional areas receiving Forms 3949-A. When Forms 3949-A are misrouted, the functional areas return the forms to the clerical unit but provide little feedback as to why the forms are being returned. The IRS is unable to provide information regarding the volume of Forms 3949-A that are returned. With better communication, the IRS could use the results to better train the Accounts Management function clerical unit on proper routing.

Sufficient procedures and guidelines are integral to a quality internal control system. Internal control is synonymous with management control and is a major part of managing an organization and also serves as the first line of defense in safeguarding assets and preventing and detecting errors and fraud. Internal controls help Government program managers achieve desired results through effective stewardship of public resources.

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<sup>18</sup> While the clerks who generally route Forms 3949-A are centrally located, the IRS uses clerks from other units in Fresno, California, when workload is heavy.





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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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**An online version of Form 3949-A would overcome some IRS challenges**

Several Federal and State agencies employ an online version of their referral forms. Although the IRS faces some unique challenges with respect to disclosure issues, an automated form would overcome many issues that plague the current process. The current process does not ensure that all needed information is included on the referral, does not aid the taxpayer in understanding the type of issues for which Form 3949-A is intended to be used, does not provide alternatives to the referral when it is not the appropriate means of communicating with the IRS, does not allow, based on the information provided, direct routing (*i.e.*, no intermediary sorting and routing) to the appropriate IRS function, and does not include the IRS sending an acknowledgement to the taxpayer.

Conversely, an online referral process could facilitate accurate tracking of referrals received and their disposition. Additionally, an online referral process could greatly reduce the costs compared to a paper-based referral process. In Fiscal Year 2011, the clerical unit that processes Forms 3949-A cost approximately \$759,000. If the current paper-based process continues over five years, the IRS would expend approximately \$3.8 million.

Burden would be reduced for taxpayers if they are offered the option of acknowledgement of receipt of referrals by the IRS (which could be efficiently administered with an online referral process). This would eliminate the need for taxpayers to submit more than one of the same referral and provide assurance that the IRS is aware of the issue they reported. Based on Fiscal Year 2011 referral volume, the IRS could potentially reduce burden each year for 116,307 taxpayers; over five years, burden could be reduced for 581,535 taxpayers.

***Recommendations***

The Commissioner, Wage and Investment Division, should:

**Recommendation 4:** Implement controls that include developing formal Internal Revenue Manual procedures, ensuring all employees have updated procedures for routing documents, developing an effective and efficient quality review process, and developing a tracking system that captures Forms 3949-A, including identifying Forms 3949-A that require rerouting.

**Management's Response:** IRS management agreed with this recommendation and recently developed a clerical staff desk guide. The IRS will also review current procedures and evaluate steps to ensure a more effective quality review process and tracking system.

**Recommendation 5:** Conduct a feasibility study for developing an online Form 3949-A that ensures sufficient information is collected so that the forms can be routed directly to the appropriate function for classification.



*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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**Management's Response:** The IRS will ascertain the feasibility of developing an online Form 3949-A; however, it believes a prudent course of action would be to implement other recommended actions so their effects on the accuracy and volume of forms submitted can be considered.

**Recommendation 6:** Evaluate the Accounts Management function clerical unit routing process to determine whether it would be more efficient if more technical employees assumed the responsibilities of processing Forms 3949-A.

**Management's Response:** As part of the IRS's evaluation on the feasibility of developing an online Form 3949-A, it will consider the effects other corrective actions have had on the handling and routing of the form and will assess the level of technical expertise required for the needs of the process.



