TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Bankruptcy Procedures Designed to Protect Taxpayer Rights and the Government's Interest Were Not Always Followed

March 6, 2014

Reference Number: 2014-30-013

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:
1 = Tax Return/Return Information

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BANKRUPTCY PROCEDURES DESIGNED TO PROTECT TAXPAYER RIGHTS AND THE GOVERNMENT'S INTEREST WERE NOT ALWAYS FOLLOWED

Highlights

Final Report issued on March 6, 2014

Highlights of Reference Number: 2014-30-013 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

The bankruptcy automatic stay provision prohibits the IRS from taking certain collection actions against a debtor (taxpayer) as soon as it learns, or is notified by a U.S. bankruptcy court, that a bankruptcy petition has been filed. Similarly, the debtor may be granted a discharge, which remains after the case is closed and is a permanent injunction order prohibiting the IRS from taking any form of collection action against the debtor personally with respect to discharged debts. If the IRS does not observe the automatic stay or the discharge injunction, taxpayers' rights could potentially be violated and the IRS could be sued for damages.

WHY TIGTA DID THE AUDIT

In Fiscal Year 2012, IRS data showed that the Field Insolvency function received 306,920 bankruptcy cases on taxpayers owing approximately $2.5 billion in taxes, penalties, and interest. This audit was initiated to determine whether the function has effective controls and procedures in place to take appropriate and timely actions to protect the Government's interest and taxpayers' rights during bankruptcy proceedings.

WHAT TIGTA FOUND

Field Insolvency function specialists frequently did not follow required procedures when working bankruptcy cases. Although TIGTA did not identify any violations of taxpayers' rights and/or failure to protect the Government's interest during this review, there is a higher risk that this could occur when procedures are not followed.

TIGTA's review of three random samples of closed bankruptcy cases showed that specialists did not always follow established procedures in 17 (57 percent) of 30 Chapter 7 cases, 15 (50 percent) of 30 Chapter 11 cases, and 13 (43 percent) of 30 Chapter 13 cases reviewed. Specifically, specialists did not always timely or properly conduct the initial case analysis, follow up on scheduled case actions within a reasonable time, or timely or properly close cases.

TIGTA also reviewed a random sample of 30 bankruptcy cases with Automated Proof of Claim flag conditions (errors that need to be resolved by a specialist). Specialists did not timely or properly resolve the flag conditions in 12 (40 percent) of 30 cases.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Director, Field Collection, Small Business/Self-Employed Division: 1) enhance casework priorities and efficiencies; 2) ensure that specialists are properly conducting the initial analysis and closing actions; 3) ensure that the Automated Insolvency System follow-up tool is the preferred method for creating follow-ups; 4) ensure that case actions are properly documented for Automated Proof of Claim flag conditions; and 5) ensure that the Flagged Cases Report is the preferred method for monitoring cases.

In their response to the report, IRS officials agreed with all of our recommendations and plan to take corrective actions.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 6, 2014

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION

FROM: Michael E. McKenney
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Bankruptcy Procedures Designed to Protect Taxpayer Rights and the Government's Interest Were Not Always Followed (Audit # 201230013)

This report presents the results of our review to determine whether the Field Insolvency function has effective controls and procedures in place to take appropriate and timely actions to protect the Government's interest and taxpayers' rights during bankruptcy[1] proceedings. This audit was included in our Fiscal Year 2013 Annual Audit plan and addresses the major management challenge of Tax Compliance Initiatives.

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 Nancy Nakamura, Assistant Inspector General for Audit (Compliance and Enforcement Operations).

[1] See Appendix V for a glossary of terms.

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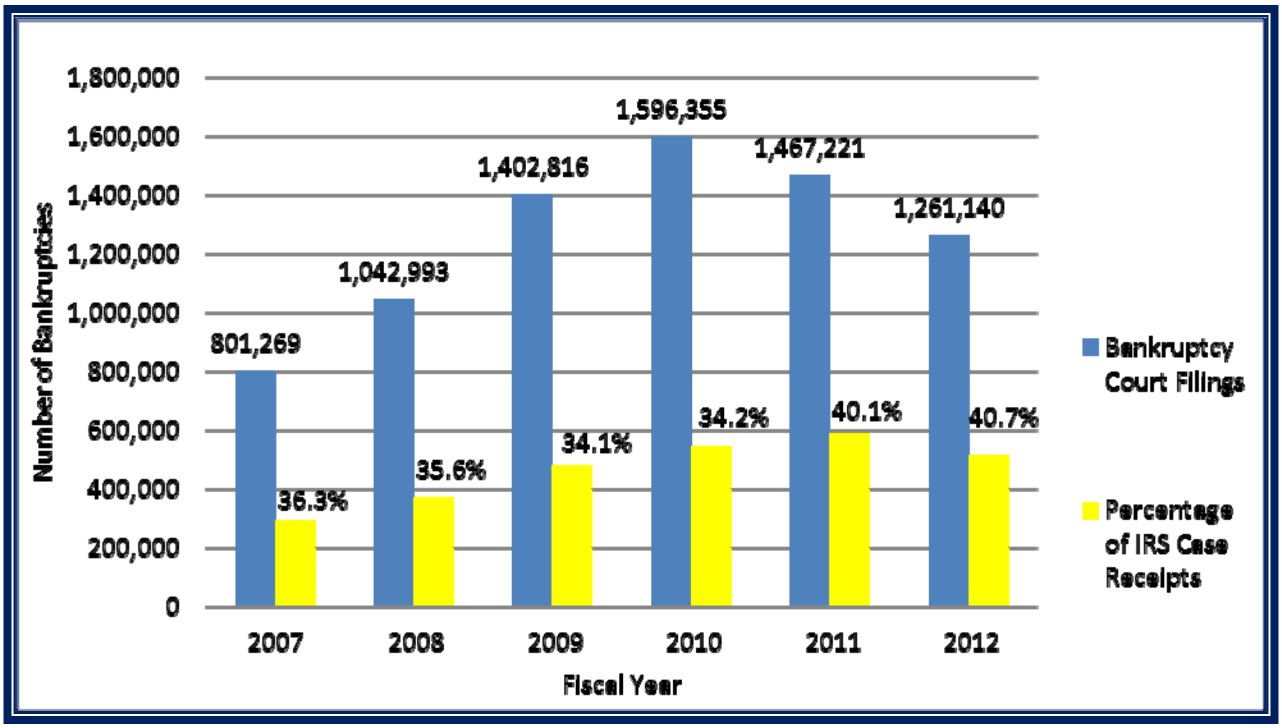
Abbreviations

AIS	Automated Insolvency System
APOC	Automated Proof of Claim
EQRS	Embedded Quality Review System
FMC	First Meeting of Creditors
IRS	Internal Revenue Service
NFTL	Notice of Federal Tax Lien
TIGTA	Treasury Inspector General for Tax Administration

Background

During Fiscal Year[1] 2012, approximately 1.26 million individuals and businesses filed for bankruptcy. Although the Internal Revenue Service (IRS) was not a creditor to each of them, a significant number of these debtors (taxpayers) have outstanding tax liabilities. As such, it is important for the IRS to timely and accurately work bankruptcy cases to ensure that both the Government's interest and taxpayers' rights are protected. Figure 1 shows the number of annual bankruptcy court filings and the percentage of filings that resulted in an IRS case receipt.[2]

Figure 1: Number of Bankruptcy Court Filings and Percentage of IRS Case Receipts



Source: U.S. Courts website (www.uscourts.gov) and IRS Collection Activity Reports 5000-23.

