TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Accounting and Controls Need to Be Improved for Excess Collections

December 15, 2015

Reference Number: 2016-30-005

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ACCOUNTING AND CONTROLS NEED TO BE IMPROVED FOR EXCESS COLLECTIONS

Highlights

Final Report issued on December 15, 2015

Highlights of Reference Number: 2016-30-005 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

IMPACT ON TAXPAYERS

The Excess Collection File (XSF) was established to contain both nonrevenue receipts and tax payments that cannot be associated with the appropriate taxpayers' accounts. Weaknesses in the administration of the XSF can create an environment in which unapplied taxpayer credits are vulnerable to loss and can either overstate or understate potential Government obligations.

WHY TIGTA DID THE AUDIT

Since January 2010, the XSF has grown from $4.7 billion to $5.8 billion, an increase of 23 percent. This audit was initiated to determine whether the controls over the XSF adequately prevent improper transactions and ensure that expired credits are appropriately accounted for and not exposed to fraud or abuse.

WHAT TIGTA FOUND

TIGTA determined that 2.94 million (90 percent) of the 3.28 million records, involving $4.75 billion (82 percent) of $5.81 billion in the XSF database, were credits transferred to the XSF due to barred statute, *i.e.*, the taxpayer no longer has a legal claim to the credit. The retention period for credits in the XSF database does not match the time frames for which taxpayers can claim the credits. The IRS retains these credits in the XSF database for seven years even though taxpayers have no legal claim to the funds. IRS management could not explain why XSF credits are maintained specifically for seven years. The XSF database actually has credits from the 1980's, 1970's, and even 1960's.

As a result, the potential liability of credits in the XSF database was overstated by $4.7 billion as of July 2014. This amount includes more than $530 million in credits that entered the XSF in Calendar Year 2013 due to barred statute. Eliminating these credits from the XSF database could decrease the IRS's exposure to potential fraud because credits will no longer be able to be viewed and accessed in the database.

The IRS's internal financial accounting for excess collections can also be improved to help the IRS manage the risks associated with the XSF. For example, although the IRS Chief Financial Officer accounts for excess collections on an annual basis there is no attempt to keep track of the overall accumulated balance of the XSF which our audit determined to be at least $5.8 billion.

TIGTA also reviewed all credits transferred from the XSF greater than $15,000 and found that transfers did not always comply with procedures and managerial approval is not required. Further, XSF controls do not allow managers to identify when taxpayer credits are transferred out of the XSF. These control weaknesses increase the risk of undetected fraud.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS: 1) change the XSF purging criteria from the XSF entry date to the IRS received date; 2) use the general refund statute of limitations as the standard for moving credits from the XSF; 3) utilize the internal accounting function to improve IRS controls over the XSF; 4) capture and report data specific to transfers from the XSF; 5) ensure that employees comply with XSF documentation requirements; and 6) require management approval of all transfers out of the XSF.

IRS management agreed with two of our recommendations but declined to take action on the rest. TIGTA continues to believe all of the recommendations if implemented would strengthen controls and improve the administration of the XSF.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

December 15, 2015

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Accounting and Controls Need to Be Improved for Excess Collections (Audit # 201430024)

This report presents the results of our review to determine whether the controls over the Excess Collections File adequately prevent improper transactions and ensure that expired credits are appropriately accounted for and not exposed to fraud or abuse. This audit was included in our Fiscal Year 2015 Annual Audit Plan and addresses the major management challenge of Achieving Program Efficiencies and Cost Savings.

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

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations.

If you have any questions, please contact me or Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations).

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Abbreviations

CFO	Chief Financial Officer
IDRS	Integrated Data Retrieval System
I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
XSF	Excess Collection File

Background

The Excess Collection File (XSF)[1] is a control file within the Integrated Data Retrieval System (IDRS) containing nonrevenue receipts and tax revenue payments that cannot be associated with the correct taxpayer's account. When the Internal Revenue Service (IRS) is unable to determine which taxpayer's account to apply a payment, the payment is sent to the Unidentified Remittance File. If these payments are not resolved and their transaction date is a year old, they are moved to the XSF. Situations in which the IRS cannot identify the appropriate account to associate taxpayer payments include when a taxpayer:

Since Fiscal Year 2010, the XSF has grown 23 percent, and now includes more than $5.8 billion

- Submits a tax payment but does not file a tax return.
- Files a tax return past the time period to receive a refund.

The XSF is also used when taxpayers can no longer utilize credits due to the expiration of the date that the law allows taxpayers to claim a refund or use a credit (Refund Statute Expiration Date).[2] Such credits are moved to the XSF because the taxpayers are no longer entitled to a refund, unless one of the narrow statutory exceptions applies.

Most transfers to the XSF originate in the Wage and Investment Division's Accounts Management unit or the Statute unit within the Accounts Management function. When payments and the associated documents are not received or processed as expected, the Accounts Management function at each IRS campus is responsible for ensuring resolution. If the case is still not resolved after the Accounts Management function research has been performed and the payment is more than one year old, the payment is transferred to the XSF.

After a payment is moved to the XSF, it is no longer associated with the taxpayer's account, but the payment is still identifiable by the taxpayer's name. As of July 28, 2014, there was approximately $5.8 billion in the XSF, which is a 23 percent increase since January 2010 ($4.7 billion).

[1] See Appendix V for a glossary of terms.
[2] Internal Revenue Code (I.R.C.) Section (§) 6511(a) provides the general rule that taxpayers must claim their refunds within the later of three years from the date of the return or two years from the date that the tax was paid. There are numerous exceptions to this general rule such as I.R.C. § 6511(d)'s exception for bad debts and worthless securities which extends the statute to seven years, as well as § 6511(h)'s exception for taxpayers who were unable to manage their financial affairs due to disability which suspends the running of the time frames described in § 6511(a).

XSF credits should be established, corrected, and transferred (in/out) only by IRS employees who work in the Unidentified/Excess Collection function. These employees can manually transfer credits from the XSF to taxpayer accounts by using specific IDRS command codes.

Transfer requests must be processed by the same campus that placed funds in the XSF, and such requests are supported by Form 8765, *IDRS Control File Credit Application*. Examples of acceptable reasons for a refund from the XSF include payments sent in error; payments intended for another payee or agency; and receipt of Form 1310, *Statement of Person Claiming Refund Due a Deceased Taxpayer*.

Unidentified/Excess Collection function employees may use a variety of IDRS command codes to manage the XSF, including:

- Adding credits to the XSF.
- Researching credits for proper disposition.
- Applying or refunding credits to taxpayer accounts or directly to the taxpayer from the XSF.
- Contacting taxpayers and third parties through correspondence.

