



*Fiscal Year 2007 Statutory Audit of
Compliance With Legal Guidelines
Prohibiting the Use of Illegal Tax Protester
and Similar Designations*

July 3, 2007

Reference Number: 2007-40-112

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

Phone Number | 202-927-7037

Email Address | Bonnie.Heald@tigta.treas.gov

Web Site | <http://www.tigta.gov>



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

July 3, 2007

MEMORANDUM FOR DEPUTY COMMISSIONER FOR SERVICES AND
ENFORCEMENT
DEPUTY COMMISSIONER FOR OPERATIONS SUPPORT

FROM: (for) Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Fiscal Year 2007 Statutory Audit of Compliance
With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations (Audit # 200740006)

This report presents the results of our review to determine whether the Internal Revenue Service (IRS) complied with IRS Restructuring and Reform Act of 1998 (RRA 98)¹ Section (§) 3707 and its own internal guidelines that prohibit IRS officers and employees from referring to taxpayers as Illegal Tax Protesters (hereafter referred to as ITP or Protester) or any similar designations.

Impact on the Taxpayer

Congress enacted RRA 98 § 3707 to prohibit the IRS from labeling taxpayers as ITPs or any similar designations. While the IRS has eliminated most such references, there are still some instances in which IRS employees refer to taxpayers as Protesters or similar designations in case narratives, which may stigmatize taxpayers and cause employee bias in future contacts with these taxpayers.

Synopsis

Prior to enactment of the RRA 98, taxpayers could be designated as ITPs if their tax returns or correspondence contained specific indicators of noncompliance with the tax law, such as the use of arguments that had been repeatedly rejected by the courts. Once taxpayers' accounts were

¹ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

coded with ITP indicators, certain tax enforcement actions were accelerated. The designation was also intended to alert employees to be cautious so they would not be drawn into confrontations with taxpayers. RRA 98 prohibits the IRS from using ITP or any similar designations. The Treasury Inspector General for Tax Administration is required to annually evaluate compliance with this prohibition.²

The IRS has not reintroduced past ITP codes on the Master File,³ and formerly coded taxpayer accounts have not been assigned similar Master File designations. In addition, the IRS does not have any current publications with Protester references and has removed the one remaining reference from the Internal Revenue Manual.⁴ There were some references in case files. In 601 instances out of approximately 49.6 million records and cases, IRS employees referred to taxpayers as ITPs or other similar designations in case narratives.

Our Fiscal Year 2002 report noted employees were still using ITP or similar designations in their case narratives and recommended management reinforce that taxpayers should not be referred to as Protesters or similar designations and consult with the IRS Office of Chief Counsel on the use of these designations.⁵ In August 2002, the IRS responded that it had requested guidance from its Office of Chief Counsel regarding the designations. Once guidance was received, a memorandum was to be issued to all employees reinforcing the importance of not referring to taxpayers as Protesters. However, the Office of Chief Counsel did not agree that employee use of ITP or a similar designation in a case narrative was a potential violation of the law. We are in disagreement with IRS management over this issue and will continue to report these instances of employees using Protester or similar designations in their case narratives. We continue to believe the use of ITP or other similar designations in case narratives may stigmatize taxpayers and cause employee bias in future contacts with these taxpayers. Electronic case narratives are available to other IRS employees for future reference and may affect the opinions and actions of employees working the taxpayers' cases.

In some instances, IRS employees referred to taxpayers as ITPs and similar designations in case narratives.

Notwithstanding their disagreement with our interpretation of the law, IRS management advised us they have taken a conservative approach by implementing a policy that prohibits employees from using Protester or any similar designations. In addition, they stated they will issue a memorandum to all employees concerning this policy within the next few months.

² Internal Revenue Code § 7803(d)(1)(A)(v) (2000 Suppl. 2).

³ A database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

⁴ A manual containing the IRS' internal guidelines.

⁵ *Efforts Are Still Needed to Discourage the Use of Illegal Tax Protester and Similar Designations* (Reference Number 2002-40-162, dated September 2002).