[1] See Appendix V for a glossary of terms.
[2] IRS case receipts do not necessarily have outstanding tax debts, but the IRS has to work the case to make that determination.

This graph shows that IRS receipts compared to court filings increased from an average of 35 percent for Fiscal Years 2007 through 2010 to an average of 40 percent for Fiscal Years 2011 through 2012, indicating that more taxpayers filing bankruptcies also owe Federal taxes.

The Collection Insolvency function, a part of the Small Business/Self-Employed Division Collection function, is responsible for administering the coordination between the U.S. bankruptcy courts and the IRS. In October 2005, the IRS redesigned the Collection Insolvency function to improve operations and ensure the equitable treatment of taxpayers in bankruptcy. The redesign included centralization, standardization, and process improvement. Selected processing activities performed at Field Insolvency function locations throughout the country were consolidated at the IRS Philadelphia Campus' Centralized Insolvency Operation function. The more complex and location-specific work is still performed by the Field Insolvency function, which currently consists of 55 groups of bankruptcy specialists (hereafter referred to as specialists) located throughout the country.

The IRS generally receives bankruptcy notifications electronically from the U.S. bankruptcy courts. In addition, some notifications are sent directly by the court to the IRS through paper copies of petitions or other documents or from taxpayers or attorneys after they contact the IRS. Revenue officers or other IRS personnel may also notify the Centralized Insolvency Operation function or Field Insolvency function employees of a known bankruptcy that is related to an open case.

The moment a taxpayer files a petition with the court, an automatic stay provides immediate relief from all demands for payment and stops lawsuits, foreclosures, garnishments, and collection activity against the taxpayer. In addition, it allows individuals and businesses to seek relief by resolving debts through liquidation, a plan of reorganization, or a payment plan. The automatic stay prohibits the IRS from taking certain collection actions against the taxpayer as soon as it learns, or is notified by the court, that a bankruptcy petition has been filed. Similarly, the debtor may be granted a discharge, which remains after the case is closed and is a permanent injunction order prohibiting the IRS from taking any form of collection action against the debtor personally with respect to discharged debts. If the IRS fails to observe the automatic stay or the discharge injunction, the taxpayer's rights could potentially be violated and the IRS could be sued for damages. In addition, to receive its share in any distribution of funds from a taxpayer's bankruptcy estate, the IRS must generally file a proof of claim with the court.

Figure 2 lists the six basic types of bankruptcy filings which are provided for under the Bankruptcy Code. The type of bankruptcy filing generally depends on the individual's financial situation.

Figure 2: Types of Bankruptcy Filings

- Chapter 7 – Liquidation.
- Chapter 9 – Adjustment of Debts of a Municipality.
- Chapter 11 – Reorganization.
- Chapter 12 – Adjustment of Debts of a Family Farmer or Fisherman With Regular Annual Income.
- Chapter 13 – Adjustment of Debts of an Individual With Regular Income.
- Chapter 15 – Ancillary and Other Cross-Border Cases.

Source: Internal Revenue Manual 5.9.2.3(2), 03-01-2006.

Federal tax debts may or may not be dischargeable in a bankruptcy. For example, taxes resulting from income may be dischargeable, but taxes resulting from failure to remit payroll taxes are not dischargeable.[3] Also, even though receipt of tax revenue can be delayed when a taxpayer files for bankruptcy, the IRS may eventually receive payments through the bankruptcy.

The Centralized Insolvency Operation function performs most clerical duties for all types of bankruptcy cases, including loading cases on the Automated Insolvency System (AIS). Once loaded, e-mail notifications are systemically generated to alert Field Insolvency function specialists of newly assigned cases to work. The Centralized Insolvency Operation function also works Chapter 7 No Asset[4] cases, monitors Chapter 13 cases after plan confirmation, and processes Chapter 13 trustee payments.

The Field Insolvency function generally works Chapter 13 cases until confirmation. In Chapter 11 cases, specialists review, monitor, process payments, and take closing actions. The specialists also work all Chapter 7 Asset[5] cases; review schedules and plans for Chapter 11, 12, and 13 cases; make referrals to IRS Chief Counsel and the U.S. Attorney's office, as applicable, for all types of bankruptcy filings; appear in court as expert witnesses; attend meetings with creditors; participate in outreach efforts; and negotiate with taxpayers or their representatives. Specialists are required to document the case history with sufficient detail to record actions and decisions taken on cases.

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[3] See Appendix IV for more details on dischargeable tax debts.

[4] A Chapter 7 No Asset case is a case in which no equity in the debtor's assets is available to pay unsecured creditors because all of the debtor's assets are exempt, excluded, fully encumbered by secured liens, or have little value.

[5] A Chapter 7 Asset case is a case in which a debtor has assets that are nonexempt and available for use in paying creditors' claims.

The major duties and actions taken by specialists include:[6]

- **Filing a Proof of Claim**. The proof of claim (hereafter referred to as a claim) is the primary method in which the IRS receives funds in a bankruptcy proceeding and is needed to protect the Government's interest. Claims are electronically generated through the Automated Proof of Claim (APOC) system. When the APOC system encounters a condition that cannot be resolved, it creates a flag condition (hereafter referred to as an APOC flag condition) that specialists must timely and accurately resolve so the claim can be filed. If flags with potential stay violations are not worked timely, taxpayers' rights could be violated. In addition, the IRS generally has 180 calendar days from the bankruptcy petition date in which to file a claim. This 180-calendar-day deadline is commonly referred to as the bar date. Timely and accurately prepared claims allow the IRS to receive its share in any distribution of funds from a taxpayer's bankruptcy estate.

- **Conducting Initial Case Analysis**. Specialists must timely and appropriately conduct an initial case review after the case is assigned. This is important to allow sufficient time to identify and resolve case issues such as attending the first meeting of creditors (FMC), questioning the taxpayer, and evaluating payment plan potential.

- **Monitoring for Filing and Payment Compliance**. Specialists must monitor bankruptcy cases to ensure that taxpayers are compliant with filing current and post-petition tax returns and making Federal tax deposits, if required.

- **Initiating Closing Actions**. Specialists must timely and appropriately initiate closing actions. There are five common methods to close a bankruptcy case: 1) dismissal;[7] 2) denial of discharge; 3) discharge;[8] 4) full paid; and 5) no liability. Timely and proper closing actions help to ensure that the Government's interest is protected by allowing collection activity to resume on tax debts as appropriate, without violating the automatic stay or the discharge injunction. Timely refunds help prevent taxpayer burden and protect taxpayers' rights.

In working a bankruptcy case, specialists apply various bankruptcy procedures under which bankruptcy proceedings are commenced, administered, and closed. While the Bankruptcy Code and the Federal Rules of Bankruptcy Procedure are consistent throughout the Nation, specialists also need to follow local bankruptcy rules, standing orders, and procedures which vary from court to court. These local procedures are interpretations and modifications of the Bankruptcy Code to meet the requirements in particular jurisdictions. Local procedures also dictate the progress of a case until its closure, and the IRS usually has no control over such matters. As a result, some of these cases may be open for long periods of time.

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[6] See Appendix IV for details of bankruptcy specialist duties.
[7] 11 U.S.C. § 349.
[8] 11 U.S.C. § 524.

A growing challenge for the Collection Insolvency function is that it is required to work all incoming bankruptcy inventory; it cannot suspend or shelve incoming cases, which puts a strain on existing resources. Furthermore, diminishing resources caused by normal attrition, the inability to hire, and budget cuts makes the function's mission even more challenging.