A Form 8765 should have documentation attached identifying the credit on the XSF as well as justifying its requested application through correspondence, research performed, *etc*. When transferring a credit to/from the XSF, the tax examiner must first verify that all case documentation is present and complete. If Form 8765 is received without documentation or without proper completion of all required entries, it should be returned to the requestor immediately.

IRS policy requires that credits remain in the XSF up to seven years, long after most taxpayers can legally claim the credits. Every month, credits older than seven years should be systemically purged from the XSF. The purged credits are reported on the Unidentified Remittance File 50 (XSF)–XSF Balance Amount Drop List (sometimes referred to as the purge or the "XSF dropped listing"), which is generated monthly at each Submission Processing Center. Once credits are purged from the XSF, it is still possible for the IRS to locate and identify a taxpayer's credit from the XSF dropped listing; however, only employees from the IRS accounting function have access to this list. This limited access is an important internal control that reduces the likelihood of unauthorized access. The IRS does not otherwise manage what is placed into the XSF dropped listing or know the amount of credits that have been placed in the list over time.

Separate and apart from the IRS's functional management of the XSF, the Chief Financial Officer's (CFO) accounting function also reflects excess collections on the IRS's books and records. Annually, the IRS accounts for the receipt of excess collections on its Statement of Custodial Activity as individual income. Historically, this amount has not exceeded $2 billion. For internal accounting purposes, the IRS reflects excess collections amounts on its internal general ledger account up to one year. At the end of each fiscal year, the IRS transfers the excess collection amounts into a clearance account that houses numerous other "nominal" (meaning temporary) accounts.[3] Generally, once excess collections are moved to the clearance account, no further credits or debits are made with respect to those amounts.

This review was performed at the Wage and Investment Division Headquarters in Atlanta, Georgia, and the Customer Accounts Services function in the Kansas City Campus in Kansas City, Missouri, during the period August 2014 through June 2015. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

[3] These are accounts that begin each year with a zero balance and are closed out at the end of the year (such as revenue accounts).

Results of Review

The Retention Policies for the Excess Collections File Overstate Potential Obligations and Increase the Risk of Undetected Fraud

The XSF was established to contain all nonrevenue receipt credits that cannot be immediately identified or applied to their proper tax account. It contains credits that could potentially be returned to taxpayers (open credits), as well as credits that are prohibited by statute from being returned to taxpayers (barred statute credits).[4] Open credits represent a potential liability to the IRS while barred statute credits do not. The Unidentified/Excess Collection function employees research open credits in an effort to resolve them. Unresolved open credits can have a negative impact on the taxpayer if the credits are not resolved and timely applied to the taxpayer's account. This may result in unnecessary notices, leading to added taxpayer burden. Conversely, for barred statute credits, the general refund statute of limitations has expired, and employees are not required to research or resolve them because they are no longer available to the taxpayer. However, even though the IRS is prevented by statute from refunding these payments to taxpayers, except in the limited situations described in Internal Revenue Code (I.R.C.) § 6511, these payments are held for an additional seven years before removal from the XSF.

While IRS management could not explain why XSF credits are maintained specifically for seven years, they did provide several scenarios in which retaining the credits for a period of time assists them in researching taxpayer requests. For example, when credits remain in the XSF, it is easier for Unidentified/Excess Collection function employees to research potential taxpayer claims to offset future additional assessments for the same tax period. It is clear that there are scenarios in which taxpayers can claim credits that are in the XSF; however, our research reflects that payments from the XSF are rare. Between April 2010 and July 2014, there were 1,165 transfers out of the XSF involving $5.26 million. Of these, there were 31 transfers involving $15,000 or more which represented $4.18 million (79 percent) of the total dollar value of the transfers out. We reviewed all 31 transfers (discussed in more detail later in this report) and none of the 31 involved bad debts or worthless securities. Accordingly, we believe that situations with credits involving bad debts or worthless securities extending the statute to seven years are rare.[5]

We obtained a complete extract of the XSF database as of July 27, 2014. Our analysis determined that:

- The majority of the credits in the XSF database are barred statute credits.
- The dollar value of the XSF has grown due to a change in the purging process.

[4] I.R.C. § 6511.
[5] I.R.C. § 6511(d).

The majority of the credits in the XSF database are barred statute credits

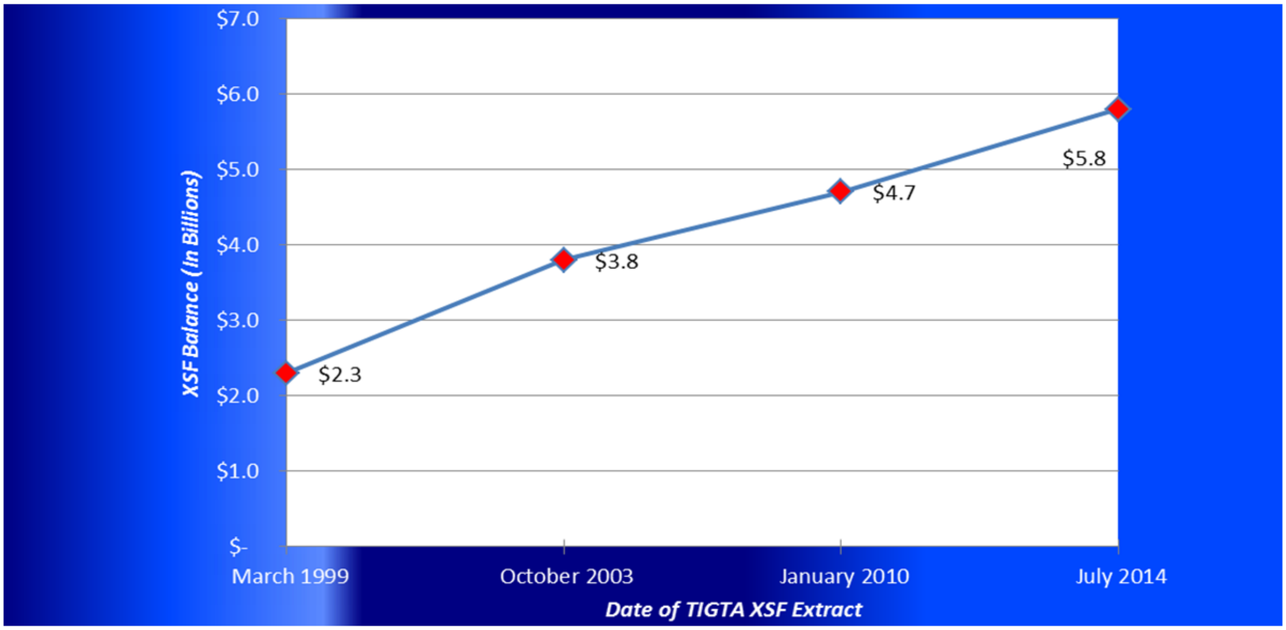
The vast majority of the credits within the XSF are statute cases in which the taxpayer no longer has any claim to the credits because the Refund Statute Expiration Date has passed.[6] Specifically, 2.94 million (90 percent) of the 3.28 million records, involving $4.75 billion (82 percent) of $5.81 billion in the XSF, were barred statute credits transferred to the XSF due to the expiration of the refund statute of limitations. There are also indications that these barred statute credits will continue to be the largest component of the XSF population. During Fiscal Year 2013, 93 percent of the XSF transfers, involving 91 percent ($530.8 million) of the dollar value, were statute-expired credits. Because barred statute credits are generally no longer legally available to the taxpayer and are not required to be researched like open credits, it is not necessary for them to remain in the XSF for more than 30 days.[7]

