Taxpayers Do Not Always Receive Quality Responses When Corresponding About Tax Issues

July 6, 2011

Reference Number: 2011-40-058

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 | 202-622-6500
Email Address | TIGTACommunications@tigta.treas.gov
Web Site | http://www.tigta.gov

HIGHLIGHTS

TAXPAYERS DO NOT ALWAYS RECEIVE QUALITY RESPONSES WHEN CORRESPONDING ABOUT TAX ISSUES

Highlights

Final Report issued on July 6, 2011

Highlights of Reference Number: 2011-40-058 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

IMPACT ON TAXPAYERS

In November 1998, the Internal Revenue Service (IRS) issued Policy Statement P-6-12 requiring employees to initiate a response to taxpayer correspondence within 30 calendar days. Although most responses to taxpayers' correspondence tested were accurate, most responses were not timely. When taxpayers' issues are not addressed timely, taxpayers are mailed interim letters. However, none of the systemically issued interim letters provide taxpayers with any information specific to their accounts, and the content is not clear regarding what taxpayers need to do.

WHY TIGTA DID THE AUDIT

This audit was initiated to determine whether the IRS was appropriately processing correspondence from taxpayers or their representatives when required to meet its own policy requirements to respond to a taxpayer within 30 calendar days or provide an update on the status of the response.

WHAT TIGTA FOUND

Two statistical samples and one judgmental sample from three IRS functions showed that most taxpayers do not receive quality responses to their correspondence.

- Of 73 correspondence cases sampled from the Accounts Management function, only 14 (19 percent) taxpayers received timely and accurate responses.
- Of 48 correspondence cases sampled in the Automated Underreporter Program, all 48 taxpayers received accurate responses, but only 27 (56 percent) of 48 taxpayers received their responses timely.
- Of 73 correspondence cases from the Field Assistance Office, only six (8 percent) taxpayers received timely and accurate responses.

In addition, interim letters, required to be sent to taxpayers if a response cannot be issued within the 30 calendar days, were not always issued.

Not all procedures are being followed. Cases are not properly categorized, suspended, or linked, and the quality review process does not ensure all procedures were followed.

Finally, the IRS is not following Policy Statement P-6-12 guidelines and has not implemented any measures or processes to monitor and evaluate Policy Statement P-6-12 correspondence to ensure taxpayers receive timely responses to their correspondence.

WHAT TIGTA RECOMMENDED

TIGTA recommended and the IRS generally agreed to: 1) clarify instructions to ensure employees follow procedures; 2) revisit Policy Statement P-6-12 guidelines to ensure they reflect the IRS's current procedures and expectations; 3) complete the study of the interim letters; and 4) update quality review procedures to include a review of correspondence category codes and a determination as to whether cases should have been suspended and/or linked.

The IRS did not agree with the outcome measures claimed in the report, stating the projections were based on non-representative samples. However, the samples were random samples from the defined universe of cases. As such, TIGTA believes they are representative. The five-year projections are, in fact, forecasts. This type of forecasting is used by the Federal Government in many circumstances.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

July 6, 2011

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

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

SUBJECT: Final Audit Report – Taxpayers Do Not Always Receive Quality Responses When Corresponding About Tax Issues (Audit # 201040022)

This report presents the results of our review to determine whether the Internal Revenue Service (IRS) was appropriately processing correspondence from taxpayers or their representatives when required to meet its own policy requirements to respond to a taxpayer within 30 calendar days or provide an update on the status of the response. This audit was requested by the IRS Oversight Board and was part of our Fiscal Year 2010 Annual Audit Plan. It addresses the major management challenge of Providing Quality Taxpayer Service Operations.

In the general comments in IRS management's response, management requested clarification on the information in *Figure 1: Quality Responses From Testing in Three IRS Functions* on page 3 of the draft report. In the final report, Figure 1 has been revised to show the functions tested, the sample size of each function, and the quality responses from each function.

Management's complete response to the draft report is included in Appendix V.

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

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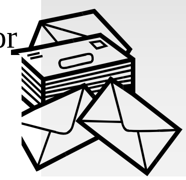
Background

Each year the Internal Revenue Service (IRS) sends out more than 200 million notices and letters to taxpayers. Many of these notices and letters require written responses from taxpayers. Although the IRS does not track the total incoming mail it receives, the Government Accountability Office recently reported that the IRS received 20 million letters, forms, and other types of taxpayer correspondence in Fiscal Year 2010.[1]

IRS Policy Statement P-6-12, Timeliness and Quality of Taxpayer Correspondence, states:

- The IRS will issue quality responses to all taxpayer correspondence.
- Taxpayer correspondence is defined as all written communication from a taxpayer or his or her representative, excluding tax returns, whether solicited or unsolicited. This includes taxpayer requests for information, as well as that which may accompany a tax return; responses to IRS requests for information; and annotated notice responses.
- A quality response is timely, accurate, professional in tone, and responsive to taxpayer needs (i.e., resolves all issues without further contact).

The key to identifying taxpayer correspondence is to ask if the taxpayer is:



- ***Waiting for a response?***
- ***Waiting for an action to be taken?***
- ***Asking a question?***

IRS internal guidelines define a quality response as timely when initiated within 30 calendar days of the IRS received date.

Much of the correspondence the IRS receives deals with the processing of individual tax returns. Two functions, the Wage and Investment Division Accounts Management function and Automated Underreporter Program, work taxpayer correspondence dealing with processing issues and underreported income.

[1] *2010 Tax Filing Season: IRS's Performance Improved in Some Key Areas, but Efficiency Gains Are Possible in Others* (GAO-11-111, dated December 2010).

- The Accounts Management function is comprised of IRS employees who assist taxpayers who call or write to the IRS with questions about their tax returns or tax accounts. Employees answer taxpayer tax-related account questions by providing taxpayers with information on the status of their tax returns and refunds. Accounts Management function employees are responsible for resolving the majority of issues and questions to settle taxpayer accounts. Taxpayers correspond to IRS letters and notices generated during the processing of their tax returns.
- The Automated Underreporter Program matches taxpayer income and deductions submitted by third parties such as banks, brokerage firms, and other payers on information returns against amounts reported on individual income tax returns. In the Automated Underreporter Program, correspondence worked includes responses from taxpayers to underreporter notices. The taxpayer may be agreeing to a proposed adjustment or sending in additional information to support the original tax return.

