



*Fiscal Year 2015 Statutory Review
of Compliance With Notice of
Federal Tax Lien Due Process Procedures*

June 26, 2015

Reference Number: 2015-30-055

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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HIGHLIGHTS

FISCAL YEAR 2015 STATUTORY REVIEW OF COMPLIANCE WITH NOTICE OF FEDERAL TAX LIEN DUE PROCESS PROCEDURES

Highlights

Final Report issued on June 26, 2015

Highlights of Reference Number: 2015-30-055 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

After filing a Form 668(Y)(c), *Notice of Federal Tax Lien (NFTL)*, the IRS must notify the affected taxpayer in writing, at his or her last known address, within five business days of the NFTL filing. Taxpayers' rights to timely appeal NFTL filings may be jeopardized if the IRS does not comply with this statutory requirement.

WHY TIGTA DID THE AUDIT

TIGTA is required by law to determine annually whether lien notices issued by the IRS comply with the legal requirements set forth in Internal Revenue Code Section 6320(a).

WHAT TIGTA FOUND

TIGTA reviewed a statistically valid sample of 133 NFTLs filed for the 12-month period beginning July 1, 2013, and ending June 30, 2014, and determined that the IRS timely and correctly mailed the taxpayers the notices of NFTL filing and appeal rights, as required by Internal Revenue Code Section 6320(a).

IRS regulations require that taxpayer representatives be provided copies of all correspondence issued to the taxpayer. However, for six of the 36 sample cases for which the taxpayers had an authorized representative, the IRS did not notify the taxpayers' representatives of the NFTL filings. TIGTA estimated that 24,237 taxpayers may have been adversely affected because the IRS did not follow requirements to notify the taxpayers' representatives of the taxpayers' rights related to the NFTLs.

In addition, while procedures were usually followed when working undelivered lien notices, more actions could be taken. IRS procedures require address verification and, if applicable, resolution of undelivered lien notices within 14 calendar days of receipt. TIGTA selected a judgmental sample of 189 undelivered lien notices returned to the Cincinnati (99 lien notices) and Fresno (90 lien notices) Campuses in October and November 2014. For 15 (three in Fresno and 12 in Cincinnati) of these 189 undelivered lien notices, employees did not perform the required research within 14 calendar days of receipt of the returned lien notice.

The envelopes for a majority of the 12 lien notices that the Cincinnati Campus did not research timely were marked by the U.S. Postal Service as both undelivered and unclaimed. IRS procedures do not address how to handle returned lien notices marked in this manner. TIGTA was advised by management that campus employees follow undocumented procedures to treat envelopes marked this way as unclaimed. As a result, these accounts were not researched to determine whether the IRS sent the NFTL to the taxpayer's last known address.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS: 1) establish procedures requiring the lien unit to verify all lien requests for which the checkbox on Form 12636, *Request for Filing or Refiling Notice of Federal Tax Lien*, Line 4, is blank and 2) establish procedures to timely research taxpayer accounts if the envelope of a returned lien notice is marked with multiple reasons for return and ensure that the notice was mailed to the taxpayer's last known address.

IRS management agreed with the recommendations and has taken or plans to take corrective actions.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

June 26, 2015

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION

Michael E. McKenney

FROM:

Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT:

Final Audit Report – Fiscal Year 2015 Statutory Review of
Compliance With Notice of Federal Tax Lien Due Process Procedures
(Audit # 201530001)

This report presents the results of our review to determine whether liens issued by the Internal Revenue Service (IRS) comply with the legal requirements set forth in Internal Revenue Code Section 6320 (a) and related guidance in the Federal Tax Liens Handbook. The Treasury Inspector General for Tax Administration is required by law to determine annually whether lien notices issued by the IRS comply with the legal requirements in Internal Revenue Code Section 6320. The audit is included in our Fiscal Year 2015 Annual Audit Plan and addresses the major management challenge of Taxpayer Protection and Rights.

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

Copies of this report are also being sent to the IRS managers affected by the report recommendations. If you have any questions, please contact me or Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations).



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Abbreviations

ACS	Automated Collection System
ALS	Automated Lien System
CAF	Centralized Authorization File
ICS	Integrated Collection System
IDRS	Integrated Data Retrieval System
I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
NFTL	Notice of Federal Tax Lien
TIGTA	Treasury Inspector General for Tax Administration



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Background

The Internal Revenue Service (IRS) attempts to collect Federal taxes due from taxpayers by sending letters, making telephone calls, and meeting face-to-face with taxpayers. As a matter of law, a lien automatically arises upon the occurrence of a tax delinquency encumbering the property of delinquent taxpayers without the IRS having to take any action; however, the automatic lien is unenforceable against certain third parties such as secured creditors.¹ To perfect the Government's claim, the IRS has the authority to file a notice of the lien in the appropriate State and local offices of record.² The IRS files a Form 668(Y)(c), *Notice of Federal Tax Lien* (NFTL), in appropriate local government offices to notify interested parties that a lien exists.³

