TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Implementation of the Passport Provisions of the FAST Act Was Generally Successful, and the Internal Revenue Service Is Working on Objective Criteria for Passport Revocations

September 19, 2019

Reference Number: 2019-30-068

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

Redaction Legend:
2 = Law Enforcement Techniques/ Procedures and Guidelines for Law Enforcement Investigations or Prosecutions.

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HIGHLIGHTS

IMPLEMENTATION OF THE PASSPORT PROVISIONS OF THE FAST ACT WAS GENERALLY SUCCESSFUL, AND THE INTERNAL REVENUE SERVICE IS WORKING ON OBJECTIVE CRITERIA FOR PASSPORT REVOCATIONS

Highlights

Final Report issued on September 19, 2019

Highlights of Reference Number: 2019-30-068 to the Commissioner of Internal Revenue.

IMPACT ON TAXPAYERS

The Fixing America's Surface Transportation Act, signed on December 4, 2015, requires the Secretary of the Treasury to transmit certifications of individuals with seriously delinquent tax debt received from the IRS Commissioner to the Secretary of State (State Department) for action with respect to denial, revocation, or limitation of a passport. Taxpayers who are certified by the IRS to the State Department may be unable to obtain a new passport or renew a current passport, or could have their passport revoked.

WHY TIGTA DID THE AUDIT

This audit was initiated to evaluate the IRS's actions taken to implement and administer applicable provisions of Internal Revenue Code Section 7345, pertaining to the revocation or denial of passports in cases of certain unpaid taxes. To certify taxpayers to the State Department, the IRS follows the requirements in the Internal Revenue Code, which provide that seriously delinquent tax debt is an unpaid, legally enforceable, assessed Federal tax liability of an individual, and is greater than the current threshold dollar amount, which is indexed annually for inflation.

WHAT TIGTA FOUND

TIGTA reviewed the population of 306,988 certified taxpayers as of December 20, 2018, and identified 1,814 taxpayers who had reached the collection statute expiration date prior to the date of the notice of certification. The review of a statistical sample of 91 tax modules (88 taxpayers) found that 19 (21.6 percent) of the 88 taxpayers were certified to the State Department even though their aggregate tax liability, without the portion of the tax module(s) with the expired collection statute, was less than the dollar threshold. Based on these results, it is reasonable to estimate that 392 of the 1,814 taxpayers were potentially certified and could have been denied a passport. After October 2018, this problem did not occur because the IRS made a programming change.

TIGTA also reviewed the population of 68,764 decertified taxpayers as of December 20, 2018, and identified four secondary taxpayers who were incorrectly decertified due to the death of the primary taxpayer.

The IRS has developed some general criteria to refer certified taxpayers for potential passport revocation to the State Department. Without objective criteria, such as considering traditional "can't pay," "will pay," "won't pay" factors based on the facts and circumstances of each case, the IRS could be neglecting to refer taxpayers for revocation whose noncompliance is willful in nature. The IRS is working on developing objective criteria to analyze taxpayers with seriously delinquent tax debt for referral to the State Department for potential revocation.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS attempt to identify and decertify those taxpayers prior to the October 2018 programming change who had an aggregate balance under the threshold amount at the time of certification, request a programming change to apply the appropriate deceased taxpayer indicator to the primary or secondary taxpayer, and develop objective criteria to apply as part of the evaluation process when selecting cases to refer to the State Department for revocation.

In response to the report, IRS officials agreed with two recommendations and partially agreed with one recommendation. The IRS plans to take corrective action on all three recommendations.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

September 19, 2019

MEMORANDUM FOR COMMISSIONER OF INTERNAL REVENUE

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Implementation of the Passport Provisions of the FAST Act Was Generally Successful, and the Internal Revenue Service Is Working on Objective Criteria for Passport Revocations (Audit # 201830030)

This report presents the results of our review to evaluate the Internal Revenue Service's actions taken to implement and administer applicable provisions of Internal Revenue Code Section 7345, pertaining to the revocation or denial of passports in cases of certain unpaid taxes. This audit is included in our Fiscal Year 2019 Annual Audit Plan and addresses the major management challenge of Improving Tax Reporting and Payment Compliance.

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).

Table of Contents

Abbreviations

CDP	Collection Due Process
CSED	Collection Statute Expiration Date
FAST Act	Fixing America's Surface Transportation Act
I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service

Background

The Fixing America's Surface Transportation Act (FAST Act), signed on December 4, 2015, requires the Secretary of the Treasury to transmit certifications of individuals with seriously delinquent tax debt received from the Commissioner of the Internal Revenue Service (IRS) to the Secretary of State for action with respect to denial, revocation, or limitation of a passport.[1] The U.S. Department of State (State Department) has the sole authority to take action to deny passport applications for taxpayers certified by the IRS. The FAST Act also allows for the revocation of existing passports and the limitation of travel by the State Department. When the IRS certifies taxpayers to the State Department, the taxpayer will be unable to obtain a new passport or renew an existing passport. The State Department also may revoke an existing U.S. passport of a certified taxpayer.