The dollar value of the XSF has grown due to a change in the purging process

The Internal Revenue Manual (IRM) establishes the criteria for which credits should be removed from the XSF.[8] Every month, credits greater than seven years old should be systemically purged from the XSF and moved into the XSF dropped listing, for which there is limited IRS employee access. Until Calendar Year 1998, the purging of these credits was correctly based on the date the IRS received the payment. However, in Calendar Year 1999, the IRS made computer programming modifications that changed the basis from the received date to the date that the credit was transferred into the XSF. We identified a correlation between this change and the trend of the increasing balance of the XSF database. In March 1999, the XSF had a balance of approximately $2.3 billion. Between March 1999 and July 2014, the balance increased to approximately $5.8 billion (152 percent). Figure 1 shows the growth in the dollar value of the XSF after the change.

[6] I.R.C. § 6511.
[7] Thirty days would act as a grace period to allow time to identify barred statute credits that may have been transferred into the XSF in error.
[8] IRM 3.17.220, *Accounting and Data Control, Excess Collections File* (01-01-2014).

Figure 1: Growth in the Dollar Value of the XSF



Source: TIGTA analysis of XSF database extracts obtained for this audit and three prior XSF audits.

For barred statute credits, this change altered the purge date by several months to several years and had the effect of postponing the date that the credits would drop out of the IRS's electronic system. To illustrate, a taxpayer who had tax withheld for Tax Year 2002, but who waited to file their return until Calendar Year 2010 (after the refund/credit statute expired), is able to utilize the withholdings to satisfy his or her liability for 2002 but is barred from claiming any refund if withholdings exceeded the tax liability.[9] Under current processing procedures, the excess of the withholding over the tax liability would be transferred to the XSF in 2010 (when the late return is processed) and remain in the XSF until Calendar Year 2017. If the purge process was still based on the IRS received date, the advanced credits would be transferred to the XSF in Calendar Year 2010 but remain in the XSF only until the end of the month before being purged because the XSF would identify the IRS received date as sometime during Calendar Year 2002.

Figure 2 shows the XSF currently includes billions of dollars in withholding credits and advance tax payments that were received by the IRS more than seven years ago. The XSF actually has credits from the 1980's, 1970's, and even 1960's.

[9] While I.R.C. § 6511 provides for the general statute of limitations to use a credit or a claim a refund to be the later of two years from the date the tax is paid or three years from the date the return is filed, I.R.C. § 6513(b)(1) provides that taxes that are withheld are deemed paid as of the due date of the tax return. Therefore, the taxpayer in the example is able to utilize the withholdings from 2002 to satisfy the tax liability but is unable to claim a refund from those withholdings.

Figure 2: XSF Credits With IRS Received Dates Older Than 7 Years

IRS Received Date	Number of Credits	Value of Credits
1960's	3	$506
1970's	35	$22,752
1980's	830	$3,459,764
1990's	41,246	$128,552,998
2000-2007(July)	2,240,676	$3,434,086,663
Total	2,282,790	$3,566,122,683

Source: TIGTA analysis of an extract from the XSF database.

IRS management was unable to explain why the computer programming change was made.[10] Based on the data in the XSF extract, there are approximately 2.3 million XSF credits, involving about $3.57 billion which have IRS received dates older than seven years. This amount is 61 percent of the total value of the XSF ($5.81 billion). By changing back the XSF purge process to use the IRS received date, the IRS would immediately decrease the balance of the XSF database by 61 percent.

Eliminating barred statute credits from the XSF database could decrease the IRS's exposure to potential fraud. Even though the barred statute credits are not required to be researched, they can still be viewed and accessed by IRS employees via the IDRS. Because of control weaknesses within the XSF database, there is a risk that inappropriate and/or unauthorized transfers of barred statute credits would not be prevented or detected. For example, we identified one unauthorized employee who attempted to use the XSF command code to process refunds 37 times over the course of seven months. The control weaknesses and IRS's exposure to fraudulent activities are discussed in more detail later in this report.

The balance in the XSF represents a potential liability to the IRS if taxpayers submit a valid claim for their credit or if IRS research of open credits results in application to a taxpayer's account.[11] However, this liability is overstated because taxpayers are barred from recovering an overwhelming majority of the credits in the XSF. Specifically, we determined that as of July 2014, the dollar value of the potential liability associated with the credits in the XSF

[10] The programming was changed in 1999 under the now defunct Resource Information Services process and past the retention period for any documents supporting the reasons for the change.
[11] A claim submitted prior to statute expiration.

database was overstated by $4.7 billion in barred statute credits. This amount includes more than $530 million in credits that entered the XSF in Calendar Year 2013 due to barred statutes. The $5.8 billion total does not include the amounts moved out of the XSF into the XSF dropped listing after seven years, and the IRS Wage and Investment Division was unable to provide historical totals as to how much in total credits remains in the XSF dropped listing.

Internal accounting practices could be improved to manage XSF risks

Separate and apart from how the IRS Wage and Investment Division manages taxpayer accounts with excess collection credits in its business units, the IRS must also account for excess collections on its internal books and records. The IRS CFO reflects amounts moved into excess collections in any given year in account 6800 (Excess Collections), one of 236 nominal accounts and is reflected on the IRS's Statement of Custodial Accounts as part of its annual financial statements. The account balance is closed[12] or transferred to account 9999 (Revenue Clearance Accountability) at the end of every fiscal year.[13]

Account 9999 is an account used only at the end of the fiscal year accounting period to close account 6800 as well as all of the other 235 IRS nominal accounts, and its balance is cumulative. In addition to account 6800, account 9999 contains numerous other large nominal accounts reflecting both tax receipts and payments, such as account 6132 (Corporation Tax Assessment – Principle) and account 6140 (Excise Tax Assessment – Principle), the balances of which at the end of Fiscal Year 2014 were $5 billion and $3 billion, respectively. IRS officials informed us that once funds are closed into 9999, they generally never come out. Accordingly, the current balance of account 9999 exceeds $1 trillion. This amount does not reflect money available to the Government because this is a clearance account and it contains years' worth of closing entries from temporary accounts. However, the Excess Collections account is different from those accounts because taxpayers may come forward and claim those credits in the future. Additionally, the XSF is at risk of attempts at fraud; therefore, it is important to know what the balance of the XSF is at any given time, as well as trends that are occurring within the XSF.