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Response

We made no recommendations in this report. In their response to the draft report, IRS management disagreed that the references listed in the report are violations. However, because they understand our concern with the use of “tax protester” in case narratives, they will issue a memorandum to all employees to reinforce compliance with RRA 98 § 3707. Management’s complete response to the draft report is included as Appendix V.

Copies of this report are also being sent to the IRS managers affected by the report results. Please contact me at (202) 622-6510 if you have questions or Michael E. McKenney, Assistant Inspector General for Audit (Wage and Investment Income Programs), at (202) 622-5916.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Table of Contents

BackgroundPage 1

Results of ReviewPage 3

 Illegal Tax Protester Codes Were Not Used on the
 Master FilePage 3

 Internal Revenue Service Publications Do Not Contain
 Illegal Tax Protester ReferencesPage 3

 Illegal Tax Protester References Have Been Removed
 From the Internal Revenue ManualPage 4

 In Some Instances, Employees Used Illegal Tax Protester
 or Similar Designations in Case NarrativesPage 5

 Alternative Methods That Avoid the Need for Illegal
 Tax Protester Designations Have Been Established to Address
 Tax Compliance IssuesPage 8

Appendices

 Appendix I – Detailed Objective, Scope, and MethodologyPage 10

 Appendix II – Major Contributors to This ReportPage 13

 Appendix III – Report Distribution ListPage 14

 Appendix IV – Outcome Measures.....Page 15

 Appendix V – Management’s Response to the Draft ReportPage 17



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Abbreviations

IRM	Internal Revenue Manual
IRS	Internal Revenue Service
ITP	Illegal Tax Protester
RRA 98	Internal Revenue Service Restructuring and Reform Act of 1998
SERP	Servicewide Electronic Research Program



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Background

Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)¹ Section (§) 3707 prohibits the IRS from using Illegal Tax Protester (hereafter referred to as ITP or Protester) or any similar designations. In addition, the law requires the removal of all existing Protester codes from the Master File² and instructs IRS employees to disregard any such designation not located on the Individual Master File.³

Prior to enactment of the RRA 98, the IRS used the ITP Program to identify individuals and businesses using methods that were not legally valid to protest the tax laws. Employees identified taxpayers for referral to the Program when their tax returns or correspondence contained specific indicators of noncompliance with the tax law, such as the use of arguments that had been repeatedly rejected by the courts. There were tax protester coordinators who were responsible for determining whether a taxpayer should be included in the ITP Program. If a taxpayer was classified as a Protester, the taxpayer's record was coded as such on the Master File. Once a taxpayer's account was coded, certain tax enforcement actions were accelerated. The designation was also intended to alert employees to be cautious so they would not be drawn into confrontations with taxpayers.

Congress was concerned that some taxpayers were being permanently labeled and stigmatized by the ITP designation. There were many instances of taxpayers who subsequently complied with the tax laws but continued to be labeled as Protesters. The concern was that this label could bias IRS employees and result in unfair treatment.

Internal Revenue Code § 7803(d)(1)(A)(v) (2000 Suppl. 2) requires the Treasury Inspector General for Tax Administration to annually evaluate compliance with the prohibition against using the ITP or any similar designations. This is our ninth review since Fiscal Year 1999. These reviews have identified areas for improvement to help the IRS comply with the Protester designation prohibition.

The Treasury Inspector General for Tax Administration is required to annually evaluate IRS compliance with the prohibition against using ITP or any similar designations.

This review was performed in the National Taxpayer Advocate function and Office of Chief Counsel in Washington, D.C.; the Small Business/Self-Employed Division in

¹ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

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

³ A database that maintains transactions or records of individual tax accounts.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

New Carrollton, Maryland; and the Wage and Investment Division in Atlanta, Georgia, during the period August 2006 through March 2007. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Results of Review

Illegal Tax Protester Codes Were Not Used on the Master File

Prior to enactment of the RRA 98, the IRS used ITP indicators on the Master File to accelerate collection activity for taxpayers who were delinquent in filing tax returns or paying their taxes. These indicators were also intended to alert employees that there might be problems encountered when dealing with these types of taxpayers.