To certify taxpayers to the State Department, the IRS follows the requirements in Internal Revenue Code (I.R.C.) Section (§) 7345, *revocation or denial of passport in case of certain tax delinquencies*. I.R.C. § 7345 provides that seriously delinquent tax debt is an unpaid, legally enforceable Federal tax liability of an individual which has been assessed and is greater than the current threshold. The threshold is required by I.R.C. § 7345 to be indexed annually for inflation. The indexed amount for Calendar Year 2018 was $51,000 and for Calendar Year 2019 is $52,000. The taxpayer's aggregate balance due from all tax modules must be over the current inflation-adjusted threshold for a tax module to be certified.[2]

To be eligible for certification, the tax liability must also have one of the following conditions present:

- A Notice of Federal Tax Lien must have been filed in accordance with regulations in I.R.C. § 6323 and Collection Due Process (CDP) rights under I.R.C. § 6320 with respect to such filing have been exhausted or lapsed.
- A levy was made following guidelines set forth in I.R.C. § 6331.

CDP rights under I.R.C. § 6320 include the right to a hearing through IRS Appeals wherein the taxpayer can raise various issues with respect to the debt, including collection alternatives. While the taxpayer does have the right to appeal the collection of the debt, there is no right to appeal the certification of the debt to the State Department.

[1] Pub. L. No. 114–94, § 32101, 129 Stat. 1312m 1729-1733 (2015).
[2] See Appendix V for a glossary of terms. There are 29 different notices provided throughout the collection process which include notification of the possibility that a taxpayer's tax debt could affect obtaining a passport.

I.R.C. § 7345 and the FAST Act provide the following exceptions from taxpayers being certified to the State Department as having seriously delinquent tax debt:

- Debt currently being paid in a timely manner as part of an installment agreement.
- Debt paid in a timely manner under an offer in compromise.
- Debt paid in a timely manner as part of a settlement agreement with the Department of Justice.
- Debt on which collection is suspended for either a timely CDP hearing under I.R.C. § 6330, due to a claim for innocent spouse under I.R.C. § 6015, or the taxpayer is currently serving in a combat zone.

The Internal Revenue Manual (IRM) provides additional discretionary exclusions for some tax liabilities from being certified to the State Department. The following are the IRS's discretionary exclusions:

- Debt is currently not collectible due to hardship.
- Debt is a result of identity theft.
- Debt of a taxpayer residing in a disaster zone.
- Debt of a taxpayer in bankruptcy.
- Debt of a deceased taxpayer.
- Debt for which there is a pending offer in compromise.
- Debt for which there is a pending installment agreement.
- Debt for which there is a pending claim and the resulting adjustment is expected to result in no balance.[3]

If the taxpayer's debt meets I.R.C. § 7345 requirements and does not meet any of the statutory exceptions or discretionary exclusions, the taxpayer will be certified to the State Department as having seriously delinquent tax debt.

To certify taxpayers, the IRS prepares a list that is sent weekly to the State Department. As required by the FAST Act, at the same time the list of certified taxpayers is sent to the State Department, the IRS sends the CP508C, *Notice of certification of your seriously delinquent federal tax debt to the State Department*, to the taxpayers identified for certification. The CP508C includes the aggregate balance of the certified tax modules and is sent regular mail to the taxpayer's last known address. The notices are not sent to any powers of attorney on file because I.R.C. § 7345(d) requires that the certification be provided to the taxpayer, and because

[3] IRM 5.1.12.27.4 (Dec. 20, 2017) and IRM 5.19.1.5.19.4 (Dec. 26, 2017).

the CP508C may include information the IRS is not authorized to disclose to the power of attorney.

If the State Department receives an application for a passport from a taxpayer who has been certified by the IRS, it sends the taxpayer a notice and holds the application for 90 calendar days. This is to allow the taxpayer time to make full payment of the tax debt, enter into a satisfactory payment alternative with the IRS, or resolve any erroneous certification issues to avoid their passport application being denied. For taxpayers who resolve their tax debt, the IRS reverses the certification (decertifies) and notifies the State Department. If the applicant has not been decertified by 90 calendar days, the State Department will notify the taxpayer that the passport application or renewal is denied due to the seriously delinquent tax debt not being resolved.

In accordance with I.R.C. § 7345(d), the IRS will generally reverse a certification within 30 calendar days of the tax debt being fully satisfied, becoming legally unenforceable (for example, the collection statute expiration date (CSED) has been reached), or meeting a statutory exception or discretionary exclusion.[4] However, after taxpayers are certified to the State Department, their certification will not be reversed if the amount due falls below the certification amount. All decertifications (reversals of certifications) are included on the weekly list of certified taxpayers sent to the State Department. For example, a taxpayer who was certified to the State Department has three certified tax modules totaling $53,000. A tax module with a balance of $5,000 reaches the CSED and is therefore no longer legally enforceable.[5] The aggregate tax debt is now below the threshold; however, the provisions of I.R.C. § 7345 do not allow decertification until all of the outstanding debt is satisfied or all of the tax modules either become legally unenforceable or otherwise satisfy a statutory exception or discretionary exclusion.

The IRS stated that implementing the passport provisions of the FAST Act was a complex undertaking. No additional funding was provided by Congress for the implementation. The IRS coordinated with many stakeholders both inside and outside of the Federal Government to implement this program and brought the program into production with minor issues.

