



MANUAL TRANSMITTAL

Department of the Treasury
Internal Revenue Service

20.3.1

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EFFECTIVE DATE

(04-11-2018)

PURPOSE

- (1) This transmits revised IRM 20.3.1, *Penalty Programs Internal Processes, Civil Penalty Accuracy Review Process*.

BACKGROUND

- (1) This IRM documents the Civil Penalty Accuracy Review Process developed by the Office of Servicewide Penalties (OSP), with the assistance of the Office of the Chief Financial Officer (CFO), Corporate Planning and Internal Control (CPIC). This process was created to enhance controls of the accuracy of penalty assessments and abatements.

MATERIAL CHANGES

- (1) During this revision, minor editorial changes have been made and various subsections renumbered. Significant change to this IRM are listed in the table below:

Reference	Change Details
Throughout	Editorial changes were made throughout IRM 20.3.1.
IRM 20.3.1.1	Program Scope and Objectives - Changed subsection title from Overview and revised content to conform with new guidelines in IRM 1.11.2, <i>Internal Revenue Manual (IRM) Process</i> . In addition, existing subsections were rearranged or new subsections added to conform with the new internal control rules applicable to this program.
IRM 20.3.1.1	Removed exclusion of certain return-related penalty assessments and abatement from Overview.
IRM 20.3.1.2	Updated definition of civil penalty to reflect civil penalties administered by IRS, as detailed in IRM 20.1, <i>Penalty Handbook</i> .
IRM 20.3.1.4	Removed note excluding certain return-related penalty assessments and abatement from Sample Selection Process.

EFFECT ON OTHER DOCUMENTS

IRM 20.3.1 dated 01-19-2017, is superseded.

AUDIENCE

Office of Servicewide Penalties

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20.3.1

Civil Penalty Accuracy Review Process

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20.3.1.1
(04-11-2018)
Program Scope and Objectives

- (1) **Purpose:** This chapter provides background information, procedures and guidelines for the Civil Penalty Accuracy Review Process conducted by the Office of Servicewide Penalties (OSP).
- (2) **Audience:** This chapter contains policies and procedures for analysts located in OSP to conduct the reviews independent of the civil penalty assessment and abatement functions within IRS.
- (3) **Policy Owner:** The Business Support Office (BSO) is under Operations Support (OS). SB/SE is responsible for overseeing civil penalties.
- (4) **Program Owner:** The Office of Servicewide Penalties (OSP) is responsible for civil penalty policy including IRM 20.3.1, *Civil Penalty Accuracy Review Process*. OSP's role is to ensure fairness and consistency in penalty reviews and has overall responsibility for coordinating and approving any update to IRM 20.3.1.
- (5) **Primary Stakeholders:** Office of Servicewide Penalties

20.3.1.1.1
(04-11-2018)
Background

- (1) The Civil Penalty Accuracy Review Process was developed by OSP, with assistance from the Office of the Chief Financial Officer (CFO), Corporate Planning and Internal Control (CPIC). This review process measures the accuracy of assessed and accrued penalties. Reviews are completed semi-annually (i.e. twice a calendar year). Analysts located in OSP conduct the reviews independent of the civil penalty assessment and abatement functions within IRS.

20.3.1.1.2
(04-11-2018)
Authority

- (1) The Internal Revenue Code (IRC) and Treasury Regulations are the primary sources of authority for the administration of penalties. **Policy Statement 20-1** (IRM 1.2.20.1.1) mandates that the Service will design, administer, and evaluate penalty programs. This chapter was created to follow the guidance given in **Policy Statement 20-1**.

20.3.1.1.3
(04-11-2018)
Roles and Responsibilities

- (1) The Director, Business Support, is the director responsible for the servicewide civil penalty program, including the Civil Penalty Accuracy Review Process.
- (2) Overall responsibility of the Civil Penalty Accuracy Review Process is assigned to OSP. OSP resides in the Business Support (Small Business/Self Employed) Function. OSP coordinates policies and procedures concerning the administration of civil penalty programs, including the Civil Penalty Accuracy Review Process, ensuring consistency with the penalty policy statement, reviewing and analyzing penalty information, researching penalty effectiveness and determining appropriate action needed to promote voluntary compliance while protecting taxpayers' rights.

20.3.1.1.4
(04-11-2018)
Program Management and Review

- (1) Every function in the IRS has a role in proper penalty administration. It is essential that each function conduct its operations with an emphasis on promoting voluntary compliance. Appropriate reviews should be conducted to ensure consistency with the penalty policy statement (**Policy Statement 20-1**) and philosophy.
- (2) To promote the goal of consistency and fairness, OSP will review semi-annually a sample of penalty assessments provided by SB/SE Research as provided in this chapter.