The Internal Revenue Code (I.R.C.) has long required the IRS to notify taxpayers, in writing, of the filing of an NFTL; however, the IRS Restructuring and Reform Act of 1998⁴ expanded upon this notice requirement, creating I.R.C. Section (§) 6320 to give taxpayers additional rights.⁵ When the first NFTL is filed for a tax period, the notice must be issued within five business days of the filing of the NFTL and inform taxpayers of the right to elect a collection due process hearing (CDP Hearing) wherein the taxpayer can raise any relevant issue, including spousal defenses, the appropriateness of the collection actions, and collection alternatives. The lien notice⁶ is used for this purpose and advises taxpayers that they have 30 calendar days, after that five-day period, to request a CDP Hearing with the IRS's Office of Appeals. The lien notice indicates the date on which this 30-day period expires.

The IRS is required to notify taxpayers of their collection due process rights when the first NFTL is filed.

The law also requires that the lien notice explain, in simple terms, the amount of unpaid tax, other administrative appeal rights available to the taxpayer, provisions of the law, and procedures relating to the release of the lien on the property. The lien notice must be given in person, left at the taxpayer's home or business, or sent by certified or registered mail to the taxpayer's last known address.

¹ I.R.C. §§ 6321 and 6323.

² I.R.C. § 6323.

³ See Appendix V for a synopsis of the IRS collection and NFTL filing processes.

⁴ Pub. L. No. 105-206, 112 Stat. 685.

⁵ I.R.C. § 6320.

⁶ Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320*.

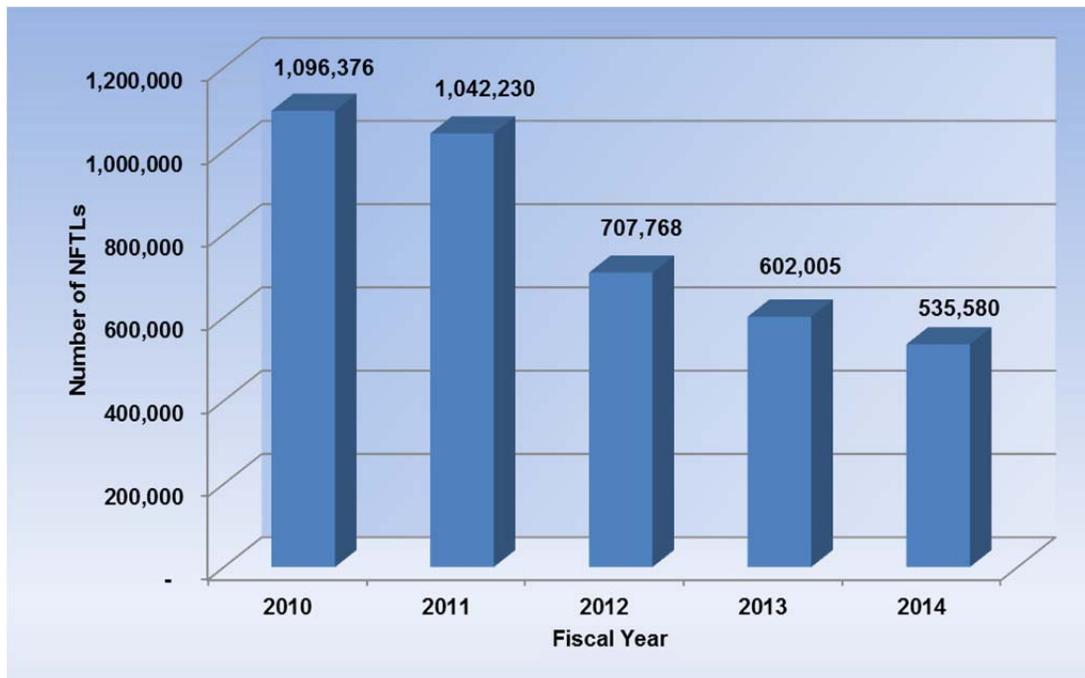


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Depending on employee access and case status, NFTL requests can be generated using one of three IRS systems:⁷ 1) the Integrated Collection System (ICS), 2) the Automated Collection System (ACS), or 3) directly input into the Automated Lien System (ALS).

In Fiscal Year⁸ 2011, the IRS implemented the Fresh Start initiative to provide aid to struggling taxpayers. This initiative increased the threshold when NFTL filing determinations are generally made from \$5,000 to \$10,000. Figure 1 shows the number of NFTLs filed for Fiscal Years 2010 through 2014 and that the number of NFTLs filed decreased from to 602,005 to 535,580 (11 percent) between Fiscal Years 2013 and 2014.

