



*Processing of Foreign Currency
Check Payments Is Causing
Unnecessary Taxpayer Burden*

March 22, 2013

Reference Number: 2013-30-027

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

Redaction Legend:

1 = Tax Return/Return Information

Phone Number | 202-622-6500

E-mail Address | TIGTACommunications@tigta.treas.gov

Website | <http://www.treasury.gov/tigta>



HIGHLIGHTS

PROCESSING OF FOREIGN CURRENCY CHECK PAYMENTS IS CAUSING UNNECESSARY TAXPAYER BURDEN

Highlights

Final Report issued on March 22, 2013

Highlights of Reference Number: 2013-30-027 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

IMPACT ON TAXPAYERS

The IRS requires taxpayers to pay their United States (U.S.) taxes in U.S. dollars. However, some taxpayers still send foreign currency payments because they are either unable or unwilling to convert their payments to U.S. dollars. Foreign currency payments that are not processed timely or are processed at lower exchange rates can cause undue burden on taxpayers and additional work for the IRS.

WHY TIGTA DID THE AUDIT

This audit is included in our Fiscal Year 2013 Annual Audit Plan and addresses the major management challenge of Globalization. The overall objective of the review was to determine whether the IRS effectively and efficiently processes taxpayer payments made in foreign currencies.

WHAT TIGTA FOUND

Our testing of 393 checks totaling \$1.4 million submitted in a foreign currency identified the following internal control issues that adversely affected the processing of the payments:

- Procedures did not exist for the type of documentation to maintain for taxpayer receipts and other information collected and processed by the Manual Deposit Unit in the five Submission Processing Centers.
- Procedures did not exist to ensure that taxpayers were provided with accurate foreign currency exchange rate information when submitting checks in a foreign currency.

- Collection notices were not always suspended after taxpayers submitted payments to fully satisfy outstanding liabilities.
- Procedures were inadequate for monitoring whether taxpayer payments were timely processed and credited to their accounts.
- Procedures did not exist to verify the accuracy of bank processing fees charged to the IRS.

As a result of the internal control issues, there is increased risk that taxpayer payments and information could be lost, stolen, or misused; taxpayers could be unnecessarily burdened; and the Federal Government could be charged with excessive or incorrect check conversion fees.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Director, Submission Processing, Wage and Investment Division: 1) require employees to retain source documentation and create and maintain documentation of the corrective actions taken on rejected payments; 2) ensure that no collection notices are issued to taxpayers while their foreign currency check payments are being processed; 3) assess the benefits of initiating follow-up actions sooner to address contractor processing delays; 4) provide taxpayers with additional information on determining foreign currency exchange rates; and 5) explore the feasibility of establishing a process to verify foreign currency check processing charges.

In their response to the report, IRS officials agreed with all the recommendations and stated that they have taken or plan to take corrective actions.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 22, 2013

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

FROM: Michael E. McKenney
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Processing of Foreign Currency Check Payments
Is Causing Unnecessary Taxpayer Burden (Audit # 201130047)

This report presents the results of our review to determine whether the Internal Revenue Service effectively and efficiently processes taxpayer payments made in foreign currencies. This review is included in our Fiscal Year 2013 Annual Audit Plan and addresses the major management challenge of Globalization.

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

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. If you have any questions, please contact me or Carl Aley, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations).



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Abbreviations

CY	Calendar Year
FMS	Financial Management Services
IDRS	Integrated Data Retrieval System
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
OTCnet	Over the Counter Channel Application Network
SPC	Submission Processing Center
TIN	Taxpayer Identification Number
U.S.	United States



Processing of Foreign Currency Check Payments Is Causing Unnecessary Taxpayer Burden

Background

According to Internal Revenue Service (IRS) Publication 54, *Tax Guide for U.S. Citizens and Resident Aliens Abroad*, taxpayers must pay their taxes in their functional currency. The United States (U.S.) dollar is the functional currency for all taxpayers paying U.S. Federal income taxes. However, there are still some taxpayers who will send in a foreign currency payment because they are either unable or unwilling to convert their payment to U.S. dollars, even though the publication clearly states that income taxes should be paid in U.S. dollars.

The IRS receives foreign currency check payments into its Submission Processing Centers (SPC) through various sources, such as directly from taxpayers, lockboxes,¹ field offices, and Accounts Management Centers.² The SPCs are responsible for processing all foreign currency check payments. Currently, the IRS has SPCs located in Fresno, California; Covington, Kentucky;³ Kansas City, Missouri; Austin, Texas; and Ogden, Utah.

The Internal Revenue Manual (IRM)⁴ requires the SPCs to process foreign currency check payments using regular manual processing procedures. These payments are generally received with some type of source documentation, such as a payment voucher or a taxpayer's tax return. The Manual Deposit Unit ensures that the source documentation is annotated with the original received date, processes the foreign currency payment using manual processing procedures, and prepares a bank deposit ticket through the Over the Counter Channel Application Network (OTCnet) system.

IRS employees are instructed to look for and correct IRS-caused errors before sending any payments to Citibank.⁵ When a taxpayer-caused error is discovered, the IRS employee is required to return the original check to the taxpayer and request a new one. Once a foreign currency check is determined to be error free, the IRS employee will then forward it to Citibank for conversion to U.S. dollars. However, foreign currency checks are still rejected by Citibank for various IRS- or taxpayer-caused errors.

During Calendar Year (CY) 2010, the IRS processed a total of 10,337 foreign check payments.⁶ This consisted of 9,476 (92 percent) check payments drawn on a foreign bank in U.S. dollars,

¹ See Appendix VII for a glossary of terms.

² The IRS's Accounts Management Centers are located in Chamblee, Georgia; Andover, Massachusetts; Holtville, New York; Philadelphia, Pennsylvania; and Memphis, Tennessee.

³ The SPC located in Covington, Kentucky, is known as the Cincinnati SPC.

⁴ IRM 3.8.45.1.10 (Jan. 1, 2011).

⁵ Citibank is the current financial institution that has a contract with the Federal Government for converting foreign currency check payments into U.S. dollars.

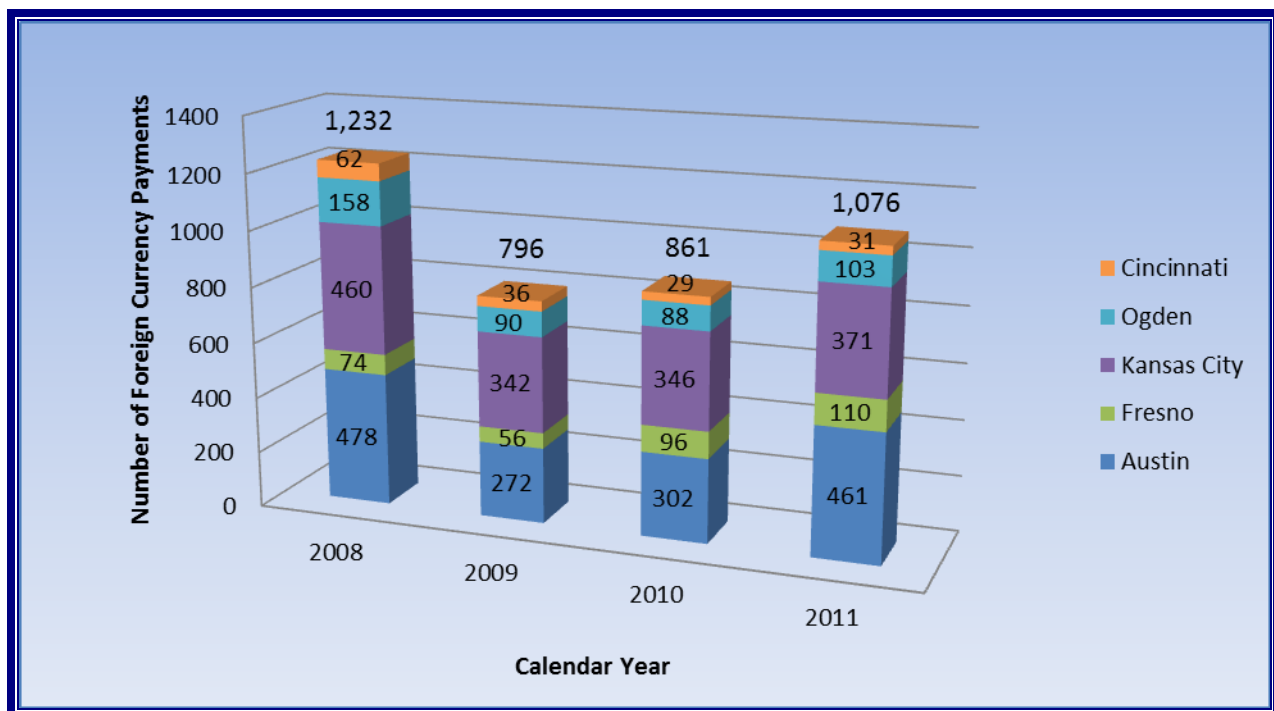
⁶ The Atlanta SPC located in Chamblee, Georgia, was in the process of closing down its submission processing function during CY 2010. As such, we did not include the Atlanta SPC in any of our SPC analyses or population totals.