The IRS's CFO does not track excess collection amounts on a historical basis. Additionally, the CFO does not track the current balance of the XSF maintained by the Submission Processing function. Even if the CFO wanted to account for the cumulative excess collection amount, it would not be possible because excess collections are comingled with other nominal accounts in account 9999 as previously described. When a taxpayer makes a claim to utilize a credit contained within the XSF, the IRS makes an adjustment to account 9998 (a contra account to 9999), but it does not make the adjustment with an intention of accounting for adjustments to the overall balance of excess collections in the XSF. The IRS (including the CFO and the IRS Submission Processing function) does not know what the XSF balance is at any given time.

[12] The balance in account 6800 is closed by transferring the balance to account 9999.
[13] The end of the IRS fiscal year is also the end of the IRS accounting year.

Recommendations

Recommendation 1: The Commissioner, Wage and Investment Division, should reverse the programming change made in 1998 so that the XSF purging criteria counts the number of years the credit should be in the XSF based on the year the payment is received by the IRS.

> ***Management's Response:*** Management disagreed with this recommendation. In their response, management stated that the year payment is received by the IRS is not an optimal indicator for determining the purge dates of transactions contained in the XSF. Management stated that the change would be burdensome to both taxpayers and the IRS because it would impede their ability to effectively administer the tax system and provide efficient and accurate service to taxpayers. Management provided an example supporting their position.

Office of Audit Comment: We believe that the example management provided is not a typical situation, but instead is an infrequent occurrence. None of the transfers out of the XSF that we sampled involved the application of an overpayment from a late filed return to satisfy an additional assessment due to examination (of the late filed return). Accordingly, we disagree with management's position that changing the purging criteria would be burdensome to both taxpayers and the IRS. As we reported, the general statute of limitations for using a credit or claiming a refund is the later of two years from the date the tax is paid or three years from the date the return is filed. I.R.C. § 6513(b)(1) provides that taxes that are withheld are deemed paid as of the due date of the tax return. Therefore, the taxpayer in management's example would still be able to utilize the withholdings to satisfy the tax liability but would be unable to claim a refund for those withholdings. Management advised us that overpayments such as the kind in their example could remain in the taxpayer's account for 36 months before transfer to the XSF, which is consistent with the assessment statute management referenced. Therefore, purging this type of credits in a more timely manner (based on IRS received date) would not impact the IRS's ability to effectively administer the tax system. Further, even after purging, it is still possible to locate and identify a taxpayer's credit from the XSF dropped listing maintained on its data systems. Access to this data is limited to employees from the IRS accounting function as an important internal control that reduces the likelihood of unauthorized access.

Recommendation 2: The Commissioner, Wage and Investment Division, should utilize the general refund statute of limitations (*i.e.*, the later of two years from the date the tax is paid or three years from the date the return was filed) as the standard for moving credits from the XSF and request programming changes that are consistent with this recommendation. In the interim, purge those credits that are older than seven years based on the IRS received date.

> ***Management's Response:*** Management disagreed with this recommendation stating the same reasons as for the first recommendation.

> ***Office of Audit Comment:*** We reiterate our position from the Office of Audit Comment in the first recommendation.

Recommendation 3: The CFO, in consultation with the Department of the Treasury, should develop an accounting treatment that allows the IRS to account for excess collections in such a way that it can provide management information on the balance of the XSF at any given time.

> ***Management's Response:*** Management disagreed with this recommendation. In their response, management stated that the IRS is accounting for excess collections on a modified cash basis which is in accordance with Generally Accepted Accounting Principles (GAAP) per Federal Accounting Standards Advisory Board Standard 7. Management added that the Department of the Treasury agrees that the accounting and reporting of excess collections is at the discretion of the IRS.
>
> ***Office of Audit Comment:*** TIGTA's recommendation does not relate to whether the CFO's accounting practices satisfy GAAP but rather the importance of tracking the balance of this account, which is approximately $5.8 billion. The current accounting treatment for excess collections does not provide IRS management with complete information about the balance of the XSF. TIGTA demonstrated to the IRS how such information could be used to enhance its internal controls and continues to believe such information would help strengthen controls and the administration of the XSF.

Transfers From the Excess Collection File Are Not Always Prepared Properly

To determine whether transfer requests from the XSF were appropriate, we reviewed all individual taxpayer and business taxpayer transfers greater than $15,000. Results showed that Forms 8765 were not always completed in compliance with established procedures. Specifically,

- Transfers and transfer requests were not always properly documented.
- Reviews of Forms 8765 by the Unidentified/Excess Collection function were not effective.
- Review or approval by a manager is not required for transfers from the XSF.

Transfers and transfer requests were not always properly documented

Internal control standards require that agencies establish control activities that ensure that management's directives are enforced and carried out.[14] The standards require that all transactions and other significant events be clearly documented and that the documentation be readily available for examination. All documentation and records should be properly managed and maintained. Proper documentation could provide transparency and support for the transfer of taxpayer credits from the XSF.

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[14] Government Accountability Office, GAO-14-704G, Standards for Internal Controls in the Federal Government (Sept. 2014).

The XSF database is not configured to capture audit trail information that tracks transfers from the XSF, nor does it include specific fields that capture credit or payment amounts that are transferred from the XSF. As a result, transfers to taxpayer accounts from the XSF are not transparent and cannot be readily monitored or tracked by Unidentified/Excess Collection function management. To identify a transfer from the XSF, IRS personnel must manually calculate for each record the difference between the original XSF credit and the current XSF balance. The resulting difference is the amount transferred out. In addition, the XSF database does not capture the details of the transfers out such as the taxpayers' identification number, address, or the employee number of the Unidentified/Excess Collection function employee processing the transfer.

By calculating the difference between the original balance and current balance for the data in our XSF extract, we determined that there were 1,165 transfers out of the XSF between April 2010 and July 2014 involving $5.26 million.[15] Of the 1,165 transfers, 31 (3 percent) involved transfers of $15,000 or more and represented $4.18 million (79 percent) of the total dollar value of all transfers out. Of the 31 transfers of $15,000 or more, no Form 8765 or supporting documentation was available for three cases, leaving 28 cases that were reviewable.

The IRM provides that Form 8765 should have documentation attached that identifies the credit on the XSF as well as the associated reasons for the transfer, such as correspondence, research performed, *etc*.[16] The IRM also requires case file documentation supporting the IRS employee's attempts to resolve the identity of the credit to be applied to the taxpayer's account.[17] Specifically, documentation should confirm that the credit was originally transferred from the taxpayer's account and that the credit is still available in the XSF.