Congress was concerned about the use of the ITP designation because:

- Taxpayers were labeled as Protesters without regard to their filing obligations or compliance.
- Protester indicators were not always reversed when taxpayers became compliant with their tax obligations.

RRA 98 § 3707 required the IRS to remove the existing Protester designations from taxpayers' accounts on the Master File beginning January 1, 1999.

In prior reviews, we reported the IRS had removed the ITP codes from the Master File as required by the law. Based on our analysis of approximately 1.2 million taxpayer accounts coded for accelerated collection activity, the IRS has not reintroduced these Protester designation codes on the Master File. The law also prohibits using any designation similar to ITP. We reviewed approximately 57,000 taxpayer accounts formerly coded as Protesters on the Master File and confirmed that the IRS had not input any other Master File designations similar to ITP on these accounts.

Internal Revenue Service Publications Do Not Contain Illegal Tax Protester References

To help promote compliance with RRA 98 § 3707, IRS management issued directives for employees to update various publications to eliminate references to ITP terminology and programs. Our reviews prior to Fiscal Year 2002 identified several publications that contained Protester references. When notified of the problem, the IRS had either revised the publication



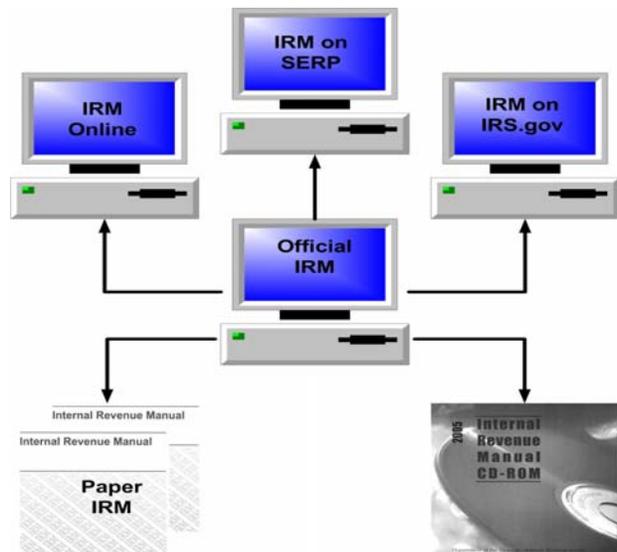


Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

or labeled it as being obsolete. Our review of available publications on the Servicewide Electronic Research Program (SERP),⁴ IRS public Internet web site (IRS.gov), Electronic Publishing web site, and 2005 Federal Tax Products CD-ROM did not identify any current Protester references. By eliminating the Protester references from its forms, documents, letters, and training materials, the IRS prevents employees from using or following these outdated references or guidelines.

Illegal Tax Protester References Have Been Removed From the Internal Revenue Manual

In each of our eight prior reviews, we identified ITP references throughout the various electronic and paper formats of the Internal Revenue Manual (IRM),⁵ the Electronic Publishing web site, the IRM online, the SERP, IRS.gov, CD-ROM, and the paper IRM. The graphic to the right shows the relationship between the Official IRM and the various formats of it available to IRS employees.



During our Fiscal Year 2006 review, we reported there was still one unique ITP reference throughout the various formats of the IRM.⁶ This reference had been previously identified and brought to the attention of Small Business/Self-Employed Division management during our Fiscal Year 2005 review.⁷ In response to both reports, the IRS stated it had initiated actions to remove this last remaining Protester reference.

We again found the ITP reference in our current review and brought it to the attention of Small Business/Self-Employed Division management, who immediately removed it from the IRM. Removing all Protester references from the IRM will help avoid any inappropriate implication that the use of this designation is permitted.

⁴ An electronic researching tool containing many former paper research applications (e.g., publications, the Internal Revenue Manual, the Probe and Response Guide).

⁵ A manual containing the IRS' internal guidelines.

⁶ *Fiscal Year 2006 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Reference Number 2006-40-098, dated July 13, 2006).