In Fiscal Year 2012, the Field Insolvency function received 306,920 bankruptcy cases on taxpayers owing approximately $2.5 billion in taxes, penalties, and interest. In addition, the function closed 360,431 bankruptcy cases, collecting approximately $607 million. The scope of this review focused specifically on the responsibilities of the Field Insolvency function.

This review was performed at the IRS Small Business/Self-Employed Division's Collection Field function Field Insolvency function offices in Jacksonville, Florida; Atlanta, Georgia; and Dallas, Texas, during the period August 2012 through June 2013. 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.

Results of Review

Overall, the Field Insolvency function has established procedures for specialists to take appropriate and timely actions on bankruptcy cases. However, procedures were not always followed, which put the Government's interest and taxpayers' rights at risk. Specifically, we determined that specialists:

- Did not always take or did not timely take initial case analysis actions.
- Did not always timely or properly close cases.
- Delayed taking some follow-up actions.
- Did not always timely or accurately resolve APOC flag conditions.

Although we did not identify any violations of taxpayers' rights and/or failure to protect the Government's interest during this review, this is an area where IRS management needs to place greater attention and oversight.

The Field Insolvency Function Has Established Procedures and Tools to Work and Control Case Inventory

Field Insolvency function employees obtain guidance on tax law and internal procedures to work bankruptcy cases from the Internal Revenue Manual, interim guidance memorandums, and local bankruptcy policy and procedures. Employees are required to follow these procedures when working bankruptcy cases.

Additionally, the AIS has many systemic features that assist managers and specialists to effectively work bankruptcy cases. Some of these features are used to:

- Establish bankruptcy case files.
- Maintain case histories.
- Prepare and process claims.
- Monitor tax compliance.
- Schedule and monitor follow-up actions.
- Monitor payment plans and post payments.
- Request referrals or investigations.
- Review open and closed case files.

Most importantly, the AIS provides report tools that specialists and managers are expected to use to ensure that cases in their inventories are worked properly, with the intent of protecting taxpayers' rights and the interests of the Government. Generating and using AIS reports help to ensure that the Field Insolvency function inventory is processed efficiently and effectively. For example, the AIS Follow-Up Report lists all cases in which a scheduled follow-up action is required, including the action needed. The Flagged Cases Report lists all cases in which the APOC system has identified an unresolved APOC flag condition. Proper and consistent use of these reports would help to ensure that required actions, such as following up and resolving error conditions, are taken timely.

In addition, there are various resource materials to help specialists perform a quality case analysis. For example, specialists may access the Integrated Data Retrieval System and/or available court documents to obtain business, corporate officer, income, expense, and asset information, which helps them properly calculate and classify a claim or determine if a payment plan is sufficient.

Bankruptcy Procedures Designed to Protect Taxpayer Rights and the Government's Interest Were Not Always Followed

Our review of three random samples (30 Chapter 7, 30 Chapter 11, and 30 Chapter 13) of bankruptcy cases closed between June 1, 2011, and May 31, 2012, showed some positive results when specialists followed procedures and took appropriate actions. For example, specialists took proper actions, when applicable, to:

- Determine if a lien refile was appropriate on cases in which a Notice of Federal Tax Lien (NFTL) was filed.
- Determine if a Trust Fund Recovery Penalty was applicable.
- Monitor compliance related to bankruptcy payment plans and taxpayers' filing and payment requirements.

In addition, a separate test of a random sample of 30 bankruptcy cases with APOC flag conditions that were cleared by specialists between June 1, 2011, and May 31, 2012, showed that in all 30 cases, the proof of claim was timely filed within the required 180 calendar days or, if filed later, was accepted by the court. Specialists also properly verified the classification of secured tax periods[9] in all applicable cases.

However, we found that specialists and managers frequently did not follow all of the required procedures. The remainder of the report discusses these deficiencies.

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[9] Secured tax periods are those in which the IRS has an NFTL attached to the taxpayer's assets to secure a tax liability.

Field Insolvency function specialists' case actions were not always properly or timely performed

Test results show that in 17 (57 percent) of 30 Chapter 7 cases, 15 (50 percent) of 30 Chapter 11 cases, and 13 (43 percent) of 30 Chapter 13 cases, specialists did not always follow established procedures to perform some case actions.[10] Specifically, specialists did not always:

- Timely or properly conduct the initial case analysis.
- Follow up on scheduled case actions within a reasonable time.
- Timely or properly close cases.

Based on the results of our review from a population of 30,664 Chapter 7, 5,859 Chapter 11, and 86,299 Chapter 13 bankruptcy cases, we estimate there were 11,584 Chapter 7 cases, 2,511 Chapter 11 cases, and 37,396 Chapter 13 cases with untimely or improper actions on the initial case analysis, untimely or improper closure of cases, or follow-up delays on scheduled case actions.[11]

Initial case analysis actions were not always taken or were untimely

IRS guidelines in place when the IRS works the cases require that the initial case review of Chapters 7, 11, and 13 cases be completed by specialists at least five calendar days prior to the FMC date. If the case is not assigned at least five calendar days prior to the FMC date, the specialist has 30 calendar days to complete the initial analysis.[12]

Specialists generally conduct the initial case analysis after the claim has been filed. Actions taken during the initial analysis may include determining if IRS attendance is required at the FMC to address any pending issues, reviewing the payment plan to determine if the plan adequately provides for the filed claim, and identifying potential stay violations. In addition, IRS management issued streamline procedures for certain Chapter 13 cases to help minimize the required actions for the initial case analysis. For example, there is no requirement to attend the FMC in certain cases or to review the payment plan.

In 13 Chapter 7, 10 Chapter 11, and 12 Chapter 13 cases, specialists did not always timely or properly conduct the initial case analysis. Figure 3 shows the number of errors in each of the

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[10] The count on the breakdown of cases under each issue (initial analysis, follow-up, and closing actions) will not add up to these figures because one case could have more than one type of issue.
[11] We are 95 percent confident that the range of cases with some instances of untimely or improper actions on the initial case analysis, untimely or improper closure of cases, or follow-up delays on scheduled case actions is between 7,195 and 15,974 for Chapter 7 cases, between 1,539 and 3,483 for Chapter 11 cases, and between 21,835 and 52,958 for Chapter 13 cases. See Appendix I for details on how the projections were calculated.
[12] Initial case analysis for Chapter 7 and 11 cases assigned prior to July 2010 should be completed within 10 workdays of assignment.

three samples in which specific initial analysis actions were not taken, were untimely, or were improper.

Figure 3: Number of Errors for Initial Case Analysis Actions[13]

Errors for Initial Case Analysis Actions	Chapter 7	Chapter 11	Chapter 13
Did Not Timely Conduct Initial Analysis	**1**	4	5
Did Not Conduct Initial Analysis	3	N/A	N/A
Did Not Investigate for Exempt, Abandoned, or Excluded Properties	6	0	0
Did Not Determine if FMC Attendance Was Required	0	7	**1**
Did Not Research to Identify Financial Condition or Hidden Assets	7	0	3
Did Not Review or Document Payment Plan	N/A	**1**	5
Did Not Address Filing Requirements or Unfiled Tax Returns	3	0	0
TOTAL	****1****	****1****	****1****

Source: Treasury Inspector General for Tax Administration (TIGTA) analysis of sampled bankruptcy cases.