The review was performed with information obtained from the offices of the Small Business/Self-Employed Division Headquarters located in Lanham, Maryland, during the period of October 2018 through July 2019. 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.

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[4] The IRS generally has 10 years from the date of assessment to collect a delinquent tax. I.R.C. § 6502(a).
[5] This is a hypothetical example.

Results of Review

Some Taxpayers Were Incorrectly Certified or Decertified to the State Department

The IRS began certifying taxpayers with "simple debt" to the State Department in February 2018. The IRS considers simple debt to be tax liabilities that result from filing single, head of household, married filing separately, or married filing jointly status for which the filing status of the primary and secondary filers is consistent from tax year to tax year.[6] We identified the population of taxpayers with simple debt who were identified for certification and/or decertified from January 18, 2018, through October 18, 2018. We found 291,208 certified and 54,455 decertified taxpayers which included 1,044,443 certified and 152,365 decertified tax modules.

The IRS was generally successful in implementing the certifications and decertifications for these taxpayers. Our review of statistically valid samples of certified and decertified taxpayers (150 of each) did not identify any issues.[7] In our reviews, we verified that the certified taxpayers met the certification requirements, including that there were no statutory exceptions or discretionary exclusions that applied at the time of certification. For the decertified taxpayers, we verified that the decertified taxpayers met a statutory exception or discretionary exclusion that caused them to become decertified. However, we did identify some taxpayers who were inconsistently certified or incorrectly decertified to the State Department when we reviewed the entire population of certified and decertified taxpayers.

We reviewed the entire population of taxpayers with simple debt who were identified for certification and/or decertified from January 18, 2018, through December 20, 2018. We identified 306,988 certified and 68,764 decertified taxpayers which included 1,101,865 certified and 275,080 decertified tax modules. We reviewed these tax modules to determine if the IRS satisfied the legal requirements of I.R.C. § 7345 with respect to the certifications, *e.g.*, whether a levy and/or a lien had been issued or filed prior to certification, whether decertification occurred when the CSED was reached, and if any statutory exceptions or discretionary exclusions were recognized when included on the tax module.[8] We identified some taxpayers who were certified

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[6] The IRS considers "complex debt" to be when the aggregate debt consists of varied filing statuses on different tax modules with an outstanding tax liability. The IRS is currently testing the certification of complex debt.

[7] Our samples were selected using a 95 percent confidence interval, 50 percent error rate, and ±5 percent precision factor. See Appendix I for sampling plan details.

[8] The following statutory exceptions and discretionary exclusions were reviewed: deceased taxpayers, bankruptcies, settlement agreements, identity theft, CDP hearing, currently not collectible, installment agreements, innocent spouse, offers in compromise, pending installment agreements, and pending offers in compromise.

to the State Department and potentially denied a passport when the CSED was reached on a tax module(s) in the same processing cycle as the certification notice date. Additionally, we identified some secondary taxpayers who were incorrectly decertified when the primary taxpayer was decertified as deceased.

Some taxpayers were incorrectly certified as having seriously delinquent debt when they had tax modules that reached the CSED

Our population review of certified taxpayers identified 1,756 tax modules of 1,814 taxpayers who were certified as having seriously delinquent tax debt with some tax modules that had reached the CSED prior to the date of the CP508C notice.[9] These taxpayers were sent a CP508C notice informing them of being certified as having seriously delinquent tax debt that included tax modules that had reached the CSED at the same time that the notification was sent.

From the list of 1,756 tax modules covering 1,814 taxpayers, we reviewed a statistically valid sample of 91 tax modules (88 taxpayers) and found that 90 of the tax modules (87 taxpayers) were identified for certification during the same processing cycle in which the CSED transaction code was applied. These 87 taxpayers were sent CP508C notices informing them of their seriously delinquent debt which, in part, consisted of modules that had expired CSEDs.

We then expanded our review to all certified modules associated with the 88 taxpayers to determine if their aggregate debt would have met the certification threshold without the CSED tax module. We identified 19 (21.6 percent) of the 88 taxpayers were certified to the State Department even though their aggregate tax liability without the portion of the CSED tax module(s) was less than the threshold required for certification. Based on these results, it is reasonable to estimate that 392 of the 1,814 taxpayers were certified and could have been denied a passport.[10] As of June 5, 2019, 11 of the 19 taxpayers still had tax modules that were certified.[11]

Taxpayers are first identified for certification at least three weekly computer processing cycles prior to being certified to the State Department as having seriously delinquent tax debt.[12] The processing timing for systemic generation, printing, and mailing of a taxpayer's notice is two weeks. The following timeline is an example of how the CSED situation occurred for five taxpayers we identified. On:

- June 7, 2018, the taxpayers were identified as having seriously delinquent tax debt.

[9] This includes primary and secondary taxpayers; therefore, one tax module may have two taxpayers associated with it.
[10] We selected a random sample of tax modules; therefore, we could not project the results to the population of taxpayers. The stated estimate of 392 taxpayers is reasonable based on 21.6 percent of 1,814 taxpayers.
[11] The eight taxpayers were decertified due to discretionary exclusions (disaster zone and identity theft), full payment of other certified tax modules, or all other tax modules reached their CSED.
[12] The IRS performs a weekly processing cycle of the Master File that runs Thursday to Wednesday.