⁷ *Fiscal Year 2005 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Reference Number 2005-40-104, dated July 2005).



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

In Some Instances, Employees Used Illegal Tax Protester or Similar Designations in Case Narratives

We found that, out of approximately 49.6 million records and cases, there were 601 instances in which employees had referred to taxpayers as “tax protester,” “ITP,” “constitutionally challenged,” or other similar designations in case narratives on the following computer systems.

- Automated Collection System:⁸ A review of approximately 2.6 million open cases identified 5 cases in which 4 employees used ITP or a similar designation when referring to specific taxpayers in the case narratives.
- Desktop Integration:⁹ A review of approximately 46.3 million open records identified 278 cases in which 171 employees used ITP or a similar designation when referring to specific taxpayers in the case narratives.
- Integrated Collection System:¹⁰ A review of approximately 563,000 open cases identified 292 cases in which 251 employees used ITP or a similar designation when referring to specific taxpayers in the case narratives.
- Taxpayer Advocate Management Information System:¹¹ A review of approximately 49,000 open cases identified 4 cases in which 4 employees used ITP or a similar designation when referring to specific taxpayers in the case narratives.¹²
- Taxpayer Information File:¹³ A review of approximately 110,000 open records identified 22 cases in which 19 employees used ITP or a similar designation when referring to specific taxpayers in the Activity Code field.

We believe these references are prohibited by law. Figure 1 contains the number of ITP or similar designations identified in computer system case narratives or the Activity Code field during our Fiscal Years 2006 and 2007 reviews.

⁸ A telephone contact system through which telephone assistants collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.

⁹ Provides employees access to multiple IRS systems through their computers and allows for inventory management, case delivery, history narratives, print-to-fax capabilities for sending information to taxpayers, and electronic referral generation.

¹⁰ A computerized system used by Collection function employees to report taxpayer case time and activity.

¹¹ An electronic database and inventory control system used by Taxpayer Advocate Service employees.

¹² Due to some anomalies in the records provided by the IRS, any of our conclusions or opinions based on these data are qualified. More information on this qualification can be found in Appendix I.

¹³ Provides tax account information for taxpayers selected for the Integrated Data Retrieval System (the IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer’s account records).



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Figure 1: ITP and Similar Designations in Case Narratives

Computer System	Fiscal Year 2006			Fiscal Year 2007		
	Employees Involved	Protester Designation Used	Similar Designation Used	Employees Involved	Protester Designation Used	Similar Designation Used
Automated Collection System	18	16	5	4		
Desktop Integration ¹⁴	N/A	N/A	N/A	171	225	53
Integrated Collection System	211	102	151	251	132	160
Taxpayer Advocate Management Information System				4		
Taxpayer Information File ¹⁵	N/A	N/A	N/A	19		

Source: Case narratives found on various IRS computer systems, the Activity Code field of the Taxpayer Information File, and the Treasury Inspector General for Tax Administration report entitled Fiscal Year 2006 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations (Reference Number 2006-40-098, dated July 13, 2006). N/A = not applicable.

We also identified 111 case narratives in which employees made references about the taxpayers' actions [REDACTED]

[REDACTED] We agree with the IRS that merely making references to a taxpayer's actions does not constitute a designation prohibited by statute. However, we are concerned these references could become, or be considered, permanent labels that could subsequently stigmatize taxpayers in future contacts with the IRS. We did not include any instances in which employees were only documenting statements made by a taxpayer and/or his or her representative. Quoting a taxpayer's self-designation as a Protester is not prohibited by the law.

¹⁴ Fiscal Year 2007 is the first year we analyzed Desktop Integration during our review.