Figure 1: Number of NFTLs Filed for Fiscal Years 2010 Through 2014



Source: IRS Data Book for Fiscal Years 2010 through 2014.

The Treasury Inspector General for Tax Administration (TIGTA) is required to determine annually whether the IRS complied with the law regarding the notification of affected taxpayers and their representatives when filing NFTLs.⁹ This is our seventeenth annual audit to determine whether the IRS complied with the legal requirements of I.R.C. § 6320(a) and its own related internal guidelines for issuing lien notices.¹⁰ In the past five years, including this year, we have

⁷ See Appendix VI for detailed descriptions of the IRS computer systems used in the filing of the NFTLs.

⁸ Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.

⁹ I.R.C. § 7803(d)(1)(A)(iii).

¹⁰ See Appendix VIII for a list of the prior five TIGTA reports.



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reported full compliance with the law of timely notifying taxpayers three times and twice reported an error rate of 2 percent or less. In all five years, we reported that the IRS had not achieved full compliance with internal guidelines involving power of attorney notifications.

This review was performed at the Small Business/Self-Employed Division's Centralized Lien Processing Operation and the ACS Support function in Covington, Kentucky, and Fresno, California, and with information obtained from the Small Business/Self-Employed Division's Office of Collection Policy in New Carrollton, Maryland, during the period October 2014 through March 2015. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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Results of Review

Lien Notices Were Mailed Timely

Tests of a statistically valid random sample of 133 NFTLs from the 537,257 NFTLs filed between July 1, 2013, and June 30, 2014, showed that the IRS timely and correctly mailed a copy of the NFTL and notice of appeal rights to all 133 taxpayers, as required by I.R.C. § 6320(a).

The Internal Revenue Service Did Not Always Comply With Regulations for Notifying Taxpayer Representatives

Taxpayer representative information is contained on the Centralized Authorization File (CAF)¹¹ that is located on the Integrated Data Retrieval System (IDRS).¹² Using the IDRS, employees can research the CAF to identify the types of authorizations given to taxpayer representatives. IRS procedures¹³ require that any notice or other written communication (or a copy thereof) required or permitted to be given to a taxpayer in any matter before the IRS must be given to the taxpayer and, unless restricted by the taxpayer, to the representative. Accordingly, IRS procedures require the requestor of an NFTL to ensure that he or she notifies the Centralized Lien Processing Operation of all powers of attorney that are to be notified. More specifically, when an NFTL is filed, IRS procedures require that a copy of the lien notice be sent to the taxpayer's representative as soon as possible after the lien notice is sent to the taxpayer.

Tests of a statistically valid sample of 133 NFTLs included 36 taxpayers with representatives authorized to receive notifications at the time the NFTLs were filed. For six (17 percent) of the 36 taxpayers, ALS records did not indicate that the IRS sent copies of the lien notice to the taxpayer's representative. Specifically:

- *****1*****¹⁴ *****
*****1*****

¹¹ The CAF contains information about the types of authorizations taxpayers have given their representatives for their tax returns.

¹² IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.

¹³ Conference and Practice Requirements, Statement of Procedural Rules, 26 C.F.R. § 601.506 (2009).

¹⁴ Employees in the Collection Field function who attempt to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses or the ACS. Campuses are 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.



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We project that 24,237 taxpayers may have been adversely affected because the IRS did not follow procedures to notify the taxpayers’ representatives of the taxpayers’ rights related to the NFTLs.¹⁵ Figure 2 shows the error rates reported on the notification of taxpayer representatives in our last five reports, including this year.¹⁶

Figure 2: Error Rates Reported on the Notification of Taxpayer Representatives

Report Fiscal Year	Sample Cases Requiring Representative Notification	Cases Not Receiving Representative Notification	Error Rate
2011	30	4	13%
2012	22	4	18%
2013	47	5	11%
2014	**1**	**1**	**1**
2015	36	6	17%

Source: Prior and current year results of TIGTA’s tests on the notification of taxpayer representatives. We reviewed an ALS extract for the 12-month period ending June 30 for each of the report fiscal years.

¹⁵ The point estimate projection is based on a two-sided 90 percent confidence interval. We are 90 percent confident that the range of potential violations is between 8,005 and 46,795.

¹⁶ See Appendix VII for the confidence intervals pertaining to the notification of taxpayer representatives error rates reported during Fiscal Years 2011 through 2014.



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While the error rate dropped to ****1*** in our Fiscal Year 2014 report, this year's error rate of 17 percent¹⁷ shows that the potential for taxpayers being adversely impacted still exists for cases requiring taxpayer representative notification.