- June 14, 2018, the transaction coding to generate taxpayer notices and remove the tax liability for CSED tax modules was applied.[13] The taxpayers' cases entered the print processing function work stream for the preparation of the CP508C.
- June 26, 2018, the CSED was reached on one tax module of the taxpayers' total tax modules identified for certification. (If all of a taxpayer's tax modules had reached the CSED at this point, the Information Technology organization would not certify the taxpayer to the State Department.)
- June 29, 2018, the Information Technology organization created the list to send to the State Department and analyzed the taxpayers' accounts to determine if a statutory exception or discretionary exclusion existed on the account subsequent to initial identification.
- July 2, 2018, the certification file was sent to the Commissioner, Small Business/ Self-Employed, for review and approval.
- July 2, 2018, the liability was removed from the taxpayers' CSED tax modules and the CP508C was sent to the taxpayers notifying them of the certification for passport denial.
- July 6, 2018, the certification file was transmitted to the State Department.

IRS management stated that in October 2018, a programming change was made to implement a "threshold check." This check would prevent taxpayers from being certified to the State Department if their aggregate liability had been reduced below the threshold amount in the time between identification and certification to the State Department.

Our review of the certification dates verified that all 19 taxpayers we identified were certified prior to the implementation of the programming change in October 2018. If these taxpayers had been identified for certification after October 2018, they would not have been provided to the State Department for certification. I.R.C. § 7803(a)(3) includes that taxpayers have the right to a fair and just tax system which would include equitable treatment. Because of the change in the criteria for certification, taxpayers with the CSED date in the same cycle prior to the programming change were certified, and therefore treated differently than taxpayers after the change.

The IRS should identify those certified taxpayers who, prior to October 2018, had an aggregate balance below the threshold for certification at the same time the certification letter was sent. Once identified, the IRS should determine which taxpayers have an aggregate balance due on certified tax modules that were under the threshold at the time of certification and decertify them to the State Department.

[13] When the CSED on a tax module is reached, the Transaction Code 608 removes the balance due.

Some secondary taxpayers were incorrectly decertified when the primary taxpayer on the account was deceased

From the population of 68,764 decertified taxpayers, we identified seven secondary taxpayers who were decertified due to the death of the primary taxpayer. Of those seven, three had other statutory exceptions or discretionary exclusions allowing for decertification. For the other four taxpayers, we did not identify any other applicable statutory exceptions or discretionary exclusions. Also, the aggregate assessed balances on the four taxpayers' certified tax modules were still over the current threshold amount.

IRS procedures provide that only the taxpayer identified as deceased should be excluded from certification.[14] However, the Passport Program Manager explained that IRS information technology programming does not distinguish between a primary and secondary taxpayer on the deceased taxpayer indicator. Therefore, when the deceased indicator is added to a primary taxpayer's account, it applies to both the primary and the secondary taxpayers. A programming change is needed to differentiate between the primary and secondary taxpayers for the certification and decertification process. The Passport Program Manager has requested that the Information Technology organization assess the difficulty of changing the programming so the deceased indicator only applies to the appropriate primary or secondary taxpayer.

By not distinguishing between the primary and secondary taxpayers, the IRS is not administering the discretionary exclusion properly, and secondary taxpayers are incorrectly decertified even though they meet the threshold for certification. Therefore, these taxpayers are able to obtain a new passport or renew a current passport when they should be unable to because they have seriously delinquent tax debt.

Despite these two issues we identified, the IRS has existing processes in place to periodically analyze the population of certified and decertified taxpayers. These processes include:

- Passport analysts review new decertifications to determine the accuracy of the actions and elevate any inconsistences to the Information Technology organization for potential programming updates.
- The Passport group analyzes taxpayer accounts when items such as an expedited decertification, a Taxpayer Assistance Order, or a general case inquiry about a passport certification is received to ensure that the certification was correct.[15]
- The Research, Applied Analytics, and Statistics office analyzes the new weekly identified certification cases by performing a scan to ensure that the certifications are correct.

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[14] IRM 5.1.12.27.4 (Dec. 20, 2017).

[15] When a certified taxpayer is eligible for decertification, has a pending application for a U.S. passport, and identifies to the IRS that foreign travel is scheduled within 45 calendar days or less, the IRS may make an expedited decertification request to the State Department. The IRS will fax the expedited decertification request directly to the State Department and contact the State Department by e-mail that an expedited decertification request is pending.

- The IRS and the State Department are finalizing plans to start performing biannual file matches to compare certified taxpayers, which will happen in March and September.

Recommendations

The Director, Headquarters Collection, Small Business/Self-Employed Division, should:

Recommendation 1: Attempt to identify taxpayers who were certified prior to the October 2018 programming change and had an aggregate balance under the threshold amount at the time of certification, and decertify those taxpayers.

> ***Management's Response:*** The IRS agreed with this recommendation. The IRS will determine if it can identify taxpayers who were certified prior to the October 2018 programming change who had an aggregate balance under the threshold amount at the time of certification and, if so, it will decertify those taxpayers who were under the threshold at the time of certification. The IRS will monitor this corrective action as part of its internal management system of controls.

Recommendation 2: Request a programming change to apply the appropriate deceased taxpayer indicator to the primary or secondary taxpayer, and recertify secondary taxpayers who were mistakenly decertified.

