

**The Delinquent Tax Return Investigation
Program for Employment Taxes Within the
Collection Field Function Can Be Improved**

July 2002

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INSPECTOR GENERAL
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ADMINISTRATION

DEPARTMENT OF THE TREASURY
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July 2, 2002

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION

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FROM: (for) Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Delinquent Tax Return Investigation
Program for Employment Taxes Within the Collection Field
Function Can Be Improved (Audit # 200130030)

This report presents the results of our review of the Internal Revenue Service's (IRS) delinquent tax return investigation program for employment taxes. The overall objective of our review was to evaluate the effectiveness of Collection Field function (CFf) actions to bring employment tax non-filers into compliance.

In summary, Revenue Officers (ROs) used effective collection techniques when securing delinquent returns. However, they did not adequately use available internal and external sources to locate taxpayers, and closing actions were not effective when determining if taxpayers were not liable to file. In addition, although the CFf's new risk-based inventory delivery process may ensure that the most potentially productive returns are assigned for investigation, management needs to closely monitor this new process.

We recommended that the Director, Compliance, Small Business/Self-Employed (SB/SE) Division, consider both more specific reviews of delinquent return investigations closed as not liable through the Collection Quality Measurement System (CQMS)¹, and a group manager review of cases closed as unable to locate. The Director, Compliance, SB/SE Division, should also provide national guidelines for the use of locator sources for unable to locate cases to ensure consistency. In addition, the Director should establish a process to monitor and refine, as needed, the new risk-based methodology for delivering inventory to ensure the CFf is getting the most potentially productive delinquent tax return investigation cases.

¹ The CQMS is a case review process that provides for a qualitative assessment of CFf cases.

Management's Response: SB/SE Division management agreed with the first and the third recommendations. They plan to develop review criteria and to implement CQMS reviews for delinquent return investigation cases. They also plan to revise the Internal Revenue Manual to require group managerial approval when closing unable to locate cases. In addition, SB/SE Division management plans to establish a process to monitor the new risk-based methodology for delivering delinquent return investigation cases.

SB/SE Division did not agree with the second recommendation to provide national guidelines to ensure effective and consistent use of locator services for unable to locate cases. However, they responded that the new requirement for group managers to approve unable to locate closures will ensure they use the appropriate locator services and provide consistency.

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

Copies of this report are also being sent to the IRS managers who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Gordon C. Milbourn III, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-3837.

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Background

To provide service to taxpayers and increase overall compliance, one of the strategic goals of the Small Business/Self-Employed (SB/SE) Division is addressing non-filing of tax returns. One of the four major strategies for Fiscal Years (FY) 2002 and 2003 is to increase compliance among small business taxpayers.

The SB/SE Division has a National Non-filer Strategy, which is an integrated and sustained effort to bring non-filers into the Federal tax system and keep them there. The National Non-filer Strategy is a two-prong approach using education and outreach to the public to achieve voluntary filing, and a comprehensive compliance program to secure tax returns when taxpayers do not voluntarily file.

Included in this strategy are six strategic initiatives, one of which is to increase employment tax compliance. Many of the taxpayers served by the SB/SE Division are required to file Employment Tax Returns (Form 941).¹ If a taxpayer does not file a required Form 941, the return is considered a “delinquent return” and the taxpayer is considered a non-filer. In the Internal Revenue Service’s (IRS) Annual Performance Plan, the SB/SE Division has a goal to increase delinquent return investigation case closures.

When the taxpayer does not file a return, the IRS first tries to contact the taxpayer by letter and then by telephone to resolve why the taxpayer has not filed and also try to secure the return. If the return cannot be secured, a case may be assigned directly to a Revenue Officer (RO) in the Collection Field function (CFf) to contact the taxpayer and secure the return. The process for assigning cases to the ROs is being changed in an attempt to provide the most potentially productive cases to be worked, and assign them to the employees best suited to resolve the cases.

