

**Fiscal Year 2005 Review of Compliance With
Legal Guidelines When
Conducting Seizures of Taxpayers' Property**

June 2005

Reference Number: 2005-30-091

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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

June 3, 2005

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Fiscal Year 2005 Review of Compliance
With Legal Guidelines When Conducting Seizures of Taxpayers'
Property (Audit # 200430025)

This report presents the results of our review of the Internal Revenue Service's (IRS) compliance with legal guidelines when conducting seizures of taxpayers' property. The overall objective of this review was to determine whether seizures conducted by the IRS complied with the legal provisions set forth in Internal Revenue Code (I.R.C.) Sections (§§) 6330 through 6344 (1994 & Supp. IV 1998) and with the IRS' own internal procedures. This audit focused on determining whether the IRS conducted seizures in compliance with these legal and internal procedures. It was not intended to determine whether the decision to seize was appropriate or to identify the cause of any violations.

In summary, we found that the IRS did not comply with all legal and internal guidelines when conducting seizures. Our review of a random sample of 50 of 375 seizures conducted between July 1, 2003, and June 30, 2004, identified 17 instances in 12 of the seizures in which the IRS did not fully comply with the I.R.C. While we did not identify any instances where the taxpayers were adversely affected, not following legal and internal guidelines could result in abuses of taxpayers' rights.

In addition, we identified three areas where internal guidelines for conducting seizures can be improved to help prevent possible abuses of taxpayers' rights. First, the Internal Revenue Manual (IRM) does not provide specific guidelines to address instances where additional property is identified for seizure while the authorized seizure is being conducted. We identified two seizures where the seizure requests were made for a specific piece of property and the approvals were granted for that property. However, during the seizures, additional properties not included in the seizures requests were

also seized. Second, we believe the IRS' policy of limiting the minimum bid of seized property to no more than the taxpayer's tax liability plus estimated expenses of the seizure and sale does not provide for the equitable preservation of the taxpayer's interest in the seized property. We identified two seizures, where the minimum bids were established at the amount of the taxpayers' liabilities plus expenses, which were less than the calculated minimum bids using the standard formula by approximately \$16,200 and \$1,400. Finally, the IRM procedures are unclear with respect to charging the taxpayer's account for expenses incurred in obtaining title searches and encumbrance information reports. We identified two seizures where these types of expenses were charged to the taxpayers' accounts and two seizures where they were not charged to the taxpayers' accounts. We also identified one seizure where the taxpayer's account was not charged for all title searches conducted.

Since the specific violations of the I.R.C. we identified this year were the same as those we reported in last year's mandatory review of seizures audit report¹ and this year's seizures were conducted prior to implementation of the corrective actions taken in response to that report, we made no recommendations in these areas. However, we did recommend the Director, Collection, Small Business/Self-Employed Division, develop procedures for obtaining seizure approval in situations where revenue officers identify additional property that can be subject to seizure while carrying out the prior approved seizure. Also, the Director should reconsider the IRS policy limiting the minimum bid in all instances to an amount not to exceed the tax, penalty, interest, lien fees, expenses of seizure and sale, and other charges, which represent the Federal Government's interest in the seized property. Finally, the Director should clarify the IRM procedures to ensure consistency when charging title search or encumbrance information report expenses to taxpayers' accounts.

Management's Response: The IRS management agreed with our recommendations. They advised the IRM will be updated to include appropriate instructions for obtaining seizure approval in situations where revenue officers identify additional property that can be subject to seizure while carrying out the prior approved seizure. They will also evaluate their existing guidelines to determine if the current minimum bid policy should be changed. In addition, the IRM will be updated to include the required instructions for if and when expenses incurred in obtaining title searches and encumbrance information reports are to be charged to the taxpayers' accounts. Management's complete response to the draft report is included as Appendix VIII.

¹ *Legal and Internal Guidelines Were Not Always Followed When Conducting Seizures of Taxpayers' Property* (Reference Number 2004-30-149, dated August 2004).

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have any questions or Richard Dagiolo, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs), at (631) 654-6028.

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Background

The collection of unpaid tax by the Internal Revenue Service (IRS) generally begins with letters to the taxpayer followed by telephone calls and personal contacts by an IRS employee. The employees who make personal contact are referred to as revenue officers. They consider the taxpayer's ability to pay the tax and discuss alternatives, such as installment payment agreements or offers in compromise.¹ If these actions have been taken and the taxpayer has not fully paid the tax due, the revenue officer has the authority to take the taxpayer's funds or property for the payment of tax. Taking a taxpayer's property for unpaid tax is commonly referred to as a "seizure."