> ***Management's Response:*** The IRS agreed with this recommendation. On July 25, 2019, the IRS requested a programming change via Unified Work Request Number 227921 for the Information Technology organization to develop a process to distinguish which taxpayer is deceased for "married filing joint" tax liabilities. The IRS will monitor this corrective action as part of its internal management system of controls.

The Internal Revenue Service Has Not Started Certifications of Complex Debt or Completed a Prioritization Plan for Revocation Referrals

The IRS implemented the process to certify and decertify taxpayers with simple tax debt. The certifications have brought many taxpayers back in payment compliance and have resulted in hundreds of millions in tax revenue. However, the IRS has not yet started certifications of taxpayers with complex debt.

Certifications of taxpayers with simple debt has resulted in hundreds of millions of dollars in tax revenue

The IRS implemented the first phase of certifying individuals with simple debt with a combined tax liability over the dollar threshold to the State Department for potential passport denial as required under I.R.C. § 7345.

According to the Passport Program Office, as of May 17, 2019:

- 388,701 taxpayers have been certified as having seriously delinquent tax debt.[16] Since these certifications, $961 million has been credited to taxpayer accounts and, of this amount, $550.7 million is the result of full paid balances.[17] As of this date, there are still 264,306 currently certified taxpayers who owe $49.4 billion in tax liabilities.
- 99,867 taxpayers have been decertified. Of those decertifications, 40,062 (40 percent) are due to taxpayers either becoming or working towards being tax compliant. These are taxpayers who fully paid; entered into an installment agreement; had an accepted offer in compromise; or have a pending installment agreement, full pay adjustment, or offer in compromise. Figure 1 provides a breakdown of the reasons for decertifications.

Figure 1: Reasons for Decertifications As of May 17, 2019

Decertification Reason	Number of Taxpayers	Percentage of Decertifications
Pending Installment Agreement	18,516	19%
Installment Agreement	8,596	9%
Full Paid	6,815	7%
Pending Offer in Compromise	5,887	6%
Pending Full Pay Adjustment	224	<1%
Accepted Offer in Compromise	24	<1%
Total of Compliant Taxpayers	**40,062**	**40%**
Disaster Zone	27,137	27%
CSED Expiration	11,507	12%
Currently Not Collectible Hardship	8,716	9%
Bankruptcy	3,597	4%
Deceased taxpayer	2,696	3%
CDP Hearing	2,262	2%
Identity Theft	1,663	2%
Threshold[18]	1,045	1%
Manual Block/Other	472	<1%
Innocent Spouse	438	<1%
Erroneous Decertification	244	<1%
Combat Zone	28	<1%
Total of Noncompliant Taxpayers	**59,805**	**60%**
Total of All Decertifications	**99,867**	**100%**

Source: Passport Program Office.

[16] The total number of certified taxpayers includes instances of repeat certifications. Taxpayers may be certified, decertified, and then recertified. Taxpayers may be certified for one tax year and later certified for an additional tax year.
[17] The amount collected to date exceeds the Joint Committee on Taxation's estimate of $395 million through 2025.
[18] Accounts that met the aggregate debt threshold when identified for certification; however, the aggregate debt fell below the threshold prior to certification to the State Department.

The remaining 60 percent (59,805 of 99,867) of taxpayers were decertified due to I.R.C. § 7345 exceptions or IRS discretionary exclusions; the top three being taxpayers in disaster zones, liabilities reaching the CSED, and taxpayers in currently not collectible hardship situations.

Taxpayers with complex debt are still being tested

As of May 10, 2019, the second phase of implementing I.R.C. § 7345 is being tested and will involve certifying taxpayers with complex debt. The IRS considers complex debt to be when the aggregate debt consists of varied filing statuses on different tax modules with an outstanding tax liability. For example:

- In Calendar Year 2016, Taxpayer A files a Form 1040, *U.S. Individual Income Tax Return*, with a single filing status for Tax Year 2015, with an unpaid balance of $25,000. Taxpayer A marries Taxpayer B.
- In Calendar Year 2017, Taxpayer A files a Form 1040 with a married filing jointly filing status with Taxpayer B for Tax Year 2016, with an unpaid balance of $25,000. Taxpayer A and Taxpayer B divorce and Taxpayer A marries Taxpayer C.
- In Calendar Year 2018, Taxpayer A files a Form 1040 with a married filing jointly filing status with Taxpayer C for Tax Year 2017, with an unpaid balance of $40,000.

In this example, Taxpayer A would be considered as having seriously delinquent debt because the balance is more than $52,000 (threshold for Calendar Year 2019) but would not be certified until the IRS begins certifying complex debt. Taxpayers B and C will not be certified because neither of their balances exceeds the $52,000 threshold.[19]

As of March 22, 2019, the IRS estimated that 69,460 taxpayers had complex debt that meets the requirements for certification. The IRS has developed programming to identify these taxpayers, and it is in the process of testing the programming to begin certifications of taxpayers with complex debt. The IRS expects to begin sending these taxpayers to the State Department for certification, using a phased approach, by September 2019.