In our Fiscal Year 2013 report,¹⁸ we recommended that the IRS revise the NFTL request form to include a checkbox indicating whether a valid power of attorney is required to be sent a copy of the lien notice and establish procedures requiring the lien unit to verify all NFTL requests for which the checkbox is blank. Form 12636, *Request for Filing or Refiling Notice of Federal Tax Lien*, was revised in August 2013 in accordance with our recommendation. In January 2014, the appropriate procedures were revised to require the lien unit to verify all lien requests for which the checkbox on Form 12636, Line 4, was blank; however, the procedures could not be fully implemented at that time because the updates to programming for the use of revised Form 12636 were not completed until January 2015.

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Recommendation

Recommendation 1: The Director, Collection, Small Business/Self-Employed Division, should establish procedures requiring the lien unit to verify all NFTL requests for which the checkbox on Form 12636, Line 4, is blank.

Management's Response: IRS management agreed with this recommendation and has updated procedures¹⁹ to require the lien unit to verify that Line 4 on Form 12636 has been completed and to specify the actions to be taken if the checkbox is blank.

Procedures to Process Undelivered Lien Notices Were Usually Followed

IRS procedures²⁰ require that employees send taxpayers another lien notice to a new address if all of the following factors are present:

¹⁷ The point estimate projection is based on a two-sided 90 percent confidence interval. We are 90 percent confident that the true percentage of taxpayers with representatives whose representative was not notified is between 4.51 percent and 27.07 percent.

¹⁸ TIGTA, Ref. No. 2013-30-072, *Fiscal Year 2013 Statutory Review of Compliance With Lien Due Process Procedures* (Jul. 2013).

¹⁹ Internal Revenue Manual (IRM) 5.19.12.2.1.2.



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- The originally mailed notice is returned as undelivered mail.
- Research confirms that the original lien notice was not sent to the last known address.
- The new address was effective prior to or during the same cycle²¹ the NFTL was requested.

Collection function employees are responsible for certain actions when notices are returned as undelivered. For example, ACS Support employees are required to research the IDRS within 14 calendar days of receipt of the undelivered lien notice to ensure that the address on the original lien notice is correct.²² If the employee cannot find a new address on the computer system, the undelivered lien notice will be destroyed and a new notice is not issued.

If the address on the lien notice is not the last known address and a different address was in effect prior to the NFTL being requested, employees should issue a new lien notice to the new address. A new lien notice is created by using an option in the ALS.

We selected a judgmental sample²³ of 189 undelivered lien notices returned to the Cincinnati (99 lien notices) and Fresno (90 lien notices) Campuses in October and November 2014. The sample included returned lien notices identified as undelivered. A test of 189 undelivered lien notices identified 18 lien notices for which the address on the IRS computer system and the original lien notice did not agree. For 12 of the 18 notices, the address on the IRS computer system was updated after the original lien notice was sent to the taxpayer. Therefore, no additional action was required. However, for six of the 18 notices, the address was updated prior to the cycle the NFTL was prepared in the ALS. We determined that a lien notice was sent to the six taxpayers using the updated address in accordance with IRS procedures.

Internal procedures for undelivered NFTLs were usually followed

IRS procedures require address verification and, if applicable, resolution (request to have the lien notice reissued) of the undelivered lien notices within 14 calendar days of receipt in the ACS Support function.²⁴ For our judgmental sample of 189 lien notices, we reviewed computer system audit trails to assess whether IRS employees performed timely research to determine whether the addresses were correct on the originally mailed notices. We determined that 174 of the 189 cases were researched timely (15 cases were not researched timely) by ACS Support function employees.

²⁰ Internal Revenue Manual (IRM) 5.19.6.17.4, Undeliverable Notice of Federal Tax Lien (NFTL).

²¹ Cycle refers to the IRS method of documenting dates, e.g., Processing Cycle 201102 is the second week of January 2011.

²² IRM 5.19.6.17.4.

²³ A judgmental sample is a nonstatistical sample, the results of which cannot be used to project to the population.

²⁴ IRM 5.19.6.17.4.



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In January 2012, IRS procedures were revised to require ACS Support function employees to document the date undelivered lien notices are received in the ACS Support function and the date research is completed.²⁵ Documentation should be noted in the ACS action history codes (if the taxpayer's account is still open) or in the Accounts Management System²⁶ narrative history (if the taxpayer's account is closed). While 174 cases were researched timely, four of the 174 cases did not have the research properly documented.

Fresno Campus: Three of the 15 undelivered lien notices that were not researched timely were processed by the Fresno Campus. The Fresno Campus ACS Support function properly documented the received date in all 87 cases that they timely researched.

