

# TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



## Procedures Are Needed to Prevent Backdating Penalty Approvals

May 1, 2026

Report Number: 2026-300-021

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

**Why TIGTA Did This Audit**

Internal Revenue Code (I.R.C.) Section (§) 6751 was enacted under the IRS Restructuring and Reform Act of 1998 as a safeguard and requires the IRS to provide taxpayers with an explanation of how penalties are imposed upon them, to ensure that penalties are imposed where appropriate, and to ensure that penalties are not used as a “bargaining chip,” (*i.e.*, as leverage in negotiations during an audit). I.R.C. § 6751(b) requires supervisory approval of certain penalties before their assessment. Without adequate procedures, if manager approval is not timely, managers might be tempted to backdate their approval to make it appear as though the approval was timely under the law.

In *LakePoint Land II, LLC v. Comm’r*, T.C.M. (RIA) 2023-111 (hereafter referred to as *LakePoint*), the Tax Court found that the IRS had backdated the approval of certain penalties and had misrepresented that fact to the court. We assessed the IRS’s compliance with I.R.C. § 6751(b), the extent to which penalty backdating occurs, and whether processes are in place to prevent it.

**Impact on Tax Administration**

The purpose of tax-related penalties is to encourage taxpayer compliance. When IRS supervisors backdate penalty approvals, it undermines confidence in both the fairness of tax administration and the integrity of the IRS. This can make it less likely that taxpayers voluntarily comply with their tax obligations.

**What TIGTA Found**

In August 2023, following the *LakePoint* decision, the IRS and the Office of the Chief Counsel initiated a review of 1,268 cases to assess compliance with I.R.C. § 6751(b). The review focused on a particular type of case involving syndicated conservation easements, a transaction the IRS deems abusive. The section 6751(b) issue in the *LakePoint* case resulted from the failure of employees to follow policies, procedures, and appropriate practices. Additionally, the lack of guidance on how to document penalty changes contributed to the compliance issues in other cases identified in this report.

The review included 829 docketed cases (*i.e.*, pending in Tax Court) and 439 nondocketed cases (*i.e.*, pending administratively with the IRS). The IRS identified 13 docketed cases that did not comply with I.R.C. § 6751(b) due to a lack of valid supervisory approval. Of the 13 cases, 7 involved backdated penalty approvals where the IRS conceded over \$68 million in penalties (*i.e.*, withdrew its position in the taxpayer’s favor). The other six cases involved the addition of an alternative penalty after supervisory approval, and the IRS conceded the unapproved alternative penalty.

We reviewed the 439 nondocketed cases and identified 6 potential exceptions where there was missing documentation that would verify managerial approval was obtained before the summary report was mailed to the taxpayer. We also identified other documentation issues, including multiple versions of penalty lead sheets with identical digital signatures; penalties listed in taxpayer correspondence not documented on an approved lead sheet; and summary reports reflecting penalties without supervisory approval.

The IRS also reviewed the conduct of ■ employees involved in some of the 13 docketed cases that lacked valid supervisory approval. Disciplinary actions ranged from non-disciplinary counseling letters to written reprimands. ■ the IRS lacked clear and consistent internal guidance for when penalties must be approved and how to hold employees accountable at the time.

**What TIGTA Recommended**

We made five recommendations for improvements, including that the IRS should update procedures to align with the regulations and communicate to compliance employees that it is not appropriate to backdate penalty approvals documents and promote the use of digital approvals on all penalty lead sheets and key documents.

IRS management agreed with all five recommendations.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

**U.S. DEPARTMENT OF THE TREASURY**

**WASHINGTON, D.C. 20024**

May 1, 2026

**MEMORANDUM FOR:** COMMISSIONER OF INTERNAL REVENUE

A handwritten signature in black ink that reads "Diana M. Tengesdal".

**FROM:** Diana M. Tengesdal  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – Procedures Are Needed to Prevent Backdating  
Penalty Approvals (Audit No.: 2025300009)

This report presents the results of our review to determine whether penalty approvals complied with the procedural requirements set forth in Internal Revenue Code (I.R.C.) § 6751(b). This review was part of our Fiscal Year 2025 Annual Audit Plan and addresses the major management and performance challenge of *Ensuring Tax Compliance*.