To ensure taxpayers' rights are protected, the IRS Restructuring and Reform Act of 1998 (RRA 98)² amended the seizure provisions in Internal Revenue Code (I.R.C.) Sections (§§) 6330 through 6344 (1994 & Supp. IV 1998). These provisions and the IRS' internal procedures are very specific regarding how a seizure should be performed. See Appendix V for a synopsis of the applicable legal provisions.

The Treasury Inspector General for Tax Administration is required under I.R.C. § 7803(d)(1)(A)(iv) (Supp. IV 1998) to annually evaluate the IRS' compliance with these legal seizure provisions to ensure taxpayers' rights were not violated while conducting seizure actions. We have evaluated the IRS' compliance with the seizure provisions since Fiscal Year (FY) 1999. See Appendix VI for a list of all prior audit reports issued on the IRS' compliance with seizure procedures.

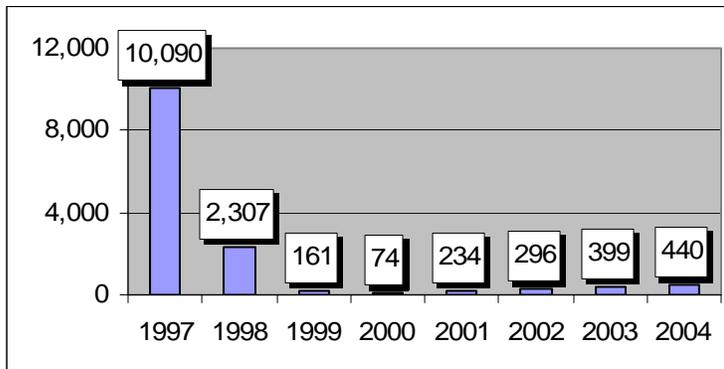
Since the enactment of the RRA 98, the number of seizures conducted by the IRS has significantly decreased. Figure 1 illustrates the number of seizures for the past 8 fiscal years.

¹ An offer in compromise is a proposal by a taxpayer to settle unpaid account(s) for less than the full amount of the balance due.

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

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Figure 1: IRS Seizures by Fiscal Year



Source: IRS Oversight Board Annual Report 2001 for FYs 1997–1999 and the IRS 2004 Databook for FYs 2000–2004.

We performed this audit in the IRS Small Business/Self-Employed (SB/SE) Division Headquarters in New Carrollton, Maryland, during the period September 2004 through February 2005. This audit focused on determining whether the IRS conducted seizures in compliance with legal provisions and internal procedures. It was not intended to determine whether the decision to seize was appropriate or to identify the cause of any violations. The audit was performed 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 Internal Revenue Service Did Not Always Comply With Legal Provisions and Internal Procedures When Conducting Seizures

Our review of a random sample of 50 of 375 seizures conducted between July 1, 2003, and June 30, 2004, determined the IRS did not comply with all legal and internal guidelines when conducting seizures. In 12 (24 percent) of the 50 seizures reviewed, we identified 17 instances in which the IRS did not fully comply with the I.R.C. While we did not identify any instances where the taxpayers were adversely affected, not following the legal and internal guidelines could result in abuses of taxpayers' rights.

The types of I.R.C. violations we discuss below are the same as those we reported in last year's mandatory review

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of seizures audit report.³ Since the seizures we reviewed this year were all conducted prior to implementation of the corrective actions taken in response to that report, we are making no additional recommendations in those areas. The corrective actions were scheduled to be completed between July 26, 2004, and January 15, 2005.

The 17 instances include:

- One where the IRS did not provide the intent to levy notice for every period on the Levy⁴ (Form 668-B). (I.R.C. § 6330(a))
- Seven where all the required forms relating to the sales of the seized property were not provided to the taxpayers. (I.R.C. § 6340(c))
- Seven where the balance due letters required to be sent to taxpayers after the sales proceeds were applied to liabilities were not provided to the taxpayers or the balances due reported were not correct. (I.R.C. § 6340(c))
- Two where the proceeds resulting from the seizures were not properly applied to the taxpayers' accounts. (I.R.C. § 6342(a))

A description of each follows.

The IRS did not provide the intent to levy notice for every period on the Form 668-B

I.R.C. § 6330(a) requires that a levy may not be made on any property or right to property of any person, unless the IRS has notified that person in writing of his or her right to a hearing before the levy is made. The notice is required for all the taxable periods to which the unpaid tax relates. I.R.C. § 6331(d) also requires that a levy can be made only after the IRS has notified the taxpayer in writing of the

³ *Legal and Internal Guidelines Were Not Always Followed When Conducting Seizures of Taxpayers' Property* (Reference Number 2004-30-149, dated August 2004).

⁴ A levy is a means to take property by legal authority to satisfy a tax debt. The IRS uses a levy as a tool to collect on balance due accounts that are not being voluntarily paid.

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intention to make the levy no less than 30 days before the day of the levy.

