



*Improved Procedures Are Needed
to Prevent the Fraudulent Use of
Third-Party Authorization Forms
to Obtain Taxpayer Information*

August 27, 2018

Reference Number: 2018-40-062

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:

2 = Law Enforcement Techniques/ Procedures and Guidelines for Law Enforcement Investigations or Prosecutions.

4 = Attorney Client/ Attorney Work Product

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HIGHLIGHTS

IMPROVED PROCEDURES ARE NEEDED TO PREVENT THE FRAUDULENT USE OF THIRD-PARTY AUTHORIZATION FORMS TO OBTAIN TAXPAYER INFORMATION

Highlights

Final Report issued on August 27, 2018

Highlights of Reference Number: 2018-40-062 to the Commissioner of Internal Revenue.

IMPACT ON TAXPAYERS

Taxpayers can grant a power of attorney to individuals (*i.e.*, representatives) who are given the authority to represent a taxpayer before the IRS. These representatives can be an attorney, certified public accountant, or enrolled agent. Internal Revenue Code Section 6103(c) also allows taxpayers to authorize a designee to review and receive their returns and return information.

WHY TIGTA DID THE AUDIT

This audit was initiated to evaluate the IRS's controls to authenticate requests received from individuals seeking to represent taxpayers and access taxpayer information.

WHAT TIGTA FOUND

TIGTA's review identified that IRS management has not implemented sufficient processes and procedures to authenticate the validity of Forms 2848, *Power of Attorney and Declaration of Representative*, and Forms 8821, *Taxpayer Information Authorization*. Tax examiner reviews of these forms do not include steps to verify that the legitimate taxpayer submitted or signed the form to authorize access to his or her tax information. Based on the IRS's statistically valid sample, TIGTA estimates that the IRS has at least one unauthorized request form for 1.1 million taxpayers who have an authorization in the Centralized Authorization File (CAF).

Also, the IRS did not protect 300 taxpayers after identifying that their Taxpayer Identification Numbers were obtained by fraudsters. The IRS should have placed the Taxpayer Identification

Numbers on its Dynamic Selection List to monitor their use on future tax returns submitted.

TIGTA's review also identified that the IRS did not take sufficient action to prevent some taxpayer refunds from being erroneously issued to representatives. Finally, tax examiners are not following internal guidelines that limit the assignment of one CAF number to one representative at one location.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS: 1) develop a confirmation letter program to ensure that taxpayers authorized the third-party access; 2) revoke the authorizations for those representatives and designees that taxpayers did not authorize; 3) develop a process to ensure that all Taxpayer Identification Numbers associated with confirmed fraudulent CAF authorizations are forwarded to the appropriate office; 4) develop procedures for all functions involved with fraudulent authorization requests and stolen CAF numbers to timely report their findings to CAF management; 5) remove the refund indicator from all 72,095 authorizations that were processed prior to January 2013; 6) ensure that tax examiners follow guidelines to limit the issuance of CAF numbers to one CAF number per representative/designee at each office; and 7) correspond with representatives and designees assigned multiple CAF numbers to inform them that they are permitted to have one CAF number per location.

The IRS agreed with six recommendations and partially agreed with the recommendation to correspond with representatives and designees assigned multiple CAF numbers. IRS management plans to correspond only with those individuals it identifies as having used the multiple CAF numbers to determine if there is a need for the multiple numbers and identify those that can be removed.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

August 27, 2018

MEMORANDUM FOR COMMISSIONER OF INTERNAL REVENUE

FROM:

Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT:

Final Audit Report – Improved Procedures Are Needed to Prevent the Fraudulent Use of Third-Party Authorization Forms to Obtain Taxpayer Information (Audit # 201740038)

This report presents the results of our review to evaluate the Internal Revenue Service (IRS) controls to authenticate requests received from individuals seeking to represent taxpayers and access taxpayer information. This audit was part of our Fiscal Year 2017 discretionary audit coverage and addresses the major management challenge of Security Over Taxpayer Data and Protection of IRS Resources.

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

Copies of this report are also being sent to the IRS managers affected by the report recommendations. If you have any questions, please contact me or Russell P. Martin, Assistant Inspector General for Audit (Returns Processing and Account Services).



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Abbreviations

IRS	Internal Revenue Service
CAF	Centralized Authorization File
DSL	Dynamic Selection List
TIN	Taxpayer Identification Number



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Background

Taxpayers can grant a power of attorney to individuals (*i.e.*, representatives) who are given the authority to represent a taxpayer before the Internal Revenue Service (IRS). These representatives can be an attorney, certified public accountant, enrolled agent, enrolled actuary, or unenrolled tax return preparer.¹ In addition, Internal Revenue Code Section (§) 6103(c)² allows taxpayers to authorize a designee to receive or review their return or return information. Figure 1 details the two forms that taxpayers may use to grant these authorizations.

Figure 1: Authorization Forms

Form Number and Name	Type of Authorization Granted	Requirements for Processing
Form 2848, Power of Attorney and Declaration of Representative	Authorizes a representative to perform acts specified in 26 Code of Federal Regulations § 601.502(c) (1) and (2), including authorization to represent a taxpayer before the IRS (includes signing returns and making agreements with the IRS). Representatives may request, receive, and submit forms such as Forms 1040, <i>U.S. Individual Income Tax Return</i> ; Forms W-2, <i>Wage and Tax Statement</i> , and others.	Form must include elements such as the taxpayer's Social Security Number, name, address, and dated signature. The form must have the representative's name, address, acts authorized, designation under which he or she is authorized to practice before the IRS, type of tax or tax forms, specific period(s), and representative's signature.
Form 8821, Taxpayer Information Authorization	Permits a third-party designee to receive returns and return information. The designee may request the same form types as a power of attorney.	Form submission must include basic identifying information for the taxpayer such as Social Security Number, name, address, and dated signature. In addition, the form must include the designee's name and address.

