
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



***Fiscal Year 2017 Statutory Audit of
Compliance With Legal Guidelines
Prohibiting the Use of Illegal Tax Protester
and Similar Designations***

August 28, 2017

Reference Number: 2017-30-059

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

Redaction Legend:

1 = Tax Return/Return Information

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HIGHLIGHTS

FISCAL YEAR 2017 STATUTORY AUDIT OF COMPLIANCE WITH LEGAL GUIDELINES PROHIBITING THE USE OF ILLEGAL TAX PROTESTER AND SIMILAR DESIGNATIONS

Highlights

Final Report issued on August 28, 2017

Highlights of Reference Number: 2017-30-059 to the Internal Revenue Service Deputy Commissioner for Services and Enforcement and Deputy Commissioner for Operations Support.

IMPACT ON TAXPAYERS

Congress enacted the IRS Restructuring and Reform Act of 1998 (RRA 98) Section 3707 to prohibit the IRS from labeling taxpayers as Illegal Tax Protesters or any similar designations. Using Illegal Tax Protester or other similar designations may stigmatize taxpayers and may cause employee bias in future contacts with these taxpayers.

WHY TIGTA DID THE AUDIT

Congress enacted the prohibition against Illegal Tax Protester designations because it was concerned that some taxpayers were being permanently labeled as Illegal Tax Protesters even though they had subsequently become compliant with the tax laws. TIGTA is required to annually evaluate IRS compliance with the prohibition against using Illegal Tax Protester or similar designations.

The purpose of this audit was to determine whether the IRS complied with RRA 98 Section 3707 and its own internal guidelines that prohibit IRS officers and employees from referring to taxpayers as Illegal Tax Protesters or any similar designations.

WHAT TIGTA FOUND

The IRS has not reintroduced past Illegal Tax Protester codes or similar designations on taxpayer accounts. However, in reviewing the narrative data entered for approximately 22.1 million taxpayers in the Account

Management Services system, TIGTA found that there were 11 instances in which nine employees referred to taxpayers as “Tax Protester/Protestor.”

WHAT TIGTA RECOMMENDED

TIGTA recommended that IRS management emphasize to all employees with access to the Account Management Services system the importance of compliance with RRA 98 Section 3707 and reinforce that taxpayers are not to be referred to as Illegal Tax Protesters or any other similar designations. This may include, but is not limited to, updating procedures, issuing a memorandum, or adding a module to an existing training course.

In their response, IRS management agreed with TIGTA’s recommendation and stated that it has implemented corrective actions.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

August 28, 2017

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

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Fiscal Year 2017 Statutory Audit of Compliance
With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations (Audit # 201730005)

This report presents the results of our review to determine whether the Internal Revenue Service (IRS) complied with the IRS Restructuring and Reform Act of 1998 (RRA 98)¹ Section 3707 and internal IRS guidelines that prohibit IRS officers and employees from referring to taxpayers as “illegal tax protesters” (Illegal Tax Protesters) or any similar designations. This audit is included in our Fiscal Year 2017 Annual Audit Plan and addresses the major management challenge of Taxpayer Protection and Rights.

Management’s complete response to the draft report is included as Appendix VI.

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

¹ Pub. L. No. 105-206, 112 Stat. 685.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Table of Contents

[Background](#).....Page 1

[Results of Review](#).....Page 3

[Illegal Tax Protester Codes Were Not Used on the Master File](#).....Page 3

[In a Few Instances, Employees Used Illegal Tax Protester or
Similar Designations in Case Narratives](#)Page 3

[Recommendation 1:](#)Page 5

[Alternative Methods Are in Place to Address Tax Compliance
Issues With Taxpayers Who Protest the Legality of Income Taxes](#).....Page 5

Appendices

[Appendix I – Detailed Objective, Scope, and Methodology](#)Page 6

[Appendix II – Major Contributors to This Report](#)Page 8

[Appendix III – Report Distribution List](#).....Page 9

[Appendix IV – Recent Audit Reports Related to This Statutory Review](#)Page 10

[Appendix V – Glossary of Terms](#).....Page 11

[Appendix VI – Management’s Response to the Draft Report](#)Page 13



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Abbreviations

IRS	Internal Revenue Service
RRA 98	Restructuring and Reform Act of 1998
TIGTA	Treasury Inspector General for Tax Administration



Fiscal Year 2017 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations

Background

Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)¹ Section (§) 3707 prohibits the IRS from using Illegal Tax Protester or any similar designations. In addition, the law required the removal of all existing Illegal Tax Protester codes from the Individual Master File² and instructed IRS employees to disregard any such designation located on any other databases. In prior reviews, the Treasury Inspector General for Tax Administration (TIGTA) reported that the IRS removed the Illegal Tax Protester codes from the Individual Master File as required by the law.