Upon receipt of Form 8765, Unidentified/Excess Collection function tax examiners are required to ensure that every Form 8765 is complete and accurate and includes sufficient supporting documentation such as documentation of the prior research performed, pertinent IDRS transcripts of the taxpayer account where payment is to be applied, and correspondence from the taxpayer (and copy of the check for the original payment, when applicable).

Although the Form 8765 was available for the 28 cases we reviewed, the documentation was not sufficient in 24 (86 percent) of the 28 requests. The 24 cases involved more than $4 million in credits transferred out of the XSF and contained the following documentation errors:

- While correspondence with the taxpayer would generally initiate a transfer of credits or payments from the XSF, 24 of the 28 cases did not include documented taxpayer correspondence; *i.e.,* letters or written narrative describing the interaction and circumstances for the credit or refund.

[15] We eliminated any transfers less than 99 cents.
[16] IRM 3.17.220.2.11 (08-16-2013).
[17] IRM 3.17.220.2.1.3 (01-01-2012).

- Form 8758, *Excess Collections File Addition*, and Master File transcripts of the taxpayer's account would show that the credit or payment was originally transferred from that taxpayer into the XSF, and the IDRS transcripts of the XSF would show that the credit was still available in the XSF. However, 23 cases did not include a Form 8758 or a Master File transcript that correctly identified the credit with the request, and seven cases did not have the IDRS transcript of the XSF supporting that the credit was still available in the XSF.

An accurate, complete, and properly documented Form 8765 with documentation attached identifying the credit helps ensure correct application of XSF credits. Without proper documentation, management does not have evidence to determine if the actions taken on the cases were appropriate.

Reviews of Forms 8765 by the Unidentified/Excess Collection function were not effective

To ensure that requests for transfers to the XSF are accurate, complete, and properly documented, Unidentified/Excess Collection function accounting technicians are required to review submitted Forms 8765 and all supporting documentation, when attached.[18] The accounting technicians are required to reject Forms 8765 that are not compliant with the documentation requirements or without proper completion of all required entries. If a Form 8765 is rejected, it should be immediately sent back to the originator to be corrected. However, none of the 24 documentation error cases we identified were rejected by Unidentified/Excess Collection function accounting technicians, and the credits were transferred out of the XSF. Applying credits from the XSF to the correct taxpayer's account is critical because applying or refunding to the wrong taxpayer may result in erroneous refunds. Additionally, insufficient controls in the XSF could allow IRS employees to inappropriately generate refunds from the XSF.

Manager review and approval is not required for transfers from the XSF

Internal control standards[19] provide that first-line managers are an important control component because they are responsible for the quality of work performed by the employees they supervise. Management review of Form 8765 would help ensure that no credits are transferred from the XSF without a complete and accurate Form 8765 supporting the transfer. However, the IRM does not require managerial review or approval of requests for transfers out of the XSF by Unidentified/Excess Collection function employees. In addition, because there are no data fields specific to transfers out of the XSF, reports detailing specific transfers out are not available for managers to review for accuracy, completeness, and appropriateness. As a result, managers may

[18] IRM 3.17.220.2.11 (08-16-2013).
[19] Government Accountability Office, GAO-14-704G, Standards for Internal Controls in the Federal Government (Sept. 2014).

not be aware when taxpayer credits are transferred out of the XSF. These control weaknesses increase the risk that fraudulent or improper XSF transfers will not be prevented or detected.

Recommendations

The Director, Submission Processing, Wage and Investment Division, should:

Recommendation 4: Request XSF database programming changes that will capture and report data specific to transfers from the XSF. Managers should periodically reconcile the XSF transfer report with Form 8765 requests.

> ***Management's Response:*** Management disagreed with this recommendation. In their response, management stated that the data specific to transfers from the XSF are already captured and reported, and managerial case load reviews are conducted at least quarterly per IRM 3.17.220.1.4, *Excess Collections File, Managerial Reviews*. Management stated that in addition to the case load reviews, IRM 3.17.220.1.4(8) provides instructions for conducting a sample review of the Restricted Apply Register and the Dropped Listing, which includes any received Forms 8765 to ensure that adequate and proper actions are being taken by all employees.
>
> ***Office of Audit Comment:*** The IRM 3.17.220.1.4(8) cited by IRS management refers to an annual report which captures only the credits dropped (*i.e.*, after seven years) from the XSF database. IRM 3.17.220.1.4, which was also cited, applies to employee quality reviews, which would not provide adequate or timely oversight to ensure the proper processing of transfers from the XSF and does not address the need for periodic reconciliation of XSF transfers with Form 8765 requests.
>
> Data specific to transfers out of the IRS are not captured on existing XSF reports. The recommendation addresses this limitation of the XSF database. During the audit, key IRS personnel and data programmers advised us that the only way to identify transfers out of the XSF database is by subtracting the current balance amount from the original balance amount. An extract of the database is required to perform this calculation. The recommended program changes would routinely provide specific information on credits transferred out of the XSF without the need for an extract of the database and separate analysis. This information could then be reconciled with the Forms 8765.

Recommendation 5: Ensure that Unidentified/Excess Collection function employees comply with documentation requirements pertaining to Form 8765, as well as the IRM requirement to reject Forms 8765 that lack sufficient documentation.

> ***Management's Response:*** Management agreed with this recommendation and plans to review and update the IRM to clarify the documentation requirements pertaining to Form 8765 and the requirement to reject Forms 8765 that lack sufficient documentation.

A Servicewide Electronic Research Program alert will be issued to ensure that the current or updated procedures are communicated to applicable employees.

Recommendation 6: Revise the IRM to require management review and approval of all requests to transfer funds out of the XSF. Form 8765 should also be revised to provide a dedicated box/space for managerial approval.

Management's Response: Management agreed with this recommendation and plans to update the IRM to add additional managerial review and approval to transfer funds out of the XSF and will update Form 8765.

Controls Over Integrated Data Retrieval System Command Codes Prevented Unauthorized Access to the Excess Collections File

XSF credits should be established, corrected, and transferred (in/out) only by IRS employees who work in the Unidentified/Excess Collection function, located in the Accounting Control/Services Operations of the following IRS Campus locations:

- Fresno, California
- Kansas City, Missouri
- Cincinnati, Ohio.
- Austin, Texas.
- Ogden, Utah.

Based on the IRS employee's specific role and responsibilities, he or she is granted access to input certain IDRS transactions (command codes). A command code is considered "sensitive" if it can be used to adjust account balances, change the status of a tax module account, or affect the tax liability. IRS employees outside the Unidentified/Excess Collection function should not have access to XSF sensitive command codes. The IRM requires that front-line managers review employees' use of sensitive command codes at least monthly to ensure that no inappropriate actions have been performed.[20] IRS management indicated that when a person leaves the Unidentified/Excess Collection function, any sensitive command codes associated with the XSF should be purged from his or her IDRS profile.