The Internal Revenue Manual (IRM) requires that, before a seizure can be conducted, a Notice of Intent to Levy and Notice of Your Right to a Hearing (Letter 1058) must have been provided to the taxpayer at least 30 days before the seizure and for each tax period that will be identified on the Form 668-B.

We identified one seizure where there was no indication in the case file that the taxpayer was provided a Letter 1058 for every period on the Form 668-B. The case file indicated a Letter 1058 was issued for all but one of the liabilities shown on the Form 668-B.

Taxpayers were not provided all the required forms relating to the sale of the seized property

I.R.C. § 6340(a) requires the IRS to keep a record of all sales of property. The record shall set forth the tax for which any such sale was made, the dates of the seizure and sale, the name of the party for which the tax was assessed, and all proceedings in making the sale. I.R.C. § 6340(c) also requires the taxpayer be furnished the record of the sale.

The IRM requires the IRS to maintain a permanent record of all sales conducted under I.R.C. § 6335. The IRM provides a list of the forms that are to be retained in the permanent record and requires copies of the forms be sent to the taxpayer, unless previously provided.

Our review of the 50 seizures included 22 that resulted in a sale of the seized property. There was no indication in 7 of the 22 seizure files that the taxpayers had been provided, as of the time of our review, all of the required forms relating to the sale of the seized property. See Appendix VII for a list of the forms that were not provided to the taxpayers.

The IRM states that the Technical Support function is responsible for maintaining the permanent record of the seizure file and providing the taxpayer with copies of the permanent record.

The IRM also requires the Technical Support function to post review the seizure file upon receipt of the Seized

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Property Sale Report (Form 2436) to ensure conformity with statutes, regulations, and procedural guidelines of the IRM. The IRS has developed a Post-Seizure Review Checksheet (Form 13361) to assist in the post-review. The IRM requires the Form 13361 (or comparable form) to be completed during the post-review, to ensure all required actions were taken, and to be maintained as part of the seizure file in the Technical Support function. Page 1 of the Form 13361 contains line entries to document when the required forms were mailed to the taxpayers.

A Form 13361 was in the case file for all seven seizures where the taxpayers were not provided all the required forms. There were no entries for the forms that were not mailed to the taxpayers on four of the Forms 13361. The other three Forms 13361 were marked "not applicable" for the forms that were not mailed to the taxpayers.

Taxpayers were not notified of their balances due after the sales proceeds were applied to their liabilities or the balances due reported were not correct

I.R.C. § 6340(c) requires the taxpayer, with respect to whose liability the sale was conducted, to be furnished with the amount from the sale that was applied to the taxpayer's liability and the remaining balance of the liability.

The IRM requires the Technical Support function to provide the taxpayer a Form 2436 and include a letter explaining the form (which shows how the sales proceeds were applied). The letter should also identify the balance of each account after the application of the proceeds from the sale of seized property.

As previously stated, our review of the 50 seizures included 22 that resulted in a sale of the seized property. The taxpayers were sent the Form 2436 showing how the proceeds were applied in 18 of the 22 seizures. Three other seizures involved recent sales and the Forms 2436 had not been sent at the time of our review. In the remaining seizure, the taxpayer was deceased at the time of sale, thus a Form 2436 was not required.

However, in 2 of the 18 seizure files where the taxpayers were sent the Form 2436, there is no indication that the taxpayers were notified of their balances due after the sale

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proceeds were applied to their liabilities. In another five seizures, the balances due reported to the taxpayers were not correct.

Proceeds resulting from seizures were not properly applied to the taxpayers' accounts

I.R.C. § 6342(a) requires any money realized by proceedings under this subchapter (whether by seizure or by sale of seized property) shall be applied first against the expenses of the proceedings, then against any unpaid tax imposed by any internal revenue law against the property seized and sold (for example, an excise tax), and finally against the liability in respect to which the levy was made or the sale was conducted (the accounts appearing on the Form 668-B).

The IRM requires the same order for applying the proceeds. It also states that, since the I.R.C. requires funds realized under seizure and sale proceedings be applied first to the expenses of levy and sale, the proceeds should be credited to the taxpayer's account using a TC 694, Designated Payment of Fees and Collection Costs. If the seizure results in a sale, the proceeds should be recorded on the Form 2436, which should be transmitted to the Accounting Control/Services Operation for application of the proceeds to the taxpayer's account. Funds obtained from a release or redemption⁵ of seized property will be credited to the taxpayer's account using a general posting document.

As stated previously, seizure expenses were incurred in 37 of the 50 seizures reviewed. Proceeds were realized in 31 of these 37 seizures. In 1 of the 31 seizures, while the expenses were correctly posted with a TC 360, the proceeds realized were not applied first to the seizure expenses with a TC 694. This seizure resulted in the property being redeemed by the taxpayer. We could not find a posting

⁵ Seized property can be released to the taxpayer under a number of circumstances, including (1) the Federal Government receives its interest in the property, (2) future collection potential is enhanced by the release, or (3) release will facilitate the collection of the liability. Any person whose property has been seized can redeem the property prior to a sale if the taxpayer pays the full amount of taxes, penalties, and interest due and any expenses of the seizure and preparation for sale.