Objective criteria is needed for the development of a prioritization plan for revocation referrals

The FAST Act provides that the State Department "may" revoke the existing U.S. passport of a taxpayer who has been certified as having seriously delinquent tax debt.[20] Under the FAST Act, the IRS's role in the process is to provide certifications of taxpayers with seriously delinquent debt to the Secretary of State who then may revoke passports belonging to those taxpayers. *2*
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[19] This is a hypothetical example.
[20] Pub. L. No. 114-94, § 32101(e)(2)(A), 129 Stat. 1312, 1732 (2015).

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********2*********. The IRS is working on developing objective criteria to analyze taxpayers with seriously delinquent tax debt for referral to the State Department for potential revocation.

There is no law or regulation that directly authorizes the IRS to prioritize taxpayers to be referred to the State Department for revocation; however, we believe it is reasonable for the IRS to provide the State Department with taxpayers for possible revocation to comply with the law. IRS management is working on criteria for revocation referrals which they plan to publish in the IRM when it is finalized. The initial criteria included that the IRS will consider referring taxpayers to the State Department for a revocation decision for the following reasons:

- To protect the integrity of the legislation, *e.g.*, such as when a taxpayer obtains a decertification based on a promise to pay and failed to act as agreed.
- If revocation is needed to encourage payment of the tax by incentivizing taxpayers with offshore activities or interests to resolve their liabilities.
- In other instances in which the facts and circumstances indicate that revocation would facilitate payment of tax.

This IRS's initial revocation criteria is general in nature. The criteria did not contain specific examples of when or how each of these three criteria would apply, nor does it provide a reasonable prioritization plan for the different types of criteria. When we asked the IRS for examples of which taxpayers the IRS would send to the State Department to have their passport revoked, IRS management indicated they would first prioritize those taxpayers with seriously delinquent tax debt who ****************2*******************************
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*************************************2******* The initial criteria also provides that the IRS will consider the taxpayer's history of compliance and level of taxpayer contact and cooperation. In addition, the taxpayer would have to be systemically recertified before being considered for referral to the State Department for revocation. ***********2**************
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Without a reasonable prioritization plan with objective criteria, such as taking into consideration the factors which the IRS traditionally uses to prioritize enforcement action (including whether the taxpayer appears to fall into any of these categories: "can't pay," "will pay," "won't pay"), the IRS could be neglecting to refer taxpayers for revocation whose noncompliance is willful in

nature. ******************************2*************************************
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****2**** After discussions with IRS management, the IRS has agreed to continue working on objective revocation criteria.

As of June 12, 2019, the IRS has processed 1,098 expedited decertifications and identified that 728 of these accounts were either decertified because they entered into an installment agreement or had a pending installment agreement. *****2*************************************
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Recommendation

Recommendation 3: The Commissioner, Small Business/Self-Employed Division, should continue developing objective criteria based on the IRS's traditional approach to enforcement which takes into consideration an individual taxpayer's facts and circumstances when selecting cases to refer to the State Department for passport revocation.

> ***Management's Response:*** The IRS partially agreed with this recommendation. The IRS will develop objective criteria to apply as part of an evaluation of an individual taxpayer's facts and circumstances when selecting cases to refer to the State Department for passport revocation. However, it does not view making a referral to the State Department for passport revocation as being analogous to a traditional enforcement action. The IRS plans to consider the utility of the "will pay" and "won't pay" framework as it refines the selection process, but it is possible that those factors may not control the criteria in the end. The IRS will monitor this corrective action as part of its internal management system of controls.
>
> ***Office of Audit Comment:*** While the IRS only partially agreed with the recommendation, it agreed to develop objective criteria to apply as part of an evaluation

[21] ***2**
2*******************************

of an individual taxpayer's facts and circumstances when selecting cases to refer to the State Department for passport revocation and will consider the utility of the "can't pay," "will pay," and "won't pay" framework as it refines the selection process, which meets the intent of our recommendation.

Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to evaluate the IRS's actions taken to implement and administer applicable provisions of I.R.C. Section (§) 7345, pertaining to the revocation or denial of passports in cases of certain unpaid taxes. To accomplish our objective, we:

I. Identified current IRS policy, procedures, guidelines, and guidance used by Small Business/Self-Employed Division employees during the audit period and determined the coordination between the IRS and the U.S. Department of State (State Department) for achieving compliance with I.R.C. § 7345.

II. Evaluated the IRS's implementation of the Passport Program to include certification, decertification, and potential revocation of taxpayers to the State Department.

   A. Obtained the total number of taxpayers who are currently certified to the State Department as having significantly delinquent tax debt using a data extract of the Individual Master File performed by the Treasury Inspector General for Tax Administration's Strategic Data Services Division.

   B. Identified the population of taxpayers with simple debt who were certified and decertified from January 18, 2018, through October 18, 2018. We found 291,208 certified and 54,455 decertified taxpayers which included 1,044,443 certified and 152,365 decertified tax modules.[1]

      1. Selected a statistical sample of 400 taxpayers who were certified. We reviewed the first 150 taxpayers in the sample using the IRS Integrated Data Retrieval System to determine if the certifications were valid and complied with all pertinent I.R.C. and IRM sections.[2] We found no exceptions and concluded the review at 150 taxpayers. We selected a statistical sample so that we could project our results to the population. Our contracted statistician reviewed and assisted in developing the sampling plans.