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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## **Appendix I**

### *Detailed Objective, Scope, and Methodology*

Our overall objective was to evaluate whether the IRS is effectively processing Form 3949-A, *Information Referral*. To accomplish our objective, we:

- I. Determined whether the method taxpayers use to report fraud is effective and reduces taxpayer burden.
  - A. Identified the methods the IRS has for taxpayers to report fraud and determined whether those methods reduce taxpayer burden.
  - B. Identified the purposes of Form 3949-A and determined whether the IRS is ensuring that taxpayers use the form for its intended purposes.
  - C. Assessed Form 3949-A to determine whether the intended purpose and instructions are clear.
- II. Determined whether the process the IRS uses to handle, track, and control reports of fraud is effective.
  - A. Identified the procedures and processes the IRS has in place to accept and process Forms 3949-A.
  - B. Determined the procedures used to process the referrals received, placed in Retention, and forwarded to IRS functions and the actions taken to document the volumes.
  - C. Determined the procedures used to evaluate referrals to determine the next appropriate action to be taken (retain, forward, or destroy).
  - D. Determined whether the IRS provides an acknowledgement of receipt to taxpayers who submit referrals.
- III. Determined whether Accounts Management function clerical unit oversight is sufficient to ensure fraud referrals are effectively processed and routed to the appropriate IRS functions or offices.
  - A. Interviewed responsible officials to determine what oversight is provided.
  - B. Identified any guidelines, procedures, and reports used to oversee the referral process.
  - C. Obtained and reviewed management information reports to assess the accuracy and usefulness of the data.



*The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

D. Identified and evaluated the quality control process.

Reviewed two random statistical samples and three 100 percent samples of Forms 3949-A (including referrals made using other forms or letters) to determine the type of referrals and assess the effectiveness of the routing process, including the effectiveness of procedures and the quality assurance process. A 95 percent confidence level, a 10 percent expected error rate, and a  $\pm 5$  percent precision rate were used to select the samples. The population and sample details are as follows:

<b>Area Routed</b>	<b>Population Size</b>	<b>Sample Size</b>
Small Business/Self-Employed	390	118 <sup>1</sup>
Wage and Investment Division	422	117 <sup>2</sup>
Retention	210	210
Identity Theft Unit	45	45
Correspondence	40	40
<b>TOTAL</b>	<b>1,107</b>	<b>530</b>

- E. Evaluated the process the Accounts Management function clerical unit has in place to obtain feedback from the IRS functions and offices that ultimately receive Forms 3949-A. This would include if the referrals were timely transferred and were sufficient to work.
- F. Determined whether oversight is effective, and if not, determined the reasons why and measured the effect on tax administration.

**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 internal controls relevant to our audit objective include the IRS's internal guidelines used by the Accounts Management function clerical unit that processes Forms 3949-A and the management information systems used to control the referrals. We evaluated these controls by interviewing management and reviewing policies and procedures. We also reviewed a statistical sample of 530 Forms 3949-A.

<sup>1</sup> Rounded up from a required statistical sample size of 111 forms.

<sup>2</sup> Rounded up from a required statistical sample size of 113 forms.



*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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**Appendix II**

*Major Contributors to This Report*

Michael E. McKenney, Assistant Inspector General for Audit (Returns Processing and Account Services)

Augusta R. Cook, Acting Assistant Inspector General for Audit (Returns Processing and Account Services)

Paula W. Johnson, Acting Director

Lena Dietles, Audit Manager

Robert Howes, Lead Auditor

Lynn Faulkner, Senior Auditor

Patricia Jackson, Senior Auditor

Geraldine Vaughn, Senior Auditor

Jerome Antoine, Auditor

Kathy Coote, Auditor

Nelva Usher, Auditor

Joseph L. Katz, Ph.D., Contractor, Statistical Sampling Consultant



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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**Appendix III**

*Report Distribution List*

Commissioner C  
Office of the Commissioner – Attention: Chief of Staff C  
Deputy Commissioner for Operations Support OS  
Deputy Commissioner for Services and Enforcement SE  
Deputy Commissioner, Small Business/Self-Employed Division SE:S  
Deputy Commissioner of Services and Operations, Wage and Investment Division SE:W  
Chief Technology Officer OS:CTO  
National Taxpayer Advocate TA  
Director, Customer Account Services, Wage and Investment Division SE:W:CAS  
Director, Strategy and Finance, Wage and Investment Division SE:W:S  
Director, Customer Account Services, Accounts Management SE:W:CAS:AM  
Chief, Program Evaluation and Improvement, Wage and Investment Division SE:W:S:PEI  
Chief Counsel CC  
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: Chief, Program Evaluation and Improvement, Wage and Investment Division  
SE:W:S:PEI  
Commissioner, Small Business/Self-Employed Division SE:S



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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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 Congress.