Management's complete response to the draft report is included as Appendix II. 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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## Background

Internal Revenue Code (I.R.C.) Section (§) 6751(b) was enacted as part of the Internal Revenue Service Restructuring and Reform Act of 1998 to provide oversight and accountability when the Internal Revenue Service (IRS) imposes penalties.<sup>1</sup> Section 6751(b) states that no penalty shall be assessed unless the initial determination receives written approval from the immediate supervisor of the individual making the determination (*e.g.*, a revenue agent).<sup>2</sup> Certain penalties are excluded from the supervisor approval requirement, such as failure to file or pay taxes, failure to pay estimated tax, and penalties that are calculated through electronic means.<sup>3</sup>

The supervisory approval requirement was established as a safeguard to provide taxpayers with an explanation of how penalties are imposed upon them, to ensure that penalties are imposed where appropriate, and to ensure that penalties are not used as a “bargaining chip,” (*i.e.*, leverage used during an audit).<sup>4</sup> Although the time frame in which supervisory approval must be given is not clearly specified in § 6751(b), case law and Treasury Regulations provide some guidance. In addition, the Internal Revenue Manual (IRM) requires supervisory approval before issuing any written communication of penalties to the taxpayer that offers the taxpayer an opportunity to sign an agreement or consent to assessment of proposal of the penalty.<sup>5</sup> Without adequate procedures, manager approval may not be timely for various reasons. For example, penalties may be proposed late, after the taxpayer and the IRS have discussed adjustments and penalties. In such cases, managers might be tempted to backdate approval to appear timely under the law.

In *LakePoint Land II, LLC v. Commissioner* (hereafter referred to as *LakePoint*), the Tax Court concluded that an IRS supervisor backdated the approval of certain penalties on a penalty approval lead sheet (*i.e.*, the document used to record decisions on the assertion or nonassertion of penalties) that were proposed to be assessed against the taxpayer. In addition, the court found that IRS Counsel knew or should have known that the representations to the court as to when the supervisor signed the penalty lead sheet were not accurate and that IRS Counsel failed to timely advise the court of the erroneous declaration.<sup>6</sup> Consequently, the court held the IRS subject to monetary sanctions pursuant to I.R.C. § 6673(a)(2) due to conduct that the court deemed unreasonable.

*LakePoint* involved a syndicated conservation easement (SCE) transaction, which the IRS has deemed abusive in nature.<sup>7</sup> The penalties at issue in *LakePoint* included the gross valuation misstatement penalty, among other alternative penalties. Taxpayers are permitted to donate conservation easements to qualified organizations and claim charitable contribution deductions for the value of the contribution. However, the IRS believes the deductions involved in certain

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685.

<sup>2</sup> I.R.C. § 6751(b)(1).

<sup>3</sup> I.R.C. § 6751(b)(2). A penalty is calculated through electronic means if it is proposed by an IRS computer program without human involvement.

<sup>4</sup> S. Rep. No. 105-174, at 65 (1998).

<sup>5</sup> IRM 20.1.1.2.3.1(1) (November 2025).

<sup>6</sup> *LakePoint Land II, LLC v. Comm’r*, T.C.M. (RIA) 2023-111.

<sup>7</sup> See Appendix II for a glossary of terms.

SCE transactions are excessive. As a result, the IRS has taken steps to put taxpayers on notice that certain SCE transactions are going to be closely scrutinized, and over 1,200 SCE transactions were examined and/or litigated.<sup>8</sup>

## Results of Review

### Penalty Approval Documents in Syndicated Conservation Easement Cases Were Backdated, Missing, or Lacked Proper Supervisory Approval

#### **The IRS identified 13 docketed cases that lacked valid supervisory approval**

In August 2023 following the *LakePoint* decision, the IRS and the Office of the Chief Counsel initiated a review of 1,268 cases to assess compliance with I.R.C. § 6751(b). The IRS's review focused on a particular type of case involving SCE, a transaction that the IRS has deemed abusive. According to the IRS, the § 6751(b) issue in *LakePoint* resulted from the failure of employees to follow policies, procedures, and appropriate practices. Additionally, the lack of guidance on how to document penalty changes contributed to the compliance issues in other cases identified in this report.

The IRS's review included 829 docketed (*i.e.*, pending in Tax Court) and 439 nondocketed (*i.e.*, pending administratively in the IRS) cases from the Small Business/Self-Employed (SB/SE) and Large Business and International (LB&I) Divisions. The IRS identified 13 docketed cases that did not comply with § 6751(b) due to a lack of valid supervisory approval, and we agreed with the IRS's assessment of those 13 cases.<sup>9</sup> Of the 13 cases, 7 involved backdated penalty approvals and the IRS conceded over \$68 million in penalties.<sup>10</sup> The other six cases involved the addition of an alternative penalty after supervisory approval of the primary penalty, and the IRS conceded the unapproved alternative penalty. The IRS did not identify any nondocketed SCE cases where the penalty approval documents did not comply with § 6751(b).