Source: Our analysis of IRS form instructions.

Processing Forms 2848 and 8821 (authorization requests)

Tax examiners in the IRS's Centralized Authorization File (CAF) unit located in Philadelphia, Pennsylvania; Memphis, Tennessee; and Ogden, Utah, Accounts Management Sites process Forms 2848 and 8821. The CAF units in these locations process authorization requests for taxpayers (individuals and businesses) residing in the United States; the Philadelphia site also processes authorizations submitted by or on behalf of international taxpayers.

¹ 26 C.F.R. § 601.502(c) (1) and (2).

² Internal Revenue Code § 6103, *Disclosure of returns and return information to designee of taxpayer.*



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Either a taxpayer or a taxpayer's representative can submit Form 2848. The representative listed on the form must be an individual. However, for Form 8821, an individual or a business can be listed. The CAF unit accepts forms via mail or fax. Once received, clerical staff in the CAF units sort the forms by receipt date, batch them by receipt type, and input information from the forms into the Manager Inventory Database. The IRS uses this database to track processed authorization requests. The tax examiners then select a batch of forms to work. Tax examiners are required to verify the following five elements when processing an authorization request. Specifically, tax examiners are to ensure that:

1. The form has the taxpayer's handwritten signature and is dated. Only a handwritten signature can be accepted. An electronically signed, printed, or stamped signature does not meet this requirement.
2. The representative's designation under which he or she is authorized to practice before the IRS (*e.g.*, certified public accountant, attorney) and licensing jurisdiction/number (if applicable) are included, and the representative signed and dated the Form 2848.
3. The tax year, tax period, and type of tax (*e.g.*, Form 1040) for which the taxpayer is authorizing the representative or designee is listed. The CAF unit will not process future tax years or periods listed that exceed three years from December 31 of the year that the CAF unit receives the form. For example, the CAF unit will not process a Form 8821 received in January 2018 if the tax period requested is Tax Year 2022.
4. There is identifying information for the taxpayer for whom the form is being submitted, including name, address, and Taxpayer Identification Number (TIN).³ The presence of two of the three identifiers is sufficient as long as the TIN is provided on the authorization. The tax examiner is also required to verify that the TIN is valid (*i.e.*, matches IRS records).
5. There is identifying information for the representative or designee, including name and address. For representatives and designees that have a CAF number, this number is provided along with their name and address. However, a CAF number is not a required element for processing. If a CAF number is not provided, the tax examiner will research to determine if one exists prior to assigning one.

Once the above information is confirmed, tax examiners use the Integrated Automated Technologies disclosure tool to determine the representative's status with the IRS. For example, the tool retrieves information from IRS records on whether the representative is in good standing with the IRS or suspended from representing taxpayers. This information helps the tax examiner determine if the form can be processed. Form 2848 authorizations submitted by a suspended, disbarred, or ineligible representative require the tax examiner to contact the Office of

³ A TIN is a nine-digit number assigned to taxpayers for identification purposes. The TIN is either an Employer Identification Number, a Social Security Number, or an Individual Taxpayer Identification Number.



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Professional Responsibility to verify the status.⁴ If this office confirms the status as suspended, disbarred, *etc.*, the form is rejected and a copy is sent to the Office of Professional Responsibility and the taxpayer.

The CAF units assign CAF numbers to taxpayer representatives and designees

Tax examiners are required to process authorization requests within five business days from receipt. Once verification is completed, the tax examiner will either input the information from the form into the CAF⁵ for the assignment of a CAF number to the representative or designee listed on the form or will issue the taxpayer a Letter 861C, *Power of Attorney Tax Information Authorization Incomplete for Processing*, requesting additional information. From January 1, 2016, through December 31, 2017, the CAF units issued 697,130 of these letters.

The CAF number allows the IRS to identify the representative or designee along with the taxpayers for whom the IRS has processed authorizations in the CAF. There are instances when a representative or designee is assigned multiple CAF numbers. In these instances, the representative or designee requests multiple CAF numbers to differentiate between multiple office addresses or related entities. Figure 2 provides the number of authorization requests processed to the CAF for Calendar Years 2016 and 2017.

Figure 2: Number of Authorization Requests Processed to the CAF

	Calendar Year 2016	Calendar Year 2017
Form 2848	1,512,618	849,193
Form 8821	444,756	412,977
Total Forms	1,957,374	1,262,170

Source: Our analysis of the CAF database, as of July 30, 2017.

Figure 3 provides the total number of representatives, designees, and taxpayers listed in the CAF.

Figure 3: Number of Representatives/Designees in the CAF

	CAF
Total Representatives/Designees	2,548,296
Total Taxpayers Represented	11,071,797

Source: Our analysis of the CAF database, as of July 30, 2017.

⁴ The Office of Professional Responsibility is responsible for all matters related to practitioner misconduct, discipline, and practice before the IRS. This office administers the law and regulations governing the practice of tax professionals and other individuals who interact with tax administration on behalf of taxpayers.

⁵ The CAF was created in 1983 and houses authorizations for power of attorney and requests for tax information. The Wage and Investment Division's Customer Account Services function oversees the CAF units.



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This review was performed at the Wage and Investment Division's headquarters in Atlanta, Georgia; Accounts Management sites where CAF submissions are processed in Philadelphia, Pennsylvania, and Ogden, Utah; and the IRS Campus in Andover, Massachusetts, during the period June 2017 through April 2018. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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Results of Review

**Management Has Not Implemented Sufficient Processes and
Procedures to Authenticate Request Forms**

Our review identified that tax examiner reviews of authorization forms do not include steps to verify that the taxpayer submitted or signed the form to authorize access to his or her tax information. Management stated that they submitted a work request for the Third-Party Authorization Tool in January 2017 which would strengthen security over the process for representatives or designees to access taxpayers' account information. The security features would include multifactor authentication that requires the individual submitting the authorization to pass authentication before submitting an authorization form. However, in June 2017, the IRS Strategic Development Executive Steering Committee⁶ did not approve the Third-Party Authorization Tool for funding, and in September 2017, the work request was cancelled. Officials in the Web Applications Program Management Office⁷ stated that the work request was not approved due to the level of priority it was given and availability of resources. The Committee's next opportunity to approve the development of the Third-Party Authorization Tool is June 2018.