This review was performed at the Wage and Investment Division Headquarters in Atlanta, Georgia; the Atlanta Campus[2] in Atlanta, Georgia; the Austin Campus in Austin, Texas; the Brookhaven Campus in Holtsville, New York; the Field Assistance Office in Atlanta, Georgia; and the Small Business/Self-Employed Division in Atlanta, Georgia, during the period May 2010 through March 2011. 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.

[2] 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.

Results of Review

Most Taxpayers Do Not Receive Quality Responses to Their Correspondence

Although the majority of responses to the taxpayers' correspondence tested were accurate and addressed all issues, not all taxpayers received responses as required, and most responses were not timely. As defined in IRS internal guidelines:

> *A quality response is one that is accurate, timely, and addresses all issues based on the information provided. . . . Timely means that a final response was initiated within 30 days of IRS received date.*

Testing included sampling cases from three IRS functions — the Accounts Management function, the Automated Underreporter Program, and the Field Assistance Office.[3] Some correspondence did not require that the function respond to the taxpayer by mail, but instead required some other response or action to resolve the taxpayer's issue(s). Nevertheless, the response/action is a quality response only if initiated within 30 calendar[4] days of the IRS receiving the correspondence.

Figure 1 shows the sample size and the quality responses from each of the three functions tested.

Figure 1: Quality Responses From Testing in Three IRS Functions

	Accounts Management Function	Automated Underreporter Program	Field Assistance Office
Sample Size	73	48	73
Quality Response—Accurate and Timely	14 (19%)	27 (56%)	6 (8%)

Source: Treasury Inspector General for Tax Administration analysis of taxpayer correspondence.

- **Accounts Management function –** From a statistically valid sample of 73 cases, only 14 (19 percent) taxpayers received timely *and* accurate actions and/or responses. Of 73 cases, 62 required that a written response be mailed to the taxpayers; however, only 56 responses were mailed. From the 56 cases tested that included responses that were

[3] Employees in the IRS's Field Assistance Office provide taxpayers with face-to-face assistance but at times assist the Accounts Management function by working taxpayer correspondence inventories.
[4] Hereafter, all references to days are to calendar days.

mailed to taxpayers, 45 responses (80 percent) were accurate and addressed all issues, but only 8 of the 45 responses were timely mailed.

- **Automated Underreporter Program –** From a judgmental sample of 48 correspondence cases, 27 (56 percent) taxpayers received their responses timely. All of the 48 taxpayers received accurate responses.
- **Field Assistance Office –** From a statistically valid sample of 73 cases, only 6 (8 percent) taxpayers received timely *and* accurate actions and/or responses. Of 73 cases, 72 required that a written response be mailed to the taxpayers; however, only 65 responses were mailed. From the 65 cases tested that included responses that were mailed to taxpayers, 57 (88 percent) responses were accurate and addressed all issues, but only 6 of the 57 responses were timely mailed.

IRS guidelines state that a response is timely when initiated within 30 days of the IRS received date. However, Accounts Management function officials stated that they consider a final response timely if the IRS issues interim letters to the taxpayers. They emphasized that 30 days is not realistic considering the magnitude of correspondence and the available resources. Accounts Management function guidelines state:

> *Final response to taxpayer(s) must be initiated by the 30th day from the earliest IRS received date, unless the taxpayer has received an interim contact or interim contact has been initiated from us by the 30th day. . . .*

Nevertheless, Accounts Management function guidelines continue by stating:

> *Timely means that a final response was initiated within 30 days of IRS received date. However, when possible, you should try to initiate quality responses in less time.*

Figure 2 shows that interim letters were not always mailed to taxpayers.

Figure 2: Analysis of Responses and Interim Letters

	Accounts Management Function	Automated Underreporter Program	Field Assistance Office
Quality Response Within 30 Days	14	27	6
Response Within 30 Days, but Required Response Not Mailed			3
Response > 30 Days and Interim Letters Mailed	41	9	59
Response > 30 Days and Interim Letters Not Mailed	18	12	5
Total Cases Sampled Per Function	73	48	73

Source: Treasury Inspector General for Tax Administration analysis of taxpayer correspondence.

If a case takes more than 60 days to resolve, the IRS may send more than 1 interim letter to a taxpayer. From our samples, the Accounts Management function mailed 54 interim letters and the Field Assistance Office mailed 82 interim letters. IRS officials stated that assistors must give taxpayers 45 days to respond to any additional information the IRS must request. During this time, the case is suspensed and interim letters become necessary. However, for our statistical sample, the cases were closed without suspending.

If correspondence were processed timely, the potential cost savings for the Accounts Management function and the Field Assistance Office would be $424,318 related to 1,039,997 interim letters that were issued as a result of correspondence cases being processed untimely, projected to $2,121,590 over 5 years.

Most taxpayer responses were accurate, but some taxpayers did not receive the required responses

From the 56 cases tested from the Accounts Management function that included responses mailed to taxpayers, 11 (20 percent) responses were inaccurate and/or did not address all issues. From the 65 cases tested from the Field Assistance Office that included responses mailed to taxpayers, 8 (12 percent) responses were inaccurate and/or did not address all issues. In addition, issues in 13 cases from these 2 samples required that taxpayers receive responses to their correspondence, but responses were not sent—6 of these were from the Accounts Management function and 7 were from the Field Assistance Office.

This occurred because of employee error or employees were not following procedures and guidelines. For example:

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The cases were all closed, even though the issues may not have been resolved.

<u>Case guidelines were not always followed</u>

IRS guidelines require that Accounts Management function and Field Assistance Office employees (called assistors) control each case if the case meets Policy Statement P-6-12 criteria and is not closed within 14 calendar days. Any action taken while the case is in an assistor's inventory must be documented and updated appropriately.