#### **Some nondocketed cases had no prior supervisory approval or supporting records**

As a result of the IRS's findings in the 829 docketed cases, we reviewed the 439 nondocketed cases (184 from SB/SE and 255 from LB&I) to assess compliance with I.R.C. § 6751(b). We focused on whether supervisory approval was obtained before issuing written communications of penalties to taxpayers such as summary reports. We found:

- 6 cases where neither we nor the IRS could verify that supervisory approval was obtained before the summary report was mailed to the taxpayer due to missing documentation. In all six, explanatory letters to taxpayers were not included in the case files. According to the IRS, signed copies of these documents are not required to be retained in the case

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<sup>8</sup> IRS Notice 2017-10, *Syndicated Conservation Easement Transactions* (December 2016). There were 1,268 SCE cases selected for examination for Tax Years 2016 through 2021.

<sup>9</sup> Documentation reviewed includes SAIN 011, *Penalty Consideration*, Lead Sheet 300, *Civil Penalty Approval Form*, Form 5701, *Notice of Proposed Adjustment*, email records, review memoranda, activity logs, and delegation orders.

<sup>10</sup> The term concede (or conceded) in this context refers to the IRS withdrawing an asserted position or issue to the taxpayer's favor because its position cannot be sustained under applicable law, facts, or required procedures.

file. However, because the supporting documentation was missing, proper supervisory approval under I.R.C. § 6751(b) cannot be confirmed. If any of these cases were challenged in court, it would be up to the court to determine whether I.R.C. § 6751(b) compliance was satisfied despite the missing documents. In IRS management's response to this report, the IRS asserts that alternative documentation supports compliance with I.R.C. § 6751(b); however, the absence of key documents prevents our verification of supervisory approval timing. While the IRS cites Treasury Regulations and appellate case law, our assessment is based on verifiable documentation. Accordingly, we still consider these cases exceptions, and as noted, if litigated, a court would determine if compliance was satisfied.

- [REDACTED]

Our review of the nondocketed cases also identified:

- [REDACTED]
- [REDACTED]
- [REDACTED]

In addition, we identified five potential violations of I.R.C. § 6103 involving unauthorized disclosures of taxpayer information.<sup>11</sup> These potential disclosure violations included [REDACTED] and including another taxpayer's name and/or Taxpayer Identification Number on correspondence intended for a different taxpayer. One employee self-reported a potential violation to TIGTA in accordance with disclosure guidance. The remaining potential disclosure violations were brought to IRS management's attention for awareness.

The exceptions we identified resulted from a lack of supervisory oversight and systemic weaknesses in documentation practices and internal controls related to the penalty approval process. The IRS risks undermining its enforcement efforts and violating taxpayers' rights by failing to demonstrate supervisory approval of penalties as required by law. These deficiencies compromise the integrity and fairness of the penalty assessment process, expose the IRS to reputational risk and increased legal scrutiny in future court proceedings, and may erode public trust in tax administration and confidence in the IRS's commitment to enforce tax laws consistently and lawfully.

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<sup>11</sup> I.R.C. § 6103 governs the confidentiality and disclosure of tax returns and return information. It generally prohibits the disclosure of such information by federal employees, including IRS personnel, unless specifically authorized by law, to protect taxpayer privacy.

### Digital signatures could help prevent backdating and improve its detection

The Office of the Chief Counsel conducted an internal review and identified issues involving penalty lead sheets that were altered after being digitally signed. This determination was made through analysis of electronic document properties and whether those documents had been modified. The analysis showed that edits were made without the application of a new digital signature. This raises concerns about the authenticity of supervisory approval and whether it was obtained before issuing any written communication of penalties to the taxpayer.

The identification of these alterations contributed to the IRS's decision to concede penalties in 6 of the 13 cases. However, agency policy does not require:

- Secure digital signatures that prevent edits or prompt re-signing.
- Electronic document analysis as part of the penalty approval process.

IRS Counsel initially stated that electronic document analysis is mandatory for all docketed cases. However, instead of including this requirement in the Chief Counsel Directives Manual (CCDM), IRS Counsel issued informal guidance to its employees in November 2023. Further, IRS employees are not required to use digital signatures. When digital signatures are used, they provide the best available evidence of penalty approval. Further, reviewing electronic document properties helps determine whether a penalty approval document is defensible in court. Therefore, not formalizing this requirement may cause inconsistent application across cases and reduces the enforceability of an important safeguard.