In FY 2001, the IRS’ management information reports indicated that the CFf closed 217,041 employment tax delinquent return investigation tax periods, of which 118,352 (55 percent) were non-productive (i.e., no return was secured). The 217,041 investigations represent about

¹ Employers who withhold income tax on wages, or who must pay social security or Medicare tax, must file a quarterly employment tax return.

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29 percent of the balance due delinquent accounts and delinquent return investigations closed during FY 2001 by ROs. The percentage of non-productive cases indicates that improvement in the selection process is critical in order for the SB/SE Division to become more productive in resolving these delinquencies. Figure 1 shows how ROs closed these cases.

Figure 1. Cff Delinquent Return Investigations in FY 2001 – Employment Tax Returns²

Type of Dispositions	# of Modules	Percent
Return Posted	16,253	7.5%
Return Secured	80,174	36.9%
Not Liable for this period	21,128	9.7%
No Longer Liable	75,929	35.0%
Unable to Locate	13,618	6.3%
Previously Filed	1,251	0.6%
Referred to Examination Function	1,011	0.5%
Surveyed	1,716	0.8%
Shelved	5,961	2.7%
Total	217,041	100.0%

Source: NO-5000-4 National Report.

Failure to file required tax returns undermines the United States' system of voluntary compliance. If the IRS does not effectively address non-filers, it could risk a decline in taxpayer confidence. Employees who have their taxes withheld from their wages expect their withheld funds to be properly deposited and credited to their accounts, and employers expect their competitors to also pay their taxes.

We conducted the audit from August 2001 to February 2002 in the Baltimore, Maryland; Boston, Massachusetts; Philadelphia, Pennsylvania; Richmond, Virginia; and Wethersfield, Connecticut SB/SE Division field offices. We reviewed a nationwide sample of employment tax delinquent return investigation cases closed from

² "Return Posted" is when the taxpayer files a return. "Referred to the Examination function" is when an RO refers a case for examination because the taxpayer fails to file a return. "Surveyed" and "Shelved" are situations in which managers determine cases are not worth working, possibly due to minimal taxes due or age of the case.

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The Collection Field Function Was Not Always Working Delinquent Return Investigation Cases Effectively

October 1, 2000, through May 31, 2001. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

The goal of working a delinquent return investigation case³ is to achieve full compliance, including securing the full payment of the tax liability at the time the return is secured. Disposition of a delinquent return investigation case depends upon the circumstances of the individual case. The Internal Revenue Manual (IRM) provides guidelines to ROs for conducting delinquent return investigations, and requires them to make appropriate entries in case histories regarding all actions taken.

When a return cannot be secured, it is usually because the taxpayer cannot be located or is not liable (i.e., no taxes are due). Before closing a case as unable to locate, the RO should check, at a minimum, some internal and external sources to resolve the delinquent return investigation. Before closing a case as not liable for a specific period, the RO should obtain sufficient evidence that the taxpayer had no employees, was not in business for that period, or had minimal tax due. Before closing a case as no longer liable, the RO should obtain sufficient evidence from independent sources, or the taxpayer, that the business is no longer operating.

We reviewed employment tax delinquent return investigation cases that were closed from the Integrated Collection System (ICS)⁴ between October 1, 2000, and May 31, 2001, with the following types of closings: returns secured, unable to locate the taxpayer, not liable for a specific period, and no longer liable to file. We selected these types of closings because they were the majority of the delinquent return investigation closures in the CFf (see Figure 1). The number of delinquent return investigation

³ A case refers to one taxpayer who may have one or more delinquent returns.

⁴ The ICS is a computer inventory system for the CFf. Cases being worked by ROs are controlled on the system, and the ROs document the case actions electronically on the system.

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periods closed, based on our ICS analysis, was 91,336 (28,330 taxpayers/cases). They were closed as follows:

- 52,600 with returns secured.
- 26,930 as no longer liable.
- 7,984 as not liable for a specific tax period.
- 3,822 as unable to locate.

We reviewed 120 judgmentally sampled cases (30 from each type of closing) to determine if they were worked effectively. We determined actions were effective when returns were secured; however, actions could have been more effective on cases closed without a return secured.