¹⁵ This is the first time we analyzed the Taxpayer Information File as a followup to our Fiscal Year 2004 review.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Our Fiscal Year 2002 report noted IRS employees were still using ITP or similar designations in their case narratives and recommended management reinforce that taxpayers should not be referred to as Protesters or similar designations and consult with the IRS Office of Chief Counsel on the use of these designations.¹⁶ In August 2002, the IRS responded that it had requested guidance from its Office of Chief Counsel regarding the designations. Once guidance was received, a memorandum was to be issued to all employees reinforcing the importance of not referring to taxpayers as Protesters. However, the Office of Chief Counsel did not agree that employee use of ITP or a similar designation in a case narrative was a potential violation of the law. We are in disagreement with IRS management over this issue and will continue to report these instances of employees using Protester or similar designations in their case narratives.

The statute states that officers and employees of the IRS shall not designate taxpayers as ITPs or any similar designations. It further specifies that existing designations in the Master File must be removed and any other designations made before the effective date of the statute, such as those on paper records that have been archived, must be disregarded. *Senate Committee on Finance Report 105-174* (dated April 22, 1998), related to the RRA 98 § 3707 provision, stated the Committee was concerned that taxpayers might be stigmatized by a designation as an “illegal tax protester.” Based upon the language of the statute and the Senate Committee Report, we believe IRS officers and employees should not label taxpayers as Protesters or similar designations in any records, which include paper and electronic case files. Officers and employees should not designate taxpayers as such because a designation alone contains a negative connotation and appears to label the taxpayer. Given the continued use of these terms by employees, we believe the IRS should reinforce to all its employees the importance of not referring to taxpayers as Protesters or similar designations.

Despite its disagreement with our position on the matter, the IRS has taken some actions to prevent ITP and similar designations from being used in case narratives. On October 11, 2002, it issued an alert,¹⁷ reminding employees of the prohibition regarding the use of Protester or any similar designations in case narratives. Some business units continue to remind employees of the prohibition regarding the use of Protester or any similar designations. For example, the Wage and Investment Division conducts periodic quality reviews for ITP use in its Automated Collection System function and counsels employees who designate taxpayers as Protesters or other similar designations. In addition, the Small Business/Self-Employed Division issued an alert on May 6, 2005, reminding the employees in its Compliance service functions to refrain from using Protester or any similar designations in case narratives. In December 2006, the Small Business/Self-Employed Division Director of Collection Policy issued a memorandum to all Collection Compliance Field Operations employees advising them to stop using Protester and similar designations in any documentation and/or oral communications.

¹⁶ *Efforts Are Still Needed to Discourage the Use of Illegal Tax Protester and Similar Designations* (Reference Number 2002-40-162, dated September 2002).

¹⁷ Only those employees that use the SERP would have had access to this alert.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

In response to the recommendation in our Fiscal Year 2006 report, IRS management stated they would issue a memorandum by June 15, 2007, to all employees to reinforce compliance with RRA 98 § 3707.¹⁸ In addition, management stated they would work with Treasury Inspector General for Tax Administration management to reconcile differences regarding the IRS' legal guidance and take actions as appropriate. We contacted IRS management to determine what actions have been taken by them to resolve this issue. Management responded that, even though they continue to disagree with our interpretation of the law, they have taken a conservative approach by implementing a policy that prohibits employees from using Protester or any similar designations. In addition, they stated that they are on track to issue a memorandum to all employees concerning this policy within the next few months.

Alternative Methods That Avoid the Need for Illegal Tax Protester Designations Have Been Established to Address Tax Compliance Issues

IRS tax compliance operations have not been significantly affected by the prohibition against using ITP or similar designations because alternative programs exist to address issues previously handled by the ITP Program. These include:

- The Frivolous Return Program, which handles taxpayers who file tax returns based on some type of frivolous argument that justifies payment of little or no income tax. This would include filing a tax return claiming no income because paying taxes is voluntary, claiming to be a citizen of a State but not a citizen of the United States, etc.
- The Nonfiler Program, which handles taxpayers that refuse to file their required tax returns.
- The Potentially Dangerous Taxpayer/Caution Upon Contact Program, which handles taxpayers that have assaulted and/or threatened IRS employees.

Each of these Programs is set up to address various issues IRS employees may encounter when dealing with taxpayers protesting the legality of paying their income taxes. Unlike the former ITP Program, each of the new Programs addresses a specific taxpayer behavior. In addition, taxpayers are not assigned to these individual Programs on a permanent basis, as was the case in the ITP Program.