This decision highlights the need for stronger procedural controls to improve transparency, accountability, and the integrity of the penalty approval process. The IRS should promote the use of digital approvals and conduct reviews of document properties so they can ensure that supervisory approvals are authentic and not altered after the fact. Digital signatures provide a secure way to verify that a document has not been changed after signing, prevent backdating, and make it easier to detect any unauthorized edits. These steps would also strengthen internal controls by ensuring that approvals are properly documented, safeguarded from alteration, and consistently managed across cases. Given the risk of errors or changes to approval records, IRS Counsel should strongly consider updating the CCDM to address electronic document properties review requirements, so that guidance is clear, consistent, and followed in every case.

The Chief Tax Compliance Officer, should:

**Recommendation 1:** Promote the use of digital approvals on penalty approval documents to enhance record integrity, accountability, and evidentiary reliability.

**Management's Response:** IRS management agreed with this recommendation and will continue to promote the use of digital signatures and other secure electronic approval methods and remind employees in conjunction with Recommendation 4.

**Recommendation 2:** Work with the Commissioners of the SB/SE and LB&I Divisions to review and revise penalty procedures, as needed, to ensure consistency when obtaining and documenting penalty approvals and verifying compliance with I.R.C. § 6751(b) requirements.

**Management's Response:** IRS management agreed with this recommendation. Penalty procedures have been updated to align with I.R.C. § 6751(b) and Treasury Regulation § 301.6751(b)-1, including revisions to IRM 20.1.1.2.3 (November 25, 2025).

The IRS has also implemented enhanced review procedures to verify compliance. The IRS will continue to monitor the effectiveness of these actions and will make and communicate additional revisions, as necessary, to ensure consistent compliance.

The Chief Counsel, should:

**Recommendation 3:** Formalize procedures in the CCDM for Chief Counsel attorneys to require verification of I.R.C. § 6751(b) compliance in all docketed cases, which may include reviewing electronic document properties and corroborating evidence (e.g., case activity records and emails).

**Management's Response:** Chief Counsel agreed with this recommendation and will update the CCDM to require attorneys to verify Section 6751(b) compliance in all docketed cases, which may include reviewing electronic document properties and corroborating evidence.

### Backdating Penalty Approvals Was Caused by a Lack of Clear Guidance

The IRS believed the instances of backdating identified in its review occurred due to the employees' failure to follow policies, procedures, and appropriate practices. The disciplinary inquiries conducted following *LakePoint*, and other similar cases raised questions about whether IRS employees' actions complied with the IRS's procedures for assessing penalties under I.R.C. § 6751(b). The LB&I Division conducted disciplinary reviews for [REDACTED] employees involved in some of the 13 docketed cases that lacked valid supervisory approval. A panel of three IRS executives, who were not involved in the SCE program and did not supervise the employees, recommended disciplinary actions. The Deputy Commissioner of the LB&I Division served as the deciding official.

Disciplinary actions proposed by the IRS ranged from non-disciplinary counseling letters to written reprimands. However, based on the facts identified, several other categories of employee misconduct outlined in the IRS Penalty Guide could have applied, with potential penalties ranging from a written reprimand to a suspension from 5 to 30 days, or removal.<sup>12</sup>

According to the IRS, [REDACTED] it lacked clear and consistent procedures for when penalties must be approved and how to hold employees accountable at the time. The IRS also did not have a policy prohibiting the backdating of penalty approvals, further limiting its ability to hold employees accountable when approval dates were altered.

There have been recent developments as to when supervisory approval of penalties is required. As the National Taxpayer Advocate explained in her legislative recommendation, there is a difference among the courts as to when supervisory approval must be given for a penalty assessment. Some courts allow the IRS to delay supervisory approval anytime up to the assessment of the tax, while other courts require supervisory approval earlier in the examination process.<sup>13</sup> In the National Taxpayer Advocate's view, the earlier that supervisory approval is

<sup>12</sup> The three applicable categories from the IRS Penalty Guide were: Failure to Follow IRS Rules or Procedures; False or Misleading Statements; and Negligence or Carelessness in Carrying Out Duties.

<sup>13</sup> National Taxpayer Advocate, 2024 Purple Book, p. 74.

provided, the less likely that penalties can be used as a “bargaining chip” later in the IRS examination process, which I.R.C. § 6751(b) was intended to discourage.

In 2023, the Department of the Treasury issued proposed regulations. Specifically, for pre-assessment penalties subject to judicial review, the IRS can delay supervisory approval until the issuance of a notice of statutory deficiency. In contrast, for penalties subject to judicial review post-assessment, supervisory approval can occur at any time up to the assessment. While the IRS lacked clear guidance as to when supervisory approval was required, internal procedures were updated to be consistent with these proposed regulations. However, in December 2025, Congress proposed legislation, that if enacted, would amend I.R.C. § 6751(b)(1) to require supervisory approval before any written communication with respect to such penalty (including proposal of a penalty as an adjustment) is provided to the taxpayer.<sup>14</sup> This proposed legislation is consistent with the National Taxpayer Advocate’s recommendation.