ROs used effective collection techniques when securing delinquent returns

Our review of 30 cases closed with returns secured having tax liabilities of \$577,547, showed that they were effectively worked. ROs took appropriate actions to secure the returns and tried to collect full payment of the tax liabilities with the delinquent returns. Examples of the effective actions included contacting the taxpayer either by letter, telephone, or field visits, which many times brought about filing compliance of the taxpayers. Other examples were appropriately using enforcement actions, such as levies and liens⁵ on open related balance due accounts of the same taxpayer in order to get the taxpayer to file.

We determined that although the ROs took sufficient actions to collect the tax liabilities, they did not collect much tax because of the taxpayers' inability to pay. Of the \$577,547 in tax liabilities, \$182,481 in Federal Tax Deposit (FTD)⁶ credits was already on the accounts. Of the remaining \$395,066 owed, \$9,360 (2 percent) was collected at the time the return was secured.

⁵ A lien is a charge upon a property or rights to property as security for the tax liability. A levy is an enforcement action that takes the taxpayer's property that is held by someone else, such as the taxpayer's bank account, wages, or commissions.

⁶ FTDs are tax deposits that business taxpayers make periodically during a quarter to offset their future tax liabilities.

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ROs did not adequately use available internal and external sources to locate taxpayers before closing cases as unable to locate

Twenty-two of the 30 cases closed as unable to locate could have been worked more effectively. Generally, these cases were not effectively worked because the ROs did not perform sufficient research of internal and external locator sources to try to locate addresses for the taxpayers.

Insufficient research included one or more of the following:

- Five cases where requests for addresses from the post office could have been made.
- Eight cases where field taxpayer visits could have been made.
- Eighteen cases where motor vehicle records could have been searched.
- Fifteen cases where real estate records could have been searched.

Also, we determined that balance due accounts and delinquent return investigations were not always worked consistently. In three cases, the balance due tax periods were closed as being out of business; however, the delinquent return investigations for the same taxpayer were closed as unable to locate. Also, in two other cases, the delinquent return investigations were closed as unable to locate, but the manager did not approve the unable to locate closings for the balance due tax periods because more research was needed. Managers do not approve closures for delinquency investigations closed as unable to locate.

One of the possible reasons that unable to locate closures were not proper is that managers informed us that the amount of research needed to locate a taxpayer is dependent on the judgment of the RO and the manager. The IRM is internally inconsistent; one chapter sets minimum requirements, while another leaves it to the judgment of the RO with some guidance of locator choices. The SB/SE Division plans to delete the reference showing minimum requirements. However, we believe that procedures should include minimum requirements or specific procedures

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including locator sources to be used. We found that in some instances, ROs were closing cases too quickly without conducting sufficient research.

In addition, there is inconsistency in the managerial review process whereby managers are required to review a balance due account if it is closed as unable to locate but, as previously stated, are not required to review a delinquent return investigation closed in the same way.

ROs did not always take proper closing actions when determining if taxpayers were not liable for a specific tax period or were no longer liable to file

ROs could have more effectively worked 9 of the 60 cases closed as either not liable for a specific tax period (30 cases) or no longer liable to file (30 cases).

- In six cases closed as not liable for a specific period, there was evidence in the case file that the taxpayer was actually out of business.
- In one case, the taxpayer was still in business but the case was closed as no longer liable and the filing requirements for that taxpayer were improperly closed.
- In two cases, there was not sufficient documentation in the case files to determine why the cases were closed as no longer liable or not liable for specific tax periods.

The primary cause for not taking the proper closing actions was that ROs were not using all the evidence they obtained to close the case as not liable for a specific tax period or no longer liable. For example, in one particular case history, the RO documented that the taxpayer was out of business as of a specific date; however, this information was not used in the decision of how to close the case.

In addition, delinquent return investigations are not reviewed by the Collection Quality Measurement System (CQMS)⁷ unless there is a balance due account worked

⁷ The CQMS is a case review process that provides a qualitative assessment of Cff cases.