**Type and Value of Outcome Measure:**

- Inefficient Use of Resources – Potential; \$3.8 million (see page 9).

**Methodology Used to Measure the Reported Benefit:**

In Fiscal Year 2011, the routing operation in Fresno, California, cost approximately \$759,000. If the current paper-based process continues more than five years, the IRS would expend approximately \$3.8 million, a cost that an online process would greatly reduce. The online process would also facilitate accurate electronic tracking of referrals received and their disposition. There would, however, be a cost to the IRS to develop/implement an online Form 3949-A process.

**Type and Value of Outcome Measure:**

- Taxpayer Burden – Potential; 581,535 taxpayers affected (see page 9).

**Methodology Used to Measure the Reported Benefit:**

Burden would be reduced for taxpayers if they are offered the option of acknowledgement of receipt of referrals by the IRS. Acknowledgements of receipt would eliminate the need for taxpayers to submit more than one of the same referral and provide assurance that the IRS is aware of the issue they reported. Based on Fiscal Year 2011 referral volume, the IRS could potentially reduce burden each year for 116,307 taxpayers; over five years this figure could reach 581,535 taxpayers.



The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective

Appendix V

Form 3949-A, Information Referral

Form <b>3949 A</b> (2-2007)	Department of the Treasury – Internal Revenue Service <b>Information Referral</b> <i>(See instructions on reverse)</i>	OMB # 1545-1960
1. Taxpayer Name		2. Business Name
a. Street Address		a. Street Address
b. City/State/ZIP		b. City/State/ZIP
c. Social Security Number (SSN)		c. Employer Identification Number
d. Occupation		d. Principal Bus Activity
e. Date of Birth		
3. Marital Status <input type="checkbox"/> Married <input type="checkbox"/> Single <input type="checkbox"/> Head of Household <input type="checkbox"/> Divorced <input type="checkbox"/> Separated		3a. Name of Spouse
4. Alleged Violation of Income Tax Law (Check all that apply).		
<input type="checkbox"/> False Exemption <input type="checkbox"/> Unsubstantiated Income <input type="checkbox"/> Unreported Income <input type="checkbox"/> Failure to Withhold Tax <input type="checkbox"/> False Deductions <input type="checkbox"/> Kickback <input type="checkbox"/> Narcotics Income <input type="checkbox"/> Wagering/Gambling <input type="checkbox"/> Multiple Filing <input type="checkbox"/> False/Altered Documents <input type="checkbox"/> Public/Political Corruption <input type="checkbox"/> Earned Income Credit <input type="checkbox"/> Organized Crime <input type="checkbox"/> Failure to Pay Tax <input type="checkbox"/> Failure to File Return <input type="checkbox"/> Other (Describe below)		
5. Unreported Income and Tax Years (Fill in Tax Years and dollar amount(s), if known, e.g., TY2005 \$10,000)		
TY _____ \$ _____ TY _____ \$ _____ TY _____ \$ _____ TY _____ \$ _____ TY _____ \$ _____ TY _____ \$ _____		
a. Comments (Briefly describe the facts of the alleged violation - Who/What/Where/When/How. Attach another sheet, if needed).		
_____ _____ _____ _____ _____ _____ _____		
b. Are books/records available? <input type="checkbox"/> Yes <input type="checkbox"/> No		c. Do you consider the taxpayer dangerous? <input type="checkbox"/> Yes <input type="checkbox"/> No
d. Banks, Financial Institutions used by the taxpayer:		
Name: _____		Name: _____
Address: _____		Address: _____
City/State/ZIP: _____		City/State/ZIP: _____
e. Please describe how you learned and/or obtained the information in this report (Attach another sheet, if needed):		
_____ _____ _____		
6. Your Name:		
a. Address: _____		
b. City/State/ZIP: _____		
c. Telephone Number (Please include the Area Code): _____		
For Mailing Address, see Instructions		
For Paperwork Reduction Act, see Instructions		
Catalog Number 47872E		Form <b>3949 A</b> (Rev. 2-2007)