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and 861 (8 percent) check payments made in a foreign currency. Of the 9,476 check payments made in U.S. dollars, 9,273 (98 percent) were deposited by Citibank, resulting in more than \$125 million in revenue collected, and 203 (2 percent) were rejected by Citibank. Of the 861 check payments made in a foreign currency, 793 (92 percent) were converted by Citibank, resulting in more than \$2.26 million in revenue collected, and 68 (8 percent) were rejected by Citibank. Our review was limited to the 861 check payments made in a foreign currency processed during CY 2010. Figure 1 shows the number of IRS-processed foreign currency check payments by the SPCs during CYs 2008 through 2011.

Figure 1: Number of Foreign Currency Check Payments Processed by the SPCs During CYs 2008 Through 2011



Source: IRS data obtained from the OTCnet system.

This review was performed at the Wage and Investment Division Headquarters in Atlanta, Georgia, and in the SPCs located in Fresno, California; Covington, Kentucky;⁷ Kansas City, Missouri; Austin, Texas; and Ogden, Utah, during the period June 2011 through May 2012. 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

⁷ Hereafter, we will refer to the SPC located in Covington, Kentucky, as the Cincinnati SPC.



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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.



Processing of Foreign Currency Check Payments Is Causing Unnecessary Taxpayer Burden

Results of Review

We identified a number of internal control issues that adversely affected the processing of foreign currency checks in CY 2010. As a result, there is increased risk that 1) taxpayer payments and information could be lost, stolen, or misused; 2) taxpayers could be unnecessarily burdened; and 3) the Federal Government could be charged with excessive or incorrect check conversion fees.

Controls Need to Be Strengthened Over Foreign Currency Check Payments

We reviewed a stratified random sample of 393 payments totaling \$1.4 million out of a population of 861 foreign currency checks processed by the IRS in CY 2010 and found internal control issues involving the maintenance of important documentation, the accuracy of foreign currency exchange rates, the issuance of collection notices, and the timeliness of processing tax receipts. Specifically, we found that:

- Procedures did not exist on the type of documentation to maintain for taxpayer receipts and other information collected and processed by the Manual Deposit Unit in the five SPCs.
- Procedures did not exist to ensure that taxpayers were provided with accurate foreign currency exchange rate information when submitting checks in a foreign currency.
- IRS employees were not always initiating actions to suspend collection notices after taxpayers submitted payments to fully satisfy outstanding liabilities.
- Procedures were inadequate for monitoring whether taxpayer receipts and information were timely processed and credited to accounts.

Maintaining documentation of taxpayer receipts and other information

When foreign currency check payments arrive at the IRS, they are routed to the SPC's Manual Deposit Unit for processing. The IRM⁸ instructs the Manual Deposit Unit to hold the source documentation in a suspense file while the foreign currency checks are converted to U.S. dollars, deposited by Citibank, and credited to the Department of the Treasury's general account. The suspense file is important because Citibank may reject foreign currency check payments for a number of reasons, such as checks that appear to be altered, have missing signatures, or are

⁸ IRM 3.8.45.15(5) (Jan. 1, 2011).



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postdated. If a check is rejected, the Manual Deposit Unit is required to perform and document specific corrective actions so the check can be processed and the payment credited to the correct account. For example, if a rejected payment is due to a taxpayer error, the IRS employee is instructed to return the check along with a letter to the taxpayer, notifying him or her of the rejection, and request a new check that can be processed. Once processing is completed, the underlying source documentation for the payments, such as payment posting vouchers and the actions taken to correct rejected payments, should be forwarded to the IRS's record retention files.

The retention of such source documentation is an important internal control that provides verifiable evidence to ensure that tax payments and other taxpayer information were appropriately collected, timely processed, and accurately posted to taxpayer accounts. According to the Government Accountability Office's *Standards for Internal Control in the Federal Government*:⁹

Internal control and all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination.... All documentation and records should be properly managed and maintained.

In testing the transactions from a stratified sample of 393 check payments submitted in a foreign currency during CY 2010, we determined that 365 payments were converted by Citibank, while 28 payments were rejected. For the 365 converted foreign currency check payments, we reviewed the underlying source documentation obtained from the SPCs and the IRS's retention files. Next, we traced the payments to the IRS's Master File of taxpayer accounts to ensure that converted payments were credited to the correct account. Except for 21 payments,¹⁰ the source documentation retained for the 365 converted foreign currency check payments showed the payments were accurately credited to taxpayer accounts.

For the 28 rejected foreign currency check payments, we tried to review the corrective actions taken by the IRS since these payments were unable to be processed by Citibank. However, we determined that corrective action documentation was not retained by the IRS for all 28 rejected payments; therefore, we could not determine if the payments were returned to the taxpayers or if the payments were resubmitted for deposit. In addition, the IRS did not retain any source documentation in 20 of these 28 payments.¹¹

⁹ Government Accountability Office (formerly known as the General Accounting Office), GAO/AIMD-00-21.3.1, *Standards for Internal Control in the Federal Government* p. 15 (Nov. 1999).

¹⁰ After the source documentation was ordered from file retention, 21 (6 percent) of 365 converted payments had insufficient documentation. This consisted of eight payments that had missing Taxpayer Identification Numbers and 13 payments that had a missing received date stamp.

¹¹ See Appendix V for more details.



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During discussions with IRS officials over the absence of source documentation for the converted and rejected payments, we learned that steps were subsequently taken to update the IRM¹² to specify the retention period and type of documentation required for a foreign currency check payment once it is converted by the bank. Effective January 1, 2012,¹³ the Manual Deposit Unit at each SPC is now required to retain source documentation for foreign currency payments¹⁴ on-site for three years. In addition, the IRS clarified in the IRM that the Manual Deposit Unit is “to date stamp the payment posting voucher and/or tax return with [a] received date, if not present.” While the changes should improve the collection and retention of critical source documentation for converted foreign currency check payments, steps will also need to be taken to ensure that the underlying source documentation and corrective actions for rejected payments are similarly collected and retained.