¹⁸ *Fiscal Year 2006 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Reference Number 2006-40-098, dated July 13, 2006).



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Our reviews over the past 8 years have not identified instances in which the ITP indicator was needed on a taxpayer's account to either accelerate tax enforcement actions and/or alert IRS employees to be cautious when dealing with the taxpayer. Management has also advised us that prohibiting the use of the ITP designation has had no negative impact on collection or examination activities.

Management's Response: IRS management disagreed that the references listed in the report are violations. However, because they understand our concern with the use of "tax protester" in case narratives, they will issue a memorandum to all employees to reinforce compliance with RRA 98 § 3707.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Appendix I

Detailed Objective, Scope, and Methodology

The objective of this review was to determine whether the IRS complied with RRA 98¹ Section (§) 3707 and its own internal guidelines that prohibit IRS officers and employees from referring to taxpayers as ITPs (also referred to as Protester) or any similar designations. The Treasury Inspector General for Tax Administration is required to annually evaluate compliance with the prohibition against using ITP or any similar designations.² Unless otherwise noted, our limited tests of the reliability of data obtained from various IRS systems did not identify any errors. We tested the reliability of the data by scanning the data received for blank, incomplete, illogical, or improper data. In addition, we traced a judgmental sample for each data set to the source IRS files to ensure accuracy. We did not perform any testing of internal controls over the systems that were the sources of our data. To accomplish the objective, we:

- I. Determined if the ITP coding on the Master File³ was removed by reviewing all Accelerated Issuance Codes (Transaction Code 148) as of September 2006 for Business Master File⁴ records and Individual Master File⁵ records. We analyzed 179,900 Business Master File records and 1,033,525 Individual Master File records containing a Transaction Code 148 on the account.

We also compared our historic computer extract of approximately 57,000 taxpayers designated as Protesters before the RRA 98 was enacted to our records with a Transaction Code 148 to determine if any new common codes were being used to classify the taxpayers as Protesters.

- II. Determined if the IRM⁶ contained ITP or any similar designations by performing key word searches of the IRS Electronic Publishing web site, the IRM online, the SERP,⁷ IRS.gov, CD-ROM, and the paper IRM.

¹ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

² Internal Revenue Code § 7803(d)(1)(A)(v) (2000 Suppl. 2).

³ A database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

⁴ A database that consists of Federal tax-related transactions and accounts for businesses. These include employment taxes, income taxes on businesses, and excise taxes.

⁵ A database that maintains transactions or records of individual tax accounts.

⁶ A manual containing the IRS' internal guidelines.

⁷ An electronic researching tool containing many former paper research applications (e.g., publications, the IRM, the Probe and Response Guide).



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

- III. Determined if IRS publications contained ITP or any similar designations by performing key word searches of the SERP, IRS.gov, the IRS Electronic Publishing web site, and the IRS 2005 Federal Tax Products CD-ROM in October 2006.
- IV. Determined if employees were using ITP or any similar designations within taxpayer case narratives on the Integrated Collection System⁸ by securing a copy of the database and analyzing approximately 563,000 cases open as of October 2006 with history action dates between October 2005 and September 2006.
- V. Determined if employees were using ITP or any similar designations within taxpayer case narratives on the Automated Collection System⁹ by securing a copy of the database¹⁰ and analyzing 2,618,670 cases open as of October 2006 with history action dates between October 2005 and September 2006.
- VI. Determined if employees were using ITP or any similar designations within taxpayer case narratives on the Taxpayer Advocate Management Information System¹¹ by securing a copy of the database and analyzing 48,513 open cases with activity between October 2005 and September 2006.

During our limited validation of the Taxpayer Advocate Management Information System data, we found some anomalies in the records provided to us. While we are confident that we received all of the requested records, text information in some of the data is missing. Based on discussions with the IRS programmers, we determined these anomalies could not be easily corrected within the time period of our review. As a result, any Treasury Inspector General for Tax Administration conclusions/opinions based on these data are qualified.