When additional information from the taxpayer or another document from IRS files is needed, the assistor has 2 options—to close or suspend the case for 40 days (70 days for taxpayers who are living overseas). If the case is closed after the taxpayer replies to an IRS request for additional information, a new case is opened and a link between the new case and the closed case is created. If the case was in suspense and additional information is received, the information is associated with the suspensed case, the case is removed from suspense, and the information is associated with the case.

If the taxpayer does not reply to a suspense case, the case is to be closed using the available information and the appropriate closing letter sent to the taxpayer. Suspense case files should have a history sheet or record attached to reflect all actions taken and the dates.

Test results identified that assistors are not linking cases.

- 6 (8 percent) of 73 cases in the Accounts Management function should have been linked to the original case and were not.
- 17 (23 percent) of 73 cases in the Field Assistance Office should have been linked to the original case and were not.

Further, there were cases that appeared that they should have been placed in suspense; however, guidelines were not clear on when cases should be suspended. When assistors close cases instead of placing them in suspense, additional correspondence may not be associated or linked with related cases and all taxpayer issues may not be addressed.

Each function tested has its own quality assurance program, which includes an independent review of a sample of cases and a number of managerial reviews. None of these reviews include a review of whether cases are correctly placed in suspense or linked.

Most responses are not initiated within the required 30 calendar days

Figure 3 shows that the IRS is not timely responding to taxpayer correspondence within 30 days. In Fiscal Year 2010, 1,101,052 taxpayers were potentially burdened. When projected over 5 years, 5,505,260 taxpayers could potentially be burdened.

Figure 3: Analysis of Timeliness of Responses

	Accounts Management Function		Automated Underreporter Program		Field Assistance Office	
Quality Response	**14**	**19%**	**27**	**56%**	**6**	**8%**
Response Within 30 Days[5]					3	4%
Response From 31 to 60 Days	29	40%	9	19%	34	47%
Response From 61 to 90 Days	22	30%	6	13%	21	29%
Response More Than 90 Days	8	11%	6	13%	9	12%
Total Responses Not Initiated Within 30 Days	**59**	**81%**	**21**	**45%**	**67**	**92%**
Total*	**73**	**100%**	**48**	**100%**	**73**	**100%**

*Source: Treasury Inspector General for Tax Administration analysis of taxpayer correspondence. *Percentages may not add up due to rounding.*

[5] Cases were closed within 30 days, but a response was not mailed to taxpayer.

Testing showed that assistors in the Accounts Management function and the Field Assistance Office averaged only 3.6 days and 10.2 days, respectively, to actually work a case. However, it took an average 56.1 days and 50.8 days, respectively, for the Accounts Management function and Field Assistance Office to begin working the cases (i.e., the average number of days from when the IRS received the correspondence to the day assistors received the cases).

The Accounts Management function tracks the time it takes to respond to taxpayers' correspondence from the IRS received date to the date the case is closed. It also tracks the date the case is assigned to an assistor. However, its management information system does not capture the time an assistor spent actually working a case. Figure 4 provides an analysis of the time it took to resolve the Accounts Management function and Field Assistance Office cases sampled.

Figure 4: Analysis of the Time Taken to Work Cases Sampled in the Accounts Management Function and Field Assistance Office

	Accounts Management Function	Field Assistance Office
Average Days From Correspondence Received to Assistor First Action	56.1	50.8
Average Days From Assistor First Action to Taxpayer Response	3.6	10.2
Average Days From Correspondence Received to Taxpayer Response[6]	59.8	60.9

Source: Treasury Inspector General Tax Administration analysis of sampled cases.

The IRS generally considers any case in process more than 45 days as over-age inventory. Taxpayer correspondence inventories and workloads are monitored by the number of closures and over-age inventories.

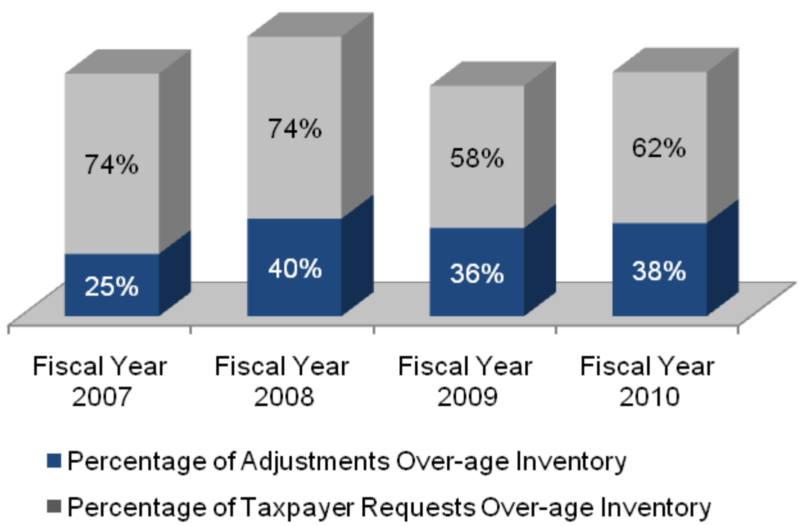
Over-age inventories remain a challenge for the Accounts Management function

Accounts Management function inventories include correspondence-coded Taxpayer Requests[7] and Adjustments. The IRS reports for correspondence-coded Taxpayer Requests show the average over-age inventory has fluctuated from 74 percent in Fiscal Year 2007 to 62 percent in Fiscal Year 2010. The over-age inventory for Adjustments inventories has also fluctuated from 25 percent to about 40 percent for Fiscal Years 2007 through 2010. Figure 5 shows the average

[6] When action taken by the assistor could not be determined, the closing date was used.
[7] Correspondence-coded Taxpayer Requests include Policy Statement P-6-12 correspondence.

over-age inventory percentage for Taxpayer Requests and Adjustments for Fiscal Years 2007 through 2010.

Figure 5: Average Over-age Inventories for Taxpayer Requests and Adjustments[8]



Source: IRS management information system reports.

Most incoming mail is received at each of the 10 IRS campuses and deals with a significant number of tax issues. Correspondence to be worked in the Accounts Management function and the Field Assistance Office is scanned into the Correspondence Imaging System.[9] Correspondence to be worked in the Automated Underreporter Program is shipped to the respective functions.