Management's inaction on the implementation of the online Third-Party Authorization Tool is contrary to their own identification and confirmation that fraudulent authorizations are being submitted and processed. For example, tax examiners identified 1,897 authorization forms faxed to the CAF unit from April 4 to April 19, 2017, *****2***** for the taxpayers. Further analysis found that the forms were submitted using two CAF numbers. Since discovering this fraud, management has identified 16 stolen CAF numbers associated with 72,986 fraudulent authorizations that CAF units processed into the CAF since September 2010.

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⁶ This committee oversees the delivery of investments, programs, and projects. Oversight includes the authority to approve information technology projects based on established funding and targeted business results.

⁷ Office established to drive innovation and create digital services to meet taxpayer needs by operating across multiple business and delivery partners in the IRS in order to deliver web-based applications.



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Survey results further confirm that fraudulent authorization forms are being received and processed

To determine the extent of potentially fraudulent authorization requests that CAF units have processed into the CAF, IRS management selected a statistically random sample of 789 taxpayer representatives and designees from the CAF. These representatives and designees were authorized to represent 11,289 taxpayers. On October 20, 2017, the IRS mailed Letter 6018, *Request Verification of 3rd Party Access to Tax Information*,⁸ to the 11,289 taxpayers asking them to check one of two responses:

- I did authorize the third party listed in the letter to have access to my tax information.
- I did not authorize the third party listed in the letter to have access to my tax information.

As of February 6, 2018, the IRS received responses for 809 (7.2 percent) of the 11,289 taxpayer accounts⁹ for which the taxpayer stated that they did not authorize the third party listed in the letter to have access to their tax information. Based on the results of the IRS's statistically valid sample, we estimate that the IRS may have processed over 1.1 million unauthorized request forms for the 15,567,365 taxpayers who have an authorization in the CAF.¹⁰

CAF authorizations were not revoked for the majority of taxpayers who responded that they did not authorize the third-party listed in the IRS letter to have access to their tax information

We identified that the IRS did not revoke the authorization in the CAF for 787 (97 percent) of the 809 taxpayers who responded to the IRS's survey letter stating that they did not authorize the representative or designee listed in the letter. As such, the 787 taxpayers remain at risk of having their tax information accessed by an unauthorized individual. It should be noted that some responses to these letters were received as early as November 2017. For the 22 authorizations that the IRS revoked, the taxpayers not only checked the box to indicate that they did not authorize the third party listed in the letter, they also wrote a notation on their letter response asking the IRS to revoke the authorization.

When we asked Customer Account Services management why the authorizations were not revoked, they stated that they requested the authority to delete all authorizations for taxpayers who responded that they did not authorize the representative or designee. However, management officials in the Wage and Investment Division's Accounts Management function stated that taxpayers may not have recognized the representative or designee listed on the letter or may have forgotten that they submitted the authorization. As such, the IRS sent a follow-up

⁸ See Appendix V for Letter 6018.

⁹ There were 5,586 responses for the 11,289 taxpayer accounts.

¹⁰ We are 95 percent confident that the number of unauthorized requests is between 1,042,568 and 1,192,091 taxpayer requests.



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Letter 6018-A, *Third-Party Verification Follow-Up*,¹¹ to the 787 taxpayers on February 13, 2018. This follow-up letter requested that the taxpayers sign, date, and return their follow-up letter if they want the IRS to revoke the authorization. The follow-up letter also states that authorizations will remain in effect if the taxpayers do not return a signed copy of this letter. As of April 5, 2018, the IRS received and revoked the authorizations for 593 taxpayers who responded with a request for the IRS to revoke their authorization.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 1: Develop a program to send confirmation letters to taxpayers to confirm submissions prior to authorizing third-party access to their tax information. This confirmation letter program should be implemented until the Third-Party Authorization Tool is deployed and, after deployment, to taxpayers who continue to mail or fax authorization requests to the IRS.

Management's Response: The IRS agreed with this recommendation. However, IRS management believes that it would be cost prohibitive to do this for all authorizations received and processed by the CAF units. Alternatively, management plans to send confirmation letters to a statistically valid sample of new authorizations and use the response results to develop risk-based criteria that will be used to identify specific instances when confirmation letters should be sent. IRS management also stated that our estimate that over 1.1 million taxpayer accounts may be associated with unauthorized request forms in the CAF is substantially overstated.

Office of Audit Comment: Management provided no support for their statement that our forecast of potentially unauthorized request forms processed and added to the CAF is overstated. We calculated our forecast of over 1.1 million taxpayer accounts using the results from the IRS's own statistically valid sample. The IRS states that, of the 809 responses it received back from taxpayers, 787 taxpayers "did not ask to have the authorization removed from their account" and, as such, the IRS did not remove the authorization. However, the IRS's initial letter did not provide an option for the taxpayer to request removal of the authorization. Based on the options in this letter, these taxpayers responded, "I did not authorize the third party listed in the letter to have access to my tax information." When the IRS sent a follow-up letter, 593 taxpayers (as of April 5th) responded to confirm that they wanted the authorization revoked.

Recommendation 2: Revoke the 194 remaining authorizations in the CAF for which taxpayers responded to the IRS's initial survey letter stating that they did not authorize the representative or designee in the letter to access their tax account, and notify the taxpayers of this action.

¹¹ See Appendix VI for Letter 6018-A.



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Management's Response: The IRS agreed with this recommendation and has removed the authorizations as of June 2018.