Cincinnati Campus: Twelve of the 15 undelivered lien notices that were not researched timely were processed by the Cincinnati Campus. The Cincinnati Campus ACS Support function properly documented the received date in 83 of the 87 cases that they timely researched.

The envelopes²⁷ for **1** of the 12 lien notices that were not researched timely in the Cincinnati Campus were marked by the U.S. Postal Service as both undelivered and unclaimed.²⁸ The IRM does not address how ACS Support should handle returned lien notices marked in this manner. ACS management advised us that ACS Support function employees follow unwritten procedures to treat envelopes marked this way as unclaimed. As a result, the returned notices were never researched to determine whether the IRS sent the lien notice to the taxpayer's last known address. We believe that because it is unclear whether or not the lien notice was returned due to a valid taxpayer address change, the IRS should research returned mail that is marked in this manner.

Without timely research of undelivered lien notices, the IRS cannot ensure that taxpayer rights are protected if the IRS did not send the lien notice to the taxpayer's last known address. The IRS is required to issue a new lien notice to the new address if this research determines that a lien notice was not sent to the taxpayer's last known address.

Procedures designed to monitor undelivered lien notices were usually followed

In August 2007, procedures²⁹ for handling undelivered lien notices were revised so that:

- An undeliverable notice is returned directly to the requesting employee or function.

²⁵ IRM 5.19.6.17.4.

²⁶ The Account Management System is a computer-based system used to answer and resolve all taxpayer account inquiries. The Accounts Management System provides a common interface that allows users of multiple IRS systems to view history and comments from other systems.

²⁷ For this year's review, the ACS Support function at the Cincinnati Campus saved the envelopes of the undelivered lien notices they worked in an effort to determine the cause of untimely processing.

²⁸ IRS procedures do not require research for cases that are returned from the U.S. Postal Service as unclaimed (or refused) by the taxpayer.

²⁹ IRM 5.19.6.17.4.



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- Employees handling undelivered lien notices should input a specific IDRS transaction code with an appropriate action code. The transaction code signifies that the lien notice was returned, and the action code indicates the reason, *e.g.*, undelivered, unclaimed, or refused.

In August 2009, the weekly systemic extract from the ALS to the Master File³⁰ was enhanced to include the undeliverable status (transaction code and action code). When a lien notice is returned undelivered and research has been completed regarding an updated address, the employee can request that the lien notice screen on the ALS be updated with the undelivered status or go to the lien notice screen themselves and indicate the undelivered status. When the ALS is used to update the status of the lien notice, no additional input is necessary to update the status on the IDRS.

In November 2013, the ACS Support function's IRM was updated to require ACS Support function employees to use the ALS lien notice screen to prompt the input of this transaction code and action code combination.³¹ For 169 of the 174 cases that were researched timely, a transaction code and action code were input to the IDRS. Compliance with these procedures is important; otherwise, the information about the undelivered lien notice would be limited to only those employees working the undelivered mail. As a result, other IRS functional employees, such as Taxpayer Assistance Center³² employees, would be unable to answer taxpayer questions about whether the lien notices were delivered.

In response to our Fiscal Year 2013 report, the IRS issued a Service-Wide Electronic Research Program Alert and updated the IRM³³ to require that the ACS Support function document the received date on either the ACS or the Accounts Management System (dependent on where the case resides). In addition, the ACS Support function employees were required to use the ALS to systemically generate the transaction code and action code combination on lien notices returned undelivered. These corrective actions have improved compliance with the procedures.

³⁰ The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

³¹ IRM 5.19.6.17.4 (Nov. 4, 2013).

³² A Taxpayer Assistance Center is an IRS office with employees who answer questions, provide assistance, and resolve account-related issues for taxpayers face to face.

³³ IRM 5.12.7.3.1, Creating the Notice of Federal Tax Lien, Form 668(Y)(c).



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Recommendation

Recommendation 2: The Director, Collection, Small Business/Self-Employed Division, should establish IRM procedures to timely research taxpayer accounts if the envelopes of returned lien notices are marked with multiple reasons for return and ensure that the lien notice was mailed to the taxpayer's last known address.

Management's Response: IRS management agreed with this recommendation. To reduce the number of envelopes with multiple stamps, the IRS will request that the U.S. Postal Service place the proper stamp on envelopes based on the data in their files. The IRS will also select a sample of unclaimed mail to pursue a pilot to test the effectiveness of their address verification research procedures and to ensure that these actions are an efficient and effective use of their limited resources. They will revise their guidance to align with their findings and clarify their procedures as needed.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to determine whether lien notices issued by the IRS comply with the legal requirements set forth in I.R.C. § 6320(a) and related guidance in the Federal Tax Liens Handbook. To accomplish this objective, we:

- I. Determined whether lien notices issued by the IRS complied with legal requirements set forth in I.R.C. § 6320(a) and related internal guidelines.
 - A. Selected a statistically valid random sample of 133 NFTLs for review from an ALS¹ extract of all NFTLs filed by the IRS nationwide between July 1, 2013, and June 30, 2014.