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document in the case file for the posting of the proceeds; however, the case file is notated that the request for posting of the proceeds was for a TC 670, Subsequent Payment, and not for a TC 694, as required.

We also identified one seizure where the proceeds were applied to a liability for an account not on the Form 668-B before being applied to satisfy all the liabilities on the Form 668-B. The proceeds resulted from a sale of seized property, and the Form 2436 was prepared requesting posting to that liability.

The order in which proceeds are to be applied is not affected by how the seizure is closed – either by sale or by release. Both the I.R.C. and IRM state the order in which the proceeds are applied pertains to any money realized under seizure and sale proceedings, whether by seizure or by sale of seized property.

As previously stated, the IRM requires the Technical Support function to post review the seizure file upon receipt of the Form 2436. The IRS developed Form 13361 to assist in the post-review.

There is no place on the Form 13361 for noting whether the proceeds from the seizure or sale were properly applied. However, in one of the two seizures identified above, the Technical Services function advisor noted in the case file that proceeds had been properly credited to balance due accounts.

Internal Guidelines for Conducting Seizures Can Be Improved to Help Prevent Possible Abuses of Taxpayers' Rights

We identified three areas where internal guidelines for conducting seizures can be improved to help prevent possible abuses of taxpayers' rights. First, while the IRS has established procedures to follow in obtaining approval prior to conducting a seizure, the IRM does not provide specific guidelines to address instances where additional property is identified while the authorized seizure is being conducted. Second, we believe the IRS' policy of limiting the minimum bid of seized property to no more than the taxpayer's tax liability plus estimated expenses of the seizure and sale does not provide for the equitable preservation of the taxpayer's interest in the seized property. Lastly, while the IRS has established procedures for charging seizure- and sale-related expenses to taxpayers'

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accounts, the IRM procedures need to be clarified with respect to expenses incurred for obtaining title searches and encumbrance information reports to ensure equitable treatment of taxpayers.

IRM guidelines do not address instances where additional property is identified while seizures are being conducted

The RRA 98 required the IRS to develop and implement procedures under which a determination by an employee to seize any property would, where appropriate, be required to be reviewed by a supervisor before the action is taken. The review process may include a certification that the employee has reviewed the taxpayer's information and affirmed the action proposed to be taken is appropriate given the taxpayer's circumstances, the amount due, and the value of the property.

The IRS has established procedures to follow in obtaining approval prior to conducting a seizure. When it is determined that seizure is the appropriate action, the IRM requires the revenue officer to prepare the Form 668-B and a preseizure checklist designed to document that certain required preseizure action was taken. The revenue officer should circle on the preseizure checklist the type of asset to be seized, such as vehicle, machinery/equipment, real property, etc.

The case file must contain adequate documentation to justify the seizure action and then be submitted for approval through the appropriate levels of management. The approval package should contain, among other things, the preseizure checklist, case history and/or fact sheet, a draft minimum bid, and any other relevant items.

We identified two seizures where the preseizure checklists, draft minimum bids, and fact sheets submitted for approval of the seizures only mentioned seizing vehicles. Proper approval was granted for the seizure actions in both cases.

However, in both cases, the revenue officers seized additional property not included in the seizure approval package, such as other business equipment and machinery. There was no documentation anywhere in the case files, prior to the seizures, about potentially seizing any other

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property. Therefore, the seizure of the additional property could be considered an unauthorized seizure.

Since seizures of different types of property have somewhat different pre-seizure requirements, not adequately describing the property to be seized may result in procedural violations and lead to possible abuse of taxpayers' rights.

The IRS' policy of limiting the minimum bid of seized property does not, in some instances, provide for the equitable preservation of the taxpayer's interest in the seized property

I.R.C. § 6335(e) requires that, before the sale of seized property, the IRS shall determine a minimum bid price below which such property shall not be sold.

The IRM states the minimum bid price must be correctly determined to provide for the equitable preservation of both the taxpayer's and the Federal Government's interest in the property and provides specific instructions for determining the minimum bid.

The fair market value of the property is the starting point for the calculation of the minimum bid. A property value reduction, not to exceed 25 percent, should then be taken to determine the forced sale value. This reduction is taken to reflect the fact that the sale is a forced sale and is not taking place between a willing seller and a willing buyer. The forced sale value may then be reduced by a maximum of 20 percent to determine the reduced forced sale value. The total of all prior claims against the property should then be subtracted from the reduced forced sale value to arrive at the minimum bid price.