- VII. Determined if employees were using ITP or any similar designations within the taxpayer case narratives on Desktop Integration¹² by securing a copy of the database and analyzing 46,282,566 open records with activity between October 2005 and September 2006.

⁸ A system used by Collection function employees to report taxpayer case time and activity.

⁹ A telephone contact system through which telephone assistants collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.

¹⁰ The Automated Collection System database did not always contain employee identifying information from which we could determine the number of employees using ITP or a similar designation. We assumed each comment was made by a different employee.

¹¹ An electronic database and inventory control system used by Taxpayer Advocate Service employees.

¹² Provides employees access to multiple IRS systems through their computers and allows for inventory management, case delivery, history narratives, print-to-fax capabilities for sending information to taxpayers, and electronic referral generation.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

- VIII. Determined if employees were using ITP or any similar designations within the Activity Code field on the Taxpayer Information File¹³ by securing a copy of the database and analyzing 109,877 open records with activity between October 2005 and September 2006.
- IX. Determined if the IRS is using any Frivolous Return Program¹⁴ codes as replacements for ITP designations by reviewing guidance provided for the Frivolous Return Program and interviewing its Program Coordinator.
- X. Determined if the IRS Nonfiler Program¹⁵ is in compliance with the provisions established by RRA 98 § 3707(b) by reviewing guidance provided for the Nonfiler Program and interviewing its Program Coordinator.
- XI. Determined if there is any relationship between ITP designations and Potentially Dangerous Taxpayer/Caution Upon Contact indicator use on the Master File by reviewing guidance provided for the Potentially Dangerous Taxpayer/Caution Upon Contact Program¹⁶ and interviewing its Program Coordinator.
- XII. Determined the current status of IRS corrective actions resulting from prior Treasury Inspector General for Tax Administration audits.

¹³ Provides tax account information for taxpayers selected for the Integrated Data Retrieval System (the IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records).

¹⁴ The Frivolous Return Program handles taxpayers who file tax returns based on some type of frivolous argument that justifies payment of little or no income tax. This would include filing a tax return claiming no income because paying taxes is voluntary, claiming to be a citizen of a State but not a citizen of the United States, etc.

¹⁵ The Nonfiler Program handles taxpayers that refuse to file their required tax returns.

¹⁶ The Potentially Dangerous Taxpayer/Caution Upon Contact Program handles taxpayers that have assaulted and/or threatened IRS employees.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Appendix II

Major Contributors to This Report

Michael E. McKenney, Assistant Inspector General for Audit (Wage and Investment Income Programs)

Mary V. Baker, Director

Bryce Kisler, Director (Acting)

Alan Lund, Audit Manager (Acting)

David Hartman, Lead Auditor

Craig Pelletier, Auditor

Sylvia Sloan-Copeland, Auditor



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Appendix III

Report Distribution List

Acting Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Department of the Treasury, Director, Office of Accounting and Internal Control MDA
Department of the Treasury, Assistant Director, Office of Accounting and Internal Control MDA
Commissioner, Small Business/Self-Employed Division SE:S
Commissioner, Wage and Investment Division SE:W
Chief Counsel CC
National Taxpayer Advocate TA
Chief Information Officer OS:CIO
Office of Internal Control OS:CFO:CPIC:IC
Director, Communications and Liaison, National Taxpayer Advocate TA:CCL
Director, Office of Research, Analysis, and Statistics RAS
Director, Office of Servicewide Policy, Directives, and Electronic Research RAS:SPDER
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Communications, Liaison, and Disclosure, Small Business/Self-Employed Division SE:S:CLD
Director, Compliance, Wage and Investment Division SE:W:CP
Director, Strategy and Finance, Wage and Investment Division SE:W:S
Chief, Performance Improvement, Wage and Investment Division SE:W:S:PI
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaisons:
GAO/TIGTA Liaison, Deputy Commissioner for Operations Support OS
GAO/TIGTA Liaison, Deputy Commissioner for Services and Enforcement SE
GAO/TIGTA Liaison, National Taxpayer Advocate TA
GAO/TIGTA Liaison, Chief Information Officer OS:CIO:SM:PO
Chief, GAO/TIGTA/Legislative Implementation Branch SE:S:CLD:PSP:GTL
Senior Operations Advisor, Wage and Investment Division SE:W:S



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. While no recommendations were made in this report, the Treasury Inspector General for Tax Administration has made prior recommendations that continue to provide benefits. These benefits will be incorporated into our Semiannual Report to Congress.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Actual; 601 taxpayers potentially affected (see page 5).

