COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

March 29, 2001

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MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: John M. Dalrymple
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report--Oversight of the Philadelphia Lockbox Bank Should Be Improved (Reference No. 2000-40-058)

We appreciate the opportunity to respond to your draft report and recommendations for the Philadelphia Lockbox Bank. Your overall summary concludes that the lockbox bank deposited taxpayer payments within required time frames, complied with the security guidelines, but did not always sort tax returns correctly. We agree with your recommendations that IRS improve its oversight of lockbox operations to ensure that the banks are processing tax payments according to established guidelines and meeting their contractual agreement.

We would like to note that at the time of your audit, Wage and Investment Headquarters had already taken steps to address and measure the overall quality and oversight of our lockbox processing program. Security, timeliness, and accuracy of processing tax payments was, is, and will continue to be of paramount importance to the IRS. Although your findings show the Philadelphia Lockbox Coordinator did not complete the required reports, we want to assure you that the Director of the Philadelphia Submission Processing Center (PSPC) and his staff have fully supported and continue to support ongoing efforts to improve lockbox processing. For example, PSPC employees played a major role in identifying, assessing, developing, and implementing the Lockbox Deposit Business Measures and the Lockbox Quality Review Process. Their efforts have enabled the IRS to revamp the lockbox quality review and oversight process to eliminate the weaknesses you outlined.

You raised concerns with the cost effectiveness of our decision last April to use 60 PSPC employees to conduct a 100 percent quality review of over 600,000 tax returns to correct the bank's sorting errors. The Outcome Measures section of your report states we could have saved $109,056 had we not conducted the 100 percent review. We disagree with your estimated cost savings because it is not balanced against potential and actual benefits realized by the review. The review identified 162 undiscovered remittances (checks attached to tax returns) totaling $435,052, which authorized PSPC personnel promptly deposited and credited to taxpayers' accounts.

Tangible benefits of the review include:

- Actual dollars accrued in Interest Earned on timely tax payment deposits
- Potential dollars saved in Interest Paid on refunds lost due to the bank's missorting
- Potential resource expenditures for Payment Tracers, Refund Inquiries, and Taxpayer Advocate Hardship Referrals

Non-tangible benefits of the review include:

- Increased customer satisfaction
- Accurate tax account deposits for taxpayers
- Decreased taxpayer contact with the IRS

The actions we have taken to improve lockbox processing should enable us to work proactively with the bank(s) to take up-front preventive measures in the future. Our long-term solution to lower the number of missorted tax returns is to have employees at the Submission Processing Centers who are knowledgeable in sorting returns conduct annual training sessions at the lockbox sites. However, should we encounter future sorting errors, we are committed to taking the necessary action, including 100 percent reviews, to minimize processing delays for taxpayers and avoid additional internal costs for subsequent tax account corrections.

Our goal as we continue to modernize the IRS is recognizing and meeting the needs of our customers, and we welcome feedback from you on our progress.

Our comments on the specific recommendations in your report are as follows:

RECOMMENDATION 1
The IRS should ensure that the bank correctly sorts tax returns.

ASSESSMENT OF CAUSE
Lockbox banks have high employee turnover rates, so new employees must constantly learn a new process.

CORRECTIVE ACTION
The Headquarters Lockbox staff will research the feasibility of having employees at the Submission Processing Centers (SPC) who are knowledgeable in sorting returns train employees at the lockbox sites prior to the April peak.

PROPOSED IMPLEMENTATION DATE
January 2002

RESPONSIBLE MANAGEMENT OFFICIALS
Director, Submission Processing
Chief, Individual Master File Branch

CORRECTIVE ACTION MONITORING PLAN
The SPC Lockbox Coordinators and the Headquarters Lockbox staff will review the April Peak On-Site Review reports to determine if the prior to April peak training is beneficial. If the return sort error rate is still high, the Headquarters Lockbox staff will convene a task force to review the return sort procedures.

RECOMMENDATION 2
The IRS should ensure that the PSPC lockbox coordinator conducts the required on-site visits to the bank and prepares and submits required reports.

ASSESSMENT OF CAUSE
In the past, Headquarters oversight of Lockbox and SPC Lockbox Coordinators needed improvement. The Headquarters Lockbox staff has already identified the deficiencies and is improving those processes.

CORRECTIVE ACTION
We directed all Lockbox Coordinators to complete their monthly reviews until implementation of the new Quality Review Process. The Headquarters Lockbox staff will track the receipt of the monthly reviews. The first phase of the Quality Review Process began on January 15, 2001. This phase includes a procedural and administrative review of lockbox processing from the time the lockbox site receives the mail to the time the lockbox site forwards the package to the SPC and the money is deposited.

The second phase will focus on reviewing the process from the time the SPC receives the package to just before the transaction posts to the taxpayer's account. The National Deposit Accuracy Measure will then see if the deposit posted correctly to the taxpayer's account. This new process will require the Lockbox Coordinators to be on-site during the four peak months (January, April, June, and September).

Additionally, Headquarters is now issuing "Lockbox Alerts" to quickly disseminate important information to Lockbox Banks and Coordinators.

PROPOSED IMPLEMENTATION DATE
Implemented: January 15, 2001

RESPONSIBLE MANAGEMENT OFFICIALS
Director, Submission Processing
Chief, Individual Master File Branch

CORRECTIVE ACTION MONITORING PLAN
We will update IRM 3.0.230, Lockbox Processing Procedures, to reflect the four mandatory on-site visits in 2001. The total redesign of the review process for Lockbox is near completion and will include new reporting requirements that the Headquarters Lockbox staff will track. This staff will roll up the review data and share it with management and the field.

If you have any questions or need additional information regarding this response, please contact me, or your staff may contact Joyce A. Parson at (202) 283-0927.