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simultaneously with the delinquent return investigation. In these cases, the review is only to determine whether the RO used the proper closing code and locator services. Finally, there is some confusion on the priorities of the workload. Our discussions with managers indicated that although keeping taxpayers current in filing returns is a priority, many ROs consider collecting taxes more important. However, recent procedures give equal priority to delinquent return investigation and balance due accounts.

When cases are not worked properly and tax returns are not secured when due, the SB/SE Division is not meeting its goal of improving compliance. When ROs do not close the filing requirements, additional delinquent return investigation notices could be sent to taxpayers, causing unproductive work for ROs and unnecessary burden on taxpayers. On the other hand, when taxpayer cases are closed no longer liable and there is not sufficient evidence the taxpayer is not in business, there is a potential for those taxpayers to continue not filing and have no actions taken by the IRS.

Recommendations

The Director, Compliance, SB/SE Division, should:

1. Consider implementing both more specific reviews of delinquent return investigations closed as not liable through the CQMS, and a group manager review of cases closed as unable to locate, similar to the requirement for balance due accounts.

Management's Response: SB/SE Division management agreed with the recommendation and plans to develop review criteria and implement CQMS reviews for delinquent return investigations. In addition, they will revise the IRM to require group managers to approve delinquent return investigations that are closed as unable to locate.

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2. For unable to locate cases, provide national guidelines to ensure sufficient use of locator sources and consistency among various field groups, especially considering that ROs will be working only high-priority cases.

Management's Response: SB/SE Division management did not agree with the recommendation. However, they responded that the new requirement for group managers to approve unable to locate cases will help ensure the use of the appropriate locator sources and provide consistency.

The Collection Field Function Needs to Monitor Whether the Most Potentially Productive Returns Are Being Assigned

Our review of 120 cases showed that many non-productive cases involving low-dollar amounts and old tax periods are being assigned to the Cff. On the other hand, our analysis of more current inventory in the Queue⁸ showed cases with high-dollar potential were sitting in the Queue rather than being worked by ROs.

One reason these low-dollar amounts and old tax period cases were assigned is because they were selected under a process in which cases would not be assigned to ROs until there were a certain number of delinquent tax periods, which could have taken a few years. By working these older, low-dollar cases the ROs are spending some of their time working less or non-productive cases, which does not leave them enough time to work more productive cases.

SB/SE Division management has set goals to work more productive cases, close more delinquent return investigation cases, and improve business results. In December 2001, they implemented a new risk-based methodology for assigning cases to ROs to improve case selection. They will be assigning delinquent return investigation cases with the most current delinquencies and certain dollar amounts.

Although the new risk-based inventory delivery process may improve the assignment of old tax periods by assigning the most current delinquencies, SB/SE Division management needs to closely monitor this new process to

⁸ The Queue is an electronic holding place for work that will be assigned to ROs when their inventories are low.

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ensure that the most potentially productive returns are assigned.

Cases assigned to ROs generally were old tax periods and low dollars

From our review of the 120 cases closed by ROs, we determined that the Last Filed Return Amounts (i.e., tax amount of the latest return filed by the taxpayer) on the cases were generally small tax liabilities, with 73 of 120 (61 percent) cases less than \$5,000 (see Figure 2).

Figure 2. Last Filed Return Amounts of Cases Reviewed

Latest Filed Return Amount	Number of Cases (Taxpayers)
\$100,000 - 245,000	3
\$50,000 - 99,999	3
\$10,000 - 49,999	24
\$5,000 - 9,999	17
\$1,000 - 4,999	38
\$.01 - 999	15
\$0 or No Return	20
Total	120

Source: Treasury Inspector General for Tax Administration (TIGTA) case review.

In addition, the 559 tax periods involved in these cases were generally old tax periods. In 435 instances (78 percent), returns were for a tax period ending in 1999 or earlier, and in 302 instances (55 percent) returns were for a tax period ending in 1998 and earlier (see Figure 3).

Figure 3. Tax Periods of Cases Reviewed

Tax Periods	Number of Tax Periods
2001	2
2000	122
1999	133
1998 and earlier	302
Total	559

Source: TIGTA case review.