Currency fluctuations cause problems for taxpayers and the IRS

Because currency exchange rates can fluctuate daily, taxpayers who submit checks in a foreign currency to satisfy tax liabilities with the IRS do not always receive the amount of U.S. dollars anticipated. Taxpayers who receive fewer U.S. dollars than expected will have to pay more taxes and submit additional payments to satisfy the debt, while those receiving a higher amount will likely get a refund.

The fluctuating exchange rates can also lead to confusion over amounts owed, especially when the payments are not timely converted, processed, and credited to the correct taxpayer account. In turn, this can create unnecessary burden on taxpayers and additional work for the IRS because more correspondence will likely be needed between the two parties to resolve the confusion. The amount of contact and the amount of additional information that may need to be exchanged between the IRS and the taxpayer will vary with each situation.

To minimize burden to taxpayers who submit checks in a foreign currency and to avoid creating additional work for their personnel, IRS managers have established a combination of controls. However, we identified shortcomings in three controls that diminished their effectiveness.

The information the IRS provided to taxpayers for determining foreign currency exchange rates was not complete

For taxpayers who make payments in a foreign currency, the IRS suggests that they research the three foreign currency exchange rate sites¹⁵ listed on IRS.gov that can be used to calculate the foreign value of the taxes they owe in U.S. dollars. When a foreign payment is received by

¹² IRM 3.8.45.25.5 (Jan. 1, 2011).

¹³ The IRS issued an IRM procedure update change in November 2011 that became effective in January 2012.

¹⁴ The source documentation required to be maintained and retained for three years includes payment posting vouchers, tax returns, copies of checks, and bank deposit tickets.

¹⁵ The three exchange rate sites are Oanda.com, X-Rates.com, and XE.com.



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Citibank for processing, Citibank converts the payment to U.S. dollars and sends the confirmed bank deposit ticket back to the originating SPC. We analyzed our sample of 365 converted foreign currency check payments to determine how close the Citibank exchange rate was to the exchange rate on the three sites recommended by the IRS. Eight foreign currency check payments in our sample were missing the Taxpayer Identification Number (TIN). As a result, we were only able to compare 357 of the payments.

Because the contract with Citibank does not specify an exchange rate to be used, we calculated the foreign currency conversion amounts using an average of the exchange rates from the three sites suggested by the IRS and the Citibank confirmation date from each deposit ticket. We then took the average conversion amount and compared it to the Citibank conversion amount. We found that 353 (99 percent) of the 357 foreign currency check payments were converted by Citibank at a lower exchange rate. When comparing Citibank's exchange rate to the average of the three exchange rate sites, we identified differences in dollar amounts ranging from a low of \$.03 to a high of \$2,642.90.

As a result, we determined that taxpayers received a total of \$27,150 less for their payments (an average of \$77 less per payment) than what they expected as a result of Citibank using lower exchange rates. This occurred because taxpayers relied on the information provided by the IRS on IRS.gov, which did not accurately reflect the exchange rates used by Citibank. Based on our stratified random sample, we project that taxpayers submitting 781 (99 percent)¹⁶ foreign currency check payments received a total of \$60,137 less from the conversion process during CY 2010. If IRS.gov is not updated to provide taxpayers with exchange rate information comparable to the exchange rates used by Citibank, we estimate that taxpayers submitting 3,905 foreign currency check payments will receive approximately \$300,685 less from the conversion process over the next five years due to the differences in the foreign currency exchange rates being used by Citibank.

In addition, 12 (3 percent) of the 353 foreign currency check payments would have paid off the taxpayers' accounts in full had Citibank used exchange rates comparable to those on the three exchange rate sites suggested by the IRS. We determined that taxpayers who submitted 10 of these foreign currency check payments were assessed additional penalties and interest totaling \$906 (an average of \$91 per payment) because their accounts were not paid off in full due to lower exchange rates. As a result, taxpayers had to send in additional payments. Based on our stratified random sample, we estimate that taxpayers who submitted 40 (5 percent) foreign currency tax payments during CY 2010 would have paid their accounts off in full if comparable exchange rates were used by Citibank. We also estimate that taxpayers who submitted 32 (4 percent) foreign currency check payments may have unnecessarily been assessed additional

¹⁶ This percentage is calculated using a weighted average error rate based on the stratified sample results. See Appendix IV for more details.



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interest and penalties totaling \$2,912 for CY 2010, or \$14,560 when projected over the next five years.

When we discussed this issue with IRS management, they were unaware that the exchange rates used by Citibank provided a lower conversion amount than the rates of the sites suggested by the IRS and reflected on IRS.gov. This has resulted in some taxpayers being frustrated with the lower conversion amounts, as reflected *****1*****
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Collection actions were not always suspended as required

IRS employees were not always initiating actions to suspend collection notices after taxpayers submitted payments to fully satisfy outstanding liabilities. The IRM¹⁷ directs IRS employees to put a code on a taxpayer's account when a foreign currency payment is received as a result of a balance due notice. The code delays collection activities for four cycles and temporarily stops the issuance of all taxpayer notices to allow for the payment to post to the taxpayer's account. We found that taxpayers who submitted 19 foreign currency check payments from our sample of 344 payments¹⁸ with proper source documentation had erroneously received a collection notice after their payments were received by the IRS. This occurred because the code was not placed on any of these taxpayers' accounts while the foreign payments were being processed. More specifically:

- Twelve (63 percent) of the 19 payments were received with a tax return or payment voucher. When we discussed these cases with IRS management, they stated the code was not required to be placed on the taxpayers' accounts because there were not any outstanding tax liabilities. However, these accounts became delinquent while the foreign currency check payments were being processed, which resulted in the taxpayers erroneously receiving collection notices.
- Seven (37 percent) of the 19 payments were received as a result of a balance due notice. If the code had been properly entered on the taxpayers' accounts when the payment was received, it would have prevented subsequent collection notices from being erroneously issued. When we discussed these cases with IRS management, they stated it appears that

¹⁷ IRM 3.8.45.15(3) (Jan. 1, 2011).

¹⁸ Of the 365 converted payments, 21 payments had missing source documentation and, as a result, could not be reviewed. The remaining 344 converted foreign currency check payments had proper source documentation to conduct a complete review.



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the employees need to be reminded of the procedures to prevent the erroneous issuance of notices.

Collection notices erroneously issued to taxpayers create burden and confusion on the amount of taxes owed, which has caused some taxpayers to send in unnecessary payments. For example, taxpayers who submitted three (16 percent) of the 19 foreign currency check payments sent in additional payments because of the collection notices and received full refunds of their additional payments plus interest due on their overpayments. These notices also created additional work for the IRS in terms of mailing the collection notices, responding to taxpayers' inquiries regarding the notices, and processing and refunding additional payments. Based on our stratified random sample, we estimate that taxpayers submitting 58 (7 percent)¹⁹ foreign currency check payments erroneously received collection notices during CY 2010. Projected over five years, an estimated 290 taxpayers would erroneously receive collection notices.

Foreign currency payments were not always timely processed

IRM procedures do not adequately ensure that Citibank processing delays are resolved timely. When Citibank receives a foreign currency payment for processing, the contract has a guaranteed funds delivery date²⁰ of three business days for Canadian currency checks and five business days for all other foreign currency checks. However, despite the emphasis on expedited processing, the IRM²¹ does not require the Manual Deposit Unit to start follow-up actions for resolving processing delays until four weeks has elapsed without confirmation from Citibank that the payment was deposited. Since foreign currency exchange rates change daily, delays in processing can affect the dollar amounts that taxpayers receive for their payments.

Foreign currency check payments arrive into the IRS processing system from various sources. Payments received in the field or in Accounts Management Centers are to be mailed overnight to an SPC within 24 hours of receipt. The SPCs are required to deposit all payments daily.²² The Manual Deposit Unit within the SPC prepares the bank deposit ticket and the foreign currency check payment that is sent to Citibank by overnight mail for processing.