**Actions Were Not Always Taken After Identifying That Fraudsters
Obtained Taxpayer Identification Numbers**

Our review identified that 300 TINs of taxpayers associated with confirmed fraudulent CAF numbers the IRS identified in June 2017 were not added to the IRS's Dynamic Selection List (DSL). The DSL is a list of TINs that the IRS identified as stolen in a data breach and, thus, at risk of tax-related identity theft. TINs placed on a DSL pass through a series of systemic filters to monitor their use on future tax returns submitted to the IRS. Those tax returns identified as potential identity theft are sent for further screening and verification.

When we met with Privacy, Governmental Liaison, and Disclosure¹² office officials to discuss the 300 TINs missing from the DSL, they stated that this was due to an oversight. Once we brought this issue to their attention, they immediately sent the 300 TINs to the Return Integrity and Compliance Services to be added to the DSL.

Timely actions were not always taken to mark fraudulent CAF numbers in the CAF

Our review identified that actions were not always taken to timely update the CAF when CAF numbers are identified as fraudulent. For example:

- IRS Criminal Investigation officials identified five stolen CAF numbers in March 2017 while investigating a business tax fraud case. These CAF numbers are associated with \$20.5 million in fraudulent business tax refunds that fraudsters stole by posing as attorneys for businesses. The CAF unit was not timely notified of this. As a result, the CAF units did not update the CAF with "confirmed fraudulent" for the five CAF numbers for five to seven months after Criminal Investigation identified the fraud scheme.
- The CAF unit did not timely update the CAF accounts with "confirmed fraudulent" for the 16 CAF numbers that were stolen by fraudsters. The CAF units took between four and ten months to update the CAF accounts after identifying that the CAF numbers were stolen.

Without timely updates to the CAF to identify CAF numbers that are confirmed fraudulent, customer service representatives,¹³ responsible for authenticating individuals who call the IRS and claim they are authorized to obtain taxpayers' information, are not aware that the CAF

¹² Organization responsible for performing a risk assessment to evaluate the risk of harm to taxpayers for all reported IRS breaches, including those resulting from the loss or compromise of Personally Identifiable Information.

¹³ The customer service representatives work in the Wage and Investment Division's Customer Account Services Accounts Management function.



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numbers were stolen. As a result, the customer service representatives may unknowingly release taxpayer information to a fraudster.

When we notified IRS management of the delays in updating confirmed fraudulent CAF numbers in the CAF, they stated that the lack of coordination between functions is partly due to the fact that CAF breaches are a recently identified security issue for which they have no specific written procedures for sharing information and coordinating with other functions. Management stated that it would develop procedures.

Management also noted that they issued an alert on December 5, 2017, to inform all IRS employees that they need to research the CAF when authenticating third parties. Management also coordinated with the Information Technology organization and initiated a work request in January 2018 to add two new fields to the Integrated Data Retrieval System¹⁴ to mark any CAF numbers that are identified as stolen. The Integrated Automated Technologies tool was also enhanced to enable customer service representatives to research the Integrated Data Retrieval System for the new fields. IRS management also explained that they strengthened internal procedures for customer service representatives to authenticate third parties who call the IRS requesting taxpayer information. For example, beginning in January 2018, customer service representatives are required to validate the representatives by performing basic authentication on the caller's Social Security Number.

Recommendations

Recommendation 3: The Director, Privacy, Governmental Liaison, and Disclosure, should develop a process to ensure that all TINs associated with confirmed fraudulent CAF authorizations are forwarded to the Return Integrity and Compliance Services.

Management's Response: The IRS agreed with this recommendation and has established procedures that address identified fraudulent CAF authorizations. IRS management updated its procedures in June 2018 to include guidance specifically addressing the treatment of improper authorizations.

Recommendation 4: The Commissioner, Wage and Investment Division, should develop procedures for all functions involved with investigating and responding to fraudulent authorization requests and stolen CAF numbers to timely share their findings and report them to CAF management. The procedures should provide steps for IRS functions to share compromised CAF numbers throughout the IRS.

¹⁴ The IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.



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Management’s Response: The IRS agreed with this recommendation and updated its procedures in June 2018 to provide guidance for all employees to report suspicious third-party authorizations.

Actions Were Not Taken to Prevent Some Taxpayer Refunds From Being Erroneously Issued to Representatives

Our review of the CAF identified that refund indicators are still set for 20,064 CAF representatives associated with 72,095 taxpayer authorizations. Because these indicators were not removed, 833 taxpayer refunds totaling \$4.78 million were erroneously issued to the associated representatives for Tax Years 2013 through 2015.

IRS management explained that, in October 2011, IRS Counsel removed the authority from Form 2848 for representatives to receive taxpayer refunds. The intent of this decision was to mitigate fraud and prevent representatives from negotiating and depositing taxpayers’ refund checks. In addition, IRS management took the following actions to mitigate this risk:

- Instructed employees not to input the refund indicator to the CAF on any authorizations received after the release of the October 2011 revision of Form 2848.
- Submitted a programming change request, in December 2011, to remove the refund indicators from the CAF. This programming was completed in January 2013 and removed the capability for representatives to receive refund checks *for future authorizations*.

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 *****4*****.” Counsel provided this instruction because it believed the new programming would operate to bypass any existing refund indicators on the CAF accounts. ***** 4*****
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Recommendation

Recommendation 5: The Commissioner, Wage and Investment Division, should either remove the refund indicator from all 72,095 authorizations that were processed prior to January 2013 or update refund issuance programming to ignore all refund indicators on the CAF file.

Management’s Response: The IRS agreed with this recommendation and has submitted a programming change request to have the existing refund indicators removed from the CAF.