Population:	537,257
Confidence Level:	90 percent
Expected Rate of Occurrence:	2 percent
Precision Rate:	± 2 percent
 - B. Validated the ALS extract by comparing a sample of records to online data. We determined that the data were sufficiently reliable for purposes of this report.
 - C. Determined whether the sampled NFTLs adhered to legal guidelines regarding timely notifications of NFTL filings to the taxpayer, the taxpayer's spouse, business partners, and taxpayer representatives by reviewing data from the ALS, the ICS, the ACS, the IDRS, and the certified mail lists (U.S. Postal Service Form 3877, *Firm Mailing Book for Accountable Mail*).
 - D. Evaluated the controls and procedures established for transferring, storing, and safeguarding certified mail lists at the Centralized Lien Processing Operation for recordkeeping.
 - E. Determined if taxpayers' representatives were provided a copy of the NFTL due process notice by reviewing data from the ALS, the IDRS, the ICS, and the ACS.
 1. Reviewed IDRS screens for CAF indicators (Transaction Code 960) for all sample cases.
 2. Reviewed ALS history screens for accounts with CAF indicators to see whether notices were mailed to taxpayers' representatives.

¹ See Appendix V for detailed descriptions of the IRS computer systems used in the filing of NFTLs.



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- F. For the sampled lien notices without the taxpayer's representative/power of attorney notifications on the ALS histories, reviewed the ACS and the ICS for taxpayer representative indicators and determined whether taxpayer representatives/powers of attorney should have been notified.
- II. Evaluated the procedures for processing lien notices (Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320*) that are returned undelivered.
- A. Selected a judgmental² sample of unprocessed (unopened) mail containing 189 undelivered lien notices returned to the Fresno (90) and Cincinnati (99) Campuses³ in October and November 2014 and recorded the taxpayer's name, address, Social Security Number, Serial Lien Identification number, and date received at the respective campus mailroom. Mailroom personnel from the Fresno and Cincinnati Campuses provided us with confirmation of the dates the sampled undelivered lien notices were delivered to the ACS Support functions. We used a judgmental sample because we could not determine the population of undelivered lien notices at those two campuses.
- B. For each sample case, researched the IDRS to determine whether the address on the Master File⁴ matched the address on the undelivered lien notice.
- C. For each sample case of an undelivered lien notice, review taxpayer audit trails to determine whether lien employees performed the required IDRS research during creation of the NFTL.
- D. For each sample case, reviewed taxpayer audit trails and the ACS and Accounts Management System histories to determine whether employees performed the required IDRS research for resolution of the undeliverable status within 14 calendar days of receipt of the undelivered lien notice.
- E. For each sample case of an undelivered lien notice for which appropriate research was completed for resolution of the undeliverable status, verified that a Transaction Code 971 with an Action Code 253 was entered into the IDRS. Action Code 253 means that the lien notice was returned undelivered.
- III. Determined whether internal guidelines have been implemented or modified since our last review by discussing procedures and controls with appropriate IRS personnel in the National Headquarters.

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

³ A campus is 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.

⁴ The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.



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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 for timely notifying taxpayers of lien filings and timely verifying addresses of undelivered lien notices. We evaluated these controls by reviewing samples of lien notices sent to taxpayers and lien notices returned to the IRS as undelivered.



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Appendix II

Major Contributors to This Report

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Meaghan Tocco, Senior Auditor
Mark Willoughby, Senior Auditor
Brian G. Foltz, Auditor
Steve Meyers, Auditor



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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE:ACA
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Campus Collection, Small Business/Self-Employed Division SE:S:CC
Director, Headquarters Collection, Small Business/Self-Employed Division SE:S:C:HQ
Director, Collection Policy, Small Business/Self-Employed Division SE:S:C:CP
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Audit Coordination OS:PPAC:AC
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



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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 Burden – Potential; 24,237 taxpayers whose representatives may not have been provided Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320*¹ (see page 4).

Methodology Used to Measure the Reported Benefit:

From a statistically valid sample of 133 NFTL cases, we identified 36 cases with representatives authorized to receive notifications at the time the liens were filed. From those 36 cases, we identified six cases for which IRS employees did not provide notice to taxpayer representatives, resulting in potential taxpayer burden. The sample was selected based on a confidence level of 90 percent, a precision rate of ± 2 percent, and an expected rate of occurrence of 2 percent. We projected the error rate (six of 133 = 4.51 percent) to the total population (provided by the IRS) of 537,257 NFTLs generated by the ALS between July 1, 2013, and June 30, 2014, to arrive at 24,237 taxpayers whose representatives may not have been provided Letter 3172. We are 90 percent confident that the range of potential violations is between 8,005 and 46,795.