To measure timeliness, we compared the date the IRS's Manual Deposit Unit created and mailed the bank deposit ticket to Citibank with the date Citibank converted and deposited the payment. Our analysis showed that more than 10 calendar days²³ had elapsed before payments were

¹⁹ This percentage is calculated using a weighted average error rate based on the stratified sample results. See Appendix IV for more details.

²⁰ The date Citibank will credit funds to the Department of the Treasury's general account.

²¹ IRM 3.8.45(6) (Jan. 1, 2011).

²² IRM 3.30.123.3.1 (Jan. 1, 2011) states that the deposit processing cycle can be extended to three business days during filing season.

²³ While the Citibank contract states business days, we measured Citibank's timeliness by calendar days taking into consideration the time needed for the IRS to mail payments to Citibank, Citibank's processing time, and additional processing time for weekends.



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processed and deposited by Citibank for 90 (26 percent) of the 344 converted payments in our sample that had complete source documentation for us to review. The average processing time for these 90 payments was 18 days, and the time elapsed ranged from 11 days to 69 days. Based on our stratified random sample, we project that 116 (15 percent)²⁴ foreign currency check payments were not processed timely during CY 2010; this projects to 580 payments over the next five years.

Foreign currency check payment processing timeliness could be improved by taking follow-up actions with Citibank sooner. For example, 68 of the 90 untimely payments in our sample were processed by one Manual Deposit Unit that generally followed IRM guidelines by waiting four weeks before following up with Citibank. However, another Manual Deposit Unit that generally followed up with Citibank within one week processed only four untimely payments. IRS management was unsure why the IRM was not consistent with the contract for initiating follow-up actions. It is important that processing delays are resolved timely because fluctuations in the foreign currency exchange rates directly impact the amount taxpayers are credited with paying.

Recommendations

The Director, Submission Processing, Wage and Investment Division, should:

Recommendation 1: Update the IRM to specify that employees responsible for processing foreign currency check payments retain the source documentation and create and maintain documentation of the corrective actions taken on rejected foreign currency payments.

Management's Response: IRS management agreed with this recommendation. IRM 3.8.45.15, *Foreign Check Remittances*, was updated on June 7, 2012, to require the maintenance of logs and case files for all foreign deposits and rejected foreign deposits. The IRM updates specify the information to be recorded and retained in the case files as well as the applicable retention period.

Recommendation 2: Ensure that no collection notices are issued to taxpayers while their foreign currency check payments are being processed.

Management's Response: IRS management agreed with this recommendation and implemented changes to procedures in IRM 3.8.45.15, *Foreign Check Remittances*, on June 7, 2012, to reduce the risk of issuing collection notices to taxpayers while their foreign currency check payments are being processed. The IRS has also increased the frequency of its monitoring of foreign currency cash conversions to further ensure that they are completed prior to collection notices being issued.

²⁴ This percentage is calculated using a weighted average error rate based on the stratified sample results. See Appendix IV for more details.



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Recommendation 3: Assess the four-week criteria used to initiate follow-up actions when contractor delays occur in the processing of foreign currency check payments to determine the benefits, if any, of initiating follow-up actions earlier in the process.

Management's Response: IRS management agreed with this recommendation. On June 7, 2012, IRM 3.8.45.15, *Foreign Check Remittances*, was updated to require follow-up action with the contractor if a confirmed deposit ticket has not been received within one week.

Recommendation 4: Coordinate with the function responsible for maintaining IRS.gov to provide additional information to the site on how the exchange rate used for foreign currency payment conversions is calculated and applied by the processing bank.

Management's Response: IRS management agreed with this recommendation and will update IRS.gov to clarify that exchange rate information is to be used for determining the U.S. dollar equivalent of taxable transactions conducted in foreign currencies. They will also clarify that taxpayers are required to remit tax payments in U.S. dollars and that exchange rate information should not be used for calculating the amount of tax payments to remit in foreign currency.

Office of Audit Comment: While IRS management agreed with this recommendation, they did not agree with its related outcome measure attributable to taxpayer burden arising from exchange rates at the time foreign currency payments are converted because taxpayers are required to pay their tax liabilities in U.S. dollars. However, as a matter of policy, the IRS accepts and processes checks in foreign currencies. Any delays in the processing of these checks, as described in this report, will continue to burden taxpayers.

The Internal Revenue Service Does Not Verify Foreign Check Processing Charges

As part of our review, we obtained from the Financial Management Services (FMS) the CY 2010 billing invoices related to charges incurred by the IRS for processing foreign checks as well as the foreign check-processing contract with Citibank. The most recent contract provided to us was dated January 3, 1994. A FMS Treasury General Account Financial Program Specialist stated that the contract was still in effect and that the FMS has started the process of renegotiating the contract. The current contract in effect for foreign check processing was set up to cover multiple Federal agencies.

Under the existing contract, Citibank charges a fee for each foreign check processed during the month.²⁵ The contract with Citibank states that the fee to process a check in Canadian currency

²⁵ This includes all foreign currency checks as well as checks written in U.S. dollars from a foreign bank account.



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or in U.S. currency drawn on a Canadian bank is \$2, all other foreign currencies or in U.S. currency drawn on another foreign country bank is \$5, and a rejected payment is \$15.

Each month, Citibank sends a billing statement directly to the FMS for payment.²⁶ However, on the monthly statement, the foreign check processing charges are combined for all Federal agencies. As a result, we were unable to validate the specific IRS charges submitted by Citibank.

Based on the population of foreign currency payments processed by the IRS during CY 2010, we estimate the fees that Citibank would have charged the FMS were approximately \$6,294. Under the same contract, we determined that Citibank also charges the FMS for payments processed by the IRS in U.S. dollars but drawn on a foreign bank. Although these payments are outside the scope of the review, we estimate the fees that Citibank would have charged the FMS are approximately \$24,840 to \$52,659, depending on whether the foreign bank was Canadian or in another foreign country.

In addition, we determined that the IRS does not verify the accuracy of its monthly charges, and the FMS pays the monthly fees to Citibank without verification from any of the individual Federal agencies supported by the contract. The FMS also told us that the only time a monthly billing statement from Citibank would be questioned is if the statement is greater than \$30,000.

According to the Government Accountability Office's *Standards for Internal Control in the Federal Government*, "Periodic comparison of resources with the recorded accountability should be made to help reduce the risk of errors, fraud, misuse, or unauthorized alteration." While the IRS has no further role in the process once a foreign check payment is sent to Citibank, the lack of controls regarding verification of the processing charges creates a risk for the Federal Government in erroneous expenditures and fraudulent charges. We believe that better controls are needed so that the IRS can verify that its foreign check processing charges on the monthly billing statements are accurate.

Recommendation

Recommendation 5: The Director, Submission Processing, Wage and Investment Division, should coordinate with the FMS to explore the feasibility of establishing a process to verify foreign check processing charges for IRS-submitted taxpayer payments.

Management's Response: IRS management agreed with this recommendation. They have discussed the issue with the FMS and have been advised that the FMS is responsible for establishing all depository relationships for all Federal Government agencies under the Treasury General Account. The FMS is responsible for compensating the depositories for processing these deposits and does not require the depositories to

²⁶ See Appendix VI for an example of a Citibank monthly billing statement.