         Population – 291,208 taxpayers
         Sample Size – 400 taxpayers
         Confidence Level – 95 percent

[1] See Appendix V for a glossary of terms.
[2] The Integrated Data Retrieval System is an IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.

Expected Error Rate – 50 percent
Precision Factor – ± 5 percent

2. Selected a statistical sample of 400 taxpayers who were decertified. We reviewed the first 150 taxpayers in the sample using the IRS Integrated Data Retrieval System to determine if the decertifications were valid and complied with all pertinent I.R.C. and IRM sections. We found no exceptions and concluded the review at 150 taxpayers. We selected a statistical sample so that we could project our results to the population. Our contracted statistician reviewed and assisted in developing the sampling plans.

   Population – 54,455 taxpayers
   Sample Size – 400 taxpayers
   Confidence Level – 95 percent
   Expected Error Rate – 50 percent
   Precision Factor – ± 5 percent

C. Obtained the entire population of taxpayers with simple debt who were certified and decertified from January 18, 2018, through December 20, 2018, using the Treasury Inspector General for Tax Administration's Data Center Warehouse. Using statistical software, we analyzed the population for trends. We reviewed identified trends using the IRS Integrated Data Retrieval System to determine if the certifications were valid and complied with certain pertinent I.R.C. and IRM sections. We identified 306,988 certified and 68,764 decertified taxpayers, which included 1,101,865 certified and 275,080 decertified tax modules.

1. From the population of certified taxpayers, identified 1,756 tax modules of 1,814 taxpayers that had reached the CSED and were identified for certification as having seriously delinquent tax debt in the same processing cycle.[3] Because we selected a random sample of tax modules instead of taxpayers, we could not project the results to the population of taxpayers. Our contracted statistician reviewed the estimate of taxpayers in the population and verified that the estimate of 392 of the 1,814 taxpayers (for the population of 1,756 tax modules) was reasonable (1,814 taxpayers times the 21.6 percent error rate is 392 taxpayers).

   Population – 1,756 tax modules
   Sample Size – 91 tax modules
   Confidence Level – 95 percent
   Expected Error Rate – 50 percent
   Precision Factor – ± 5 percent

[3] This includes primary and secondary taxpayers; therefore, one tax module may have two taxpayers associated with it.

2. From the population of decertified taxpayers, identified and reviewed seven secondary taxpayers who were decertified due to the death of the primary taxpayer.

D. Evaluated the progress of certification for taxpayers with complex debt and the revocation portion of the program.

Data reliability methodology

During this review, we assessed the reliability of the data we received from the Treasury Inspector General for Tax Administration's Strategic Data Services Division and Data Center Warehouse for reasonableness by performing validity tests and tracing a judgmental sample of cases to the IRS Integrated Data Retrieval System. The validity tests supported that the data were sufficiently reliable and could be used to meet the objective of this audit.

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: the Small Business/ Self-Employed Division Collection function's policies, procedures, and practices related to I.R.C. § 7345. We evaluated these controls by reviewing appropriate internal procedures and guidelines.

Appendix II

Major Contributors to This Report

Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Phyllis Heald London, Director
Beverly K. Tamanaha, Audit Manager
Eugenia Smoak, Lead Auditor

Appendix III

Report Distribution List

Deputy Commissioner for Services and Enforcement
Director, Collection, Small Business/Self-Employed Division
Director, Collection Policy, Small Business/Self-Employed Division
Director, Headquarters Collection, Small Business/Self-Employed Division
Director, Enterprise Audit Management

Appendix IV

Outcome Measure

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

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 19 taxpayers (see page 4).

Methodology Used to Measure the Reported Benefit:

We reviewed the entire population of taxpayers with simple debt who were identified for certification (306,988 taxpayers that included 1,101,865 tax modules) from January 18, 2018, through December 20, 2018, and identified 1,756 tax modules (1,814 taxpayers) with seriously delinquent tax debt in which the CSED transaction code was applied during the same processing cycle as the identification for certification.[1] These taxpayers were sent a CP508C notice informing them of being certified as having seriously delinquent tax debt. From the 1,756 tax modules, we reviewed a random sample of 91 tax modules (88 taxpayers) and found that 90 of the tax modules (87 taxpayers) were identified for certification during the same processing cycle that the CSED transaction code was applied. These 87 taxpayers were sent notices concerning modules that had expired CSEDs. We then expanded our review to all certified modules associated with the 88 taxpayers to determine if their aggregate debt would have met the certification threshold without the CSED tax module. We identified 19 of the 88 taxpayers were certified to the State Department even though their aggregate tax liability without the portion of the CSED tax module(s) was less than the dollar threshold; therefore, a violation of these taxpayers' rights.[2]

[1] See Appendix V for a glossary of terms.
[2] We did not project the 19 taxpayers to the population because we sampled by tax module, not by taxpayer.