However, according to IRS policy, the minimum bid price, in all instances, will be limited to an amount not to exceed the tax, penalty, interest, lien fees, expenses of seizure and sale, and other charges, which represent the Federal Government's interest in the seized property.

We identified two seizures where the minimum bids were established at the amount of the taxpayers' liabilities plus expenses, which were less than the calculated minimum bids using the standard formula by approximately \$16,200 and \$1,400.

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In both cases, the property was redeemed prior to going to sale and therefore did not have any adverse effect on the taxpayers. However, had the properties been sold for the minimum bids determined under the current policy, the taxpayers would have received nothing from the sales after their tax liabilities and expenses were satisfied.

For instance, in this fictitious example, if a piece of vacant real estate with a value of \$75,000 was seized, the reduced forced sale value and the minimum bid using the standard formula would be \$45,000, assuming there were no outstanding liens. If the taxpayer owed \$10,000 and the estimated seizure and sale expenses were \$2,000 then the minimum bid under the current policy would be limited to \$12,000. Assuming, the property could have been sold for the reduced forced sale value, the taxpayer would lose \$33,000 on the sale (\$45,000 less \$12,000).

Under the current IRS policy, the minimum bid could be set much lower than that determined using the standard minimum bid formula and not necessarily reflect the value of the taxpayer's ownership interest in the seized property. This IRS policy seems to be contrary to the IRM section that states the minimum bid price must be correctly determined to provide for the equitable preservation of both the taxpayer's and the Federal Government's interest in the property.

The Government Accountability Office (GAO) expressed a similar concern in a 1999 review of IRS seizures.⁶ In its report, the GAO stated, "Under this policy, the minimum price could be set much lower than the formula, using maximum percentage reductions, would allow. The minimum price then would not necessarily reflect the value of the taxpayers' ownership interest in the seized property."

The GAO recommended that, to strengthen the sales process for assuring the highest prices are obtained from seized asset sales, the IRS Commissioner should develop guidelines to preclude the use of the amount of delinquency as the minimum price. The Commissioner responded the IRS was

⁶ *IRS Seizures Needed for Compliance but Processes for Protecting Taxpayer Rights Have Some Weaknesses* (GAO/GGD-00-4, dated November 1999).

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“previously required by the IRC to bid in the property for the government, but precluded by the U.S. Code from bidding in property for more than the amount of the tax liability plus costs.” The Commissioner went on to state the IRS Office of Chief Counsel has continued to support that position. However, in light of the GAO recommendation, the Commissioner stated, “we can again raise the issue with Counsel.”

While we agree the IRS can legally set the minimum bid at the amount of the taxpayer's total liability, we agree with the GAO that the taxpayer's interests and rights could be better protected.

IRM guidelines need to be clarified as to when expenses incurred for title search and encumbrance information reports are to be charged to the taxpayers' accounts

The I.R.C. and IRM require the revenue officer to make a determination that there will be sufficient net proceeds to apply to the liability prior to recommending a case for seizure. To determine if there will be sufficient net proceeds available, the revenue officer must complete an equity determination, which includes a complete public records search, to identify all recorded encumbrances and interests in the property to be seized. The IRM states that, at local management option, commercial firms may be contracted to provide title search and encumbrance information reports.

I.R.C. § 6341 states the IRS shall determine the expenses to be allowed in all cases of levy and sale. The IRM states it is essential all expenses of sale be debited against the taxpayer's account so the expenses are satisfied from the proceeds of the sale. The IRM also states the cost of title search and encumbrance information reports “may be charged” to the balance due accounts as an expense. The IRM provides a list of expenses that should be considered as an expense of the seizure and, while not all-inclusive, the list does not include expenses for title search and encumbrance information reports.

IRS management advised us that, based on prior practice, judgment searches, title searches, etc., were viewed as administrative or investigative expenses and not considered

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related to expenses for seizure. Thus, they were not charged to the taxpayers' accounts.

Our review determined taxpayers were being inconsistently treated when it came to charging them for these types of expenses. We identified five seizures that contained expenses for title search or encumbrance information reports. In two of the seizures, these expenses were not charged to the taxpayers' accounts. In two other seizures, these expenses were charged to the taxpayers' accounts. In the remaining case, the taxpayer's account was not charged for all title searches conducted.

Recommendations

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

1. Develop procedures for obtaining seizure approval in situations where the revenue officers identify additional property that can be subject to seizure while carrying out the prior approved seizure.

Management's response: SB/SE Division management advised the IRM will be updated to include the appropriate instructions.

2. Reconsider the IRS policy limiting the minimum bid in all instances to an amount not to exceed the tax, penalty, interest, lien fees, expenses of seizure and sale, and other charges, which represent the Federal Government's interest in the seized property.