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segregate agency checks for compensation. These accounts are Treasury General Accounts, are not agency-specific, and multiple agencies deposit into the foreign check depository account. The IRS considers this action to be complete.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to determine whether the IRS effectively and efficiently processes taxpayer payments made in foreign currencies. Specifically, we determined what methods the IRS uses to ensure that payments are timely and properly credited to the IRS's and taxpayers' accounts. To accomplish our audit, we:

- I. Evaluated the controls and procedures followed by the SPCs¹ for processing foreign currency check payments.
 - A. Conducted a walk-through of the Austin, Cincinnati,² Fresno, Kansas City, and Ogden SPCs and determined how foreign currency check payments are processed.
 - B. Interviewed IRS officials at the Andover, Atlanta,³ Brookhaven,⁴ Memphis, and Philadelphia Accounts Management Centers and obtained an understanding of their policies, procedures, and controls related to processing foreign currency check payments.
 - C. Analyzed all of the SPC procedures and controls and determined whether changes are needed to current processes to ensure consistency among the SPCs.
 - D. Obtained the policy criteria used by the IRS to determine the correct date for posting to a taxpayer's account a foreign currency check payment received by the IRS.
- II. Calculated the costs and burden to taxpayers and the IRS for processing foreign currency check payments.
 - A. Selected a 100 percent sample of foreign currency check payments processed during CY 2010 at the Cincinnati, Fresno, and Ogden SPCs. Our contract statistician assisted and reviewed our sampling plan and projections. The number of foreign currency check payments in our sample from each of the following SPCs were:
 - Cincinnati SPC – 29 foreign currency check payments.
 - Fresno SPC – 83 foreign currency check payments.
 - Ogden SPC – 88 foreign currency check payments.

¹ See Appendix VII for a glossary of terms.

² The Cincinnati SPC is located in Covington, Kentucky.

³ The Atlanta Accounts Management Center is located in Chamblee, Georgia.

⁴ The Brookhaven Accounts Management Center is located in Holtsville, New York.



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Selected a statistically valid random sample of foreign currency check payments processed during CY 2010 at the Austin and Kansas City SPCs using a 95 percent confidence level, 10 percent error rate, and ± 5 percent precision rate. The contract statistician assisted and reviewed our sampling plan and projections. The numbers of foreign currency check payments in our sample from each of the following SPCs were:

- Austin SPC – 94 foreign currency check payments.
 - Kansas City SPC – 99 foreign currency check payments.
- B. Prepared a case review sheet used to capture information for each of the following steps.
- C. Determined whether the received date of the foreign currency check payment was the same date posted to the taxpayer's Master File account by obtaining the received date from the source documentation and comparing to the posting date on the Integrated Data Retrieval System (IDRS).
- D. Conducted analyses and determined whether delays in converting foreign currency checks to U.S. dollars caused the taxpayer to incur additional penalties or interest or to erroneously receive collection notices.
1. Conducted research using the IDRS and compared the date the payment posted to the taxpayer's account to the date it was received from the taxpayer to determine the number of days expended during the conversion process.
 2. Reviewed IDRS taxpayer account data and identified whether any penalties and/or interest accrued during the conversion period.
 3. Compared the amount posted on the IDRS to what the exchange rate amount was on the date the payment was received from the taxpayer using the websites OANDA.com, X-Rates.com, and XE.com to determine whether the taxpayer received a lesser amount for his or her check due to the delay in the conversion process. If the amount on the IDRS was less, we reviewed the taxpayer's account to determine whether a collection notice was issued for the difference.
 4. Reviewed IDRS taxpayer account data and determined whether collection notices were issued between the date the payment was received from the taxpayer and the date the payment posted to the taxpayer's account.
 5. Reviewed IDRS taxpayer account data and determined whether any account holds placed on the account were released to ensure that a collection notice could be issued for the remaining balance.



Processing of Foreign Currency Check Payments Is Causing Unnecessary Taxpayer Burden

6. Compared the bank conversion report, *e.g.*, bank deposit ticket, to the amount posted to the taxpayer's account on the Master File and determined whether the conversion amount was posted properly.
- E. Determined the costs the IRS incurred for converting foreign currency check payments to U.S. dollars. We analyzed the accounts using the IDRS to determine whether delays in converting the payments caused the IRS to refund a portion of the taxpayer's payment due to differences in the exchange rates from the date the taxpayer made the payment to the date the payment was converted.
- F. Determined whether Citibank was converting foreign currency payments timely and whether the exchange rate was comparable to the three exchange rate sites suggested by the IRS on IRS.gov.
 1. Interviewed FMS management and gained an understanding of the contract between the FMS and Citibank, the monthly invoice process, and payment of the monthly invoices.
 2. Obtained Citibank's contract, *International Check Collections Services*, and monthly billing statements and determined the procedures and costs for processing foreign currency check payments.
 3. Analyzed the contract and determined the contract fees charged, conversion rates used, and processing times expected of Citibank.
 4. Analyzed the payments selected from Step II.A. and compared to the three exchange rate sites suggested by the IRS on IRS.gov. We determined whether Citibank was providing a comparable exchange rate.
 5. Analyzed the payments selected from Step II.A. and determined whether Citibank processed the payments timely.

Data validation methodology

During this review, we evaluated the reasonableness of the foreign currency data received from each SPC through comparison of foreign currency check payment data stored on the OTCnet system, which is used by the IRS to deposit foreign currency check payments to Citibank. Specifically, we compared the number of total payments we received from each of the five individual SPCs to the total number of foreign currency payments located on the OTCnet system by SPC. We then verified the data to ensure that the data from the SPC matched what is on the OTCnet system (voucher number, dollar amount, currency type, *etc.*). These tests determined that the data were sufficiently reliable and could be used to meet the objective of this audit.



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Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective: Wage and Investment Division Submission Processing function's policies, procedures, and practices for processing foreign currency check payments. We evaluated these controls by reviewing source materials, interviewing management, and analyzing a sample of foreign currency check payments processed during CY 2010.



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Appendix II

Major Contributors to This Report

Margaret E. Begg, Assistant Inspector General for Audit (Compliance and Enforcement Operations)

Carl Aley, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations)

Frank Dunleavy, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations)

Bryce Kisler, Director

Christina M. Dreyer, Audit Manager

Carole E. Connolly, Acting Audit Manager

Michele S. Jahn, Lead Auditor

Margaret F. Filippelli, Senior Auditor



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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner for Operations, Wage and Investment Division SE:W
Director, Submission Processing, Wage and Investment Division SE:W:CAS:SP
Deputy Director, Submission Processing, Wage and Investment Division SE:W:CAS:SP:D
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Commissioner, Wage and Investment Division SE:W



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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 Burden – Potential; \$63,049 for 781 foreign currency check payments in CY 2010, or \$315,245 for 3,905 foreign currency check payments over the next five years¹ (see page 4).

Methodology Used to Measure the Reported Benefit:

From our sample of 365 converted foreign currency check payments, we found eight payments had missing documentation and were excluded from our sample. As a result, we were only able to review 357 foreign currency check payments for the exchange rate used to convert the payments to U.S. dollars.

We determined that 353 of the 357 foreign currency check payments were converted by Citibank at a lower exchange rate when compared to the average of the three exchange rate sites suggested by the IRS on IRS.gov. As a result, taxpayers received \$27,150 (\$77 per payment) less than what they expected for their foreign currency check payments as a result of the lower exchange rates used by Citibank. To project the results of our sample, we used a stratified random sample, with a weighted average for each SPC. Figure 1 shows the weighted average calculations and projections to the population.

¹ Taxpayers submitting 781 foreign currency check payments received \$60,137 less for their payments, and 32 of those payments would have paid accounts off in full. Instead, taxpayers paid \$2,912 in penalties and interest in CY 2010 ($\$60,137 + \$2,912 = \$63,049$, or \$315,245 over five years).