20.3.1.1.5
(04-11-2018)

**Terms/Definitions/
Acronyms**

(1) The terms below are defined for use with this IRM.

Term	Definition
Business Master File (BMF)	Tax returns and forms found on the Business Master File that reflect at least one civil penalty assessment and/or abatement. Business returns and forms include, but are not limited to: <ol style="list-style-type: none"> Form 1065, <i>U.S. Return of Partnership Income</i>, Form 1120, <i>U.S. Corporation Income Tax Return</i>, Form 1120-S, <i>U.S. Small Business Corporation Income Tax Return</i> Form 940, <i>Employer's Annual Federal Unemployment Tax Return</i>, and Form 941, <i>Employer's Quarterly Federal Tax Return</i>.
Civil Penalty	Civil Penalties administered by IRS are detailed in IRM 20.1, <i>Penalty Handbook</i> .
Computation sheet	Worksheets developed by OSP to compute specific penalties, such as failure to file and failure to pay. Instructions for using the computations sheets are detailed in the <i>Civil Penalty Review Job Aid</i> .
Integrated Data Retrieval System (IDRS)	Reviewers are required to use IDRS to conduct civil penalty review as detailed in this IRM. IDRS is a key component of the review process. Reviewers recompute all civil penalties applicable to a specific tax module and compare the result to the civil penalty assessments and/or abatements reflected on the tax module.
Individual Master File (IMF)	Tax returns and forms found on the Individual Master File that reflect at least one civil penalty assessment and/or abatement (e.g. Form 1040, <i>U.S. Individual Income Tax Return</i>).

Term	Definition
Lead Sheet	Documents developed by OSP that detail the steps to compute specific penalties, such as failure to deposit. Instructions for using the lead sheets are detailed in the <i>Civil Penalty Review Job Aid</i> .
Penalty abatement	Reversal of a civil penalty assessment due to reasonable cause, administrative waiver (including first time abatement), correction of IRS error, or statutory exception (see IRM 20.1.1.3). Reviewers are required to review all civil penalty abatements reflected on a specific tax module.
Penalty assessment	The assessment of a civil penalty on a specific tax module when taxpayer behavior fails to meet prescribed tax obligations (see IRM 20.1.1.2). Reviewers are required to review all civil penalty assessments reflected on a specific tax module. Penalty assessment information is detailed in IRM 20.1, <i>Penalty Handbook</i> .

Term	Definition
Review cycle	<p>The review cycle includes the following steps:</p> <ol style="list-style-type: none"> Planning of the review, including the securing of the sample from SB/SE Research, Conducting training for the review team, Assigning the tax modules to the reviewers, Conducting the reviews, Determining results, Documenting the audit trail and results, Identifying potential inconsistencies and errors, Referring potential inconsistencies and errors to subject matter experts (SMEs) for review and evaluation, Determining corrective actions and monitoring for completion, Finalizing and distributing the report of findings, and Continue monitoring to ensure corrective actions are implemented and functioning properly.

20.3.1.1.6
(04-11-2018)

Related Resources

- (1) IRM 20.1, *Penalty Handbook*
- (2) *Civil Penalty Review Job Aid*

20.3.1.2
(04-11-2018)

Office of Servicewide Penalties (OSP) Responsibilities

- (1) This section covers team members and their responsibilities for the accuracy review process

20.3.1.2.1
(04-11-2018)

Program Manager Responsibilities

- (1) To begin each review cycle, the program manager or project lead makes a written request to SB/SE Research to identify the sample of tax modules to be reviewed. SB/SE Research provides the sample to the program manager or project lead directly. The project lead and specific penalty SMEs (see IRM 20.3.1.2.4) prepare the sample for review. The program manager sets a completion date for the specific review cycle.
- (2) The program manager ensures the review team is provided with adequate training and tools to conduct the review, including a copy of the *Civil Penalty*

Review Job Aid and all lead and computation sheets. The program manager ensures that the project lead organizes and schedules training for the reviewers (see IRM 20.3.1.2).

- (3) The program manager finalizes the report of findings. The program manager reviews and assesses the documented review process, results and corrective actions to ensure the report of findings is accurate and complete. The report of findings is considered final when signed by the program manager.
- (4) The program manager shares the report with Director, Business Support Office and other leadership, as needed. In addition, the report of findings will be shared with the CFO, specifically Financial Management Revenue Oversight and Support (ROS) and CPIC.
- (5) The program manager ensures corrective actions are properly implemented, tested and documented as an addendum to the finalized report of findings (see IRM 20.3.1.8).