Management's response: SB/SE Division management advised they will evaluate the existing guidelines to determine if the current minimum bid policy should be changed.

3. Clarify the IRM procedures as to if and when expenses incurred in obtaining title searches and encumbrance information reports are to be charged to taxpayers' accounts.

Management's response: SB/SE Division advised the IRM will be updated to include the required instructions.

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether seizures conducted by the Internal Revenue Service (IRS) complied with legal provisions set forth in Internal Revenue Code Sections 6330 through 6344 (1994 & Supp. IV 1998) and with the IRS' own internal procedures.¹

To accomplish our objective, we:

- I. Obtained documentation of national guidance provided to employees; identified IRS systems, policies, and practices for ensuring compliance with legal provisions and internal procedures related to seizures; and determined how these tools were used.
- II. Reviewed a random sample of 50 of the 375 seizures conducted by the IRS from July 1, 2003, through June 30, 2004. The seizures were reviewed to determine compliance with legal provisions and internal procedures and whether the proceeds and applicable expenses of the seizures and sales were properly recorded to taxpayers' accounts on the IRS' main computer system. A random sample was used to ensure each of the 375 seizures had an equal chance of being selected.

¹ This audit focused on determining whether the IRS conducted seizures in compliance with legal and internal procedures. It was not intended to determine whether the decision to seize was appropriate.

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Outcome Measures

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

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 12 taxpayers for whom the Internal Revenue Service did not comply with legal provisions and internal procedures when conducting seizures (see page 2). While we did not identify any instances where the taxpayers were adversely affected, not following legal and internal guidelines could result in abuses of taxpayers' rights.
- Taxpayer Rights and Entitlements – Potential; 9 taxpayers for whom internal guidelines for conducting seizures can be improved to help prevent abuses of taxpayers' rights (see page 7). (Four of these nine are also included in the 12 above.) While we did not identify any instances where the taxpayers were adversely affected, not following legal and internal guidelines could result in abuses of taxpayers' rights.

Methodology Used to Measure the Reported Benefit:

We selected a random sample of 50 seizures from a population of 375 seizures conducted from July 1, 2003, through June 30, 2004. A random sample was used to ensure each of the 375 seizures had an equal chance of being selected.

Synopsis of Selected Legal Provisions for Conducting Seizures

Internal Revenue Code (I.R.C.) Section (§) 6330 (Supp. IV 1998) requires the Internal Revenue Service (IRS) to issue the taxpayer a notice of his or her right to a hearing prior to seizure action. The notice must be (1) given in person, (2) left at the taxpayer's home or business, or (3) mailed certified-return receipt requested, not less than 30 days before the day of the seizure. The notice must explain in simple terms (1) the amount owed, (2) the right to request a hearing during the 30-day period, and (3) the proposed action by the IRS and the taxpayer's rights with respect to such action.

The statute of limitations for collection is suspended from the time a taxpayer requests a hearing and while such hearings and appeals are pending, except when the underlying tax liability is not at issue in the appeal and the court determines the IRS has shown good cause not to suspend the seizure. No limitation period may expire before 90 days after a final determination. These procedures do not apply if the collection of tax is at risk.

I.R.C. § 6331 (1994 & Supp. IV 1998) authorizes the IRS to seize a taxpayer's property for unpaid tax after sending the taxpayer a 30-day notice of intent to levy.¹ This section also prohibits seizure (1) during a pending suit for the refund of any payment of a divisible tax, (2) before a thorough investigation of the status of any property subject to seizure, or (3) while either an offer in compromise² or an installment agreement is being evaluated and, if necessary, 30 additional days for the taxpayer to appeal the rejection of the offer in compromise or installment agreement.

I.R.C. § 6332 (1994 & Supp. IV 1998) requires a third party in possession of property subject to seizure to surrender such property when a levy notice is received. It contains sanctions against third parties that do not surrender such property when a levy notice is received.

I.R.C. § 6333 (1994 & Supp. IV 1998) requires a third party with control of books or records containing evidence or statements relating to property subject to seizure to exhibit such books or records to the IRS when a levy notice is received.

I.R.C. § 6334 (1994 & Supp. IV 1998) enumerates property exempt from seizure. The exemption amounts are adjusted each year and included \$6,890 for the period July 1, 2003, through December 31, 2003, and \$7,040 for the period January 1, 2004, through June 30, 2004, for fuel, provisions, furniture, and personal effects, and \$3,440 for the period July 1, 2003,

¹ A levy is a means to take property by legal authority to satisfy a tax debt. The IRS uses a levy as a tool to collect on balance due accounts that are not being voluntarily paid.

² An offer in compromise is a proposal by a taxpayer to settle unpaid accounts for less than the full amount of the balance due.