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

TIGTA is required to annually evaluate IRS compliance with the prohibition against using Illegal Tax Protester or any similar designations.

Congress was concerned that some taxpayers were being permanently labeled and stigmatized by the Illegal Tax Protester designation. The concern was that this label could bias IRS employees and result in unfair treatment of the taxpayer. Internal Revenue Code § 7803(d)(1)(A)(v) requires TIGTA to annually evaluate IRS compliance with the prohibition against using the Illegal Tax Protester or any similar designations. This is our nineteenth review since Fiscal Year 1999. These reviews have identified areas for improvement to help the IRS comply with the Illegal Tax Protester designation prohibition.

To conduct this audit, TIGTA reviews the Individual Master File and related systems annually, as required by the RRA 98, and each year TIGTA additionally selects other IRS systems for review on a periodic basis. This year we focused on the Automated Collection System, Integrated Collection System, and Accounts Management Services system.

¹ Pub. L. No. 105-206, 112 Stat. 685.

² See Appendix V for a glossary of terms.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

This review was performed with information obtained from electronic files accessed through the TIGTA network and with information from the Small Business/Self-Employed Division in New Carrollton, Maryland, and the Wage and Investment Division in Atlanta, Georgia, during the period October 2016 through April 2017. This performance audit was conducted 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.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Results of Review

Illegal Tax Protester Codes Were Not Used on the Master File

Prior to enactment of the RRA 98, the IRS used Illegal Tax Protester indicators on the Master File to accelerate collection activity for taxpayers who were delinquent in filing tax returns or paying their taxes. These indicators were also intended to alert employees that they might encounter problems when dealing with nonfilers and delinquent taxpayers.

Congress was concerned about the use of the Illegal Tax Protester designation because:

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

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

In prior reviews, TIGTA reported the IRS had removed these designation codes from the Master File as required by the law. Based on our analysis of approximately 1.2 million taxpayer records that had been coded for accelerated collection activity, the IRS has not reintroduced Illegal Tax Protester codes on the Master File. The law also prohibits using any designation similar to Illegal Tax Protester.

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

In reviewing the narrative data entered for approximately 22.1 million taxpayers during the period October 2015 through September 2016 in the Account Management Services system, we found 11 instances in which nine employees had labeled taxpayers as an Illegal Tax Protester. TIGTA believes the 11 instances identified in the Account Management Services system are prohibited by law. Figure 1 contains the number of Illegal Tax Protester or similar designations identified in IRS computer systems' case narratives during our Fiscal Years 2013³ and 2017 reviews. The Automated Collection System, Integrated Collection System, and Account Management Services System were not reviewed in Fiscal Years 2014 through 2016.

³ TIGTA, Ref. No. 2013-30-085, *Fiscal Year 2013 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Aug. 2013).



**Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations**

Figure 1: Use of Illegal Tax Protester and Similar Designations in Case Narratives

Computer System	Fiscal Year 2013 Review			Fiscal Year 2017 Review		
	Employees Involved	Protester Designation Used	Similar Designation Used	Employees Involved	Protester Designation Used	Similar Designation Used
Account Management Services System	33	38	*1*	9	11	0
Automated Collection System	0	0	0	0	0	0
Integrated Collection System	12	4	11	0	0	0

Source: Case narratives found on various IRS computer systems and TIGTA's Fiscal Year 2013 report.

We also reviewed the Remarks sections of the Automated Collection System for approximately 13.3 million records, the Integrated Collection System for 376,369 records, and the Taxpayer Information File for 321,451 records between October 1, 2015, and September 30, 2016. Our review found no use of Illegal Tax Protester or other similar designations in any of the text narratives for these systems.

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



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Recommendation

Recommendation 1: The Commissioner, Wage and Investment Division, should emphasize to all employees with access to the Account Management Services system the importance of compliance with RRA 98 § 3707 and reinforce that taxpayers are not to be referred to as Illegal Tax Protesters or any other similar designations. This may include, but is not limited to, updating procedures, issuing a memorandum, or adding a module to an existing training course.

Management's Response: IRS management agreed with our recommendation and stated that they have emphasized to all employees with access to the Account Management Services system the importance of compliance with Section 3707 and reinforced that taxpayers are not to be referred to as Illegal Tax Protesters or any other similar designations.