Although the IRS updated its internal procedures to clarify when supervisors must approve penalties, its procedures still have not been updated to prohibit the backdating of penalty approvals. The purpose of tax-related penalties is to encourage taxpayer compliance. When IRS supervisors backdate penalty approvals, it creates the appearance that approval was obtained improperly, which can undermine confidence in both the fairness of tax administration and the integrity of the IRS. Since the sole purpose of civil penalties is to enhance voluntary compliance, penalties conceded due to backdating may weaken voluntary compliance. This can make it less likely that taxpayers voluntarily comply with their tax obligations.

**Recommendation 4:** The Commissioners of the Small Business/Self-Employed and Large Business and International Divisions should communicate to compliance employees that it is not appropriate to backdate penalty approvals and penalty approval documents must be dated contemporaneously, remind employees when supervisory approval is required, and provide guidance on how to update signed documents when a change is needed.

**Management’s Response:** IRS management agreed with this recommendation and will issue a memo advising employees that penalty approval documents must be dated contemporaneously and that backdating is not appropriate. The IRS will also remind employees when supervisory approval is required, how to properly update signed documents when a change is needed, and that securing electronic penalty approval is a best practice.

### Operational Reviews Are Not Always Initiated Following Court Identification of Attorney Conduct Issues

The IRS uses operational reviews to evaluate a unit’s performance toward achieving organizational goals and satisfying other legal and administrative requirements. The court in the *LakePoint* case found that the IRS was subject to sanctions for making inaccurate statements and submitting a false declaration. Despite these findings, the IRS did not conduct an operational review to determine how and why the inaccurate statements and false declaration occurred. In contrast, in another SCE case, *Everest Granite*, that was active during the same time in 2023, IRS Counsel faced potential sanctions for delaying litigation but reached an agreement

<sup>14</sup> *Fair and Accountable IRS Reviews Act*, H.R. 5346, 119<sup>th</sup> Cong. § 2 (2025).

with the opposing parties before final sanctions were imposed.<sup>15</sup> [REDACTED]

[REDACTED] The different responses in these two cases, despite both involving serious judicial concerns, highlights the inconsistency in how IRS Counsel uses operational reviews following court identification of attorney conduct issues.

IRS procedures state that operational reviews identify strengths and weaknesses and include corrective and follow-up actions. For these reviews to be effective, they must be applied consistently. However, IRS Counsel has no formal requirement in the CCDM to conduct operational reviews following court sanctions or findings of employee error. This led to varied responses in cases such as *LakePoint* and *Everest Granite*.

Without formal procedures in the CCDM, IRS Counsel's responses to attorney conduct issues rely on individual judgment rather than uniform standards. This inconsistency may increase the risk of repeated mistakes, unaddressed systemic weaknesses, and erosion of public trust in the IRS. Establishing formal procedures will help ensure that operational reviews and corrective actions are applied consistently whenever courts identify attorney conduct issues.

**Recommendation 5:** IRS Chief Counsel should update the CCDM to ensure that Chief Counsel management will direct a review following a court's imposition of sanctions against Chief Counsel.

**Management's Response:** Chief Counsel agreed with this recommendation and will update the CCDM to ensure that Chief Counsel management will direct a review following a court imposition of sanctions against Chief Counsel.

<sup>15</sup> *Everest Granite, LLC et al, v. Comm'r*, Dkt. No. 29477-21. This case did not involve potential noncompliance with IRC § 6751(b).

## Appendix I

### **Detailed Objective, Scope, and Methodology**

The overall objective of this audit was to determine whether penalty approvals comply with the procedural requirements set forth in I.R.C. § 6751(b). To accomplish our objective, we:

- Identified current guidance, procedures, and applicable laws related to procedural requirements of I.R.C § 6751(b) by evaluating the procedures and guidelines outlined in the IRM.
- Determined the effectiveness of the IRS's strategies to ensure compliance with the supervisory approval process by reviewing training materials and programs provided to employees.
- Reviewed the IRS digital approval requirements for field examination employees.
- Conducted a review of the SCE cases reviewed by the IRS starting in August 2023.
- Interviewed IRS Chief Counsel, Appeals Officers, and relevant employees to gather insight on I.R.C. § 6751(b) compliance determinations, criteria used in the determination process, and challenges encountered during reviews.
- Analyzed all docketed exception cases (paper and electronic files) identified by the IRS to evaluate documentation for completeness and accuracy and identify any discrepancies or inconsistencies in the case files.
- Reviewed all nondocketed cases and performed a review of the case files to assess the quality and completeness of documentation.
- Evaluated the consistency of decision-making across the nondocketed population to identify discrepancies in case handling.