In some cases, specialists delayed processing the claim, which affected the timeliness of the initial analysis. In other cases, specialists delayed conducting the initial analysis until after the claim was submitted to the APOC system for processing. It appears that the delays were caused by caseworkers not monitoring case actions, although IRS management could not confirm this. In addition, ********************************1****************************** ***************************************1*********************************** ****1******However, streamline procedures only apply to Chapter 13 cases, indicating that the specialist may not have been aware of the different criteria.

Conducting the initial case analysis accurately, completely, and early in the case is important to allow sufficient time to identify and resolve case issues such as attending the FMC, questioning the taxpayer, and evaluating payment plan potential. In addition, there is a risk that the IRS may not receive the revenue to which it is entitled if specialists do not carefully assess the taxpayer's financial condition during the initial analysis.

[13] A case can have more than one type of error.

Specialists delayed taking follow-up actions

The Field Insolvency function Embedded Quality Review System (EQRS) job aid addresses the importance of timely actions on bankruptcy cases. It states that actions should be timely to resolve case issues and help move the case towards resolution. Employees should take timely actions and avoid unexplained lengthy gaps in case activity. It also states that cases progress appropriately when they are monitored.

However, management has not established standards for timeliness on follow-up actions because of the nature of bankruptcy inventory and limited resources. All incoming bankruptcy notices are worked by the Collection Insolvency function. Cases are assigned to Field Insolvency function specialists on a continuing basis regardless of the size of their current inventory. To address this challenge, management has given specialists the authority to continuously prioritize their work and determine if a scheduled follow-up action takes priority over other actions, such as filing a claim. Because there are no standards, we used a 30-calendar-day criterion as a reasonable time for which scheduled follow-up actions should be taken by specialists.

In four Chapter 7, eight Chapter 11, and **1** Chapter 13 cases, specialists delayed following up on scheduled case actions by more than 30 calendar days. For example, specialists delayed following up to:

- Secure requested delinquent returns needed to file an amended claim.
- Obtain information from the taxpayer's attorney to clarify discrepancies in the financial records.
- Obtain the bankruptcy schedules and the Employer Identification Number that could potentially affect taxpayers' assets and figures on the claim.
- Confirm the adequacy of the plan after it was reviewed by the specialist and before a payment plan is confirmed by the court.

Figure 4 shows the number of instances in which scheduled case actions were not followed up within 30 calendar days by type of bankruptcy chapter.

Figure 4: Delays in Follow-Up Actions

Number of Calendar Days Delayed	Chapter 7	Chapter 11	Chapter 13
31–90 days	**1**	8[14]	**1**
91–180 days	**1**	**1**	0
>180 days	**1**	**1**	0
TOTALS	****1****	****1****	****1****

Source: TIGTA analysis of sampled bankruptcy cases.

To assist in monitoring case actions, specialists have the ability to use the AIS Follow-Up Report, which shows the scheduled date and action needed to be taken for all cases for which a follow-up action is required. However, this tool is available only for cases in which specialists use the AIS follow-up tool to schedule follow-up actions. Currently, specialists are not required to use the AIS follow-up tool and may instead use other tools, such as the calendar feature on their computers. For the 17 instances of untimely follow-ups, there were eight instances in which specialists did not use the AIS follow-up tool. When follow-up actions are not taken timely, it can affect the timeliness of subsequent enforcement actions. For example, we determined that **1** Chapter 7 **1**, four Chapter 11 cases, and **1** Chapter 13 **1** could have potentially been released to Collection function inventory sooner if follow-up delays had not occurred. Delays in collection enforcement action can reduce the likelihood of collecting revenue.

Specialists did not always timely or properly close cases

Closing actions on cases must generally be initiated by the Field Insolvency function within 30 calendar days of receipt of the discharge or dismissal order. A lien determination is required in dismissed cases or discharged cases with nondischargeable taxes if the unpaid balance of the assessment is more than $10,000. A lien determination will ensure that an NFTL is filed after the automatic stay is lifted. In addition, cases should be transferred to the Centralized Insolvency Operation function for closing actions for Chapter 7 individual cases in which a notice of discharge has been received and for business cases in which a claim has been prepared and acknowledged by the court and certain other conditions are met.

[14] There were 11 instances of delayed follow-up actions in the eight Chapter 11 cases.

In seven Chapter 7 cases,[15] ***1*** Chapter 11 **1**, and three Chapter 13 cases, specialists did not timely or properly take closing actions. Specifically:

- In three Chapter 7 cases, specialists did not initiate closing actions timely. ****1**** ******************************1************************************ ******************************1************************************ ******************************1************************************ *********1************ Untimely closing actions ranged from 19 calendar days to 333 calendar days late.

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If bankruptcy cases are not closed timely, there is a risk that collection actions could be unnecessarily delayed on cases with nondischarged liabilities. In addition, making a lien determination is important to help protect the Government's interest.

Manager case reviews identified similar findings

We reviewed the EQRS managerial reviews from January 1, 2011, to December 31, 2012, for a judgmental sample[16] of 11 specialists who worked cases in our sample in which employee errors were identified. Our review showed that the 11 specialists' managers identified and provided feedback on the same types of employee errors that we identified. For example, the managers identified cases and provided feedback to employees when initial case analyses were not timely conducted, when case closures were not timely or appropriate, and when follow-up actions were not timely taken.

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

Field Insolvency function managers provide oversight and direction to bankruptcy specialists and are responsible for the quality of all work assigned to their group. Field Insolvency function managers' oversight responsibilities include ensuring that employee case actions are timely and in accordance with current policies and procedures. Also, managers are required to conduct mandatory case reviews of the work of each specialist under their supervision. These reviews can be a valuable tool for improving performance. For example, case reviews provide Field Insolvency function managers with opportunities to ensure that specialists are adhering to standards, reinforce the importance of completing case actions timely, and pinpoint and address performance gaps.

IRS management informed us that it is difficult to determine all the causes for these employee errors because many of the cases in our sample were opened prior to Fiscal Year 2010 and worked over a multiyear period. Also, there could have been more than one specialist working the case during this time, and if case histories did not contain sufficient documentation, management could not substantiate the actual reason for the errors. However, results of our judgmental sample review indicate that although managers are identifying and providing feedback to employees on these types of errors, EQRS managerial reviews alone were not effective at preventing the errors from occurring. For example, Field Insolvency function group managers are required to complete at least 15 reviews per employee per year. However, based on Fiscal Year 2012 bankruptcy closures and the current number of bankruptcy specialists, 15 reviews per employee was less than 3 percent of bankruptcy cases closed. Because managers are only required to review a small percentage of cases worked, there is a higher risk that untimely and improper actions will go undetected.

When specialists do not address flag conditions timely or properly, taxpayers' rights could be violated and revenue could be lost

When the APOC system encounters a condition that cannot be resolved, it creates an APOC flag condition which specialists must timely and accurately resolve so the claim can be filed. We reviewed a separate random sample of 30 bankruptcy cases with APOC flag conditions. Results showed that specialists did not timely or properly resolve the flag conditions for 12 (40 percent) of 30 cases.

- For seven (23 percent) cases, specialists did not work some of the flag conditions within the required time frames.
- For five (17 percent) cases, specialists did not take proper actions or we could not determine if proper actions had been taken.

Based on the results of our case reviews from a population of 108,327 bankruptcy cases with APOC flag conditions, we estimate there were 33,331 cases[17] with some instances of untimely or improper actions to resolve APOC flag conditions.