Alternative Methods Are in Place to Address Tax Compliance Issues With Taxpayers Who Protest the Legality of Income Taxes

In limited circumstances, it may be appropriate for the IRS to label taxpayers or their actions due to various issues IRS employees may encounter when dealing with taxpayers protesting the legality of paying their income taxes. Because of this, alternative programs exist to address issues previously handled by the Illegal Tax Protester Program. These include:

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

Unlike the former Illegal Tax Protester Program, each program addresses a specific taxpayer behavior. In addition, taxpayers are not assigned to these individual programs on a permanent basis, as was the case in the Illegal Tax Protester Program.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Appendix I

Detailed Objective, Scope, and Methodology

The objective of this review was to determine whether the IRS complied with RRA 98¹ § 3707 and its own internal guidelines that prohibit IRS officers and employees from referring to taxpayers as Illegal Tax Protesters or any similar designations. To accomplish the objective, we:

- I. Determined if the Illegal Tax Protester coding on the Master File² was removed by reviewing all tax accounts coded for accelerated collection activity as of September 30, 2016, on the Business Master File and Individual Master File. We analyzed 1,230,311 Master File records that had been coded for accelerated collection activity.³

We also matched our historic computer extract of approximately 55,000 taxpayers designated as Illegal Tax Protesters before the RRA 98 was enacted to the records that had been coded for accelerated collection activity to determine if any new common codes were being used to classify the taxpayers as Illegal Tax Protesters.

- II. Determined if employees were using Illegal Tax Protester or any similar designations within the Activity Code field on the Taxpayer Information File by securing a copy of the database and analyzing 321,451 open records with activity between October 1, 2015, and September 30, 2016.
- III. Determined if the IRS is using any Frivolous Return Program codes as replacements for Illegal Tax Protester designations by reviewing guidance provided for the Frivolous Return Program and interviewing its Program Coordinator.
- IV. Determined if there is any relationship between Illegal Tax Protester designations and Potentially Dangerous Taxpayer/Caution Upon Contact indicator use on the Master File by reviewing guidance provided for the Potentially Dangerous Taxpayer/Caution Upon Contact Program and interviewing its Program Coordinator.
- V. Determined if the IRS Nonfiler Program is in compliance with the provisions established by RRA 98 § 3707(b) by reviewing guidance provided for the Nonfiler Program and interviewing its program coordinators.

¹ Pub. L. No. 105-206, 112 Stat. 685.

² See Appendix V for a glossary of terms.

³ A Transaction Code 148 causes the accelerated issuance of a Taxpayer Delinquency Investigation or Taxpayer Delinquent Account.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

- VI. Determined if employees were using the Illegal Tax Protester or any similar designations within taxpayer case narratives on the Automated Collection System by securing a copy of the database and analyzing 13,264,696 records as of September 30, 2016, with history action dates between October 1, 2015, and September 30, 2016.
- VII. Determined if employees were using the Illegal Tax Protester or any similar designations within taxpayer case narratives on the Integrated Collection System by securing a copy of the database and analyzing 376,369 records as of September 30, 2016, with history action dates between October 1, 2015, and September 30, 2016.
- VIII. Determined if employees were using the Illegal Tax Protester or any similar designations within taxpayer case narratives on the Account Management Services system by securing a copy of the database as of September 30, 2016, and analyzing records for 22,141,838 taxpayers with activity between October 1, 2015, and September 30, 2016.

Validity and reliability of data from computer-based systems

Unless otherwise noted, our limited tests of the reliability of data obtained from various IRS systems did not identify any errors. We tested the reliability of the data by scanning the data received for blank, incomplete, illogical, or improper data. In addition, we compared the information in a judgmental sample of 25 records each for the Business Master File, Individual Master File, Taxpayer Information File, Account Management Services system, Automated Collection System, and Integrated Collection System to IRS source data on the Integrated Data Retrieval System to ensure data accuracy.

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: controls that ensure the reliability of the data used for our analysis. During our review, we tested the validity of the data used for our analyses against selected IRS data, but we did not perform any specific testing of data input controls. However, it should be noted that data from these same systems were used during prior audits of Illegal Tax Protester designations, and no significant data issues were identified.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Appendix II

Major Contributors to This Report

Matthew Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Glen Rhoades, Director
Robert Jenness, Audit Manager
Debra Mason, Lead Auditor
Ali Vaezazizi, Auditor



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Appendix III

Report Distribution List

Commissioner
Office of the Commissioner – Attn: Chief of Staff
Commissioner, Small Business/Self-Employed Division
Commissioner, Wage and Investment Division
Chief, Appeals
National Taxpayer Advocate
Chief Information Officer
Director, Accounts Management, Wage and Investment Division
Director, Communications and Stakeholder Outreach
Director, Office of Research, Applied Analytics, and Statistics
Director, Office of Servicewide Policy, Directives, and Electronic Research
Director, Office of Audit Coordination



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Appendix IV

***Recent Audit Reports Related to This
Statutory Review***

TIGTA, Ref. No. 2010-30-073, *Fiscal Year 2010 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Jul. 2010).