#### **Performance of This Review**

This review was performed with information obtained from the LB&I Audit & Legislative Liaison and the Office of the Chief Counsel at IRS National Headquarters located in Washington, D.C. Information was also obtained from an appeals officer located in [REDACTED] California during the period December 2024 through August 2025. 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.

#### **Data Validation Methodology**

We performed tests to assess the reliability of data by verifying the information contained in the documents provided by the IRS matched the corresponding information in IRS systems. Source data were verified using the Issue Management and Correspondence Examination Automation Systems. We also obtained information received in response to information document requests

to confirm the accuracy and completeness of the data. Based on these procedures, we determined the data were sufficiently reliable to this report.

### **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: policies and guidance found in the IRM, the CCDM, and Treasury Regulation § 301.6751(b)-1. We evaluated the different IRM sections by researching them while developing the document requests and, when warranted, followed up with additional questions after reviewing the responses. We evaluated the CCDM by reviewing the sections directly related to I.R.C § 6751(b) and Counsel's role in ensuring compliance with this code section. Finally, we evaluated the application of the comments section of the final regulation to learn that most, if not all, of the comments were not adopted when issuing the final regulation.

## Management's Response to the Draft Report



CHIEF TAX COMPLIANCE OFFICER

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, DC 20224

April 3, 2026

MEMORANDUM FOR DIANA M. TENGESDAL  
DEPUTY INSPECTOR GENERAL FOR AUDIT

**FROM:**

Jarod J. Koopman  
Chief Tax Compliance Officer

Michael K.  
Cockrell

Digitally signed by Michael K.  
Cockrell  
Date: 2026.04.03 13:16:09 -04'07'

**SUBJECT:**

Draft Audit Report – Procedures are Needed to Prevent  
Backdating Penalty Approvals  
(Audit # 2025300009)

Thank you for the opportunity to review and comment on the draft audit report titled *Procedures are Needed to Prevent Backdating Penalty Approvals*. The IRS takes the matters raised in this report seriously and is committed to administering the law with fairness and integrity to all taxpayers. This includes ensuring penalties are asserted and documented in full compliance with section 6751(b). As covered in detail below, the IRS conducted a penalty approval review of over a thousand cases and found proper penalty approval documentation in 99% of the cases reviewed. For the 1% of cases that presented an approval discrepancy, the IRS took immediate corrective actions.

Section 6751 was added to the Internal Revenue Code as part of the IRS Restructuring and Reform Act of 1998 to ensure penalties are only imposed where appropriate and are not used as bargaining chips. Under section 6751(b)(1), the initial determination of certain penalties must be approved in writing by the immediate supervisor of the person making the determination. No penalty subject to section 6751(b)(1) may be assessed if approval is not obtained. No particular form of written approval is required under section 6751(b)(1). Further, the statute does not provide a specific time for securing approval.

In August 2023, the Tax Court identified a penalty approval issue in *Lakepoint Land II, LLC v. Commissioner*, T.C. Memo. 2023-111, a syndicated conservation easement (SCE) case. The IRS immediately undertook a penalty approval review of SCE cases in Examination and docketed in Tax Court to identify any cases lacking proper supervisory approval, determine the cause of the issue, and take corrective actions. The IRS review noted 13 out of the 1,268 cases presented some penalty approval discrepancy. Although this is a small percentage of the cases, the IRS recognizes the seriousness of even one instance of a penalty approval discrepancy.

Through the review of the cases, the IRS identified some commonalities including:

- Application of Multiple Penalties – Some agents were inexperienced in asserting multiple penalties. This led to documentation issues. For example, after securing original managerial approval to assert some penalties, an agent may have determined another penalty applied and may not have understood how to document the additional penalty. Subsequently, issues occurred with the documentation.
- Updating Documents – As the use of digital documents became more prevalent, training was not provided to staff on how to maintain original penalty approval documents and how to update documents if an update was later needed.

Based on the findings, the IRS took multiple corrective actions to address the issues. The IRS:

- Conducted mandatory penalty approval training for examiners, managers, and Chief Counsel attorneys.
- Educated employees on best practices, including:
  - How to properly secure updated managerial approvals, and
  - The use of digital signatures.
- Revised review processes in the IRS and Chief Counsel to ensure penalty approval documentation is appropriate.
- Held penalty workshops.
- Reviewed employee conduct and took appropriate remedial actions.