## *The Process for Individuals to Report Suspected Tax Law Violations Is Not Efficient or Effective*

### Instructions

Provide the following information for the Person/Business You Are Reporting if Known:

1. Name
  - a. Street Address of Residence
  - b. City, State, and Zip Code
  - c. Social Security Number
  - d. Date of the Person's Birth
2. Business Name
  - a. Street Address of Business
  - b. City/State/Zip Code
  - c. Enter Employer Identification Number
  - d. Describe the Primary Business Activity
3. Indicate Marital Status  
**M** - Married **S** - Single **HH** - Head of Household **Div** - Divorced **Sep** - Separated  
3a. Enter name of spouse, if applicable.
4. Check all Tax Violations That Apply to Your Report or Describe in Comments If Not Listed.
5. If your report involves unreported income, indicate the year(s) and the dollar amount(s)
  - 5a. Briefly describe the facts of the alleged violation(s) as you know them. Please attach another sheet, if you need more room.
  - 5b. Indicate (Yes or No) if books and/or records are available that substantiate your report.
  - 5c. Indicate (Yes or No) if you consider the person to be violent or dangerous and provide an explanation in the comments section of this form.
  - 5d. List name and address of bank(s) and/or financial institution(s) used by the taxpayer if known.
  - 5e. Briefly explain how you learned of or obtained the information contained in your report. Please attach another sheet, if you need more room.
6. Enter your name, street address, city, state, zip code and a telephone number where you can be contacted. Indicate time of day you may be contacted if appropriate. **This Information is not Required to Process Your Report.**

**Please print and send your completed form to the Internal Revenue Service at:**

Internal Revenue Service  
Fresno, CA 93888

**PAPERWORK REDUCTION NOTICE:** We ask for the information on this form to carry out the Internal Revenue laws of the United States. This report is voluntary and the information requested helps us determine if there has been a violation of Income Tax Law. We need it to insure that taxpayers are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administrations of any Internal Revenue laws. Generally, tax returns and tax return information are confidential, as required by Code section 6103.

The time required to complete this form will vary depending on individual circumstances. The estimated average time is 15 minutes.

#### Privacy Act Notice

We are requesting this information under authority of 26 U.S.C. 7801.

The primary purpose of this form is to report potential violations of the Internal Revenue laws.

The information may be disclosed to the Department of Justice to enforce the tax laws.

Providing the information is voluntary. Not providing all or part of the information will not affect you.



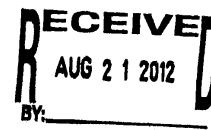
*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

**Appendix VI**

*Management's Response to the Draft Report*



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
ATLANTA, GA 30308



AUG 21 2012

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

FROM: Peggy Bogadi  
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – The Process for Individuals to Report  
Suspected Tax Law Violations Is Not Efficient or Effective  
(Audit # 201240034)

The Form 3949-A, *Information Referral*, is no longer the sole vehicle for taxpayers to report to the IRS suspected tax fraud and/or tax law violations by other taxpayers or businesses. With the rise in illegal or fraudulent activities such as identity theft and tax return preparer fraud, the reporting process has evolved to include specialized forms designed to capture the specific information needed for the IRS to address those more narrowly-defined issues. Consequently, we agree Form 3949-A instructions and the internal and external documents explaining its function and use, should be updated and clarified.

To address issues with inconsistent routing and mishandling of Form 3949-A, especially those associated with identity theft, we will review and revise our procedures for processing information referrals from a servicewide perspective. We will also review current procedures and evaluate steps to ensure a more effective quality review process and tracking system.

We will determine the feasibility of developing an online Form 3949-A; however, we plan to implement other recommended actions first, so their effects on the accuracy and volume of forms submitted can be considered. We will also consider the effects other corrective actions have on the handling and routing of the form and will assess the level of technical expertise required for the process.