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Figure 1: Projections for Stratified Random Sample (Conversion Rate)

	Austin SPC 1	Cincinnati SPC 2	Fresno SPC 3	Kansas City SPC 4	Ogden SPC 5	Total Population
Population Data						
Population (Confirmed Payments)	286	23	83	318	83	793
Population Percentage (1)	36.07%	2.90%	10.47%	40.10%	10.47%	100.00%
Sample Data						
Cases Selected for Review	94	29	83	99	88	393
Less Sample Rejected Payments	(8)	(6)	0	(9)	(5)	(28)
Subtotal (Sample Confirmed Payments)	86	23	83	90	83	365
Less Missing Documentation	0	(2)	(1)	(3)	(2)	(8)
Cases Reviewed (Confirmed Payments)	86	21	82	87	81	357
Conversion Rate Issue						
Number of Errors	85	21	81	85	81	353
Error Rate for each SPC(2)	98.84%	100.00%	98.78%	97.70%	100.00%	
SPC Weighted Average Error Rate (3)	35.65%	2.90%	10.34%	39.18%	10.47%	
Sample Weighted Average (Sum of #3 Results)						98.53%
Apply Sample Weighted Average Result to Population for CY 2010 (98.53% * 793)						781
Projected Over Five Years						3905
Conversion Rate Issue: Taxpayer would have paid off account						
Number of Errors	4	0	1	7	0	12
Error Rate for each SPC(4)	4.65%	0.00%	1.22%	8.05%	0.00%	
SPC Weighted Average Error Rate (5)	1.68%	0.00%	0.13%	3.23%	0.00%	
Sample Weighted Average (Sum of #5 Results)						5.03%
Apply Sample Weighted Average Result to Population for CY 2010 (5.03% * 793)						40
Projected Over Five Years						200
Conversion Rate Issue: Taxpayer would have paid off account, instead assessed additional penalties and interest						
Number of Errors	4	0	1	5	0	10
Error Rate for each SPC(4)	4.65%	0.00%	1.22%	5.75%	0.00%	
SPC Weighted Average Error Rate (5)	1.68%	0.00%	0.13%	2.30%	0.00%	
Sample Weighted Average (Sum of #5 Results)						4.11%
Apply Sample Weighted Average Result to Population for CY 2010 (4.11% * 793)						32
Projected Over Five Years						160
1 = SPC Population divided by Total Population						
2 or 4 = Number of Errors divided by Cases Reviewed						
3 or 5 = Number of Errors divided by Cases Reviewed						

Source: Data obtained from the IRS using the OTCnet system and our analysis of the foreign currency payments reviewed.



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As reflected, we calculated a weighted average for each SPC by multiplying the SPC population percentage to the SPC error rate. This computed weighted error rates of 35.65 percent for the Austin SPC, 2.90 percent for the Cincinnati SPC, 10.34 percent for the Fresno SPC, 39.18 percent for the Kansas City SPC, and 10.47 percent for the Ogden SPC, for a total sample weighted average of 98.53 percent. We then applied this sample weighted average to the converted population of 793 foreign currency check payments. Based on these parameters, 781 ($793 \times .9853$) of the foreign currency check payments were converted at a lower exchange rate by Citibank than the average of the three exchange rate sites suggested by the IRS on IRS.gov. As a result, taxpayers received a total of \$60,137 less ($781 \times \77) for their foreign currency check payments during CY 2010. We also project that taxpayers submitting 3,905 in foreign currency check payments will receive approximately \$300,685 less than they expect over the next five years due to differences in the foreign currency exchange rates.

In addition, we determined that 12 of the 353 payments would have paid off the taxpayers' accounts in full had Citibank used exchange rates comparable to those on the three exchange rate sites suggested by the IRS on IRS.gov. We determined that taxpayers who submitted 10 of these foreign currency check payments were assessed additional penalties and interest totaling \$906 (an average of \$91 per payment) because the accounts were not paid off in full due to the lower exchange rates.

To project the results of our sample, we used a stratified random sample with a weighted average for each SPC. Figure 1 shows the weighted average calculations and projections to population. As reflected, we calculated a weighted average for each SPC by multiplying the SPC population percentage by the SPC error rate. This computed weighted error rates of 1.68 percent for the Austin SPC, 0 percent for the Cincinnati SPC, 0.13 percent for the Fresno SPC, 2.30 percent for the Kansas City SPC, and 0 percent for the Ogden SPC, for a total sample weighted average of 4.11 percent. We then applied this sample weighted average to the converted population of 793 foreign currency check payments. Based on these parameters, taxpayers who submitted 32 ($793 \times .0411$) foreign currency check payments may have unnecessarily been assessed additional penalties and interest totaling \$2,912 for CY 2010, or \$14,560 in penalties and interest over the next five years.



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Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; 174 foreign currency check payments affected, or 870 foreign currency check payments over the next five years² (see page 4).

Methodology Used to Measure the Reported Benefit:

The IRS processed a total of 861 foreign currency check payments during CY 2010.³ The IRS sent these payments to Citibank for conversion to U.S. dollars. Out of the 861 payments, Citibank rejected 68 of them and converted 793 foreign currency check payments during CY 2010.

We selected 100 percent of the foreign currency check payments from the Cincinnati (29 payments), Fresno (83 payments), and Ogden (88 payments) SPCs and a random statistical sample from the Austin (94 payments) and Kansas City (99 payments) SPCs using a 95 percent confidence level, 10 percent error rate, and ± 5 percent precision rate. This resulted in 393 foreign currency check payments in our sample, of which 28 foreign currency check payments were rejected by Citibank. This resulted in 365 converted foreign currency check payments left in our sample. Our sample also had 21 payments with missing documentation that prevented us from doing a complete review. As a result, we were only able to review 344 payments.

Our review found that 90 of the 344 foreign currency check payments in our sample were not timely processed by Citibank. To project the results of our sample, we used a stratified random sample with a weighted average for each SPC. Figure 2 shows the weighted average calculations and projections to the population.

² There were 116 foreign currency check payments that were not timely processed by Citibank and taxpayers submitting 58 of the foreign currency check payments received an erroneous collection notice, projected for CY 2010 ($116 + 58 = 174$ taxpayer payments affected, or 870 payments over five years).

³ The Atlanta SPC located in Chamblee, Georgia, was in the process of closing down its submission processing function during CY 2010. As a result, we did not include the Atlanta SPC in any of our SPC analyses or population totals.



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Figure 2: Projections for Stratified Random Sample (Converted Payments)

	Austin SPC 1	Cincinnati SPC 2	Fresno SPC 3	Kansas City SPC 4	Ogden SPC 5	Total Population
Population Data						
Population (Confirmed Payments)	286	23	83	318	83	793
Population Percentage (1)	36.07%	2.90%	10.47%	40.10%	10.47%	100.00%
Sample Data						
Cases Selected for Review	94	29	83	99	88	393
Less Sample Rejected Payments	(8)	(6)	0	(9)	(5)	(28)
Subtotal (Sample Confirmed Payments)	86	23	83	90	83	365
Less Missing Documentation	(3)	(2)	(8)	(6)	(2)	(21)
Cases Reviewed (Confirmed Payments)	83	21	75	84	81	344
Payments Not Timely Processed by Citibank						
Number of Errors	4	0	68	3	15	90
Error Rate for each SPC (2)	4.82%	0.00%	90.67%	3.57%	18.52%	
SPC Weighted Average Error Rate (3)	1.76%	0.00%	9.59%	1.45%	1.96%	
Sample Weighted Average (Sum of #3 Results)						14.75%
Apply Sample Weighted Average Results to Population for CY 2010 projection (14.75% * 793)						116
Projected Over Five Years						580
Erroneous Collection Notice						
Number of Errors	8	2	2	7	0	19
Error Rate for each SPC (4)	9.64%	9.52%	2.67%	8.33%	0.00%	
SPC Weighted Average Error Rate (5)	3.48%	0.28%	0.28%	3.34%	0.00%	
Sample Weighted Average (Sum of #5 Results)						7.37%
Apply Sample Weighted Average Result to Population for CY 2010 (7.37% * 793)						58
Projected Over Five Years						290
1 = SPC Population divided by Total Population						
2 or 4 = Number of Errors divided by Cases Reviewed						
3 or 5 = Number of Errors divided by Cases Reviewed						

Source: Data obtained from the IRS using the OTCnet system and our analysis of the foreign currency payments reviewed.