Appendix V

Glossary of Terms

Term	Definition
Collection Statute Expiration Date	Each tax assessment has a CSED. I.R.C. Section 6502 provides that the length of the period for collection after assessment of a tax liability is 10 calendar years. The CSED ends the Government's right to pursue collection of a liability.
Installment Agreement	The IRS allows taxpayers who are unable to pay their tax debt immediately to make periodic payments over time.
Levy	A method the IRS uses to collect outstanding taxes from sources such as bank accounts and wages or a legal seizure of property to satisfy a tax debt.
Lien	An encumbrance on property or rights to property as security for outstanding taxes.
Offer in Compromise	An agreement between a taxpayer and the Government that settles a tax liability for payment of less than the full amount owed.
Tax Module	Refers to each tax return filed by the taxpayer for a specific period (year or quarter) during a calendar year for each type of tax.
Taxpayer Assistance Order	The I.R.C. authorizes the National Taxpayer Advocate to issue an order when a taxpayer is suffering or will suffer a significant hardship as a result of the manner in which the internal revenue laws are being administered.

Appendix VI

Management's Response to the Draft Report

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

COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

August 27, 2019

MEMORANDUM FOR MICHAEL E. McKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Mary Beth Murphy Mary Beth Murphy
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – Implementation of the Passport Provisions of the FAST Act was Generally Successful, and the Internal Revenue Service is Working on Objective Criteria for Revocations (Audit # 201830030)

Thank you for the opportunity to review the subject draft report. We appreciate your recognition that we successfully implemented this legislation and brought the program into production with minimal issues.

The Fixing America's Surface Transportation (FAST) Act requires transmission of certifications of individuals with seriously delinquent tax debt to the Secretary of State for action with respect to denial, revocation, or limitation of a passport. Implementing the passport provisions of the FAST Act required extensive IRS systems programming and coordination among many IRS Business Units, as well as collaboration with the U.S. Department of State. We also worked to inform taxpayers of these provisions by including explanations of the passport program in 27 taxpayer notices and publications, and by issuing press releases to ensure public awareness of the program.

While implementing the program, we were careful to include controls to ensure the accuracy of the certifications, to establish processes to expedite decertifications to assist taxpayers with an imminent need for a passport, and to ensure the protection of taxpayer data. The FAST Act excludes cases with certain characteristics, for example, cases in an approved installment agreement or offer in compromise status. The IRS also established additional discretionary exclusions to protect taxpayers. For instance, taxpayers are excluded from certification if their debt has been determined to be currently not collectible due to hardship, or the debt is the result of identity theft.

We plan to begin referring cases to the U.S Department of State for passport revocation soon. However, we do not plan to refer every taxpayer with seriously delinquent tax debt for passport revocation. Therefore, we agree with you that it is important to have objective criteria to apply as part of an evaluation of an individual taxpayer's facts and circumstances when determining which cases to refer. The report also recommends that the referral criteria should be based on the IRS' traditional approach to enforcement. However, we do not view making a referral to State for passport revocation as being analogous to a traditional enforcement action. We plan to consider the utility of the "will pay" "won't pay" framework as we refine the selection process, but it is possible that those factors may not control the criteria in the end. We agree with your other recommendations and with the outcome measures.

Attached is a detailed response outlining our corrective actions to address the recommendations. If you have any questions, please contact me or Paul Mamo, Director, Collection Operations, Small Business/Self Employed Division.

Attachment

Attachment

RECOMMENDATION 1:
The Director, Headquarters Collection, Small Business/Self-Employed Division, should attempt to identify taxpayers who were certified prior to the October 2018 programming change who had an aggregate balance under the threshold amount at the time of certification, and decertify those taxpayers.

CORRECTIVE ACTION:
We agree with this recommendation. We will determine if we can identify taxpayers who were certified prior to the October 2018 programming change who had an aggregate balance under the threshold amount at the time of certification and, if so, we will decertify those taxpayers who were under the threshold at the time of certification.

IMPLEMENTATION DATE:
September 15, 2020

RESPONSIBLE OFFICIAL:
Director, Collection Policy, Small Business/Self-Employed Division (SB/SE)

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 2:
The Director, Headquarters Collection, Small Business/Self-Employed Division, should request a programming change to apply the appropriate deceased taxpayer indicator to the primary or secondary taxpayer, and recertify secondary taxpayers who were mistakenly decertified.

CORRECTIVE ACTION:
We agree with this recommendation. On July 25, 2019, we requested a programming change via UWR #227921 for Information Technology to develop a process to distinguish which taxpayer is deceased for “married filing joint” tax liabilities.

IMPLEMENTATION DATE:
Implemented.

RESPONSIBLE OFFICIAL:
Director, Collection Policy, Small Business/Self-Employed Division (SB/SE)

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 3:
The Commissioner, Small Business/Self-Employed Division, should continue developing objective criteria based on the IRS's traditional approach to enforcement which takes into consideration individual taxpayer's facts and circumstances when selecting cases to refer to the State Department for passport revocation.

CORRECTIVE ACTION:
We partially agree with this recommendation. We will develop objective criteria to apply as part of an evaluation of an individual taxpayer's facts and circumstances when selecting cases to refer to the State Department for passport revocation. However, we do not view making a referral to State for passport revocation as being analogous to a traditional enforcement action. We plan to consider the utility of the "will pay" "won't pay" framework as we refine the selection process, but it is possible that those factors may not control the criteria in the end.

IMPLEMENTATION DATE:
March 31, 2020

RESPONSIBLE OFFICIAL:
Director, Collection Policy, Small Business/Self-Employed Division (SB/SE)

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.