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Tax Examiners Are Erroneously Assigning Multiple Centralized Authorization File Numbers to One Representative at One Location

Our review of CAF files identified CAF numbers assigned to 17,485 representatives or designees who submitted multiple authorization requests with the same representative or designee name and address. Internal procedures state that a representative or designee's request for a CAF number must contain a different name or address than a previously assigned CAF number. This procedure allows the IRS to identify the taxpayers that a representative or designee is authorized to represent.

CAF management was unaware that tax examiners were not following procedures to limit one CAF number to one representative or designee per office. We also found that management does not periodically review the CAF to identify excessive CAF numbers. After reviewing our results, management stated that they do not believe multiple CAF numbers assigned to the same representative or designee at the same address is a risk to taxpayers or tax administration. However, the excessive CAF numbers increase the risk that the IRS will release taxpayers' information to unauthorized individuals. Moreover, the IRS cannot identify the taxpayers that a representative or designee is authorized to represent.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 6: Ensure that tax examiners follow internal guidelines that require them to limit the issuance of CAF numbers to one CAF number per representative/designee at each office.

Management's Response: The IRS agreed with this recommendation and plans to review its guidance and make necessary updates or clarifications to ensure that employees research the CAF to prevent the issuance of multiple CAF numbers.

Recommendation 7: Correspond with representatives and designees assigned multiple CAF numbers to inform them that they are permitted to have one CAF number per location. The correspondence should request a response from each representative and designee specifying the CAF number that the IRS should retain. Excess numbers should then be removed from the CAF.

Management's Response: The IRS partially agreed with this recommendation. Prior to corresponding, IRS management will review the list of representatives and designees with multiple CAF numbers to identify those numbers that are being used. The IRS will correspond with those individuals to determine if there is a need for multiple numbers and identify those that can be removed.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective is to evaluate the IRS's controls to authenticate requests received from individuals seeking to represent taxpayers and access taxpayer information. To accomplish our objective, we:

- I. Evaluated the procedures and internal controls to authenticate forms received from third parties requesting to represent or access taxpayer information (*i.e.*, Form 2848, *Power of Attorney and Declaration of Representative*, and Form 8821, *Taxpayer Information Authorization*).
 - A. Evaluated the CAF¹ unit procedures for processing and authenticating Forms 2848 and 8821.
 - B. Evaluated alternatives for the IRS to authenticate individuals who requested authorization to represent and access taxpayer data via Forms 2848 and 8821.
 - C. Evaluated the use of the Office of Professional Responsibility's² representative status information (*e.g.*, disbarred, suspended) when authorizing representatives.
 - D. Determined how the CAF unit processes Forms 2848 and 8821 containing language that authorizes representatives to either receive the taxpayer's refund or endorse and negotiate the taxpayer's refund.
 - E. Evaluated the procedures and internal controls to ensure the accuracy of the data in the CAF database and the security of taxpayer data.
- II. Assessed incident response actions to evaluate the fraudulent representatives' impact on tax administration and assistance to taxpayers whose Personally Identifiable Information was accessed by fraudsters.
 - A. Evaluated the IRS's response to the broader issue of fraudulent representatives gaining access to taxpayer information on tax administration.

¹ The CAF was created in 1983 and houses authorizations for power of attorney and requests for tax information. The Wage and Investment Division's Customer Account Services function oversees the CAF units.

² The Office of Professional Responsibility is responsible for all matters related to practitioner misconduct, discipline, and practice before the IRS. This office administers the law and regulations governing the practice of tax professionals and other individuals who interact with tax administration on behalf of taxpayers.



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- B. Evaluated incident response activities that were initiated to research and investigate fraud associated with forms enabling third parties to represent taxpayers and access taxpayer information.
 - C. Evaluated the communication/coordination between IRS Criminal Investigation, the Return Integrity and Compliance Services function, and the CAF function when a fraudulent/suspicious third-party form is identified.
 - D. Determined the cause and effect for lack of response/coordination between IRS functions investigating fraudulent CAF numbers.
- III. Evaluated the processes and procedures the IRS used to identify and address potentially fraudulent forms.
- A. Interviewed Treasury Inspector General for Tax Administration Office of Investigations. We also interviewed IRS Criminal Investigation, Return Integrity and Compliance Services function, and other applicable functions, and identified common form attributes and activities regarding the fraudulent forms.
 - B. Evaluated the fraudulent processed and unprocessed CAF forms identified by the IRS for common characteristics to determine if other forms in the CAF database have these same characteristics.
 - C. Determined how many taxpayers answered the IRS's third-party verification letter and requested that authorizations be removed. A contracted statistician assisted with developing the projections. We used the results from responses to the IRS verification letter to project the results to the CAF database population. We are 95 percent confident that the percentage of taxpayers in the CAF database that have an unauthorized request is between 1.0 and 1.2 million. We used a confidence level of 95 percent, an estimated population exception rate of 7.2 percent, and a precision factor of 5 percent.
 - D. Evaluated the CAF database extract to identify invalid Taxpayer Identification Numbers.³
 - E. Evaluated the CAF unit's internal controls to identify and hold fraudulent and suspicious authorizations from processing.

Data validation methodology

During this review, we obtained data from the IRS's CAF database and our Strategic Data Services Division team worked on the CAF file transfer and validated the files. The Strategic Data Services Division team's validation process includes run-to-run balancing to ensure that the

³ A TIN is a nine-digit number assigned to taxpayers for identification purposes. The TIN is either an Employer Identification Number, a Social Security Number, or an Individual Taxpayer Identification Number.



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entire files were used with no gaps in the access or extraction of the data. In addition, and where applicable, other validation methods used include validation of the final output data back to source files; verification of the data using secondary sources, such as the Integrated Data Retrieval System;⁴ and checking the output data for “reasonableness” and expected output volume. We also selected random samples of each of the six CAF files and verified that the data in the files were the same as the data captured in the IRS’s Integrated Data Retrieval System. Based on the results of our testing, we believe that the data used in our review were reliable.