As reflected, we calculated a weighted average for each SPC by multiplying the SPC population percentage to the SPC error rate. This computed weighted error rates of 1.76 percent for the Austin SPC, 0 percent for the Cincinnati SPC, 9.59 percent for the Fresno SPC, 1.45 percent for the Kansas City SPC, and 1.96 percent for the Ogden SPC, for a total sample weighted average of 14.75 percent. We then applied this sample weighted average to the converted population of 793 foreign currency check payments. Based on these parameters, 116 (793 x .1475) foreign currency check payments were not timely processed in CY 2010, or 580 over the next five years.



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In addition, we determined that taxpayers submitting 19 of the 344 foreign currency check payments erroneously received a collection notice because the appropriate code was not input to their accounts. To project the results of our sample, we used a stratified random sample with a weighted average for each SPC. Figure 1 shows the weighted average calculations and projections to population for erroneous collection notices. As reflected, we calculated a weighted average for each SPC by multiplying the SPC population percentage by the SPC error rate. This computed weighted error rates of 3.48 percent for the Austin SPC, 0.28 percent for the Cincinnati SPC, 0.28 percent for the Fresno SPC, 3.34 percent for the Kansas City SPC, and 0 percent for the Ogden SPC, for a total sample weighted average of 7.37 percent. We then applied this sample weighted average to the converted population of 793 foreign currency check payments. Based on these parameters, taxpayers making 58 (793×0.0737) of the foreign currency check payments processed in CY 2010 erroneously received a collection notice, or 290 over the next five years.



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Appendix V

*Submission Processing Centers'
Payment Documentation Retention Results*

Converted Payments – Document Retention Per SPC					
Procedure	Austin	Cincinnati	Fresno	Kansas City	Ogden
Maintained Copies of All Converted Source Documentation	Yes	No	Yes	No	No
Available Source Documentation Contained an IRS Received Date	No	Yes	No	No	Yes
Maintained Copies of All Converted Deposit Slips	Yes	Yes	Yes	Yes	Yes

Source: Our analyses of confirmed foreign currency check payment source documentation.

Rejected Payments – Document Retention Per SPC					
Procedure	Austin	Cincinnati	Fresno	Kansas City	Ogden
Maintained Copies of All Rejected Source Documentation	Yes	No	No	No	No
Maintained Copies of All Rejected Bank Deposit Slips	Yes	Yes	No	Yes	Yes
Maintained Copies of Rejection Letters to Taxpayers Regarding Corrective Actions	No	No	No	No	No

Source: Our analyses of rejected foreign currency check payment source documentation.



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Appendix VI

*Example of a Billing Statement From Citibank for
Monthly Foreign Check Processing Charges*

Preview Monthly Statement For Monthly Statement Profile ID 001018 January 2010											
Monthly Statement Summary Information											
First Name:	[REDACTED]										
Last Name:	[REDACTED]										
Phone Number:	[REDACTED]										
Address:	[REDACTED]										
City:	[REDACTED]										
State:	[REDACTED]										
Zip Code:	[REDACTED]										
Statement Description:	CITIBANK N.A.										
Investment Rate:	0.06%										
Compensation Plan Summary Information											
Compensation Plan ID	Compensation Description	Compensation Type	Beginning Balance	ACH Transfers Since Last Statement	TTB Earnings	Total Net Gain/Loss	Cumulative Position				
001578	Citibank FX, ITGA (D)	ACH Fee Transfer	-\$10,220.39	\$10,220.39	\$0.00	-\$10,723.13	-\$10,723.13				
Compensation Plan Summary Totals											
Combined Cumulative Position:							-\$10,723.13				
There is no TTB Information for this Monthly Statement											
Net Gain or Loss											
Comp Plan ID	Comp Plan Desc	Site ID	Site Desc	DDA ID	DDA Desc	CAN	Account Name	Income	Expense	Net Gain/Loss	Total Net Gain/Loss
001578	Citibank FX, ITGA (D)					001067	CITIBANK - FOREIGN CHECK	\$0.00	\$0.00	\$0.00	-\$10,723.13
								\$0.00	\$10,723.13	-\$10,723.13	-\$10,723.13
AFP Code Information											
Compensation Plan ID	Site ID	DDA ID	CAN	AFP Code	Source	Analysis Type	Descriptor	Units	Price	Value	
				001067 010000	Derived	Expense	Demand Deposit Account Maintenance	1	150.000000	\$150.00	
				001067 1010905515	Derived	Expense	Special Depository Services - Variable SF-5515	58	0.330000	\$19.14	
				001067 609999600237	Reported	Expense	International Services - Foreign Checks in US\$	538	5.000000	\$2,690.00	
				001067 609999600238	Reported	Expense	International Services - FX Checks	31	5.000000	\$155.00	
				001067 609999600239	Reported	Expense	International Services - Canadian Checks in US\$	1038	2.000000	\$2,076.00	
				001067 609999600240	Reported	Expense	International Services - Canadian Dollar Checks	30	2.000000	\$60.00	
				001067 609999600520	Reported	Expense	International Services - ITGA Deposit Tickets	136	0.330000	\$44.88	
				001067 609999609999	Reported	Expense	International Services - Foreign Check Return	57	15.000000	\$855.00	
				001067 609999610620	Reported	Expense	International Services - Clearing Bank Fees	4673.11	1.000000	\$4,673.11	
				001067 009999NETCREDITS	Derived	Statistic	Net Credits	18506448.86	1.000000	\$18,506,448.86	
				001067 009999TOTCREDITS	Derived	Statistic	Total Credits	18849398.5	1.000000	\$18,849,398.50	
				001067 009999TOTDEBITS	Derived	Statistic	Total Debits	342949.64	1.000000	\$342,949.64	
AFP Codes denoted with an * are not included in the calculation for Net/Gain Loss											
Deposit Information											
Compensation Plan ID	Site ID	DDA ID	CAN	Total Credits	Total Debits	Net Deposits					
001578			001067	\$18,850,221.50	\$342,949.64	\$18,507,271.86					
			001067	\$18,850,221.50	\$342,949.64	\$18,507,271.86					

Source: *The FMS*. Note: ACH = Automated Clearing House. AFP = Association for Financial Professionals. DDA = Demand Deposit Account. ITGA = International Treasury General Account. TTB = Treasury Time Balance.



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Appendix VII

Glossary of Terms

Term	Definition
Accounts Management Center	IRS campuses that do not process tax returns.
Association for Financial Professionals (AFP)	Identifies product codes for the financial services recognized by the FMS. A product code is a standard six-character designation that represents a specific and defined product or service the Lockbox Depository performs to support financial services for Federal agencies.
Automated Clearing House (ACH)	The primary electronic funds transfer system used by agencies to make payments.
Calendar Year (CY)	Twelve consecutive months ending December 31.
Cycle	All transactions posting to good tape for transmittal to the Martinsburg Computing Center that are processed through the campus during a prescribed period, usually one week.
Demand Deposit Account (DDA)	An account maintained by the U.S. Department of the Treasury at the Lockbox Depository for crediting agencies for lockbox deposits.
Financial Management Services (FMS)	A bureau of the U.S. Department of the Treasury, providing central payment services to Federal program agencies, operating the Federal Government's collections and deposit systems, providing Governmentwide accounting and reporting services, and managing the collection of delinquent debt owed to the Government.
Fiscal Year	A 12-consecutive-month period ending on the last day of any month, except December. The Federal Government's fiscal year begins on October 1 and ends on September 30.
Integrated Data Retrieval System (IDRS)	A computerized system used throughout the IRS for adjusting, researching, ordering, and monitoring tax accounts.