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Also, from our review of closed cases, we determined that cases were assigned in which the taxpayers had been out of business for years. We found that 9 of the 30 cases closed as no longer liable for taxes involved taxpayers who went out of business before their cases were assigned to an RO. For example, one of the nine taxpayers had been out of business since 1993 and was not assigned until 2001. In addition, nine of the cases closed as unable to locate had indications that the taxpayers were out of business, although the exact dates of being out of business could not be determined.

On the other hand, the following analysis shows many potentially productive returns with higher dollar assessments are not being worked by ROs.

Potentially higher dollar cases are in the Queue and not being worked

When a taxpayer does not file a return, the IRS first tries to contact the taxpayer by letter and then by telephone to resolve why the taxpayer has not filed and also try to secure the return. If the return cannot be secured from these telephone contacts, a case may be created and assigned directly to an RO to contact the taxpayer and secure the return. Under certain criteria, cases may be placed in the Queue, and at a later date, selected for an RO to work.

Many cases in the Queue had a high dollar Last Filed Return Amount

As of October 2, 2001, the Queue contained 234,506 delinquent return investigation cases for at least 781,340 tax periods. Of these, 55,490 had information regarding their last filed return. The Last Filed Return Amounts for these cases ranged from credit balances to over \$1 million. As Figure 4 shows, 24,657 (44 percent) of these 55,490 cases had a Last Filed Return Amount of \$5,000 or more.

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Figure 4. Last Filed Return Amounts of Cases in the Queue

Latest Return Amount	Number of Cases Taxpayers
\$1 Million and greater	192
\$500,000 - 999,999	131
\$100,000 - 499,999	1,154
\$50,000 - 99,999	1,635
\$10,000 - 49,999	13,175
\$5,000 - 9,999	8,370
\$.01 - 4,999	29,760
Zero	1,064
Credit Balances	9
Total	55,490

Source: The Queue as of October 2, 2001.

While 44 percent of the cases in the Queue had a Last Filed Return Amount of \$5,000 or more, 61 percent of the cases in our sample of closed RO cases had a Last Filed Return Amount of less than \$5,000. Furthermore, several cases were in the Queue with a Last Filed Return Amount greater than \$1 million. The prior assignment practices may not have effectively identified the cases with the highest potential. As a result, the Government could lose significant revenue if high-dollar cases remain in the Queue and are not worked.

We further analyzed the 192 cases with a Last Return Amount greater than \$1 million and identified several attributes:

- Seventy-four cases had some or all tax periods in the Queue for over a year.
- Four months after our initial October 2, 2001, analysis, many returns still were not filed and cases were still not worked. Of the 192 taxpayer cases, 39 taxpayers had filed the necessary tax returns and 28 cases were assigned elsewhere. However, 125 cases were still in the Queue, with 113 cases having all periods still in the Queue and 12 having some periods remaining in the Queue.

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- Many cases had FTD credits in the taxpayers' account, which may minimize the potential loss to the Government. Of the 125 cases still in the Queue, 84 had FTD credits in all periods. However, 6 had FTD deposits in only some periods, and 35 had no FTD credits at all; 24 of these taxpayers had filed returns previously with the Last Filed Return Amounts totaling \$177,188,679. These cases have the greatest risk of loss to the Government, since the taxpayers made no deposits and filed returns previously.

Based upon new case assignment criteria, many cases from the Queue will be assigned to ROs

As stated previously, the CFf recently revised its inventory assignment practices, and now both delinquent return investigation and balance due cases are being assigned based on certain "Risk Definitions." Risk definitions are generally based on the age of the tax periods and the dollar amounts of the last filed return. After special situations, such as taxpayers who request contact by an RO, the highest risk category includes delinquent employment return investigations with the earliest tax period that is less than one year old and having a Last Filed Return Amount over a specified dollar amount. Included in the next highest risk category are delinquent employment return investigations with the earliest period less than two years old and having a Last Filed Return Amount over a specified dollar amount.