¹ *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320* (Mar. 2009).



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Appendix V

Synopsis of the Internal Revenue Service Collection and Notice of Federal Tax Lien Filing Processes

The collection of unpaid tax begins with a series of letters (notices) sent to taxpayers advising them of their debt and asking for payment of the delinquent tax. IRS computer systems are programmed to mail these notices when certain criteria are met. If the taxpayer does not respond to these notices, the account is transferred for either personal or telephone contact.

- IRS employees who make personal (face-to-face) contact with taxpayers are called revenue officers and work in various locations. The ICS¹ is used to track collection actions taken on taxpayer accounts.
- IRS employees who make only telephone contact with taxpayers work in call sites. The ACS is used in the call sites to track collection actions taken on taxpayer accounts.

When these efforts have been taken and the taxpayer has not paid the tax liability, designated IRS employees are authorized to file an NFTL by sending a Form 668(Y)(c), *Notice of Federal Tax Lien*, to the appropriate local government offices. The NFTLs protect the Federal Government's interest by informing the public of its claim to the taxpayer's assets for the amount of unpaid tax. The Federal tax lien is created by I.R.C. § 6321 when:

- The IRS has made an assessment and given the taxpayer notice of the assessment, stating the amount of the tax liability and demanding payment.
- The taxpayer has neglected or refused to pay the amount after the notice and demand for payment.

The right to file an NFTL is found in I.R.C. § 6323. When employees request the filing of an NFTL using either the ICS or the ACS, the ALS processes the NFTL filing requests. In an expedited situation, employees can manually prepare the NFTL. Even for manually prepared NFTLs, the ALS controls and tracks the NFTLs and initiates subsequent lien notices² to notify responsible parties of the NFTL filings and of their appeal rights. The ALS maintains an electronic database of all open NFTLs and updates the IRS's primary computer records to indicate that an NFTL has been filed.

¹ See Appendix VI for detailed descriptions of the IRS computer systems used in the filing of the NFTLs.

² Letter 3172, *Notice of Federal Tax Lien Filing and Your Right to a Hearing Under IRC 6320*.



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Most lien notices are mailed to taxpayers by certified or registered mail rather than delivered in person. To maintain a record of the notices, the IRS prepares a certified mail list (U.S. Postal Service Form 3877, *Firm Mailing Book for Accountable Mail*), which identifies each notice that is to be mailed. The lien notices and a copy of the certified mail list are delivered to the U.S. Postal Service. A U.S. Postal Service employee ensures that all notices are accounted for, date-stamps the list, and returns a copy to the IRS. The stamped certified mail list is the only documentation the IRS has that certifies the date on which the notices were mailed. IRS guidelines require that the stamped certified mail list be retained for 10 years after the end of the processing year.



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Appendix VI

Internal Revenue Service Computer Systems Used in the Filing of Notices of Federal Tax Liens

Automated Collection System (ACS) – a computerized call site inventory system that maintains balance due accounts and return delinquency investigations. ACS function employees enter all of their case file information (online) on the ACS. The NFTLs requested using the ACS are uploaded to the ALS, which generates the Form 668(Y)(c), *Notice of Federal Tax Lien*, and related lien notices and updates the IRS’s primary computer files to indicate that the NFTLs have been filed.

Automated Lien System (ALS) – a comprehensive database that prints the NFTLs, generates lien notices, stores taxpayer information, and documents all lien activity. Lien activities on both ACS and ICS cases are controlled on the ALS by Centralized Lien Operation functions at the Cincinnati Campus.¹ Employees at the Cincinnati Campus process the NFTLs and respond to taxpayer inquiries using the ALS.

Integrated Collection System (ICS) – an IRS computer system with applications designed around each of the main collection tasks such as opening a case, assigning a case, building a case, performing collection activity, and closing a case. The ICS is designed to provide management information, create and maintain case histories, generate documents, and allow online approval of case actions. NFTL requests made using the ICS are uploaded to the ALS. The ALS generates the NFTL and related lien notices and updates the IRS’s primary computer files to indicate the NFTLs have been filed.

Integrated Data Retrieval System (IDRS) – an online data retrieval and data entry system that processes transactions entered from terminals located in campuses and other IRS locations. It enables employees to perform such tasks as researching account information, requesting tax returns, entering collection information, and generating collection documents. The IDRS serves as a link from campuses and other IRS locations to the Master File² for the IRS to maintain accurate records of activity on taxpayers’ accounts.

¹ A campus is 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.

² The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.