Flags were not worked within required time frames

IRS procedures state that APOC flag conditions are generally required to be worked within five calendar days of the FMC. However, secured period flags must be worked within 10 calendar days of the APOC system notification. Flags that indicate a potential stay violation, such as payments received after the bankruptcy petition date, must be addressed within five calendar days of the APOC system's notification of the condition. In seven (23 percent)[18] of the 30 cases reviewed, we found that:

- Four cases with flags were not worked within five calendar days of the FMC. Untimely actions ranged from three to 170 calendar days late.
- Three cases with secured period flags were not worked within 10 calendar days of notifications by the APOC system. Untimely actions ranged from one to 32 calendar days late.
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The time frame to clear APOC flag conditions allows the specialist an opportunity to assess whether IRS attendance at the FMC is warranted. However, sometimes attendance is needed before APOC flag conditions can be resolved, which could lead to inefficient or ineffective case work. For example:

- If flags are not addressed prior to the FMC, specialists may not know that additional financial information should be obtained at the meeting (such as unreported wages or income). In addition, in certain cases, taxpayer assets may be available for the IRS to attach an NFTL in order to satisfy any tax liabilities but were not identified before the FMC.
- If secured period flags are not worked timely, there is a risk that taxpayer assets may be dissipated before the claim is filed with the court.
- If flags with potential stay violations are not worked timely, taxpayers' rights could be potentially violated. For example, an NFTL filed after the petition date would need to be released.

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[17] We are 95 percent confident that the range of bankruptcy cases with some instances of untimely or improper actions to resolve APOC flag conditions is between 17,438 and 49,225. See Appendix I for details on how the projection was calculated.
[18] A case can have more than one type of untimely action.

In all seven cases, the specialist did not effectively monitor the case after assignment to determine when the APOC system had completed processing and the flag condition could be worked. Specialists may use the AIS Flagged Cases Report to monitor assigned cases for APOC flag condition notifications. However, there is no requirement that specialists use this report to monitor their inventory. If the Flagged Cases Report had been used, it could have potentially identified the APOC flag conditions prior to the appropriate deadline and allowed specialists to work them timely.

Required actions to resolve APOC flag conditions were not always taken

There are various types of APOC flag conditions that may require specific actions to resolve. For example, actions may be needed when a payment is received after the petition date, when an NFTL is recorded on a specific period, and when the date of the lien is not recorded on the AIS. In five (17 percent) of 30 cases reviewed, the specialist did not take appropriate actions to resolve various APOC flag conditions or we could not determine if proper actions were taken because specialists did not adequately document their actions.

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- In three cases, we were unable to determine if proper actions were taken to calculate the claim amounts due because the AIS case histories were not sufficiently recorded. For example, specialists did not document their research of the bankruptcy schedules to determine the taxpayer's equity on a secured claim or the basis used for adjusting the amount of interest owed on a tax liability. If research and claim calculations are not documented and the amounts are later disputed, specialists may need to perform the same work again which is not an efficient use of program resources.

The IRS relies on periodic managerial reviews to determine the quality and effectiveness of casework, including the timeliness of actions taken by employees. We reviewed the EQRS results for a judgmental sample of five specialists (who worked cases with errors in our sample) from January 1, 2011, to December 31, 2012. Our review showed that the five specialists' managers identified and provided feedback on these types of flag issue errors. However, as previously mentioned, managers typically review less than 3 percent of specialists' cases, which creates a risk that untimely and improper actions will go undetected. The managers for these specialists had not selected any of the cases with errors in our sample when they conducted their managerial reviews.

If APOC flag conditions are not resolved properly, claim amounts may not be accurate, resulting in a potential loss of revenue. In addition, if specialists do not document required case actions in the AIS history, they may be unable to provide testimony in court hearings regarding claim data and computations that may be needed to protect the Government's interest.

Recommendations

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

Recommendation 1: Reevaluate the Field Insolvency function to determine whether casework priorities and efficiencies can be enhanced to ensure that the function can continue protecting taxpayer rights and the Government's interest using available resources.

> ***Management's Response:*** IRS management agreed with this recommendation. Specifically, management will: 1) implement selected Insolvency Task Force recommendations designed to increase efficiencies and enhance business results and 2) reissue a memorandum designating Field Insolvency function priorities based on available resources.

Recommendation 2: Ensure that specialists are conducting the initial analysis and closing cases appropriately and in a timely manner. In addition, a reminder should be given to specialists that streamlined procedures are for Chapter 13 cases only.

> ***Management's Response:*** IRS management agreed with this recommendation. Specifically, management will: 1) issue a Field Insolvency function memorandum on the use of Chapter 13 streamlined procedures and the use of available tools to enhance efficiencies, and hold a Field Insolvency function group manager meeting on the use of Chapter 13 streamlined procedures; 2) conduct targeted Territory case reviews on the use of Chapter 13 streamlined procedures; and 3) include a management performance standard in Fiscal Year 2014 to address complete and timely actions on cases prior to closure.

Recommendation 3: Ensure that specialists understand that the AIS follow-up tool is the preferred method for scheduling follow-up actions so that these actions will be reflected on the AIS Follow-Up Report.

> ***Management's Response:*** IRS management agreed with this recommendation. Specifically, management will: 1) issue a Field Insolvency function memorandum on the use of the AIS Follow-Up Screen to schedule next case actions and to complete follow-up

actions timely; 2) conduct group manager workshops on scheduling follow-up actions and the use of the AIS to manage follow-up activities; and 3) begin targeted case reviews addressing the use of the AIS Follow-Up Screen and timeliness of follow-up actions.

Recommendation 4: Ensure that specialists properly document case actions to support decisions taken when addressing APOC flag conditions.

Management's Response: IRS management agreed with this recommendation. Specifically, management will: 1) initiate targeted Territory reviews of documentation of case actions in accordance with the requirements of the Internal Revenue Manual; 2) conduct group manager coaching sessions or workshops on required documentation of case actions; and 3) conduct operational reviews to address documentation of case actions.

Recommendation 5: Ensure that specialists understand that the Flagged Cases Report is the preferred method for monitoring cases to identify unresolved APOC flag conditions. In addition, management should consider whether improvements can be made to ensure that specialists take appropriate, timely action to resolve flag conditions.

Management's Response: IRS management agreed with this recommendation. Specifically, management will: 1) initiate targeted reviews in each Territory of cases with APOC flag condition(s) to review whether appropriate, timely action was taken by specialists to resolve the APOC flag condition(s); 2) conduct group manager coaching sessions or workshops on APOC flag conditions emphasizing appropriate actions and time frames for completion; and 3) conduct operational reviews to address cases with APOC flag conditions.

Appendix I

Detailed Objective, Scope, and Methodology

The overall audit objective was to determine whether the Field Insolvency function has effective controls and procedures in place to take appropriate and timely actions to protect the Government's interest and taxpayers' rights during bankruptcy[1] proceedings. To accomplish this objective, we:

I. Identified the IRS's procedures and guidelines for working bankruptcy cases.

A. Reviewed applicable IRS procedures and guidelines.

B. Interviewed IRS management to discuss the bankruptcy program, procedures, and internal controls.

C. Conducted a site visit to the Field Insolvency function offices in Jacksonville, Florida; Atlanta, Georgia; and Dallas, Texas. The locations were selected by identifying the States with the highest and the lowest individual performance scores from the National Quality Review System results and a location where receivership cases were worked.

1. Interviewed Field Insolvency function management and specialists to identify and evaluate procedures to work, control, and monitor their inventory.