We analyzed an IDRS audit trail of the sensitive XSF command codes and identified 136 employees who worked outside the Unidentified/Excess Collection function and tried to access four sensitive XSF command codes. Eleven of these employees were either revenue officers or revenue agents who tried to access at least one of four XSF sensitive command codes. We did not determine why these employees attempted to access these command codes. However, we determined that the IDRS controls successfully prevented unauthorized access to the XSF by these employees because the command codes were not in their IDRS profile.

[20] IRM 10.8.34.3.1.3 (04-01-2014).

While none have been confirmed as cases of fraud, we found examples of employees repeatedly attempting to access sensitive commands codes that either control the changing of personal information associated with the credit, the application of credits to credit taxpayers' modules, or refunding of money from the XSF. For example, one employee, while attempting to access **1* ********1******XSF credit, used the refund command code **2*** (used to process refunds) 37 times over the course of seven months. The credit entered into the XSF in February 2010 and the employee in question unsuccessfully tried to use this command code:

- 17 different times on May 13, 2010.
- 9 times on May 20, 2010.
- 10 times in September 2010.
- 1 time in December 2010.

Our research ***1*** within the XSF shows **1** balance has remained unchanged as of July 2014. While IDRS controls may have prevented this employee from accessing the XSF, it appears no actions were taken, such as a reprimand or removal of IDRS access, to stop this employee from continuing to use the command code from May to December 2010.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this audit was to determine whether the controls over the Excess Collections File adequately prevent improper transactions and ensure that expired credits are appropriately accounted for and not exposed to fraud or abuse. To accomplish our objective, we:

I. Reviewed IRS policies, procedures, and other guidance for the processing and management of payments and credits transferred from the XSF.

   A. Obtained current IRS policies, procedures, and other guidance governing the XSF process. Specifically, we obtained and reviewed policies and procedures involving the process of purging XSF credits that are more than seven years old, the controls preventing non-Unidentified/Excess Collection function employees from maintaining XSF IDRS command codes in their profiles, and the controls that prevent fraudulent transfers of XSF credits out of the XSF.

   B. Interviewed managers, programmers, analysts, and other personnel responsible for purging and transferring XSF credits out of the XSF. Specifically, we discussed the process of purging XSF credits that are more than seven years old, the controls preventing non-Unidentified/Excess Collection function employees from maintaining XSF IDRS command codes in their profiles, and the controls that prevent fraudulent transfers of XSF credits out of the XSF.

II. Assessed the controls that ensure that XSF credits older than seven years are timely identified and purged from the XSF.

   A. Obtained a complete extract of the XSF database as of July 27, 2014.

   B. Using the XSF extract from Step II.A., identified XSF credits that are older than seven years by comparing the RECVD date with the date of the extract.

   C. Coordinated with the Unidentified/Excess Collection function Subject Matter Expert and programmers to determine why XSF credits were not timely identified and purged from the XSF.

   D. Determined the effectiveness of the management controls over the process of timely purging XSF credits.

   E. Validated the reliability of the data in the extract obtained in Step II.A. by reconciling a random sample of records from the extract to the Master File by using the IDRS and XSF command code and verifying the accuracy of the computer extract. We determined that the data were sufficiently reliable for purposes of this report.

III. Assessed the controls that ensure that XSF credits are appropriately transferred out of the XSF and applied to taxpayers' Master File accounts or directly refunded to the taxpayers.

A. Analyzed the XSF extract obtained in Step II.A. using data mining techniques to identify suspicious/fraudulent transfers out of the XSF to taxpayers' Master File accounts. We focused on such characteristics as: multiple credit transfers to a single Master File account; multiple transfers by one employee of credits close to expiration (seven years); or any other transactions that appeared to be irregular.

B. Identified non-Unidentified/Excess Collection function employees that have the sensitive IDRS command codes used to transfer XSF credits from the XSF in their IDRS profile.

C. Using an IDRS audit trail, identified and analyzed the taxpayer accounts accessed by non-Unidentified/Excess Collection function employees with the XSF command codes for the period January 1, 2010, through July 31, 2014.

D. From the extract obtained in Step II.A., we identified 1,165 transfers out of the XSF. From the 1,165 transfers out of XSF, we selected a judgmental sample[1] of all transfers (31) in which $15,000 or more was transferred from the XSF. We reviewed all pertinent documentation to ensure that employees followed all applicable procedures. The 31 (3 percent) cases represented $4.18 million (79 percent) of the total dollar value of all transfers out.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: documentation requirements pertaining to requests for transfers out of the XSF. To test these controls, we conducted a case review of transfers out of the XSF.

[1] A judgmental sample is a nonprobability sample, the results of which cannot be used to project to the population.

Appendix II

Major Contributors to This Report

Matthew Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Bryce Kisler, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Carl Aley, Director
Timothy Greiner, Audit Manager
Charles S. Nall, Jr., Lead Auditor

Appendix III

Report Distribution List

Commissioner
Office of the Commissioner – Attn: Chief of Staff
Deputy Commissioner for Services and Enforcement
Deputy Commissioner, Wage and Investment Division
Director, Customer Account Services, Wage and Investment Division
Director, Submission Processing, Wage and Investment Division
Director, Office of Audit Coordination

Appendix IV

Outcome Measures

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

Type and Value of Outcome Measure:

Reliability of Information – Potential; 1,741,025 barred statute credits[1] totaling $2,653,978,249 transferred into the XSF over the next five years but not available for use by taxpayers due to barred statutes (see page 4).

Methodology Used to Measure the Reported Benefit:

Using our XSF extract, we identified all barred statute credits in the XSF database. We refined our population of barred statute credits to identify those with an entry date on or between January 1, 2013, and December 31, 2013, to capture a full calendar year of barred statute credits. We determined that 348,205 barred statute credits valued at $530,795,650 entered the XSF in Calendar Year 2013. We forecasted[2] this amount over the next five years, which resulted in 1,741,025 cases, with a value of $2,653,978,249. Taxpayers would have no claim to these funds because the statute has expired.

Type and Value of Outcome Measure:

Reliability of Information – Potential; 2,938,907 barred statute credits valued at $4,701,365,378 transferred into the XSF but are not available for use by taxpayers due to barred statutes (see page 4).

Methodology Used to Measure the Reported Benefit:

Using our XSF extract, we identified all barred statute credits in the XSF database by querying the population for any case that had an unidentified remittance source code identifier of “C” which showed it originated from the statute function. We then queried that population for an unidentified remittance status code of “8” which means the case was in a barred statute status. We determined that there were 2,938,907 barred statute credits valued at $4,701,365,378.

[1] See Appendix V for a glossary of terms.
[2] The five-year forecast is based on multiplying the base year by five and assumes, among other considerations, that economic conditions and tax laws do not change.