Although the time it takes to process mail is a factor in over-age correspondence inventories, of greater significance are the resources to work the inventories. Employees who work taxpayer correspondence and/or respond to taxpayers also assist taxpayers who seek live assistance through the IRS's toll-free telephone lines and at IRS walk-in offices, called Taxpayer Assistance Centers. Limited resources require the IRS to allocate staff between these two priorities.

Employees who work taxpayer correspondence and/or respond to taxpayers also assist taxpayers calling the IRS's toll-free telephone lines and visiting IRS walk-in offices.

[8] These are not weighted results.
[9] The Correspondence Imaging System is a system used to scan and convert incoming taxpayer correspondence into digital images. It puts the scanned images into electronic case folders, which can be easily accessed and worked by assistors.

Because of new legislation and procedural changes, over the last two filing seasons, the IRS experienced increased correspondence and high call demand on its toll-free telephone lines, requiring it to choose whether to dedicate more resources to answering taxpayers' calls or to responding to taxpayers' correspondence. However, the toll-free telephone line's level of service[10] is still lower than it was in Fiscal Year 2007 (when it was above 80 percent) and over-age inventories have increased.

The IRS has worked with consulting firms and internal business units to help meet higher telephone demand, improve the overall call experience, and work paper inventories. One of the consulting firms' recommendations was to develop and deploy a Telephone and Paper Optimization tool to balance performance between the telephone and paper channels. The tool examines the performance and volume levels of both paper and telephone, and balances the resources to achieve the best-combined performance for both channels. The IRS began working with this tool in Fiscal Year 2010.

The IRS also recognizes that additional resources are needed to address both the increasing over-age inventories and decreasing telephone service. In its Fiscal Year 2011 budget request, the IRS has requested additional funding for the extension of seasonal employees and overtime in Fiscal Year 2011 to allow it to increase the telephone level of service, respond to increased workload, and enhance taxpayer service.

The IRS recognizes that additional resources are needed to address both the increasing over-age inventory and decreasing telephone service.

The Government Accountability Office and the National Taxpayer Advocate recently reported that the IRS does not process taxpayer responses timely and does not have performance measures to assess the timeliness of its taxpayer correspondence.[11] The Government Accountability Office report recommended and the IRS agreed that it should establish a taxpayer correspondence performance measure.[12] The IRS has a number of indicators to monitor correspondence workload. Developing a performance measure would allow the IRS to better evaluate timeliness, allowing IRS management to better prioritize telephone or other services, for which such measures already exist, over providing timely taxpayer correspondence.

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[10] Level of service is the IRS's primary measure of providing taxpayers with access to an assistor. It is the percentage of callers who wish to speak to an assistor and who are able to speak with one.

[11] *National Taxpayer Advocate 2010 Annual Report to Congress*, dated January 31, 2010, and *2010 Tax Filing Season: IRS's Performance Improved in Some Key Areas, but Efficiency Gains Are Possible in Others* (GAO-11-111, dated December 2010).

[12] Government Performance and Results Act of 1993 (GPRA), Pub. L. No. 103-62, 107 Stat. 285 (codified as amended in scattered sections of 5 U.S.C., 31 U.S.C., and 39 U.S.C.).

Correspondence cases are not always properly categorized

The IRS uses category codes to identify the approximately 100 types of individual taxpayer correspondence. Tests of correspondence from our 2 statistical samples identified that 17 (23 percent) of 73 Accounts Management function cases and 19 (26 percent) of 73 Field Assistance Office cases were categorized incorrectly.

Employees have received directives emphasizing the importance of using correct category codes, particularly for budget purposes. Without an accurate accounting of the type of work it receives, the IRS cannot determine the resources it needs to distribute and work the different types of correspondence. In addition, if correspondence is not accurately classified, the case may be worked incorrectly or require transfer to a subject matter expert in another office or function, further delaying the response to the taxpayer.

Correspondence category codes are used for budgeting and inventory control.

The correspondence category code should be identified during the screening of correspondence. The correspondence is separated by category code and document type and then assigned to the location that works that type of correspondence. If the assistor working the case determines the category code is incorrect, the assistor is instructed to correct the category code.

Employees are not following procedures and a review of category codes is not included in the IRS's quality review of correspondence. Inaccurate category codes cause the management information systems to be unreliable. When data are unreliable, the IRS may not make sound business decisions. During Fiscal Year 2010, 312,495 cases could potentially have incorrect category codes, projected to 1,562,475 cases over 5 years.

Interim letters can be confusing

An analysis of 2 of the 3 IRS functions identified that each use letters specific to their function to reply to taxpayers—totaling 2 initial interim letters; 2 different follow-up letters; 6 other assorted acknowledgement, apology, transfer, and closing letters; and an assortment of more than 70 letters applicable to numerous tax issues. Taxpayers can receive any number and/or combination of letters depending on their tax situation. None of the systemically issued interim letters provides the taxpayer with any information specific to his or her account and the content is not clear regarding what the taxpayer needs to do, which can generate calls to the toll-free telephone lines or potential visits to the Taxpayer Assistance Centers.

An IRS study showed that interim letters are not meeting the Policy Statement P-6-12 objectives but have become a vehicle to "buy time" in case processing.

In January 2010, an IRS study showed that interim letters are not meeting the Policy Statement P-6-12 objectives of timeliness and responsiveness but have become a vehicle to "buy time" in case processing. Problems were identified with the ever-increasing number of interim letters being issued. Feedback from taxpayers showed that the letters are confusing.

Systemically generated interim letters are issued on a cycle. If a closing letter is issued, an interim letter cannot always be stopped if it is already in the queue. An analysis of a sample of 146 cases identified 20 (14 percent) cases with interim letters issued within 5 days of the taxpayer's response. In cases when a response was not sent, the interim letters were issued within 5 days of closing the case on the IRS management information system (11 cases from the Accounts Management function and 9 cases from the Field Assistance Office).

In addition, the IRS conducted an analysis of 4,704 cases and identified numerous issues with interim letters. Figure 6 shows the IRS determined that 12 percent of the interim letters for the Automated Underreporter Program arrived after the case was closed.