2. Performed a walkthrough with a specialist to observe the procedures for handling bankruptcy cases.

II. Obtained previous and current key statistics related to bankruptcy filing from the U.S. Courts website (www.uscourt.gov) and the IRS Collection Activity Reports for trends.

III. Determined whether the Field Insolvency function is timely and properly resolving the APOC flag conditions generated by the APOC system to ensure that proofs of claim are accurately prepared.

A. Identified the population of APOC flag condition cases that were cleared between June 1, 2011, and May 31, 2012, from the AIS. The population for APOC flag condition cases was 108,327 cases.

B. Validated a random sample of 15 cases from our original data extracts in Step III.A. by verifying several fields, which included the AIS docket completion date, Taxpayer

[1] See Appendix V for a glossary of terms.

Identification Number, tax period, and Transaction Code 520 with an appropriate bankruptcy closing code on the Integrated Data Retrieval System, to determine the reliability of the data. Our validation showed that the data were sufficiently reliable for our tests.

C. Selected a random sample of 30 cases from the population identified in Step III.A. for review. We originally selected an oversample of 60 cases to ensure that we obtained enough cases meeting our criteria. We conducted our review in selection order of the first 30 cases, but we were unable to review nine cases because they did not meet our criteria. We excluded those nine cases and replaced them with the next nine cases in selection order to complete the review of 30 cases. We conducted a case review to determine whether timely and appropriate actions were taken to resolve the APOC flag conditions by reviewing the AIS case history and the Integrated Data Retrieval System.

D. Reviewed the EQRS results from January 1, 2011, to December 31, 2012, for a judgmental sample[2] of five specialists who worked cases in our sample in which employee errors were identified. We selected a judgmental sample because we only needed the EQRS results for specific employees, and there was no need to project the results of the sample to the population.

E. Projected the number of errors to the entire population of 108,327. Our projection was based on a sample of 39 because we had to select an additional nine cases to obtain our sample size of 30 cases. The actual overall error rate was 40 percent and precision was 17.83 percent. We are 95 percent confident that the range of cases with some instances of untimely or improper actions to resolve APOC flag conditions is between 17,438 and 49,225.

IV. Determined if Field Insolvency function specialists took proper actions to effectively work, monitor, and control their inventory.

A. Identified the population of Chapter 7, Chapter 11, and Chapter 13 bankruptcy cases worked by Field Insolvency function specialists and closed between the periods of June 1, 2011, through May 31, 2012, from the AIS. The population of bankruptcy cases was 30,664 Chapter 7, 5,859 Chapter 11, and 86,299 Chapter 13 cases.

B. Validated a random sample of 15 cases from our original data extracts in Step IV.A. by verifying several fields, which included the AIS closed date, Taxpayer Identification Number, tax period, and Transaction Code 521 with an appropriate bankruptcy closing code on the Integrated Data Retrieval System, to determine the reliability of the data. Our validation showed that the data were sufficiently reliable for our tests.

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

Selected three random samples of (30 Chapter 7, 30 Chapter 11, and 30 Chapter 13) bankruptcy cases from the population identified in Step IV.A for review. We selected an oversample of 60 cases for each type of bankruptcy to ensure that we obtained enough cases meeting our criteria. We conducted our review in selection order of the first 30 cases, but we were unable to review 15 Chapter 7 and five Chapter 11 cases because they did not meet our criteria. We excluded those 15 and five cases and replaced them with the next 15 and five cases, respectively, in selection order to complete the review of 30 cases for Chapter 7 and 30 cases for Chapter 11.

C. Conducted a case review to determine whether specialists were taking proper actions to effectively monitor and control their inventory, such as:

   1. Timely and properly conducting initial case analysis.
   2. Effectively monitoring cases to ensure that taxpayers were filing current and post-petition tax returns, and making required payments according to the plan.
   3. Timely and properly closing bankruptcy cases.

D. Reviewed the EQRS reviews from January 1, 2011, to December 31, 2012, for a judgmental sample of 11 specialists who worked cases in our sample in which employee errors were identified. We selected a judgmental sample because we only needed the EQRS results for specific employees, and there was no need to project the results of the sample to the population. We verified if managers identified and provided feedback on the same types of employee errors that we identified on the review.

E. Projected the number of errors to the entire population of 30,664 Chapter 7, 5,859 Chapter 11, and 86,299 Chapter 13 cases. Our projection was based on a sample of:

   1. 45 Chapter 7 cases. The actual overall error rate was 56.66 percent and precision was 18.04 percent. We are 95 percent confident that the range of cases with untimely and improper actions is between 7,195 and 15,974. Our projection was based on a sample of 45 because we had to select an additional 15 cases to obtain our sample of 30.
   2. 35 Chapter 11 cases. The actual overall error rate was 50 percent and precision was 18.20 percent. We are 95 percent confident that the range of cases with untimely and improper actions is between 1,539 and 3,483. Our projection was based on a sample of 35 because we had to select an additional five cases to obtain our sample of 30.

3. 30 Chapter 13 cases. The actual overall error rate was 43.33 percent and precision was 18.04 percent. We are 95 percent confident that the range of cases with untimely and improper actions is between 21,835 and 52,958.

V. Discussed our sampling methodologies with our contract statistician to obtain agreement and ensure that we could project the error rates to the populations when needed.

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 the following internal controls were relevant to our audit objective: Field Insolvency function policies and procedures, AIS and Integrated Data Retrieval System programing controls, and the EQRS. We evaluated these controls by observing Field Insolvency function employees receive and work bankruptcy cases, interviewing management, and reviewing samples of bankruptcy cases.

Appendix II

Major Contributors to This Report

Nancy Nakamura, Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Augusta R. Cook, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Frank Dunleavy, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Carl Aley, Director
Timothy F. Greiner, Acting Director
Phyllis Heald London, Audit Manager
Doris A. Cervantes, Lead Auditor
Michael A. Garcia, Senior Auditor
Matthew J. Schimmel, Senior Auditor

Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Director, Office of Research, Analysis, and Statistics RAS
Director, Enterprise Collection Strategy, Small Business/Self-Employed Division SE:S:CS
Director, Field Collection, Small Business/Self-Employed Division SE:S:FC
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Commissioner, Small Business/Self-Employed Division SE:S

Appendix IV

Bankruptcy Specialist Duties

The following are the major duties of bankruptcy[1] specialists, who are required to protect the Government's interest and taxpayers' rights during bankruptcy proceedings.

Filing a Proof of Claim

The proof of claim is the primary method by which the IRS receives funds in a bankruptcy proceeding. Generally, the IRS has 180 calendar days from the bankruptcy petition date in which to file a claim. This 180-calendar-day deadline is commonly referred to as the bar date.

The claim lists the taxpayer's outstanding liabilities and classifies each liability into one or more of three categories that help determine the order in which funds are distributed to creditors:

- Secured claims are those for which the IRS has an NFTL attached to the taxpayer's assets to secure a tax liability.
- Unsecured priority claims are liabilities that are not secured by an NFTL but have priority over other unsecured claims. Generally, prepetition liabilities for which the tax return was due less than three years prior to the petition date are entitled to priority, although taxes in certain other situations may also be entitled to priority.
- Unsecured general claims are liabilities that are classified as neither secured nor unsecured priority. These claims include all penalties, with the exception of the Trust Fund Recovery Penalty, and any interest associated with those penalties.