Internal controls methodology

Internal controls relate to management’s plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: the IRS processes and procedures for authenticating and processing authorizations; job aids and CAF internal revenue manuals; and IRS processes and procedures for ensuring accuracy of the CAF database.

⁴ The Integrated Data Retrieval System is an IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer’s account records.



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Appendix II

Major Contributors to This Report

Russell Martin, Assistant Inspector General for Audit (Returns Processing and Account Services)
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Jean Bell, Lead Auditor
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Laura Christoffersen, Auditor
Alexis Gomez, Auditor



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Appendix III

Report Distribution List

Deputy Commissioner for Services and Enforcement
Commissioner, Wage and Investment Division
Director, Accounts Management, Wage and Investment Division
Director, Return Integrity and Compliance Services, Wage and Investment Division
Director, Governmental Liaison, Disclosure, and Safeguards
Senior Operations Advisor, Wage and Investment Division
Director, Office of Audit Coordination



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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 Privacy and Security – Potential; 1,115,599 taxpayer accounts associated with unauthorized request forms in the CAF (see page 5).

Methodology Used to Measure the Reported Benefit:

To determine the extent of potentially fraudulent authorization requests that CAF units have processed into the CAF, IRS management selected a statistically random sample of 789 taxpayer representatives and designees from the CAF. These representatives and designees were authorized to represent 11,289 taxpayers. On October 20, 2017, the IRS mailed Letter 6018, *Request Verification of 3rd Party Access to Tax Information*, to the 11,289 taxpayers asking them to check one of two responses:

- I did authorize the third party listed in the letter to have access to my tax information.
- I did not authorize the third party listed in the letter to have access to my tax information.

As of February 6, 2018, the IRS received responses for 809 (7.2 percent) of the 11,289 taxpayer accounts¹ for which the taxpayer stated that they did not authorize the third party listed in the letter to have access to their tax information. Based on the results of the IRS's statistically valid sample, we estimate that the IRS may have processed 1,115,599 unauthorized request forms for the 15,567,365 taxpayers who have an authorization in the CAF.²

The CAF unit will not process future tax years or periods listed that exceed three years from December 31 of the year that the CAF unit receives the form. As such, the current authorizations for the 1,115,599 taxpayer accounts will eventually expire and new authorization requests will have to be approved in order for a representative or designee to be associated with the account. By developing the confirmation letter program, these taxpayers will be made aware prior to the IRS authorizing third-party access to their tax information in the future.

¹ There were 5,586 responses for the 11,289 taxpayer accounts.

² We are 95 percent confident that the number of unauthorized requests is between 1,042,568 and 1,192,091 taxpayer requests.



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Type and Value of Outcome Measure:

Taxpayer Privacy and Security – Potential; 194 taxpayer accounts whose third-party representation authorizations were not revoked even though they responded to the IRS’s survey letter and indicated that they did not authorize the listed representative or designee (see page 5).

Methodology Used to Measure the Reported Benefit:

We identified that the IRS did not revoke the authorization in the CAF for 787 taxpayers who responded to Letter 6018 stating that they did not authorize the representative or designee listed in the letter. Instead, the IRS issued the 787 taxpayers Letter 6018-A, *Third-Party Verification Follow-Up*, and subsequently received responses from 593 taxpayers who requested that the IRS revoke their authorizations in the CAF. The IRS revoked the authorizations for these taxpayers. Thus, 194 (787 – 593) taxpayers are still at risk of having their tax information accessed by an unauthorized individual.

Type and Value of Outcome Measure:

Taxpayer Privacy and Security – Actual; 300 taxpayer accounts associated with confirmed fraudulent CAF numbers that the IRS did not add to its Dynamic Selection List (see page 8).

Methodology Used to Measure the Reported Benefit:

Our review identified that 300 taxpayers’ TINs associated with confirmed fraudulent CAF numbers were not added to the IRS’s Dynamic Selection List. IRS management stated that they neglected to send the TINs to the Return Integrity and Compliance Services function for inclusion on the Dynamic Selection List.



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Appendix V

Letter 6018, Request Verification of 3rd Party Access to Tax Information



Department of the Treasury
Internal Revenue Service
Attn: CAF Team
Philadelphia, PA 19255-0625

Date:

Taxpayer ID number:
[NNN-NN-1234]
Contact telephone number:
800-829-1040
Contact fax number:
855-772-3156
International phone number:
+1-267-941-1000
International fax number:
+1-304-707-9785

Dear [Name]:

Why you're receiving this letter

We're contacting you because we want to be sure that only people you authorize, whether tax professionals or family members, are accessing your tax account.

Our records show that we have an authorization Form [number, title] on file from the following third party:
[Third Party business name or representative name based on Form 8821 or 2848 filed]

[Third Party business name or representative name based on Form 8821 or 2848 filed] currently has authority to access your tax account based on the submission of Form [number, title] to the IRS.

Please know that this is a random review of current third-party authorizations. This does not mean that there is a problem. This letter is one of the ways to verify the authorization of third-party access.

What you need to do

Check the appropriate box below and return this letter to the IRS address above within 30 days (or, if you prefer, you can fax it to the number above within 30 days) from the date of this letter, so we can complete our third-party verification process.

- I did authorize the third party listed above to have access to my account.
- I did **not** authorize the third party listed above access to my account.

If you checked the "I did not authorize...." box

Please be aware that the third party listed may be affiliated with the entity or individual that you authorized to access your account information. We will contact you and let you know if you need to take any additional action. Please review the links under the "Additional Information" section below.

If you don't respond

We'll place all actions (including refunds) on hold until you respond and we complete the third-party verification.

Additional information

- Visit www.irs.gov/ltr6018
- Visit www.irs.gov/thirdpartyauthorizations for more information.

Letter 6018 (10-2017)
Catalog Number 71014W



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We recognize that keeping your information confidential is a critical priority. We're working hard to protect your tax information and prevent unauthorized disclosures.