Figure 6: IRS Analysis of Interim Letters

Issues	Accounts Management Function	Automated Underreporter Program
Volume Analyzed	**2,296**	**2,408**
Interim Letter Arrived After Case Closure	0%	12%
Interim Letter Arrived Within 10 Days of Case Closure	19%	29%
First Interim Letter Exceeded 30 Days After Correspondence Received	12%	29%
Second and Third Interim Letters Exceeded 45 Days From First Interim Letter	11%	3%
No Interim Letters Issued	20%	0%

Source: IRS analysis of interim letters.[13]

In its Interim Letter Report January 2010, the IRS proposed a four-phase test plan to improve the taxpayer experience and use of its resources. Phase I recommended capturing call volume trends and patterns with the use of a special toll-free telephone number on two types of interim letters and use of Contact Analytics[14] to secure specific taxpayer feedback on issues and concerns raised on telephone calls. On March 23, 2011, IRS officials advised us that it could not obtain a special toll-free telephone number because of cost and timing.[15] It still plans to monitor call

[13] The data were not validated and are used for perspective only.
[14] Contact Analytics is a tool for evaluating recorded audio from contact center recordings for identifying contact center improvement opportunities.
[15] The IRS was unable to provide the cost of a toll-free telephone number.

volume patterns and use Contact Analytics to secure specific taxpayer feedback on issues and concerns with the interim letters

When an issue cannot be resolved timely, interim letters should be strategically mailed to taxpayers alerting them of the delay. The letters should be clear and provide the taxpayer with the status of the case and the expected time period to resolve the case. In addition, the IRS should ensure that all taxpayers receive responses when appropriate and that it has a systemic process to identify when a response has not been generated.

Inadequate and untimely responses to taxpayer correspondence adversely affect taxpayers and tax administration

In an IRS customer satisfaction survey administered from July to September 2010 to taxpayers who had adjustments cases closed in the Accounts Management function at each of the 10 campuses, taxpayers were least satisfied with the length of time to resolve their issues.[16] The overall satisfaction rate for the survey was 64 percent. Taxpayers provided the following five top-priority improvements for correspondence:

1. Length of time to resolve an issue.
2. Ease of getting more information about the issue.
3. Ease of understanding responses from the IRS.
4. Keeping the taxpayer informed of the status of the issue.
5. Explanation regarding the resolution of the taxpayer issue.

In the IRS 2009-2013 Strategic Plan, the IRS's first goal is to improve service to make voluntary compliance easier. To achieve this goal, the first objective is to incorporate taxpayer perspectives to improve all service interactions — every interaction the IRS has with a taxpayer must be seen from the taxpayer's point of view, regardless of whether or not the IRS ultimately agrees with the taxpayer's position.

Taxpayers are burdened when issues are not timely and appropriately resolved. If correspondence is not worked timely and systems are not updated to reflect a response by the designated time, the IRS may issue the next notice to the taxpayer automatically or move an account to the next step of the assessment or collection process.

Another downstream effect on the IRS and tax administration is that taxpayers may call the IRS or visit a Taxpayer Assistance Center when they have not received a response to their correspondence. It is more costly for the IRS to process paper correspondence than to provide telephone services, but the most costly is face-to-face services. Taxpayers' use of telephone

[16] Adjustment cases include incoming correspondence from taxpayers — responses to notices and letters, unsolicited correspondence, amended returns, and claims. Results include both individual and business taxpayers.

and/or face-to-face contact could cost the IRS more than it would cost to timely respond to taxpayers' correspondence.

The IRS cannot determine how many calls are made to its toll-free telephone lines or how many taxpayers visit Taxpayer Assistance Centers when they cannot resolve their issues by correspondence and/or they are unsure if the IRS is working on their issue. However, in Fiscal Years 2008 and 2009, the Taxpayer Advocate Service received approximately 92,000 and 89,000 requests, respectively, for assistance from taxpayers who did not receive a timely response from the IRS. The number increased to about 98,000 in Fiscal Year 2010 and is approximately 33 percent of all requests received.

According to the IRS, 20 percent of taxpayers surveyed contacted the IRS about the same issues they had on their prior year tax returns. Either the taxpayers did not get a response from the IRS before they filed their next tax returns or they did not receive a response that they understood, therefore possibly repeating the actions that required the IRS to send them the initial correspondence. At times, taxpayers are filing their current year's tax returns while trying to resolve issues from prior years. From the two statistical samples of correspondence received in Fiscal Year 2010 from 146 taxpayers—****************1**************************. However, 79 tax returns (54 percent) involved Tax Year 2009 returns, and 66 tax returns (45 percent) involved tax returns prior to Tax Year 2009.

The IRS is not following Policy Statement P-6-12 guidelines

In July 1998, the IRS Restructuring and Reform Act of 1998[17] was implemented and states that a significant hardship includes when there is a delay of more than 30 days in resolving taxpayer account problems. Policy Statement P-6-12 guidelines state that a final response to the taxpayer is to be initiated by the 30th day from the earliest IRS received date.

The IRS is not following Policy Statement P-6-12 guidelines and has not implemented any measures or processes to monitor and evaluate 30 day correspondence. Current processes do not provide a quality response—one that is accurate, timely, and addresses all issues. The IRS designated certain incoming mail to meet the Policy Statement P-6-12 criteria:

> *The key to identifying Policy Statement P-6-12 is to ask:*
>
> *"Is the initiator of the correspondence asking a question, or waiting for a reply or an action to be taken?"*

Eight examples of what meets the criteria are then provided, including incoming taxpayer responses that provide additional information. Guidelines also list more than 20 types of correspondence that do not meet the criteria including delinquent and amended tax returns, extensions to file, address changes, correspondence not dealing with a taxpayer's account, and all

[17] 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.).

correspondence received in response to IRS solicitations for information necessary to secure or complete the processing of a tax return.