In 12 out of the 13 docketed cases noted in the TIGTA report, the IRS found that the employee received timely<sup>1</sup> written supervisory approval of the penalties. However, there was at least one document in the case file, typically the penalty lead sheet, on which a

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<sup>1</sup> As previously mentioned, the statute does not provide a time by which a penalty must be approved. A Treasury Regulation, case law, and the IRM each provide timing standards.

Under Treas. Reg. § 301.6751(b)-1(c), penalties that are subject to pre-assessment review in Tax Court must be approved on or before the date on which a pre-assessment notice that provides a basis for Tax Court jurisdiction is mailed.

The Tax Court and five appellate courts that have weighed in on the timeliness issue. The Second and Tenth Circuits require approval no later than the date the IRS issues a notice of deficiency. The Fifth and Ninth Circuits require approval before assessment or, if earlier, before the relevant supervisor loses discretion to approve. The Eleventh Circuit requires approval before assessment of the penalty. Lastly, the Tax Court requires approval before the first formal written communication notifying the taxpayer that Exam has completed its work and made an unequivocal decision to assert penalties.

IRM 20.1.1.2.3.1, *Timing of Supervisory Approval*, provides “[g]enerally, written supervisory approval should be secured as soon as practicable once the initial determination to assess the penalty has been made, and prior to issuing any written communication of penalties to a taxpayer offering them an opportunity to sign an agreement or consent to assessment of a penalty, or sign a consent to proposal of a penalty. However, for penalties assessed on or after December 23, 2024, written supervisory approval must be obtained no later than the timeframe” provided in Treas. Reg. § 301.6751(b)-1.

discrepancy was identified. In the interest of sound tax administration, the IRS elected not to pursue the affected penalties.

In addition, for non-docketed cases, the report notes “6 potential exceptions where there was missing documentation that would verify managerial approval was obtained before the summary report was mailed to the taxpayer.” The IRS disagrees with this finding as there were multiple forms of contemporaneous documentation to support that penalty approval was obtained before the issuance of the summary report, including detailed case activity records, digitally signed internal forms reflecting managerial review and issuance dates, and emails that corroborate the dates and timelines set forth in the other documentation. However, TIGTA only identified these cases as exceptions because a copy of the signed transmittal letter (e.g., Letter 5895, BBA Summary Report Cover Letter) was not in the case file. The signed letter is not required to be maintained in the case file and is not the exclusive way to support the date a report was issued.

In addition, the timing standard TIGTA applied to these six cases is not the standard provided in the Treasury Regulation or appellate case law. In these six cases, the IRS met both the internal timing standard set forth in the IRM as well as the Treasury Regulation standard and the various standards provided in case law.

The IRS remains committed to strengthening documentation practices, reinforcing training, and ensuring penalties are asserted and approved in accordance with the law. We appreciate TIGTA's review and will continue working collaboratively to enhance procedural clarity and ensure legal accuracy.

Attached is our detailed response to the recommendations. If you have any questions, please contact Donnell Lewis, Large Business and International Division.

Attachment

Attachment

**RECOMMENDATION 1:**

The Chief Tax Compliance Officer should promote the use of digital approvals on penalty approval documents to enhance record integrity, accountability, and evidentiary reliability.

**CORRECTIVE ACTION:**

The IRS agrees with this recommendation. The IRS will continue to promote the use of digital signatures and other secure electronic approval methods. The IRS will remind employees of this in conjunction with Recommendation 4.

**RESPONSIBLE OFFICIAL:**

Director, Strategy, Policy and Governance, Large Business and International  
Director, Small Business/Self-Employed Field and Campus Exam Policy

**IMPLEMENTATION DATE:**

December 15, 2026

**CORRECTIVE ACTION MONITORING PLAN:**

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

**RECOMMENDATION 2:**

The Chief Tax Compliance Officer should work with the Commissioners of the SB/SE and LB&I Divisions to review and revise penalty procedures, as needed, to ensure consistency when obtaining and documenting penalty approvals and verifying compliance with I.R.C. § 6751(b) requirements.

**CORRECTIVE ACTION:**

The IRS agrees with this recommendation. The IRS has updated its penalty procedures to ensure alignment with section 6751(b) requirements and Treasury Regulation § 301.6751(b)-1. Specifically, IRM 20.1.1.2.3 was most recently updated on November 25, 2025. In addition, the IRS has implemented enhanced review procedures to verify compliance with section 6751(b). The IRS will continue to monitor the effectiveness of these procedures and will evaluate whether further revisions are necessary. Any additional changes will be communicated to employees as appropriate to ensure continued compliance and consistency.