Fiscal Year 2005 Statutory Review of Compliance With Legal Guidelines When Conducting Seizures of Taxpayers' Property

through December 31, 2003, and \$3,520 for the period January 1, 2004, through June 30, 2004, for books and tools necessary for business purposes. Also, any primary residence, not just the taxpayer's, is exempt from seizure when the amount owed is \$5,000 or less. Seizure of the taxpayer's principal residence is allowed only with the approval of a United States (U.S.) District Court judge or magistrate. Property used in an individual taxpayer's business is exempt except with written approval of the Area Office Director, and the seizure may only be approved if other assets are not sufficient to pay the liability.

I.R.C. § 6335 (1994 & Supp. IV 1998) contains procedures for the sale of seized property. Notice must be given to the taxpayer; the property must be advertised in the county newspaper or posted at the nearest post office; and such notices shall specify the time, place, manner, and conditions of sale. It requires the property be sold not less than 10 days or more than 40 days from the time of giving public notice. Finally, this section expressly prohibits selling seized property for less than the minimum bid.

I.R.C. § 6336 (Supp. IV 1998) contains procedures for the accelerated disposition of perishable property. This is property such as fresh food products or any property that requires prohibitive expenses to maintain during the normal sale time period. The property may either be sold quickly or returned to the taxpayer in exchange for payment of a bond.

I.R.C. § 6337 (1994 & Supp. IV 1998) allows the taxpayer to redeem seized property prior to sale by paying the amount due plus the expenses of the seizure. It also allows a taxpayer to redeem real property within 180 days of the sale by paying the successful bidder the purchase price plus 20 percent per annum interest.

I.R.C. § 6338 (1994 & Supp. IV 1998) requires the IRS to give purchasers of seized property a certificate of sale upon full payment of the purchase price. This includes issuing a deed to real property after expiration of the 180-day period required by I.R.C. § 6337. The deed is exchanged for the certificate of sale issued at the time of the sale.

I.R.C. § 6339 (1994 & Supp. IV 1998) provides the legal effect of the certificate of sale for personal property and the transfer deed for real property.

I.R.C. § 6340 (1994 & Supp. IV 1998) requires each Area Office to keep a record of all sales of seized property. This record must include the tax for which such sale was made, the dates of seizure and sale, the name of the party assessed, all proceedings in making such sale, the amount of expenses, the names of the purchasers, and the date of the deed or certificate of sale of personal property. The taxpayer will be furnished (1) the information above except the purchasers' names, (2) the amount of such sale applied to the taxpayer's liability, and (3) the remaining balance of such liability.

I.R.C. § 6341 (1994 & Supp. IV 1998) allows expenses for all seizure and sale cases.

I.R.C. § 6342 (1994 & Supp. IV 1998) enumerates how the proceeds of a seizure and sale are to be applied to a taxpayer's account. Proceeds are applied first to the expenses of the seizure and sale proceedings. Then, any remainder is applied to the taxpayer's liability.

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I.R.C. § 6343 (1994 & Supp. IV 1998) outlines various conditions under which a seizure may be released and property returned to the taxpayer. These conditions include full payment of the liability, determination of a wrongful seizure, financial hardship, etc. This section allows a consent agreement between the U.S. and either the taxpayer or the National Taxpayer Advocate when the return of seized property would be in the taxpayer's best interest.

I.R.C. § 6344 (1994 & Supp. IV 1998) contains cross-references for I.R.C. §§ 6330 through 6344.

Public Law Number 105-206 (IRS Restructuring and Reform Act of 1998)³ § 3443 required the IRS to implement a uniform asset disposal mechanism by July 22, 2000, for sales of seized property under I.R.C. § 6335. This mechanism was designed to remove revenue officers from participating in the sales of seized assets.

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

Prior Reports on Compliance With Seizure Procedures

The Internal Revenue Service Needs to Improve Compliance with Legal and Internal Guidelines When Taking Taxpayers' Property for Unpaid Taxes (Reference Number 199910072, dated September 1999).

The Internal Revenue Service Has Significantly Improved Compliance With Legal and Internal Guidelines When Seizing Taxpayers' Property (Reference Number 2000-10-114, dated August 2000).

Letter Report: The Internal Revenue Service Complied With Legal and Internal Guidelines When Seizing Property for Payment of Tax (Reference Number 2001-10-061, dated May 2001).

The Internal Revenue Service Has Taken Significant Actions, But Increased Oversight Is Needed to Fully Implement the Uniform Asset Disposal Mechanism (Reference Number 2002-10-005, dated November 2001).

The Internal Revenue Service Continues to Comply With the Law When Seizing Taxpayers' Property (Reference Number 2002-40-155, dated August 2002).

Fiscal Year 2003 Statutory Audit of Compliance With Seizure Procedures (Reference Number 2003-40-115, dated May 2003).