The IRS has been concerned about timely responses to taxpayers and took steps in 1990 to ensure it provides timely and quality responses to taxpayers. The IRS has formed numerous teams to study correspondence timeliness and has set policies requiring a response to the taxpayer be initiated within 30 days. Currently, all correspondence requiring a response is treated as Policy P-6-12 correspondence. Yet, IRS guidelines differentiate between what is and is not classified as Policy P-6-12 correspondence. Guidelines should be updated to reflect the IRS's actual procedures and expectations.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 1: Clarify instructions to ensure employees understand when a case requires a written response from the IRS, when a case should be placed in suspense or closed, and when correspondence should be linked to prior cases.

> ***Management's Response:*** The IRS generally agreed with this recommendation stating that there are clear instructions throughout the Internal Revenue Manual for IRS employees; however, it will review the instructions to see if clarifications are necessary to ensure proper employee understanding. Comprehensive training is also provided by the Accounts Management function, the Field Assistance Office, and Automated Underreporter Program to ensure employees understand when a case requires a written response, when it should be placed in suspense or closed, and when correspondence should be linked to prior cases. The IRS will continue to ensure that training reflects the most up-to-date procedures.
>
> ***Office of Audit Comment:*** Although the IRS believes the instructions are clear, tests of correspondence from our 2 samples required that taxpayers receive responses to their correspondence, but responses were not sent—6 (8 percent) of these were from the Accounts Management function and 7 (10 percent) were from the Field Assistance Office. Also, test results identified that assistors are not linking cases—6 (8 percent) of 73 cases in the Accounts Management function should have been linked to the original case and were not and 17 (23 percent) of 73 cases in the Field Assistance Office should have been linked to the original case and were not.

Recommendation 2: Revisit Policy Statement P-6-12 guidelines to ensure they reflect the IRS's current procedures and expectations.

> ***Management's Response:*** The IRS agreed with this recommendation and has revised the Internal Revenue Manual accordingly. Policy Statement P-6-12 includes general guidelines. Any change in specific procedures would be made within the Internal

Revenue Manual, not the Policy Statement. To ensure adherence to Policy Statement P-6-12 guidelines, the IRS recently revised the Internal Revenue Manual, Quality and Timely Responses, to clarify the definition of a timely response to include the issuance of an interim letter.

Recommendation 3: Complete the study of the interim letters to ensure they: 1) are strategically timed, 2) alert taxpayers of delays and provide taxpayers with an accurate status and time period for case resolution, 3) provide taxpayers with sufficient information to deter them from using other channels to contact the IRS regarding their case, and 4) are clear and concise.

Management's Response: The IRS agreed with this recommendation and will complete a four-phase study of interim letters. After gathering more detailed data on the current process, the IRS plans to develop new or revised interim letters using the plain language guidelines and modify the timing of interim letters to ensure it provides taxpayers with sufficient information in a timely manner.

Recommendation 4: Update quality review procedures to include a review of correspondence category codes and a determination as to whether cases should have been suspensed and/or linked.

Management's Response: The IRS agreed with this recommendation stating it is already taking steps to address quality revenue procedures. Guidance on the use of correspondence category codes and the suspension and linking of cases are covered by various portions of the Account Resolution sections in the Internal Revenue Manual. The Internal Revenue Manual instructs quality reviewers to review the entire case file from the IRS received date to the closing date and to review all actions taken on the case. This instruction includes reviewing correspondence category codes and whether a case should have been suspended or linked.

Office of Audit Comment: The IRS stated in its response that it did not agree with our 5-year projected outcomes because we used a 5 percent error rate for the sample size of taxpayer correspondence cases processed. It believes we should have used a 50 percent error rate, which would have resulted in a larger sample size.

The fact that the samples of 73 cases are random samples from the defined universe of cases makes the samples valid statistical samples, where the results of the samples can be projected to the universe. That the samples of 73 were derived from a formula using an estimated 5 percent error rate is irrelevant as to whether or not the samples of 73 cases are valid samples. Larger sample sizes would produce a more precise (narrower) confidence interval but would require a higher level of resources.

The 5-year projections are, in fact, forecasts. These forecasts assume that the error trends present in Fiscal Year 2010 will remain constant over the next 5 years. This type of forecasting is used by the Federal Government in many instances.

Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to determine whether the IRS was appropriately processing correspondence from taxpayers or their representatives when required to meet its own policy requirements to respond to a taxpayer within 30 calendar days or provide an update on the status of the response. To accomplish this objective, we:

I. Determined the process the IRS uses to respond to Policy Statement P-6-12 correspondence.

  A. Identified the process used by IRS functions to process taxpayer correspondence.

  B. Evaluated internal controls, such as time to process taxpayer correspondence, to ensure the process is an effective tool to prevent taxpayers from having to submit redundant correspondence to obtain an accurate and timely response.

  C. For each function processing correspondence, determined the types and statistical data tracked for taxpayer correspondence.

II. Evaluated whether taxpayers are provided an accurate and timely response within 30 calendar days of receipt of the correspondence.

  A. Identified which functions work Policy Statement P-6-12 correspondence and selected three. We selected the two functions with the highest volume of correspondence received – the Accounts Management function and the Automated Underreporter Program. We also selected the Field Assistance Office because its employees work correspondence inventory and assist the Accounts Management function with processing correspondence.

  B. Obtained data from the Accounts Management Services system and the Automated Underreporter database to determine the population of taxpayer correspondence cases for Fiscal Year 2010. The database and system maintain the inventories of correspondence cases.

  C. Stratified the data by determining cases closed and Taxpayer Request category code.

  D. Selected a statistically valid sample of 73 individual taxpayer correspondence cases processed in the Accounts Management function from a population of 1,221,394 cases. We used a 5 percent error rate, ±5 percent precision, and a 95 percent confidence interval.

E. Selected a statistically valid sample of 73 individual taxpayer correspondence cases in the Field Assistance Office from a population of 121,438. We used a 5 percent error rate, ±5 percent precision, and a 95 percent confidence interval.

F. Selected a judgmental sample of 48 cases from the Automated Underreporter Program database from a population of 2,716,596 taxpayer accounts. Because of the resources that would have been required to oversample, a judgmental sample was used. Most cases do not include taxpayer correspondence.