To identify cases in the Queue that would have met the new inventory high-risk criteria, we analyzed the age of the tax period and the Last Filed Return Amounts and identified the previously mentioned 55,490 taxpayers having 174,782 tax periods for which last returns had been filed. Of these, 18,015 taxpayers had 24,796 tax periods that were all less than 2 years old.

- Of these cases, 3,377 taxpayers had 3,689 tax periods that were all less than 1 year old.
- Over 80 percent of the 18,015 taxpayers had Last Filed Return Amounts over the IRS' new dollar criteria.

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The 24,796 tax periods represent approximately 11 percent of the delinquent return investigation dispositions by the CFf in FY 2001. Therefore, the CFf should have the resources to effectively work this volume of cases because as the highest priority cases, they will be assigned first.

The new inventory assignment criteria are intended to help provide more productive returns for ROs. Our data from the Queue show there are taxpayers with potentially large dollar assessments that meet the new criteria for delinquent return investigations, and SB/SE Division management needs to ensure that they are actually assigned to the CFf.

Monitoring of the assignment process will be needed to ensure that the highest dollar delinquent return investigation cases are, in fact, selected for assignment. The CFf has limited resources to work cases, and without further monitoring or screening, the most productive work may not be assigned and fewer dollars will be secured.

Recommendation

3. The Director, Compliance, SB/SE Division, should establish a process to monitor and refine as needed the new risk-based methodology for delivering inventory to ensure the CFf is getting the most potentially productive delinquent return investigation cases.

Management's Response: SB/SE Division management agreed with the recommendation. They plan to establish a process to monitor the new risk-based methodology for delivering delinquent return investigation cases.

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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to evaluate the effectiveness of Collection Field function (Cff) actions to bring employment tax non-filers into compliance. To accomplish this objective, we discussed internal controls and procedures in the Small Business/Self-Employed (SB/SE) Division's Baltimore, Maryland; Boston, Massachusetts; Philadelphia, Pennsylvania; Richmond, Virginia; and Wethersfield, Connecticut field offices, and reviewed closed Cff delinquent return investigation cases.

We conducted the following tests to accomplish the objective.

- I. Determined the effectiveness of Revenue Officers' (RO) and group managers' actions on delinquent return cases.
 - A. Determined whether instructions and guidelines issued to Cff employees regarding delinquent returns were adequate to enable employees to effectively work cases.
 1. Identified and reviewed instructions and guidelines issued to Cff employees.
 2. Discussed procedures, guidelines, priorities, and inventory with Cff management.
 3. Based on the guidelines, created a database and a case review sheet to capture information as we reviewed cases.
 - B. Identified Cff closed employment tax delinquent return investigation cases for review by requesting data extracts from the Internal Revenue Service's (IRS) Integrated Collection System (ICS).¹
 1. Identified the population of 91,336 employment tax delinquent return investigation cases closed between October 2000 and May 2001.
 2. From the 91,336 population in B.1, identified the cases closed with the following transaction codes (TC): 599 (Return Secured) – 52,600; 590 (Unable to Locate) – 7,984; 591 (No Longer Liable) – 26,930; and 593 (Not Liable for A Specific Tax Period) – 3,822.
 3. To limit the number of cases reviewed, we took judgmental samples of 40 cases (to account for any possible duplicates) for each TC and

¹ The ICS is a computer inventory system for the Cff. Cases being worked by ROs are controlled on the system, and the ROs document the case files electronically on the system.

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reviewed the first 30 cases in each sample. The samples were selected by using a random number generator.