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Term	Definition
Integrated Submission and Remittance Processing System	A system that converts paper tax and information documents and remittances received by the IRS into perfected electronic records of taxpayer data.
International Treasury General Account (ITGA)	An account maintained in the name of the U.S. Department of the Treasury.
Lockboxes	A collection and processing service provided by a network of financial institutions that accelerates the flow of funds to the U.S. Department of the Treasury. The financial institutions process and deposit the funds directly to the Department of the Treasury reducing the processing time.
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.
Over The Counter Network (OTCnet)	A web-based application used by the IRS for depositing foreign payments that combines check capture and deposit reporting using electronic collection mechanisms instead of paper-based processing.
Source Documentation	A payment posting voucher or a taxpayer's tax return containing taxpayer identifiable information, such as a TIN, and the date the IRS received the payment.
Submission Processing Center (SPC)	IRS campuses that process tax returns.
Taxpayer Identification Number (TIN)	A nine-digit number assigned to taxpayers for identification purposes. Depending upon the nature of the taxpayer, the TIN is an Employer Identification Number, a Social Security Number, or an Individual TIN.
Treasury Time Balance (TTB)	The amount of funds the U.S. Department of the Treasury has deposited with the Lockbox Depository in a non-interest-bearing time account to compensate for financial services performed by a Lockbox Depository.



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Appendix VIII

Management's Response to the Draft Report



COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

February 28, 2013

MEMORANDUM FOR MICHAEL E. MCKENNEY
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Peggy Bogadi 
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Processing of Foreign Currency Check
Payments Is Causing Unnecessary Taxpayer Burden
(Audit # 201130047)

We appreciate the opportunity to review the subject draft report. With very limited exceptions¹, taxpayers are required to remit tax due to the United States in U.S. dollars. However, as noted in your report, some taxpayers send foreign currency payments because they are either unable or unwilling to convert their payments to U.S. dollars.

We agree that controls can be strengthened to improve document retention related to the payments made in foreign currencies, and actions can be taken to improve deposit accuracy and timeliness. Procedures have been updated to ensure accounts are appropriately marked to forestall collection activities while foreign currency payments are being processed, and to require follow-up actions when deposit acknowledgements are not received within one week.

The IRS provides resources and links on IRS.gov to assist taxpayers in determining conversion rates for transactions conducted in foreign currencies to their U.S. dollar equivalents. The U.S. dollar equivalent is to be used when reporting foreign currency transactions for U.S. tax purposes. Therefore, when taxable income and tax liability for the year is determined, the foreign-denominated transactions are included as amounts expressed in U.S. dollars and there is no further need for consideration of exchange rates. We will update IRS.gov to clarify that exchange rate information is to be used for determining the U.S. dollar equivalent of taxable transactions conducted in foreign currencies. We will also clarify that taxpayers are required to remit tax payments in U.S. dollars and that exchange rate information should not be used for calculating the amount of tax payments to remit in foreign currency.

¹ The taxpayer must have been a Fulbright grantee, paid in nonconvertible foreign currency, with at least 70 percent of the grant paid in nonconvertible foreign currency.



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As a matter of policy, the IRS will not return a payment remitted in a foreign currency if it otherwise appears to be processable. Neither Publication 54, *Tax Guide for U.S. Citizens and Resident Aliens Abroad*, nor Foreign Currency and Currency Exchange Rates² information presented at IRS.gov, advises taxpayers to make payments in foreign currencies or to use the exchange rate resources for determining amounts to pay. Consequently, we do not agree with the Outcome Measure of \$315,245 attributable to taxpayer burden arising from unfavorable exchange rates at the time foreign currency payments are converted. We will take steps to clarify that exchange rate resources are provided only for determining the U.S. dollar equivalent of transactions conducted in foreign currencies, and are not to be used for calculating tax payments.

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

Attachment

² <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Foreign-Currency-and-Currency-Exchange-Rates>



*Processing of Foreign Currency Check Payments
Is Causing Unnecessary Taxpayer Burden*

Attachment

RECOMMENDATIONS

The Director, Submission Processing, W&I Division, should:

RECOMMENDATION 1

Update the IRM to specify that employees responsible for processing foreign currency check payments retain the source documentation, and create and maintain documentation of the corrective actions taken on rejected foreign currency payments.

CORRECTIVE ACTION

Internal Revenue Manual (IRM) 3.8.45.15, *Foreign Check Remittances*, was updated on June 7, 2012, to require the maintenance of logs and case files for all foreign deposits and rejected foreign deposits. The IRM updates specify the information to be recorded and retained in the case files, as well as the applicable retention period.

IMPLEMENTATION DATE

Implemented

RESPONSIBLE OFFICIAL

Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 2

Ensure that no collection notices are issued to taxpayers while their foreign currency check payments are being processed.

CORRECTIVE ACTION

We implemented changes to procedures in IRM 3.8.45.15, *Foreign Check Remittances*, on June 7, 2012, to reduce the risk of issuing collection notices to taxpayers while their foreign currency check payments are being processed. We have also increased the frequency of our monitoring of foreign currency cash conversions to further ensure they are completed prior to collection notices being issued.

IMPLEMENTATION DATE

Implemented

RESPONSIBLE OFFICIAL

Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

N/A



Processing of Foreign Currency Check Payments Is Causing Unnecessary Taxpayer Burden

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RECOMMENDATION 3

Assess the four-week criteria used to initiate follow-up actions when contractor delays occur in the processing of foreign currency check payments to determine the benefits, if any, of initiating follow-up actions earlier in the process.

CORRECTIVE ACTION

On June 7, 2012, IRM 3.8.45.15, *Foreign Check Remittances*, was updated to require follow-up action with the contractor if a confirmed deposit ticket has not been received within one week.

IMPLEMENTATION DATE

Implemented

RESPONSIBLE OFFICIAL

Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 4

Coordinate with the function responsible for maintaining IRS.gov to provide additional information to the site on how the exchange rate used for foreign currency payment conversions is calculated and applied by the processing bank.

CORRECTIVE ACTION

We will update IRS.gov to clarify that exchange rate information is to be used for determining the U.S. dollar equivalent of taxable transactions conducted in foreign currencies. We will also clarify that taxpayers are required to remit tax payments in U.S. dollars and that exchange rate information should not be used for calculating the amount of tax payments to remit in foreign currency.

IMPLEMENTATION DATE

October 15, 2013

RESPONSIBLE OFFICIAL

Director, Submission Processing, 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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RECOMMENDATION 5

The Director, Submission Processing, W&I Division, should coordinate with the FMS to explore the feasibility of establishing a process to verify foreign check processing charges for IRS-submitted taxpayer payments.

CORRECTIVE ACTION

We have discussed the issue with the Financial Management Service (FMS) and have been advised that FMS is responsible for establishing all depository relationships for all government agencies under the Treasury General Account. The FMS is responsible for compensating the depositories for processing these deposits and does not require the depositories to segregate agency checks for compensation. These accounts are Treasury General Accounts, are not agency-specific, and multiple agencies deposit into the foreign check depository account. We consider this action to be completed.

IMPLEMENTATION DATE

Completed

RESPONSIBLE OFFICIAL

Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

N/A