G. Validated the data from the Accounts Management Services system and the Automated Underreporter database by researching the IRS Integrated Data Retrieval System[1] to determine the accuracy of each case. We discussed the systems with IRS officials and researched access and process guidelines.

H. Determined the effect to the taxpayer and tax administration of taxpayer correspondence not being processed accurately and timely.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective: the IRS's internal guidelines used by the functions that process Policy Statement P-6-12 correspondence and the management information systems used to control Policy Statement P-6-12 correspondence. We evaluated controls by interviewing management and reviewing policies and procedures. We selected two statistically valid samples and one judgmental sample, and conducted tests related to Policy Statement P-6-12 correspondence.

[1] IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.

Appendix II

Major Contributors to This Report

Michael E. McKenney, Assistant Inspector General for Audit, (Returns Processing and Account Services)
Augusta R. Cook, Director
Lena Dietles, Audit Manager
Jerry Douglas, Lead Auditor
Roberta Fuller, Senior Auditor
Robert Howes, Senior Auditor
Jerome Antoine, Auditor
Kathy Coote, Auditor
Nelva Usher, Auditor

Appendix III

Report Distribution List

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Director Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaisons:
    Chief Technology Officer OS:CTO
    Commissioner, Small Business/Self-Employed Division SE:S
    Senior Operations Advisor, Wage and Investment Division SE:W:S

Appendix IV

Outcome Measures

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

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; 1,101,052 taxpayers affected, projected to 5,505,260 taxpayers over 5 years (see page 3).

Methodology Used to Measure the Reported Benefit:

From Fiscal Year 2010 data provided by the IRS, computer analysis was used to stratify and identify a universe of 1,221,394 cases closed in the Accounts Management function and 121,438 cases processed in the Field Assistance Office. Statistical sampling was used to select 73 taxpayer correspondence cases from each function. From the statistical sample, we determined whether taxpayers received a quality response to their correspondence.

Of the 73 closed taxpayer correspondence cases sampled from the Accounts Management function, 59 (81 percent) taxpayers were not provided a quality response. Projected to the universe of 1,221,394 closed taxpayer cases, there may have been 989,329 taxpayers who did not receive a quality response, and 4,946,645 taxpayers projected over 5 years.

Of the 73 closed taxpayer correspondence cases sampled from the Field Assistance Office, 67 (92 percent) taxpayers were not provided a quality response. Projected to the universe of 121,438 closed taxpayer cases, there may have been 111,723 taxpayers who did not receive a quality response, and 558,615 taxpayers projected over 5 years.

Type and Value of Outcome Measure:

- Cost Savings – Funds Put to Better Use – Potential; $424,318 related to 1,039,997 interim letters, projected to $2,121,590 over 5 years (see page 3).[1]

Methodology Used to Measure the Reported Benefit:

From Fiscal Year 2010 data provided by the IRS, computer analysis was used to stratify and identify a universe of 1,221,394 taxpayer correspondence cases closed in the Accounts

[1] Due to rounding numbers may not balance.

Management function and 121,438 cases closed in the Field Assistance Office. Statistical sampling was used to identify a statistical sample of 73 closed taxpayer correspondence cases from each function.

Accounts Management function

From the data provided, we identified 54 interim letters were mailed to taxpayers.

Based on the statistical sample of 73 closed cases, we determined:

- No interim letters were mailed for 31 cases (42.47 percent).
- 1 interim letter was mailed for 30 cases (41.10 percent).
- 2 interim letters were mailed for 12 cases (16.44 percent).

Projected over the universe of 1,221,394 cases:

- 1 interim letter mailed for 501,993 cases, resulting in 501,993 letters.
- 2 interim letters mailed for 200,797 cases, resulting in 401,594 letters.

The cost of issuing 903,587 (501,993 + 401,594) interim letters at $0.408[2] per interim letter is $368,663, projected to $1,843,315 over 5 years.

Field Assistance Office

From the data provided, we identified 82 interim letters were mailed to taxpayers.

Based on the statistical sample of 73 closed cases, we determined:

- No interim letters were mailed for eight cases (10.96 percent).
- 1 interim letter was mailed for 50 cases (68.49 percent).
- 2 interim letters were mailed for 13 cases (17.81 percent).
- ******************1************************************.

Projected over the universe of 121,438 cases:

- 1 interim letter was issued for 83,173 cases, resulting in 83,173 letters.
- 2 interim letters were mailed for 21,628 cases, resulting in 43,256 letters.
- 3 interim letters were mailed 3,327 cases, resulting in 9,981 letters.

The cost of mailing 136,410 interim letters (83,173 + 43,256 + 9,981) at $0.408 per interim letter is $55,655, projected to $278,275 over 5 years.

[2] Cost includes paper, postage, and inserts. Staff and overhead costs could not be determined.

Type and Value of Outcome Measure:

- Reliability of Information – Potential; 312,495 cases with incorrect category codes, projected to 1,562,475 cases over 5 years (see page 3).

From Fiscal Year 2010 data provided by the IRS, computer analysis was used to stratify and identify a universe of 1,221,394 cases closed in the Accounts Management function and 121,438 cases processed in the Field Assistance Office. Statistical sampling was used to select 73 taxpayer correspondence cases from each function. From the statistical sample, we determined whether taxpayer correspondence was classified with the correct category code.

Accounts Management function

Tests identified that 17 (23 percent) cases were classified with the incorrect category code. Projected over a population of 1,221,394, potentially 280,921 cases were classified incorrectly; and projected over 5 years, 1,404,605 cases were classified with the incorrect category code. The statistical sample was based on a 5 percent error rate, a ±5 percent precision, and a 95 percent confidence interval for each sample.

Field Assistance Office

Tests identified 19 (26 percent) cases were classified with the incorrect category codes. Based on a population of 121,438, potentially 31,574 cases were classified incorrectly, projected to 157,870 over 5 years. The statistical sample was based on a 5 percent error rate, a ±5 percent precision, and a 95 percent confidence interval for each sample.