We apologize for any inconvenience and thank you for your cooperation.

Sincerely,

Fred Banks

Fred Banks, Program Mgr
W&I Service Center, AM

Letter 6018 (10-2017)
Catalog Number 71014W



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Appendix VI

Letter 6018-A, Third-Party Verification Follow-Up



[Taxpayer name]
[Address line 1]
[Address line 2]
[Address line 3]
[Address line 4]

Date:
Taxpayer ID number:
Tax periods:
Contact telephone number:
Contact fax number:
International telephone number:
International fax number:

Dear [Name]:

Why you're receiving this letter

We received your response to Letter 6018 (Third Party Access Verification). You told us that you did not or no longer authorized [insert Third Party Name] to have access to your tax account. For your security, we reviewed your account and did not find any suspicious activity.

What you need to do

Because you indicated that you don't want [insert Third Party Name] to have access to your account, please return a signed and dated copy of this letter to the IRS address above (or if you prefer, you can fax it to the number above) to end the authorization. You can use this method to revoke authorization for up to 60 days after the date of this letter. You can also revoke authorizations at any time by following the instructions at IRS.gov/thirdpartyauthorizations.

Note: If you don't return a signed and dated copy of this letter or initiate a revocation following the instructions at IRS.gov/thirdpartyauthorizations, the authorization will remain in effect and [insert Third Party Name] will continue to have access to your account.

I do not/no longer authorize [insert Third Party Name] to have access to my tax accounts for all tax matters for all years and periods.

Taxpayer signature: _____ **Date signed:** _____

Additional information

- Visit www.irs.gov/ltr6018-A
- Visit www.irs.gov/thirdpartyauthorizations for more information

We recognize that keeping your information confidential is a critical priority. We're working hard to protect your tax information and prevent unauthorized disclosures.

If you have questions, call the telephone number listed at the top of this letter.

We apologize for any inconvenience and thank you for your cooperation.

Sincerely,
Fred Banks
Fred Banks, Program Manager
W&I Service Center, AM

Letter 6018-A (2-2018)
Catalog Number 71151A



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Appendix VII

Management's Response to the Draft Report



COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

AUG 0 2 2018

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Kenneth C. Corbin 
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Improved Procedures Are Needed to
Prevent the Fraudulent Use of Third Party Authorization Forms
to Obtain Taxpayer Information (Audit # 201740038)

Thank you for the opportunity to review and provide comments on the subject draft report. The Centralized Authorization File (CAF) is a repository in which information on individuals whom taxpayers have designated to either act on their behalf or have access to their tax information is stored. Designations are made by taxpayers executing Form 2848, Power of Attorney and Declaration of Representative, or Form 8821, Tax Information Authorization. Identifying information for the designees and the specific actions or access rights taxpayers have authorized them to have is maintained within the CAF. This information is available to IRS employees and certain automated systems to facilitate fulfilling service requests and administrative processing of accounts. With the CAF, burden is eliminated for taxpayers and their representatives by eliminating the need for multiple submissions of the same authorization.

The CAF was designed and implemented in an era when most taxpayer and practitioner interactions with the IRS were transacted on paper. As the use of personal computers has transformed the way business is now conducted, we have taken steps to fortify safeguards and defenses to ensure taxpayer information is protected from unauthorized disclosure. An example of those actions, as mentioned in the report, is providing for the submission of authorization forms through the Third-Party Authorization Tool (TPAT), which would require individuals submitting authorizations to pass multifactor authentication. Although this work was not funded for fiscal year 2018, due to other programming and infrastructure needs that were deemed to be more critical in supporting immediate tax administration needs, it cannot be concluded that this work is not a priority for the IRS. With limited resources, difficult decisions must be made in how those resources are used. We will continue to pursue implementation of an online authorization



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interface; however, it must be understood that this implementation alone will not mitigate all risks associated with taxpayer authorizations.

An online option will provide a more secure method of authentication; however not all taxpayers will have the ability to use this method and will continue to need to submit paper authorizations. Having a requirement for online-only submission may hamper taxpayers' ability to secure representation. As of June 2018, we have implemented several actions to reduce the risks associated with potentially fraudulent authorizations. A service wide process is in place for employees to report suspicious authorizations for referral to the Criminal Investigation Division. Enhanced third-party authentication procedures are in place for telephone assistors, as are procedures to identify CAF numbers that are pending review or confirmed as compromised. Moreover, we have updated the e-Services Transcript Delivery System to recognize CAF numbers reported as compromised or pending review and to reject any transcripts requests made with those numbers.

Using these processes, our employees identified the 1,897 potentially fraudulent authorization forms that had been faxed to the CAF unit over a 15-day period in April 2017. This discovery ultimately led to the identification of 16 stolen CAF numbers associated with 72,986 potentially fraudulent authorizations, which is 0.55 percent of the 13.2 million authorizations processed into the CAF between 2010 and 2017 that are the subject of the report. The audit did not detect any additional instances of confirmed fraudulent authorizations or instances of taxpayer information being erroneously released as a result of a fraudulent authorization. Nevertheless, the report reflects an Outcome Measure estimating there are potentially 1.1 million unauthorized requests currently residing in the CAF. We disagree with this estimate and believe it is substantially overstated.