Type and Value of Outcome Measure:

Reliability of Information – Potential; 110,569 credits valued at $216,987,710 that have IRS received dates greater than seven years (see page 4).

Methodology Used to Measure the Reported Benefit:

Using our XSF extract, we compared the IRS received date of the XSF credit to the date of the extract (July 27, 2014) and counted back seven years to calculate the population of cases greater than seven years old within our XSF extract. Through this analysis, we determined that there were 2,282,790 credits valued at $3,566,122,683 that were more than seven years old, based on the IRS received date, within the XSF database. To ensure that we did not include credits entered into the XSF due to barred statute and claimed in the prior outcome measure, we eliminated 2,172,221 credits totaling $3,349,134,973 that were barred statute and had an IRS received date older than seven years.

- Number of credits (2,282,790 – 2,172,221 = 110,569).
- Dollar value of credits ($3,566,122,683 -$3,349,134,973 = $216,987,710).

Appendix V

Glossary of Terms

Term	Definition
Account 6800	Excess Collection.
Account 9999	Revenue Clearance Accountability.
Barred Statute	The claim, agreement, or right that cannot be subject of any legal action because it is too late after the date has been exceeded.
Business Unit	A logical element or segment of a company (*e.g.*, accounting, production, marketing) representing a specific business function, and a definite place on the organizational chart, under the domain of a manager. Also called department, division, or a functional area.
Calendar Year	The 12-consecutive-month period ending on December 31.
Campus	The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.
Command Code	A five- or six-character code used to initiate contact with the IDRS.
Credit	An amount paid or transferred as payment to an account.
Entry Date	The computer generated date of an account that has been added to the Unidentified Remittance or Excess Collection File.

Term	Definition
Excess Collection File (XSF)	A file within the IDRS containing nonrevenue receipts which cannot be identified or applied. Each record within the file contains the XSF control number, amount of credit, type of credit, received date, and other identifying information, if known. The XSF reflects contents of Accounts 6800 and 9999 less than seven years and more than one year after the IRS-received date except in true statute cases, where it may be less than one year.
Federal Accounting Standards Advisory Board (FASAB)	An advisory committee that develops accounting standards for U.S. Government agencies. It is designed to improve Government accountability by issuing Federal financial accounting and reporting standards that adhere to industry best practices.
Fiscal Year	Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.
General Ledger	A complete record of financial transactions over the life of an entity. The ledger holds account information that is needed to prepare financial statements, and includes accounts for assets, liabilities, revenues, and expenses.
Generally Accepted Accounting Principles (GAAP)	The common set of accounting principles, standards, and procedures that companies use to compile their financial statements. They are a combination of authoritative standards (set by policy boards) and simply the commonly accepted ways of recording and reporting accounting information.
Integrated Data Retrieval System (IDRS)	The IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.
Internal Revenue Manual (IRM)	The operations manual for employees of the IRS.

Term	Definition
Master File	The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.
Nominal Accounts	Temporary accounts that are closed each year. Examples of nominal accounts include 6800 (Excess Collections), 5647 (Headquarter Expense, American Opportunity Tax Credit), 5891 (Tax Revenue Refunds – Individual), 6111 (Withholding Tax Assessment-Penalty), and 2340 (Photo Copy Fee).
Nonrevenue Receipts	Payments received for items other than taxes, *e.g.*, bulk forms, photocopy fees, court fines, and installment agreement user fees.
Open Credits	A credit that can be applied or refunded after identification. If the status code is left blank, the status on file will be OPEN.
Received Date	The earliest date received by any IRS office or function that can accept tax returns.
Refund	Money returned to the taxpayer as a result of overpayment of a tax liability. Usually not done if the taxpayer has any other outstanding liability against which the overpayment can be credited.
Servicewide Electronic Research Program	A taxpayer support application that provides electronic research capabilities for all IRS users. It supports more than 78,000 users in the IRS and is a 24/7 365 day application.
Statement of Custodial Activity	A statement included with the IRS financial statements that is submitted to the Office of Management and Budget and Congress. A Statement of Custodial Activity reflects collections not recognized as revenue that have been or should be transferred to others. The Statement is required for agencies that collect non-exchange revenue for the General Fund of the Department of the Treasury.

Term	Definition
Statute-expired credits	Represents a wide range of situations which may require detailed analysis to determine whether further action needs to be taken to protect the taxpayer. Assessment-barred cases represent remittances received within the last year with an amended return or increased liability determined as a result of examination which cannot be assessed because the statute of limitations for assessment expired and there is no basis for tolling or extending the statute. Other statute credits in the XSF represent the expiration of the statute of limitations for credit/refund. The tax modules from which these credits are transferred and related documentation require detailed analysis to ensure that the taxpayer has not been damaged and is not entitled to a refund despite the apparent expiration of the statute.
Unidentified Remittance File	A separate file within the IDRS containing all remittances received which cannot be immediately identified or applied.

Appendix VI

Management's Response to the Draft Report

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

COMMISSIONER
WAGE AND INVESTMENT DIVISION

NOV 1 6 2015

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Debra Holland Debra Holland
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Accounting and Controls Need to Be Improved for Excess Collections (Audit # 201430024)

Thank you for the opportunity to review the subject draft report and provide comments on the observations and findings contained therein. It is important to note that all remittances received by the IRS are deposited into Treasury accounts, generally within one to three days of receipt, and that the Excess Collections File (XSF) is an accounting control file used to record amounts that either could not be associated with a taxpayer account, such as when a payment is received with an illegible or missing documentation and/or Social Security Number, or aged account credits that have little or no likelihood of being applied to a tax debt and cannot be refunded to the taxpayer. We agree that steps can be taken to strengthen internal controls that ensure requests for transfers out of the XSF are fully documented and that managerial review and approval occurs at the time of transfer.

Generally, tax payments remitted prior to the filing of the return, such as Estimated Tax Payments or overpayments from the prior tax year that the taxpayer elects to carry over to the next tax period, are deemed as having been received on the due date of the tax return for which the payment is intended. Payments claimed on the tax return, such as credits for income tax withheld from wages or tax withheld from other sources, or other refundable credits, are also deemed to have been received as of the due date of the tax return. Tax returns with extended due dates or late-filed returns will have no effect on the deemed date of receipt for these payments or credits. For example, a return filed for Tax Year 2010, not filed until 2015, would have a deemed receipt date of April 15, 2011, for any withholding credits claimed, as well as any other refundable credits that may be claimed on the return. This is also illustrated in the report by Figure 2: XSF Credits with IRS Received Dates Older Than 7 Years. The table shows credits in the XSF going as far back as the 1960s. Our review found that those oldest credits were withholding amounts that were reported on recently filed delinquent returns. Although the returns

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were filed late, the deemed receipt date of the withholding reflects the original due dates of the returns.