- C. Reviewed the closed cases to determine if cases were effectively worked. Used the case review sheet developed in I.A.3 to record the information obtained for each case in an Access database.
 - 1. Determined whether the CFf effectively worked cases where a return was secured (TC 599).
 - a) Identified the employment tax per return, total amount collected, and any prepayments in the account.
 - b) Verified if a full compliance check was completed and performed.
 - c) Listed the actions taken by the CFf employees that enabled them to do an effective job of securing the return.
 - d) Identified the actions taken by CFf employees to collect full payment and if they were sufficient.
 - e) Determined how cases in which full payment was not received were worked.
 - f) Determined if the cases were properly closed as “return secured.” Verified that the returns were secured and the appropriate TC and closing codes were used, such as whether the cases were fully paid, had installment agreements, had no payments, or were not collectible.
 - g) Determined if balance due accounts were also in inventory for each case selected.
 - (1) If there were balance due accounts assigned in inventory, determined how they were closed and whether the actions were consistent with the way the delinquent returns were closed. For example, was there information gathered from the balance due work that should have been used for the delinquent return but was not?
 - (2) Separated cases that were combination balance due and delinquent return cases from those that were only delinquent return cases. Determined whether there were any differences in the ways the cases were worked.
 - 2. Determined whether the CFf effectively worked cases where the taxpayer could not be located (TC 593).
 - a) Verified if full compliance checks were completed and performed.

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- b) Identified any prepayments in the account.
 - c) Determined if all actions had been taken to attempt to locate the taxpayers using internal and external sources. Listed the sources that the IRS should be using and determined if all were used.
 - d) Determined if cases were properly closed as unable to locate. Verified that the appropriate TC and closing codes were used and independently determined if there were addresses for the taxpayers.
 - e) Determined if enough time was taken to attempt to locate the taxpayers before closing the cases, and that once it was determined the taxpayers could not be located, that the cases were closed quickly.
 - f) Determined if the taxpayers filed subsequent returns or had other transactions on their accounts and what actions the IRS took.
 - g) Determined if balance due accounts were also in inventory for each case selected.
 - (1) If there were balance due accounts assigned in inventory, determined how they were closed and whether the actions were consistent with the way the delinquent returns were closed. For example, was there information gathered from the balance due work that should have been used for the delinquent returns but was not?
 - (2) Separated cases that were combination balance due and delinquent return cases from those that were only delinquent return cases. Determined whether there were any differences in the ways the cases were worked.
3. Determined whether the CFf effectively worked cases where the taxpayer was no longer liable for taxes (TC 591) or not required to file a specific period (TC 590).
- a) Verified if full compliance checks were completed and performed.
 - b) Identified any prepayments in the accounts.
 - c) Determined what evidence was used to make the decisions that taxpayers were not in business.
 - d) Determined if the cases were closed timely once the decisions were made that the taxpayers were not in business.

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- e) Determined if the cases were properly closed as no longer liable for taxes or not liable for a specific period. Verified that the appropriate TC and closing codes were used.
 - f) Determined if balance due accounts were also in inventory for each case selected.
 - (1) If there were balance due accounts assigned in inventory, determined how they were closed and whether the actions were consistent with the way the delinquent return was closed. For example, was there information gathered from the balance due work that should have been used for the delinquent returns but was not?
 - (2) Separated cases that were combination balance due and delinquent return cases from those that were only delinquent return cases. Determined whether there were any differences in the ways the cases were worked.
 - D. Summarized the results of the case review and identified potential causes of ineffective actions on the cases reviewed.
- II. Determined the characteristics of the inventory of employment tax delinquent returns in the Queue² and quantified trends.
- A. Obtained the inventory of cases in the Queue by requesting extracts of the following data from the IRS' computer systems:
 - 1. Employment tax delinquent return investigation cases in the Queue on October 2, 2001.
 - 2. Employment tax delinquent return investigation cases shelved between October 2000 and May 2001.
 - B. Analyzed cases in the Queue inventory identified in II.A and identified various characteristics of cases, such as the amount of the last return filed, age of cases, and credits on the accounts. Followed up on trends relating to dollar amounts of the last returns filed.

² The Queue is an electronic holding place for work that will be assigned to ROs when their inventories are low.