Upon identification of the 16 stolen CAF numbers, we selected a statistically valid random sample of 789 representatives and designees from the CAF. We corresponded with the 11,289 taxpayers associated with these 789 representatives or designees to ascertain if the authorizations had, in fact, been made by the taxpayers. Of the 809 responses received where the taxpayer stated they did not authorize the named representative or designee, 787 did not ask to have the authorization removed from their account. We researched these 787 accounts and did not find any suspicious activity had occurred. Follow-up letters were sent to these taxpayers asking for their affirmation whether the authorizations should be revoked. It is a common practice when taxpayers seek representation in administrative matters before the IRS that alternate representatives are listed with the primary representative on Form 2848, such as another partner or associate who can continue to represent the taxpayer when the primary representative is unable to do so. Similarly, the execution of Form 8821 is a standard practice when individuals apply for mortgages and some other types of credit arrangements. In both situations, it is possible taxpayers would not be able to immediately recall the individuals included on the authorizations without researching



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their retained copies. Having found no suspicious activity on the accounts of the group receiving follow-up letters, it is not reasonable to extrapolate that 1.1 million unauthorized requests exist in the CAF based solely on the 809 initial responses.

We generally agree with the recommendations made in the report and have partially or fully implemented many of them. Attached are our comments and proposed actions to your recommendations. If you have any questions, please contact me, or a member of your staff may contact James P. Clifford, Director, Customer Account Services, Wage and Investment Division, at 470-639-3504.

Attachment



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Attachment

Recommendations

The Commissioner, Wage and Investment Division, should:

RECOMMENDATION 1

Develop a confirmation letter program to send to taxpayers to confirm submissions prior to authorizing third-party access to their tax information. This confirmation letter program should be implemented until the Third-Party Authorization Tool is deployed and, after deployment, to taxpayers who continue to mail or fax authorization requests to the IRS.

CORRECTIVE ACTION

We agree with this recommendation; however, we believe its implementation for all authorizations received and processed by the Centralized Authorization File (CAF) units will be cost prohibitive. Alternatively, we will send confirmation letters to a statistically valid sample of new authorizations and use the response results to develop risk-based criteria that will be used to identify specific instances when confirmation letters should be sent.

IMPLEMENTATION DATE

June 15, 2019

RESPONSIBLE OFFICIAL

Director, Accounts Management, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 2

Revoke the 194 remaining authorizations in the CAF for which taxpayers responded to the IRS's initial survey letter stating that they did not authorize the representative or designee in the letter to access their tax account, and notify the taxpayers of this action.

CORRECTIVE ACTION

We agree with this recommendation and, as of June 2018, have removed the authorizations for which taxpayers responded to the initial survey letter stating they did not authorize the representative or designee.

IMPLEMENTATION DATE

Implemented



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RESPONSIBLE OFFICIAL

Director, Accounts Management, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

We will monitor this corrective action as part of our internal management control system.

Recommendations

RECOMMENDATION 3

The Director, Privacy, Governmental Liaison, and Disclosure, should develop a process to ensure that all TINs associated with confirmed fraudulent CAF authorizations are forwarded to the Return Integrity and Compliance Services.

CORRECTIVE ACTION

We agree with this recommendation. Procedures have been established that address identified compromised/fraudulent CAF authorizations. The Taxpayer Treatment Guide (TTG) addresses actions and activities, such as updating the CAF, Dynamic Selection Lists, and required notifications, applied to potential victims. The TTG and related Internal Revenue Manual (IRM) sections 21.3.7.5.5.3, *How to Report a Compromised or Potentially Compromised CAF Number* and 21.3.7.5.5.1, *Criminal Investigation (CI) Involvement in the CAF/POA Suspicious Forms Log and the "Potential Fraud" Authorization Referral Process*, were updated in June 2018 to include guidance specifically addressing the treatment of improper authorizations.

IMPLEMENTATION DATE

Implemented

RESPONSIBLE OFFICIAL

Director, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 4

The Commissioner, Wage and Investment Division, should develop procedures for all functions involved with investigating and responding to fraudulent authorization requests and stolen CAF numbers to timely share their findings and report them to CAF management. The procedures should provide steps for IRS functions to share compromised CAF numbers throughout the IRS.



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CORRECTIVE ACTION

We agree with this recommendation. On June 11, 2018, IRM 21.3.7.5.5.3 was updated to provide guidance for all employees to report suspicious third-party authorizations.

IMPLEMENTATION DATE

Implemented

RESPONSIBLE OFFICIAL

Director, Accounts Management, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 5

The Commissioner, Wage and Investment Division, should either remove the refund indicator from all 72,095 authorizations that were processed prior to January 2013 or update refund issuance programming to ignore all refund indicators on the CAF file. Recommendations

CORRECTIVE ACTION

We agree with this recommendation and have submitted a Unified Work Request to have the existing refund indicators removed from the CAF. Implementation will require Information Technology's assistance and is subject to limited resources and competing priorities. An implementation date cannot be provided.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

Director, Accounts Management, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

We will monitor this corrective action as part of our internal management control system.



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Recommendations

The Commissioner, Wage and Investment Division, should:

RECOMMENDATION 6

Ensure that tax examiners follow internal guidelines that require them to limit the issuance of CAF numbers to one CAF number per representative/designee at each office.

CORRECTIVE ACTION

We agree with this recommendation. Internal guidance already requires employees to research the CAF to prevent the issuance of multiple CAF numbers. We will review the guidance and make any necessary updates or clarifications to ensure compliance with these instructions.

IMPLEMENTATION DATE

January 15, 2019

RESPONSIBLE OFFICIAL

Director, Accounts Management, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 7

Correspond with representatives and designees assigned multiple CAF numbers to inform them that they are permitted to have one CAF number per location. The correspondence should request a response from each representative and designee designating the CAF number that the IRS should retain. Excess numbers should then be removed from the CAF.

CORRECTIVE ACTION

We partially agree with this recommendation. Prior to corresponding, we will review the list of representatives and designees with multiple CAF numbers assigned to identify those numbers that are being used. We will correspond with those individuals to determine if there is a need for multiple numbers and identify those that can be removed.

IMPLEMENTATION DATE

June 15, 2019



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RESPONSIBLE OFFICIAL

Director, Accounts Management, Customer Account Services, Wage and Investment
Division

CORRECTIVE ACTION MONITORING PLAN

We will monitor this corrective action as part of our internal management control
system.