In the report, statements are made to the effect that taxpayers may no longer use credits after the Refund Statute Expiration Date (RSED) has passed. However, the credits remain available for use after the passing of the RSED, to be applied to any tax liability shown on the return or to any additional tax that may be subsequently assessed for that tax period. Additional assessments could be made after the filing of the return due to an audit or by the taxpayer filing an amended return to correct their reported tax liability. Therefore, using our previous example, if the late-filed return had claimed a refund of any overpayment of tax, the IRS would not have been permitted under the law to pay the refund; however, if an additional amount of tax is subsequently assessed, the overpayment that could not be refunded would still be available to be applied against the additional assessment. Generally, the time period in which the IRS can assess additional tax or taxpayers may correct their returns is three years from the due date of the return, or three years after the date the return is filed, whichever is later. In the example, the net amount due from the taxpayer would be reduced even though the additional assessment could potentially be made as late as 2018, seven years or more after the deemed receipt date.

We disagree with the recommendations to change programming to purge credits from the XSF based on the date of receipt, and to use the RSED as the standard for moving credits from the XSF. These recommendations would create unnecessary burden for both taxpayers attempting to resolve their tax obligations and the IRS in effectively administering the tax system and ensuring allowable credits are properly applied before sending notices and demand for payment. Our example provides a very simple overview of a typical situation in which transfers to and from the XSF can come into play. In reality, the process can become much more complex when conditions result in extensions of the time in which the IRS can assess tax or taxpayers can file amended returns. It is crucial that our employees have the ability to research the XSF when required by account activity and, using proper procedures, request transfers back to taxpayer accounts from the XSF.

We also disagree with the recommendation to modify the way in which the XSF balance is treated on the IRS financial statements and within our financial accounting system. The IRS accounts for the XSF under Generally Accepted Accounting Principles and in a manner approved by the Department of the Treasury. We also believe current internal reporting procedures reflecting transfers affecting the XSF are sufficient and do not intend to request programming changes.

We are pleased that the Treasury Inspector General for Tax Administration has recognized that our internal controls over the Integrated Data Retrieval System (IDRS) are working as they were intended. The IDRS contains built-in access controls that require employees have managerial approval to use the system. Further, the Command

Codes available to each employee require the approval of both the front-line manager and an IDRS Security Officer within the Information Technology Cybersecurity function. Although employees have the ability to invoke any command available within the IDRS, if that command has not been approved for their use, the system will not execute their request. All usage is logged and any use of an unapproved command is logged as a system security violation. Managers review the system security reports for their employees weekly, and perform a monthly review of overall usage. As noted in the report, XSF-specific commands are approved for and available only to current XSF employees.

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

Attachment

Attachment

Recommendations

RECOMMENDATION 1
The Commissioner, Wage and Investment Division, should reverse the programming change made in 1998 so the XSF purging criteria counts the number of years the credit should be in the XSF based on the year the payment is received by the IRS.

CORRECTIVE ACTION
We disagree with this recommendation. As illustrated in our management response, the year payment is received by the IRS is not an optimal indicator for determining the purge dates of transactions contained in the Excess Collections File (XSF). The change would be burdensome to both taxpayers and the IRS in that it would impede our ability to effectively administer the tax system and to provide efficient and accurate service to taxpayers.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
N/A

CORRECTIVE ACTION MONITORING PLAN
N/A

RECOMMENDATION 2
The Commissioner, Wage and Investment Division, should utilize the general refund statute of limitations (*i.e.*, the later of two years from the date the tax is paid or three years from the date the return was filed) as the standard for moving credits from the XSF and request programming changes that are consistent with this recommendation. In the interim, purge those credits that are older than seven years based on the IRS received date.

CORRECTIVE ACTION
We disagree with this recommendation for the same reasons stated for the first recommendation.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
N/A

CORRECTIVE ACTION MONITORING PLAN
N/A

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RECOMMENDATION 3
The Chief Financial Officer, in consultation with the Department of Treasury, should develop an accounting treatment that allows the IRS to account for excess collections in such a way that it can provide management information on the balance of the XSF at any given time.

CORRECTIVE ACTION
We disagree with this recommendation. The IRS is accounting for excess collections on a modified cash basis which is in accordance with Generally Accepted Accounting Principles as stated in Federal Accounting Standards Advisory Board Standard 7. The IRS records the receipt of revenue at the time the excess collection would have been processed by the deposit systems. We do not record liabilities in the general ledger. Mechanisms are in place to pull monies out of year-end closing accounts and reestablish the monies on Master File if the excess collections are determined to be applied to a specific taxpayer account. The Treasury Department agrees the accounting and reporting of this item is at the discretion of the IRS.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
N/A

CORRECTIVE ACTION MONITORING PLAN
N/A

Recommendations

The Director, Submission Processing, Wage and Investment Division, should:

RECOMMENDATION 4
Request XSF database programming changes that will capture and report data specific to transfers from the XSF. Managers should periodically reconcile the XSF transfer report with Form 8765 requests.

CORRECTIVE ACTION
We disagree with this recommendation. The data specific to transfers from the XSF are already captured and reported, and managerial case load reviews are conducted at least quarterly per Internal Revenue Manual (IRM) 3.17.220.1.4, *Excess Collections File, Managerial Reviews*. In addition to the case load reviews, IRM 3.17.220.1.4(8) provides instructions for conducting a sample review of the Restricted Apply Register and the Dropped Listing, which includes any received Forms 8765, *IDRS Control File Credit Application*, to ensure that adequate and proper actions are being taken by all employees.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
N/A

CORRECTIVE ACTION MONITORING PLAN
N/A

RECOMMENDATION 5
Ensure that Unidentified/Excess Collection function employees comply with documentation requirements pertaining to Form 8765, as well as the IRM requirement to reject Forms 8765 that lack sufficient documentation.

CORRECTIVE ACTION
We agree with this recommendation. The IRM 3.17.220, *Accounting and Data Control, Excess Collections File,* will be reviewed and updated to clarify the documentation requirements pertaining to Form 8765, and the requirement to reject Forms 8765 that lack sufficient documentation. A Servicewide Electronic Research Program alert will be issued as determined to ensure the current or updated procedures are communicated to Unidentified/Excess Collection Function employees.

IMPLEMENTATION DATE
July 15, 2016

RESPONSIBLE OFFICIAL
Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 6
Revise the IRM to require management review and approval of all requests to transfer funds out of the XSF. Form 8765 should also be revised to provide a dedicated box/space for managerial approval.

CORRECTIVE ACTION
We agree with this recommendation and will update the IRM to add additional managerial review and approval for re-applications out of XSF which would result in a refund, and will update Form 8765.

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IMPLEMENTATION DATE
July 15, 2016

RESPONSIBLE OFFICIAL
Director, Submission Processing, Customer Account Services Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
We will monitor this corrective action as part of our internal management control system.