Most of the IRS's claims are electronically generated by Field Insolvency function offices through the APOC system and electronically transmitted to the bankruptcy court. However, when the APOC system encounters a condition that cannot be resolved, a flag is issued which requires timely and accurate intervention by specialists so the claim can be processed. Flags are separated in two categories, case or period flags, with each having various types of conditions that require specific actions to resolve.

[1] See Appendix V for a glossary of terms.

Conducting Initial Case Analysis

Specialists must timely and appropriately conduct an initial case review after the case is assigned. The primary case actions taken by specialists during the initial case analysis, when applicable, include:

- Reviewing for collection potential from exempt, abandoned, or excluded properties of individual debtors.
- Researching to determine the taxpayer's financial condition or to identify potential hidden assets.
- Addressing all filing requirements or any unfiled returns.
- Determining if the Trust Fund Recovery Penalty should be assessed.
- Reviewing the plan of reorganization/payment plan to determine if the IRS claim is adequately provided for.
- Identifying any potential stay violations, such as determining whether any liens were recorded or levy proceeds were received after the petition date.
- Attending the FMC. Specialists may be required to attend these meetings to address any pending compliance issues, such as unfiled returns, or to clarify questions regarding the existence or disposition of assets or discrepancies between information secured from internal or external sources.

Specialists use a variety of tools to assist in the completion of the initial case analysis. These tools include, but are not limited to, the IRS's Integrated Data Retrieval System, Integrated Collection System, Automated Collection System, and examination files. Outside tools may include the Public Access to Court Electronic Records system, commercial locator services, local court house online records, and online real estate property valuations. The facts and circumstances of each case should determine the extent of the research conducted.

Monitoring for Filing and Payment Compliance

Specialists must monitor bankruptcy cases to ensure that taxpayers are compliant with filing current and post-petition tax returns and making Federal tax deposits, if required, while their bankruptcy cases are being worked in the court. In addition, specialists should monitor payment plans in appropriate cases to ensure that taxpayers are making required payments according to the plan.

For example, Federal income taxes generally are only dischargeable in Chapter 7 cases of individuals if:

- The tax debt is not entitled to priority. This would generally include an income tax that is more than three years old.
- The tax debt did not relate to a fraudulent return and the taxpayer did not willfully attempt to evade the tax.
- The taxpayer filed a return for the tax, and if the return was filed late, it was not filed within two years of the bankruptcy.

Initiating Closing Actions

There are five common methods of closing a bankruptcy case:

- Dismissal,[2] which returns the taxpayer to a prepetition status, *e.g.*, taxpayer is liable for all debts, including the accrual of applicable penalties and interest on liabilities. The taxpayer is no longer under the protection of the court, and the IRS is able to proceed with collection actions.
- Denial of discharge, which is treated the same as a dismissal.
- Discharge,[3] which is a permanent injunction against the collection of the debt as a personal liability of the debtor. The discharge order is made by the court and relieves the taxpayer from financial responsibility for all or certain debts.
- Full paid, which is when the taxpayer's plan is fully paid (plan satisfaction).
- No liability, which is when the IRS is notified of the bankruptcy filing, all tax returns are filed with no tax liability, and there are no pending or potential tax liabilities.

When closing a bankruptcy case, specialists should:

- Initiate timely closing actions after dismissal, discharge, plan satisfaction, or no liability.
- Determine and take any necessary actions to request a lien refiling and/or make a lien determination, if needed, to ensure that an NFTL is filed after the automatic stay is lifted.
- Use the appropriate case disposition in the AIS such as full paid, no liability, discharge, or dismissal, which are the most common methods of closure.
- Properly transfer cases to the Centralized Insolvency Operation function for closure, when appropriate.

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[2] 11 U.S.C. § 349.
[3] 11 U.S.C. § 524.

Appendix V

Glossary of Terms

Term	Definition
Automated Insolvency System	The bankruptcy database maintained by the Collection Insolvency function. Its many functions work together to allow the IRS to manage all of the bankruptcy cases in its inventory.
Automated Proof of Claim System	The APOC system is an automated system that performs a tax filing and payment compliance check on all cases selected for processing.
Automatic Stay	An injunction that arises when a bankruptcy is filed (11 U.S.C. Section (§) 362). It is a prohibition on the commencement or continuation of certain legal or enforcement activities against the debtor, the debtor's property, and property of the estate (subject to certain exceptions).
Bankruptcy	A legal proceeding administered by the U.S. bankruptcy courts and governed by Title 11 of the United States Code (11 U.S.C.), commonly referred to as the Bankruptcy Code. The Bankruptcy Code establishes the law under which bankruptcy proceedings are commenced, administered, and closed.
Bankruptcy Estate	All legal or equitable interests of the debtor in property at the time of the bankruptcy filing. The estate includes all property in which the debtor has an interest, even if it is owned or held by another person.
Bankruptcy Petition	The form filed by the debtor (or against the debtor by creditors in an involuntary bankruptcy) with the court requesting relief from creditors. It is filed to commence a case under any chapter of the Bankruptcy Code.

Term	Definition
Bar Date	The date fixed by the court or by statute as the date by which a creditor must file a proof of claim. The IRS is allowed a minimum of 180 calendar days after the order of relief in which to file a claim. The court may grant extensions for cause.
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.
Creditor	Person or entity with a claim against the debtor and/or property of the debtor at the time the bankruptcy petition is filed. If the taxpayer had Federal tax debt, the IRS would be a creditor.
Denial of Discharge	The situation in which a debtor goes through the bankruptcy proceeding and is determined to remain responsible (usually for cause) for all of the prepetition liabilities.
Discharge	A court order which extinguishes the debtor's personal liability on many prepetition debts. It is the event triggering forgiveness of debt in a bankruptcy case.
Dismissal	The term used when a bankruptcy proceeding is terminated prematurely. Debts are not forgiven, and the debtor does not receive a discharge.
Embedded Quality Review System	The system used by managers to document all case-related reviews of employees.
First Meeting of Creditors	The meeting at which the debtor is required to testify under oath about financial affairs and to respond to questions from creditors and the trustee. It is also referred to as the § 341 Meeting, 341 Meeting, or 341 Hearing (11 U.S.C. § 341).
Fiscal Year	A 12-consecutive-month period ending on the last day of any month. The Federal Government's fiscal year begins on October 1 and ends on September 30.

Term	Definition
Integrated Data Retrieval System	A major IRS application consisting of databases and operating systems that support IRS employees working active tax cases within each business function across the IRS. This system allows employees to post transaction updates to the IRS master files.
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.
National Quality Review System	A part of an integrated IRS-wide system of balanced performance measures. Performance is evaluated using attributes that identify actions that move cases toward closure through appropriate and timely case activity.
Notice of Federal Tax Lien	Document filed in a local government office to protect the Federal Government's right of priority against other creditors of the taxpayer.
Petition Date	The date the bankruptcy petition was filed in the court.
Prepetition	The period of time before the bankruptcy petition was filed.
Proof of Claim	A document a creditor files with the court to assert a right of payment from the bankruptcy estate for prepetition debts.
Public Access to Court Electronic Records (PACER)	An electronic public access service that allows users to obtain case and docket information from Federal appellate, district, and bankruptcy courts, and the PACER Case Locator via the Internet. The PACER is provided by the Federal judiciary in keeping with its commitment to providing public access to court information via a centralized service.
Receivership	A receivership proceeding is when a State or Federal court appoints a fiduciary (receiver) to take control of some or all assets of a business or individual. The court appointing the receiver has jurisdiction over the assets of the receivership.