Major Contributors to This Report

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**The Delinquent Tax Return Investigation Program for Employment Taxes Within the
Collection Field Function Can Be Improved**

Appendix III

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The Delinquent Tax Return Investigation Program for Employment Taxes Within the Collection Field Function Can Be Improved

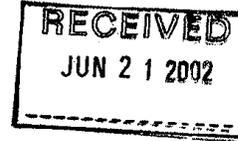
Appendix IV

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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



JUN 18 2002

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Joseph G. Kehoe 
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report -- The Delinquent Tax Return Investigation Program for Employment Taxes Within the Collection Field Function Can Be Improved (Audit # 200130030)

I reviewed your draft audit report on the effectiveness of Collection Field function actions to bring employment tax non-filers into compliance. I do not fully agree with your findings and recommendations. However, I recognize we can improve and plan to do so. We are revising our procedures to provide more guidance and have put in place revised inventory assignment practices, to help us ensure we assign the most potentially productive cases.

I do not agree having minimum requirements would ensure effective use of locator services. The actions we are taking, in response to your first recommendation will ensure sufficient and consistent use of locator sources. These actions require Collection Group Managers to review and approve all unable to locate closures, and develop a Collection Quality Measurement System (CQMS) review criteria for delinquent return investigations, with no related balance due account. This method of working cases ensures consistency among field groups working "unable to locate" cases because they use locator services as necessary.

Our responses to your recommendations follow:

RECOMMENDATION 1

The Director, Compliance, SB/SE Division, should consider implementing more specific reviews of delinquent return investigations closed as not liable through the CQMS and a group manager review of cases closed as unable to locate, similar to the requirement for balance due accounts.

ASSESSMENT OF CAUSE

CQMS does not have specific reviews for delinquent return investigations with no related balance due account. We did not require group managers to review and approve delinquent return investigations closed as not liable.

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CORRECTIVE ACTION

The Nonfiler Office will submit a request to the Office of Performance Excellence, Strategy, Research, and Performance Management (SRPM) to develop review criteria for delinquent return investigations. The Office of Performance Excellence and Compliance will develop criteria for the reviews and implement CQMS reviews for delinquent return investigations.

The Nonfiler Office will revise the IRM 5.1.11 to require Collection group managers to approve delinquent return investigations that we close under TC 593, Unable to Locate.

IMPLEMENTATION DATE

April 1, 2003

October 1, 2002

RESPONSIBLE OFFICIALS

Director, Filing and Payment Compliance, Small Business/Self-Employed Division
Director, Strategy, Research, and Performance Management

Director, Filing and Payment Compliance, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN

The Program Manager, Nonfiler Office, will monitor both corrective actions and advise the Director, Filing and Payment Compliance, Small Business/Self-Employed Division if either corrective action is delayed.

RECOMMENDATION 2

The Director, Compliance, SB/SE Division should, for unable to locate cases, provide national guidelines to ensure sufficient use of locator sources and consistency among various field groups, especially considering that ROs will be working only high-priority cases.

ASSESSMENT OF CAUSE

The Cff did not always use locator sources effectively.

CORRECTIVE ACTION

We do not agree with this recommendation. We decide which locator services are used on a case by case basis. The IRM states, "...reasonable efforts should be made prior to closing a case unable to locate". The revenue officer and the group manager should

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decide what is reasonable for each case. In making this decision, they can determine the most beneficial locator services based on costs, resources, location, experience and potential results.

The new requirement for group managers to approve TC 593, Unable to Locate closures (corrective action 2 of recommendation 1), will also ensure we use the appropriate locator sources and provide consistency.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 3

The Director, Compliance, SB/SE Division, should establish a process to monitor and refine as needed the new risk-based methodology for delivering inventory to ensure the Cff is getting the most potentially productive delinquent return investigation cases.

ASSESSMENT OF CAUSE

We did not assign the most potentially productive delinquent return investigation cases to the Cff.

CORRECTIVE ACTION

The Office of Collection Case Selection will establish a process to monitor the new risk-based methodology for delivering delinquent return investigation cases.

IMPLEMENTATION DATE

December 1, 2002

RESPONSIBLE OFFICIAL

Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division

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CORRECTIVE ACTION MONITORING PLAN

The Program Manager, Office of Collection Case Selection will advise the Director, Centralized Workload Selection and Delivery, Small Business/Self-Employed Division of any delays.

If you have any questions about this response, please call Joseph R. Brimacombe, Deputy Director, Compliance Policy, Small Business/Self-Employed, at (202) 283-2150.