TIGTA, Ref. No. 2011-30-040, *Fiscal Year 2011 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Apr. 2011).

TIGTA, Ref. No. 2012-30-066, *Fiscal Year 2012 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Jun. 2012).

TIGTA, Ref. No. 2013-30-085, *Fiscal Year 2013 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Aug. 2013).

TIGTA, Ref. No. 2014-30-060, *Fiscal Year 2014 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Aug. 2014).

TIGTA, Ref. No. 2015-30-067, *Fiscal Year 2015 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Aug. 2015).

TIGTA, Ref. No. 2016-30-087, *Fiscal Year 2016 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Sept. 2016).

¹ This list provides the most recent seven of the 18 previous reports issued by TIGTA.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Appendix V

Glossary of Terms

Account Management Services System	Provides employees access to multiple IRS systems through their computers and allows for inventory management, case delivery, history narratives, print-to-fax capabilities for sending information to taxpayers, and electronic referral generation.
Activity Code	A code that identifies the type and condition of returns selected for audit.
Automated Collection System	A telephone contact system through which telephone assistants collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.
Business Master File	The IRS database that consists of Federal tax-related transactions and accounts for businesses. These include employment taxes, income taxes on businesses, and excise taxes.
Campus	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.
Fiscal Year	A yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.
Individual Master File	The IRS database that maintains transactions or records of individual tax accounts.
Integrated Collection System	A system used by Collection function employees to report taxpayer case time and activity.
Integrated Data Retrieval System	A computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.
Internal Revenue Code	Federal tax law enacted by Congress in Title 26 of the United States Code.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Master File	The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.
Taxpayer Delinquency Investigation	An unfiled tax return for a taxpayer. One Taxpayer Delinquency Investigation exists for all unfiled tax periods for a specific taxpayer.
Taxpayer Delinquent Account	A balance due account of a taxpayer. A separate Taxpayer Delinquent Account exists for each balance due tax period.
Taxpayer Information File	A file containing entity and tax data processed at a given campus for all Taxpayer Identification Numbers.
Transaction Code	A three-digit code used to identify transactions being taken on a taxpayer's account.



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Appendix VI

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

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

JUL 27 2017

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Mary Beth Murphy *Mary Beth Murphy*
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report Fiscal Year 2017 Statutory Audit of
Compliance With Legal Guidelines Prohibiting the Use of Illegal
Tax Protester and Similar Designations (Audit # 201730005)

Thank you for the opportunity to review and comment on the subject draft audit report. Section 3707 of the Internal Revenue Restructuring and Reform Act of 1998 (RRA '98) prohibits the labeling of taxpayers as Illegal Tax Protestors. As noted in the report, we removed Illegal Tax Protester codes and references from the Master File a number of years ago as required by the law, and have not reintroduced them. This year TIGTA reviewed approximately 13.3 million records in the Remarks sections of the Automated Collection System, 376,369 records in the Integrated Collection System, and 321,451 records in the Taxpayer Information File and found no use of Illegal Tax Protester or other similar designations in any of the text narratives for these systems. TIGTA reviewed the narrative data entered for approximately 22.1 million taxpayers in the Account Management Services (AMS) system and found 11 instances in which nine employees had used such labels or designations.

We agree with your recommendation that we emphasize to all employees with access to the Account Management Services system the importance of compliance with Section 3707 and reinforce that taxpayers are not to be referred to as Illegal Tax Protesters or any other similar designations. On July 12, 2017, we issued a Servicewide Alert to our employees communicating this information.

Attached is a response outlining our corrective action to address your recommendation. If you have any questions, please contact me, or a member of your staff may contact Scott Prentky, Director Collection at (954) 991-4326.

Attachment



***Fiscal Year 2017 Statutory Audit of Compliance With
Legal Guidelines Prohibiting the Use of Illegal Tax Protester and
Similar Designations***

Attachment

RECOMMENDATION 1:

The Commissioner, Wage and Investment Division, should emphasize to all employees with access to the Account Management Services system the importance of compliance with RRA 98 § 3707 and reinforce that taxpayers are not to be referred to as Illegal Tax Protesters or any other similar designations. This may include, but is not limited to, updating procedures, issuing a memorandum, or adding a module to an existing training course.

CORRECTIVE ACTION:

We agree to reinforce to AMS users that taxpayers are not to be referred to as illegal tax protesters or any other similar designations, and on July 12, 2017, we issued a Servicewide Electronic Research Program (SERP) Alert communicating this information.

IMPLEMENTATION DATE:

Implemented

RESPONSIBLE OFFICIAL:

Director, Accounts Management, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN:

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