Legal and Internal Guidelines Were Not Always Followed When Conducting Seizures of Taxpayers' Property (Reference Number 2004-30-149, dated August 2004).

**Fiscal Year 2005 Statutory Review of Compliance With Legal Guidelines When Conducting
Seizures of Taxpayers' Property**

Appendix VII

**Forms Required to Be Provided to the Taxpayer for Sale of Seized Property and
Number of Instances Not Provided**

Notice of Encumbrances Against or Interests in Property Offered for Sale (Form 2434-B)	5 cases
Certificate of Sale of Seized Property (Form 2435)	4 cases
Public Sale Bid Tabulation (Form 4425)	2 cases
Record of Seizure and Sale of Real Estate (Record 21)	2 cases
Sealed Bid for Purchase of Seized Property (Form 2222)	1 case

Fiscal Year 2005 Statutory Review of Compliance With Legal Guidelines When Conducting Seizures of Taxpayers' Property

Appendix VIII

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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

RECEIVED
MAY 26 2005

May 26, 2005

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

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

SUBJECT: Draft Audit Report – FY 2005 Review of Compliance With Legal Guidelines When Conducting Seizures of Taxpayers' Property (Audit # 200430025)

We have reviewed your report and generally agree with the results of your audit of our seizure and sale program. Although you identified legal violations on 12 of the cases reviewed during this year's audit, we appreciate your acknowledgement that the violations were administrative in nature and that taxpayers were not adversely impacted by these errors.

The majority of the errors occurred in the post-seizure process. As a result of your audit in fiscal year (FY) 2004, we took several steps to help reduce these types of errors. We issued additional procedural guidance to the field and added instructions to the Internal Revenue Manual (IRM). Mandatory reviews are now required of all seizure cases by Technical Services prior to approval by the territory manager. We believe these changes will reduce the frequency of these errors.

Although you did not make any recommendations related to the technical errors in this audit, we are committed to ensuring that all actions we take on seizure and sale cases conform to the established legal and procedural guidelines. We continue to update and clarify procedures in the IRM to protect taxpayers' rights while still ensuring the seizure and sale process remains an effective enforcement tool.

We are reviewing the current IRM instructions and the seizure checklists to determine if any additional changes would make them more effective. In addition, we are conducting reviews of seizure case files in several offices to identify any potential areas of concern. Once the areas are identified, we will take the necessary corrective actions to help prevent these errors in the future. Finally, managers in Technical Services will be reviewing all seizure cases from FY 2004 to identify and correct any procedural errors that may have occurred.

Fiscal Year 2005 Statutory Review of Compliance With Legal Guidelines When Conducting Seizures of Taxpayers' Property

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You identified three areas where you believed internal guidelines for conducting seizures could be improved to better protect taxpayers' rights. We are providing specific comments to those recommendations below.

RECOMMENDATION 1:

The Director, Collection, SB/SE Division, should develop procedures for obtaining seizure approval in situations where the revenue officers identify additional property that can be subject to seizure while carrying out the prior approved seizure.

CORRECTIVE ACTION:

IRM 5.10.2 will be updated to include the appropriate instructions.

IMPLEMENTATION DATE:

November 15, 2005

RESPONSIBLE OFFICIAL:

Director, Collection Policy, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:

Program Manager, Field Payment Compliance, will advise the Director, Collection Policy, of any delays in implementation of the corrective action.

RECOMMENDATION 2:

The Director, Collection, SB/SE Division, should reconsider the IRS' policy limiting the minimum bid in all instances to an amount not to exceed the tax, penalty, interest, lien fees, expenses of seizure and sale, and other charges, which represent the Government's interest in the seized property.

CORRECTIVE ACTION:

We will evaluate our existing guidelines to determine if the current minimum bid policy should be changed.

IMPLEMENTATION DATE:

July 15, 2005

RESPONSIBLE OFFICIAL:

Director, Collection Policy, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:

Program Manager, Field Payment Compliance, will advise the Director, Collection Policy, of any delays in implementation of the corrective action.

RECOMMENDATION 3:

The Director, Collection, SB/SE Division, should clarify the IRM procedures as to if and when expenses incurred in obtaining title searches and encumbrance information reports are to be charged to the taxpayers' accounts.

Fiscal Year 2005 Statutory Review of Compliance With Legal Guidelines When Conducting Seizures of Taxpayers' Property

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CORRECTIVE ACTION:

IRM 5.10.1 will be updated to include the required instructions.

IMPLEMENTATION DATE:

November 15, 2005

RESPONSIBLE OFFICIAL:

Director, Collection Policy, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:

Program Manager, Field Payment Compliance, will advise the Director, Collection Policy, of any delays in implementation of the corrective action.

If you have any questions, please contact me at (202) 622-0600 or Brady R. Bennett, Director, Collection, Small Business/Self-Employed Division at (202) 283-7660.