Appendix V

Management's Response to the Draft Report

COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

RECEIVED JUN - 6 2011

June 3, 2011

MEMORANDUM FOR MICHAEL R. PHILLIPS
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Richard Byrd, Jr.
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Taxpayers Do Not Always Receive Quality Responses When Corresponding About Tax Issues (Audit # 201040022)

We have reviewed the subject draft audit report and appreciate your acknowledgment of our efforts to develop standardized procedures across all Business Operating Divisions and agree that additional measures will strengthen this program.

In recent years, we have implemented enhancements to improve our service to taxpayers and tax practitioners, including standardizing and extending the time periods for taxpayers to provide supporting documentation, granting additional time to respond to notices, changing the Internal Revenue Manual guidelines when required, providing additional training to telephone and paper assistors, and developing tools to enhance case settlement, such as the Interactive Tax Law Assistant. These changes have enabled us to provide more complete and consistent answers to taxpayers and tax professionals.

Concerning the accuracy rates identified in your report, we take exception with the chart, *Figure 1: Quality Responses From Testing in Three IRS Functions,* on page 3 of the draft report and on the following page, we note that the information appears inconsistent and is likely to be confusing or misleading to outside readers because different standards of measures were used. The chart states that 45 letters in Accounts Management (AM) equate to an accuracy rate of 62 percent and 57 letters in Field Assistance (FA) equate to an accuracy rate of 78 percent. On the next page, the same 45 letters in AM equate to an accuracy rate of 80 percent and the 57 letters in FA equate to an 88 percent accuracy rate. An 80 percent accuracy rate in AM is consistent with our own statistically valid internal quality review sample.

Your report acknowledges that, due to budget constraints, our staffing is limited. The challenge of limited staffing, while handling over 20 million pieces of paper

2

correspondence annually, and ever-increasing telephone demand in the Wage and Investment Division, contributes to delays in responding to our customers. Although we recognize that an interim letter informing the customer of our delay does not resolve their issue, it does provide an acknowledgement that we have received, and are working on, their case. As indicated in your report, we have efforts in place, including working with consulting firms and internal business units, to help us provide the best service to our customers, given our limited staffing. One such effort is the study of our interim letters. To ensure that these letters provide substantial value to the taxpayer, and that new interim letters can be accurately produced by the different systems, we are conducting a four phase study. We are currently conducting Phase 1 of the study, monitoring call volume patterns and using Contact Analytics to obtain specific taxpayer feedback on issues and concerns. We will use that feedback in Phase 2, to revise the interim letters and then test the changes for taxpayer comprehension of the letters. In Phase 3, we will test proposed changes to timing and frequency of mailing, and then conclude in Phase 4, with the production of new interim letters.

We reviewed the Outcome Measures in Appendix IV and note the following with respect to your methodology. You used a 5 percent error rate for the sample size of taxpayer correspondence cases processed. Given your assumptions, in our view, a 50 percent error rate would have been a more appropriate standard approach, and would have resulted in a larger sample size of 383 instead of the population of 73 cases that was used. Since the projections were based on non-representative samples, they are overstated and do not take trends and changing resources into account. Therefore, we do not agree with your five-year projected outcomes.

Attached are our comments to your specific recommendations. If you have any questions, please contact me, or a member of your staff may contact Peter J. Stipek, Director, Customer Account Services, Wage and Investment Division, at (404) 338-8910.

Attachment

Attachment

The Commissioner, Wage and Investment Division, should:

Recommendation 1
Clarify instructions to ensure employees understand when a case requires a written response from the IRS, when a case should be placed in suspense or closed, and when correspondence should be linked to prior cases.

Corrective Action
There are clear instructions throughout the Internal Revenue Manual (IRM) for our employees, however we will review the instructions to see if clarifications are necessary to ensure proper employee understanding. Comprehensive training is also provided by Accounts Management, Field Assistance, and Automated Underreporter, to ensure employees understand when a case requires a written response, when it should be placed in suspense or closed, and when correspondence should be linked to prior cases. We continue to ensure that training reflects the most up-to-date procedures.

Implementation Date
Implemented and ongoing

Responsible Official
N/A

Corrective Action Monitoring Plan
N/A

Recommendation 2
Revisit Policy Statement P-6-12 guidelines to ensure they reflect the IRS's current procedures and expectations.

Corrective Action
We agree with this recommendation and have revised the IRM accordingly. Policy Statement P-6-12 includes general guidelines. Any change in specific procedures would be made within the IRM, not the Policy Statement. To ensure adherence to Policy Statement P-6-12 guidelines, we recently revised IRM 21.3.3.3.4, *Quality and Timely Responses*, to clarify the definition of a timely response to include the issuance of an interim letter.

Implementation Date
Implemented

Responsible Official
N/A

2

Corrective Action Monitoring Plan
N/A

Recommendation 3
Complete the study of the interim letters to ensure they: 1) are strategically timed, 2) alert taxpayers of delays and provide taxpayers with an accurate status and time period for case resolution, 3) provide taxpayers with sufficient information to deter them from using other channels to contact the IRS regarding their case, and 4) are clear and concise.

Corrective Action
We agree with this recommendation and will complete our four phase study of interim letters. After gathering more detailed data on the current process, we plan to develop new or revised interim letters using the plain language guidelines and modify the timing of interim letters, to ensure we provide taxpayers with sufficient information in a timely manner.

Implementation Date
January 15, 2013

Responsible Official
Director, Office of Taxpayer Correspondence, Wage and Investment Division

Corrective Action Monitoring Plan
The IRS will monitor this corrective action as part of our internal management control system.

Recommendation 4
Update quality review procedures to include a review of correspondence category codes and a determination as to whether cases should have been suspensed and/or linked.

Corrective Action
The IRS is already taking steps to address quality review procedures. Guidance on the use of correspondence category codes and the suspension and linking of cases are covered by various portions of the Account Resolution IRM. The IRM 21.10.1, *Embedded Quality (EQ) Program for Accounts Management, Compliance Services, Field Assistance and TE/GE*, instructs quality reviewers to review the entire case file, from the IRS received date to the closing date, and to review all actions taken on the case. This instruction includes reviewing correspondence category codes and whether a case should have been suspended or linked.

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Implementation Date
Implemented

Responsible Official
N/A

Corrective Action Monitoring Plan
N/A