Methodology Used to Measure the Reported Benefit:

We reviewed:

- From the Automated Collection System,¹ approximately 2.6 million cases open as of October 2006 from a database with history action dates between October 2005 and September 2006 and identified 5 taxpayer case narratives that contained ITP or a similar designation.
- From Desktop Integration,² approximately 46.3 million open records with history action dates between October 2005 and September 2006 and identified 278 taxpayer case narratives that contained ITP or a similar designation.
- From the Integrated Collection System,³ approximately 563,000 cases open as of October 2006 with history action dates between October 2005 and September 2006 and identified 292 taxpayer case narratives that contained ITP or a similar designation.
- From the Taxpayer Advocate Management Information System,⁴ a total of 48,513 open cases with history action dates between October 2005 and September 2006 and identified 4 taxpayer case narratives that contained ITP or a similar designation.

¹ A telephone contact system through which telephone assistants collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.

² Provides employees access to multiple IRS systems through their computers and allows for inventory management, case delivery, history narratives, print-to-fax capabilities for sending information to taxpayers, and electronic referral generation.

³ A system used by Collection function employees to report taxpayer case time and activity.

⁴ An electronic database and inventory control system used by Taxpayer Advocate Service employees.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

- From the Taxpayer Information File,⁵ a total of 109,877 open records with history action dates between October 2005 and September 2006 and identified 22 taxpayer accounts that contained ITP or a similar designation in the Activity Code field.

Type and Value of Outcome Measure:

- Reliability of Information – Actual; one unique ITP reference in the IRM⁶ (see page 4).

Methodology Used to Measure the Reported Benefit:

We searched the various formats of the IRM available to IRS employees for ITP references. As of February 2007, one unique ITP reference was still in the IRM. This reference had been identified and brought to the attention of IRS management during our previous two audits.

⁵ Provides tax account information for taxpayers selected for the Integrated Data Retrieval System (the IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records).

⁶ A manual containing the IRS' internal guidelines.



Fiscal Year 2007 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Appendix V

Management's Response to the Draft Report

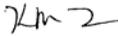


DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D. C. 20224

June 8, 2007

RECEIVED
JUN 11 2007

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Kevin M. Brown 
Acting Commissioner of Internal Revenue

SUBJECT: Draft Audit Report – Fiscal Year 2007 Statutory Audit of Compliance with Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations (Audit # 200740006)

We have reviewed your report and appreciate your acknowledgement of our ongoing efforts to comply with Section 3707 of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA '98). We have taken significant actions to comply with RRA '98 to ensure we protect the rights of all taxpayers, including those with constitutional or philosophical objections to our tax system. As you note, we have removed all Illegal Tax Protestor (ITP) codes from the Master File and all ITP references from current publications and the Internal Revenue Manual (IRM).

We understand your concerns with the use of terms such as "tax protester" in case narratives because they could suggest a negative connotation or appear to label the taxpayer. While we disagree that the references listed in the report are violations, we appreciate your acknowledgement that the use of such references has not affected the way the IRS deals with taxpayers who question the tax system. These taxpayers are treated in the same manner and given the same rights as any other taxpayer.

While no recommendations were made in this report, IRS management will issue a memorandum to all employees to reinforce compliance with Section 3707 of RRA '98.

If you have any questions, please call Kathy Petronchak, Commissioner, Small Business/Self-Employed (SB/SE) Division, at (202) 622-0600, or Fred Schindler, Director, Collection Policy, SB/SE, at (202) 283-7650.