Attached are our comments to your recommendations. If you have any questions, please contact me, or a member of your staff may contact Peter J. Stipek, Director, Customer Account Services, Wage and Investment Division, at (404) 338-8910.

Attachment



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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Attachment

The Commissioner, Wage and Investment Division, should:

**RECOMMENDATION 1**

Revise IRS.gov to ensure taxpayers know the intended purpose of Form 3949-A. It should state that the Form 3949-A is not to be used to report identity theft or complaints against tax return preparers and provide instruction and/or links for how to report those issues.

**CORRECTIVE ACTION**

We agree with this recommendation. We will revise IRS.gov content to more clearly explain the purpose of Form 3949-A, *Information Referral*, and clarify instructions on reporting issues for which specialized forms have been developed.

**IMPLEMENTATION DATE**

June 15, 2013

**RESPONSIBLE OFFICIAL**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 2**

Improve both internal and external guidance for reporting identity theft, including a revision of Form 3949-A and instructions, specifically stating the Form 3949-A should not be used for reporting claims of identity theft. In addition, ensure the language and information is consistent with internal and external guidelines and the intended purpose is fraud and/or tax law violations.

**CORRECTIVE ACTION**

We agree with this recommendation and are revising the wording on Form 3949-A to indicate it should not be used for reporting identity theft and certain other issues. We have also recently developed a desk guide for clerical staff and began training on July 16, 2012, for its use.

**IMPLEMENTATION DATE**

October 15, 2013

**RESPONSIBLE OFFICIAL**

Director, Accounts Management, Customer Account Services, Wage and Investment Division



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*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 3**

Ensure that an IRS-wide coordinated process is implemented to provide guidance for timely and effective processing of Forms 3949-A. This should include ensuring that Forms 3949-A reporting claims of identity theft are expedited to the appropriate Identity Theft unit for processing and not forwarded as regular correspondence in the Accounts Management function.

**CORRECTIVE ACTION**

We agree with this recommendation and will review current procedures for necessary changes, including the expedited routing of forms reporting claims of identity theft.

**IMPLEMENTATION DATE**

October 15, 2013

**RESPONSIBLE OFFICIAL**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

The Commissioner, Wage and Investment Division, should:

**RECOMMENDATION 4**

Implement controls that include developing formal Internal Revenue Manual procedures, ensuring all employees have updated procedures for routing documents, developing an effective and efficient quality review process, and developing a tracking system that captures Forms 3949-A, including identifying Forms 3949-A that require rerouting.

**CORRECTIVE ACTION**

We agree with this recommendation and have recently developed a clerical staff desk guide. We will also review current procedures and evaluate steps to ensure a more effective quality review process and tracking system.

**IMPLEMENTATION DATE**

October 15, 2013



*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

3

**RESPONSIBLE OFFICIAL**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 5**

Conduct a feasibility study for developing an online Form 3949-A that ensures sufficient information is collected so that the forms can be routed directly to the appropriate function for classification.

**CORRECTIVE ACTION**

We will ascertain the feasibility of developing an online Form 3949-A; however, we believe a prudent course of action will be to implement other recommended actions so their effects on the accuracy and volume of forms submitted can be considered.

**IMPLEMENTATION DATE**

June 15, 2014

**RESPONSIBLE OFFICIAL**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 6**

Evaluate the Accounts Management function clerical unit routing process to determine whether it would be more efficient if more technical employees assumed the responsibilities of processing Forms 3949-A.

**CORRECTIVE ACTION**

As part of our evaluation on the feasibility of developing an Online Form 3949-A, we will consider the effects other corrective actions have had on the handling and routing for the form and will assess the level of technical expertise required for the needs of the process.

**IMPLEMENTATION DATE**

June 15, 2014

**RESPONSIBLE OFFICIAL**



*The Process for Individuals to Report Suspected  
Tax Law Violations Is Not Efficient or Effective*

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Director, Accounts Management, Customer Account Services, Wage and Investment  
Division

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control  
system.