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Appendix VII

*Confidence Intervals for Notification of
Taxpayer Representatives Error Rates Reported
During Fiscal Years 2011 Through 2014*

***Two-sided 90 percent confidence intervals using the exact binomial
method for the exception rate for Fiscal Years 2011 through 2014***

Report Fiscal Year	Sample Cases Requiring Representative Notification	Sample Cases Not Receiving Representative Notification	Error Rate	Confidence Interval
2011	30	4	13%	Between 4.70% and 28.00%
2012	22	4	18%	Between 6.48% and 36.90%
2013	47	5	11%	Between 4.28% and 21.10%
2014	**1**	**1**	**1**	*****1*****

Source: Prior year results of TIGTA's tests on the notification of taxpayer representatives.



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Appendix VIII

*Statutory Lien Reports Issued During
Fiscal Years 2010 Through 2014*

TIGTA, Ref. No. 2010-30-072, *Actions Are Needed to Protect Taxpayers' Rights During the Lien Due Process* (Jul. 2010).

TIGTA, Ref. No. 2011-30-051, *Challenges Remain When Processing Undeliverable Mail and Preventing Violations of Taxpayers' Rights During the Lien Due Process* (May 2011).

TIGTA, Ref. No. 2012-30-057, *Problems Persist When Processing Undelivered Lien Notices and Notifying Taxpayers' Representatives* (May 2012).

TIGTA, Ref. No. 2013-30-072, *Fiscal Year 2013 Statutory Review of Compliance With Lien Due Process Procedures* (Jul. 2013).

TIGTA, Ref. No. 2014-30-061, *Fiscal Year 2014 Statutory Review of Compliance With Notice of Federal Tax Lien Due Process Procedures* (Sept. 2014).



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Appendix IX

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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

JUN 03 2015

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

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

SUBJECT: Draft Audit Report – Fiscal Year 2015 Statutory
Review of Compliance With Notice of Federal Tax
Lien Due Process Procedures (Audit# 201530001)

Thank you for the opportunity to review the subject draft report which evaluated whether the IRS is complying with the statutory requirements of notifying taxpayers when a notice of federal tax lien (NFTL) is filed. Section 6320(a) of the Internal Revenue Code requires the IRS to provide written notification to the taxpayer of the filing of a NFTL within five days after the day the NFTL was filed. The notice must include the amount of unpaid tax and it must inform the taxpayer of the right to a hearing, the administrative appeals available, and the procedures relating to the release of liens.

For the third time in the past five years, you found that we fully complied with the statutory requirement of timely notification of taxpayers. This is evidence of the IRS's commitment to protecting taxpayer rights. You also found that, absent a few exceptions, our employees followed the procedures to process undelivered lien notices and provided taxpayer representatives a copy of the notice. In fact, your findings regarding processing of undelivered lien notices showed we improved from prior years' audits by properly documenting research of undelivered NFTLs reviewed and accurately updating accounts with correct transaction and action codes.

We agree with your outcome measure. Attached is a detailed response with our corrective actions to your recommendations. If you have any questions, please contact me, or a member of your staff may contact Scott Prentky, Director, Collection, at (954) 423-7318.

Attachment



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Attachment

RECOMMENDATION 1:

The Director, Collection, Small Business/Self-Employed Division, should establish procedures requiring the lien unit to verify all NFTL requests in which the checkbox on Form 12636, Line 4, is blank.

CORRECTIVE ACTION:

We updated Internal Revenue Manual section 5.19.12.2.1.2 in April 2015 to require the lien unit to verify that Line 4 on Form 12636 has been completed and to specify the actions to be taken if the checkbox is blank.

IMPLEMENTATION DATE:

N/A

RESPONSIBLE OFFICIAL:

N/A

CORRECTIVE ACTION MONITORING PLAN:

N/A

RECOMMENDATION 2:

The Director, Collection, Small Business/Self-Employed Division, should establish IRM procedures to timely research taxpayer accounts if the envelopes of returned lien notices are marked with multiple reasons for return and ensure that the lien notice was mailed to the taxpayer's last known address.

CORRECTIVE ACTION:

We will contact the United States Post Office to request that the proper stamp is placed on the envelope based on data in their files, which should reduce the number of envelopes with multiple stamps. Once the number of envelopes with multiple stamps is reduced, we will select a sample of unclaimed mail to pursue a pilot to test the effectiveness of our address verification research procedures and to ensure that these actions are an efficient and effective use of our limited resources. We will revise our guidance to align with our findings and clarify the procedures as needed.

IMPLEMENTATION DATE:

January 15, 2017

RESPONSIBLE OFFICIAL:

Director, Collection - Quality and Technical Support, Small Business/Self-Employed Division



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2

CORRECTIVE ACTION MONITORING PLAN:

IRS will monitor this corrective action as part of our internal management system of controls.