**RESPONSIBLE OFFICIAL:**

Director, Strategy, Policy and Governance, Large Business and International  
Director, Small Business/Self-Employed Field and Campus Exam Policy

**IMPLEMENTATION DATE:**

Implemented

**CORRECTIVE ACTION MONITORING PLAN:**

N/A

**RECOMMENDATION 3:**

The Chief Counsel should formalize procedures in the CCDM for Chief Counsel attorneys to require verification of I.R.C. § 6751(b) compliance in all docketed cases, which may include reviewing electronic document properties and corroborating evidence (e.g., case activity records and emails).

**CORRECTIVE ACTION:**

Chief Counsel agrees with the recommendation and will include the following language in the CCDM: Chief Counsel attorneys are required to verify section 6751(b) compliance in all docketed cases, which may include reviewing electronic document properties and corroborating evidence (e.g., case activity records and emails).

**RESPONSIBLE OFFICIAL:**

Associate Chief Counsel, Procedure and Administration.

**IMPLEMENTATION DATE:**

December 15, 2026

**CORRECTIVE ACTION MONITORING PLAN:**

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

**RECOMMENDATION 4:**

The Commissioners of the Small Business/Self-Employed and the Large Business and International Divisions should communicate to compliance employees that it is not appropriate to backdate penalty approvals and penalty approval documents must be dated contemporaneously, remind employees when supervisory approval is required, and provide guidance on how to properly update signed documents when a change is needed

**CORRECTIVE ACTION:**

The IRS agrees with this recommendation. LB&I and SB/SE will issue a memo advising employees that penalty approval documents must be dated contemporaneously and that backdating is not appropriate. In addition, we will remind employees when supervisory approval is required and how to properly update signed documents when a change is needed. We will also address Recommendation 1 and remind employees that it is a best practice to secure electronic approval of the penalties.

**RESPONSIBLE OFFICIAL:**

Director, Strategy, Policy and Governance, Large Business and International

Director, Small Business/Self-Employed Field and Campus Exam Policy

**IMPLEMENTATION DATE:**

December 15, 2026

**CORRECTIVE ACTION MONITORING PLAN:**

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

**RECOMMENDATION 5:**

IRS Chief Counsel should update the CCDM to ensure that Chief Counsel management will direct a review following a court imposition of sanctions against Chief Counsel.

**CORRECTIVE ACTION:**

Chief Counsel agrees with this recommendation and will update the CCDM to ensure that Chief Counsel management will direct a review following a court imposition of sanctions against Chief Counsel.

**RESPONSIBLE OFFICIAL:**

Associate Chief Counsel, Procedure and Administration.

**IMPLEMENTATION DATE:**

December 15, 2026

**CORRECTIVE ACTION MONITORING PLAN:**

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

**Glossary of Terms**

<b>Term</b>	<b>Definition</b>
Correspondence Examination Automation System	A database used in the examination process to compute proposed tax adjustments, interest, and penalties.
Form 5701	Notice of Proposed Adjustment.
Issue Management System	The LB&I Division’s computerized case management system. It captures information from audits, such as the type of examination issues pursued and the amounts and reasons for adjustments.
Lead Sheet 300	An internal document used by the SB/SE Division to determine whether to proceed with penalties for the tax return under examination and includes a section for nonassertion of the substantial understatement penalty.
Non-disciplinary letters	A written memorandum documenting employee counseling on an identified issue, clarifying expectations, and reinforcing conduct or performance standards. It does not constitute formal discipline and is intended to prevent recurrence.
SAIN 011	An internal document used by the LB&I Division to approve penalty assertions and for the nonassertion of a substantial understatement penalty when it is statutorily applicable under I.R.C. § 6662(d). It is also used for the nonassertion of the erroneous claim for refund or credit penalty when a substantial portion of the claim for refund or credit is disallowed.
Syndicated Conservation Easement Transactions	An investment arrangement where multiple investors, often through a partnership or S corporation, acquire real property and donate a conservation easement (or fee simple interest) to a qualified charitable organization for conservation purposes, with investors receiving charitable contribution deductions that reduce their tax liabilities.

## **Abbreviations**

CCDM	Chief Counsel Directives Manual
I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
LB&I	Large Business and International Division
SB/SE	Small Business/Self-Employed Division
SCE	Syndicated Conservation Easement
TIGTA	Treasury Inspector General for Tax Administration



**To report fraud, waste, or abuse,  
contact our hotline on the web at  
<https://www.tigta.gov/reportcrime-misconduct>.**

**To make suggestions to improve IRS policies, processes, or systems  
affecting taxpayers, contact us at  
[TIGTACommunications@tigta.treas.gov](mailto:TIGTACommunications@tigta.treas.gov).**

Information you provide is confidential, and you may remain anonymous.