Term	Definition
Secured Tax Period	Secured tax periods are those in which the IRS has an NFTL attached to the taxpayer's assets to secure a tax liability.
Small Business/ Self-Employed Division	The IRS organization that services self-employed taxpayers and small businesses by educating and informing them of their tax obligations, developing educational products and services, and helping them understand and comply with applicable tax laws.
Trust Fund Recovery Penalty	An assessment against an individual of a corporation who failed to pay, on behalf of the corporation, all income and Federal Insurance Contributions Act taxes withheld from employees' wages.

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

JAN 30 2014

MEMORANDUM FOR MICHAEL E. MCKENNEY
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Karen Schiller
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – Bankruptcy Procedures Designed to Protect Taxpayer Rights and the Government's Interest Were Not Always Followed (Audit Number 201230013)

Thank you for the opportunity to review and respond to your draft report titled, "Bankruptcy Procedures Designed to Protect Taxpayer Rights and the Government's Interest Were Not Always Followed". We agree with the findings in your report and appreciate your recommendations which provide Field Insolvency with an opportunity to improve its procedures, create business efficiencies, and improve quality.

This is the first audit of Field Insolvency undertaken by TIGTA. We appreciate your acknowledgement that the audit did not find any violations of taxpayer rights or instances where the government's interest had been compromised. We take seriously our obligations to safeguard taxpayer rights and protect the government's interests.

Prior to receiving the draft audit report, Field Insolvency entered into negotiations with the Centralized Insolvency Organization (CIO) and the National Treasury Employee's Union (NTEU) as a part of our ongoing efforts to improve business results through greater efficiencies. The CIO and NTEU signed a Memorandum of Understanding which became effective July 8, 2013. Through these negotiations, Field Insolvency implemented the following changes to achieve efficiencies: unconfirmed Chapter 13 cases are assigned to the CIO to monitor for confirmation after completion of all field issues; large dollar Chapter 7 "no asset" cases are screened by the CIO prior to field assignment; and Chapter 7 "asset" cases are reassigned to CIO after Field Insolvency completes required case actions. This initiative has essentially removed clerical activities from Field Insolvency and has reduced field inventories allowing caseworkers more time to focus on complex bankruptcy issues.

Additionally, an Insolvency Task Force consisting of Territory Managers and bargaining unit employees was formed during Fiscal Year (FY) 2013 to review Field Insolvency procedures and make recommendations to increase program efficiencies. The Task Force achieved its objectives and submitted a list of recommendations to the Director of Advisory and Insolvency. Specific recommendations have been approved and will be implemented during FY 2014. The accepted recommendations will increase program efficiencies, protect the government's interest, and adhere to the Service's strategic plan and Field Collection's vision.

As stated above, we agree with the five recommendations you made and have developed a comprehensive plan to improve quality of casework through management and employee development, skills workshops, and increased accountability. Attached is a detailed response outlining our corrective actions.

If you have any questions, please contact me, or a member of your staff may contact Robert L. Hunt, Director, Field Collection, at (240) 613-2015.

Attachment

Attachment

RECOMMENDATION 1:
Reevaluate the Field Insolvency function to determine whether casework priorities and efficiencies can be enhanced to ensure the function can continue protecting taxpayer rights and the Government's interest using available resources.

CORRECTIVE ACTIONS:
1. We will implement selected recommendations from the Insolvency Task Force designed to increase efficiencies and enhance business results.
2. The Director of Advisory and Insolvency will re-issue a memorandum designating priorities for Field Insolvency based on available resources.

IMPLEMENTATION DATES:
1. October 15, 2014
2. May 15, 2014

RESPONSIBLE OFFICIAL:
Director, Advisory and Insolvency, Field Collection, Small Business/Self-Employed Division

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

RECOMMENDATION 2:
Ensure that specialists are conducting the initial analysis and closing cases appropriately and in a timely manner. In addition a reminder should be given to specialists that streamlined procedures are for Chapter 13 cases only.

CORRECTIVE ACTIONS:
1. The Director of Advisory and Insolvency will issue a memorandum to Field Insolvency stressing the use of Chapter 13 streamlined procedures where applicable and advising caseworkers to use available tools to enhance efficiencies. In addition, the Director of Advisory and Insolvency will hold an all managers meeting with all Field Insolvency Group Managers on the use of Chapter 13 streamlined procedures.
2. Targeted or focused case reviews will be conducted in each territory on the use of Chapter 13 streamlined Procedures.
3. FY 14 Manager Performance Commitments will include a performance standard to address complete actions on cases prior to case closure with specific focus on the measurement category for timeliness, and results will be measured by our Quality organization.

2

IMPLEMENTATION DATES:
1. May 15, 2014
2. October 15, 2014
3. November 15, 2014

RESPONSIBLE OFFICIAL:
Director, Advisory and Insolvency, Field Collection, Small Business/Self-Employed Division

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

RECOMMENDATION 3:
Ensure that specialists understand that the Automated Insolvency System (AIS) follow-up tool is the preferred method for scheduling follow-up actions, so that these actions will be reflected on the AIS Follow-Up Report.

CORRECTIVE ACTIONS:
1. The Director of Advisory and Insolvency will issue a memorandum advising Field Insolvency to use the AIS Follow-Up Screen to schedule next case actions and to complete follow-up actions timely.
2. Group managers will conduct workshops on scheduling follow-up actions and the use of AIS to manage follow-up activities.
3. Group managers will begin targeted reviews addressing the use of the AIS Follow-Up Screen and timeliness of follow-up actions.

IMPLEMENTATION DATES:
1. May 15, 2014
2. October 15, 2014
3. September 15, 2014

RESPONSIBLE OFFICIAL:
Director, Advisory and Insolvency, Field Collection, Small Business/Self-Employed Division

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

RECOMMENDATION 4:
Ensure that specialists properly document case actions to support decisions taken when addressing Automated Proof of Claim (APOC) flag conditions.

3

CORRECTIVE ACTIONS:
1. Field Insolvency territories will initiate targeted reviews of documentation of case actions in accordance with the requirements of IRM 5.9.5.4.2 and related documentation sections of the Internal Revenue Manual.
2. Filed Insolvency group managers will conduct coaching sessions or workshops on required documentation of case actions.
3. Field Insolvency operation reviews will address documentation of case actions as a facet of the review.

IMPLEMENTATION DATES:
1. September 15, 2014
2. August 15, 2014
3. November 15, 2014

RESPONSIBLE OFFICIAL:
Director, Advisory and Insolvency, Field Collection, Small Business/Self-Employed Division

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

RECOMMENDATION 5:
Ensure that specialists understand that the Flagged Case Report is the preferred method for monitoring cases to identify unresolved APOC flag conditions. In addition, management should consider whether improvements can be made to ensure specialists take appropriate, timely action to resolve flag conditions.

CORRECTIVE ACTIONS:
1. Each Field Insolvency territory will initiate targeted reviews of cases with APOC flag(s) by July 31, 2014. The focus of these reviews will be appropriate action by specialists to resolve the APOC flag and the timeliness of actions.
2. Field Insolvency group managers will conduct coaching sessions or workshops on docketed and period APOC flags emphasizing appropriate actions and timeframes for completion.
3. Operational reviews conducted by Advisory and Insolvency will address cases with APOC flag conditions as a facet of the review.

IMPLEMENTATION DATES:
1. September 15, 2014
2. August 15, 2014
3. November 15, 2014

4

RESPONSIBLE OFFICIAL:
Director, Advisory and Insolvency, Field Collection, Small Business/Self-Employed Division

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