20.3.1.2.2
(04-11-2018)
**Project Lead (Oversight)
Responsibilities**

- (1) The program manager designates a project lead for oversight of the Civil Penalty Accuracy Review process. The project lead is an OSP analyst serving as an intermediary between the program manager, reviewers, SMEs, the CFO and other internal stakeholders with an interest in the review process.
- (2) The project lead monitors the progress of each review cycle from identification of the sample through completion of the report of findings. The project lead develops the civil penalty master listing for monitoring purposes (see IRM 20.3.1.3). The project lead should be aware of the status of the tax modules being reviewed at all times. The project lead assigns the tax modules to the reviewers and ensures all case reviews are properly tracked and documented. The project lead maintains a listing of tax modules included in the sample. This listing is referred to as the civil penalty review master listing.
- (3) The project lead provides instructions for completing the reviews and communicates expectations for use of the *Civil Penalty Review Job Aid* in the review process. The project lead communicates the due date for completion of the reviews to the review team. The project lead organizes and schedules training for the reviewers. The project lead coordinates with the SMEs to ensure the reviewers understand how to compute specific penalties and how to use the lead and computation sheets (see IRM 20.3.1.2.4).
- (4) On completion of the reviews by the reviewers, the project lead collects and compiles the results. The project lead conducts a review of the documentation and results to ensure the documentation is complete and the findings are accurate.
- (5) The project lead ensures all documents related to the review process, including a copy of the final report of findings, are uploaded to an enterprise shared folder and retained for five years from the date of issuance of the final report of findings, based on IRM 20.3.1.8 and IRM 1.15.2, *Records and Information Management - Types of Records and Their Life Cycles*.
- (6) The project lead addresses questions and issues as they arise by interacting with all related parties, including Director, Business Support Office and other leadership.

- (7) The project lead coordinates with the SMEs to monitor the implementation of corrective actions and to ensure corrective actions are functioning properly through testing. The project lead incorporates testing results as an addendum to the finalized report of findings (see IRM 20.3.1.8.1).

20.3.1.2.3
(04-11-2018)
**Reviewer
Responsibilities**

- (1) The penalty review team performs the reviews under the direction of the program manager, while also working in conjunction with the project lead. Generally, the team will consist of four OSP analysts, who serve as reviewers.
- (2) Prior to conducting the reviews, the reviewers receive training and guidance to ensure understanding of each specific penalty computation. Training includes a review of the *Civil Penalty Review Job Aid* and direction from the SMEs on how to compute specific penalties and how to use the lead and computation sheets (see IRM 20.3.1.2.4). The reviewers ensure they understand the review process, including the documentation of the audit trail and conclusions reached and the computation of the various civil penalties identified on the tax modules.
- (3) Reviewers must have access to IDRS, to conduct the reviews. Reviewers use IDRS research, along with lead and computation sheets (see IRM 20.3.1.2.4) and manual computations to review and recompute all civil penalties identified on the tax modules assigned.
- (4) Reviewers document each review, including the steps taken to recompute each penalty. Reviewers maintain supporting documentation for each review based on IRM 20.3.1.8 and IRM 1.15.2, *Records and Information Management - Types of Records and Their Life Cycles*.
- (5) The reviewers communicate the results of each review to the project lead.
- (6) During the course of each review cycle, the review team meets periodically to assess the process and address issues.

20.3.1.2.4
(04-11-2018)
**Subject Matter Expert
Responsibilities**

- (1) As part of the review team, analysts located in OSP will serve as SMEs for specific penalties. To allow for segregation of duties, reviewers should not serve as SMEs during the same review cycle. The SMEs:
 - a. prepare the sample for assignment,
 - b. develop lead and computation sheets to be used to review specific penalties,
 - c. provide training to the reviewers on how to compute specific penalties,
 - d. provide training to the reviewers on how to use the lead and computation sheets during the review,
 - e. answer penalty-specific questions as the reviews are completed,
 - f. review penalty computations to confirm errors identified by the reviewers,
 - g. determine and implement corrective actions when errors are identified,
 - h. monitor to ensure corrective actions are implemented and functioning properly,
 - i. conduct testing to ensure corrective actions are functioning properly and document results of testing, and
 - j. provide results of testing to project lead.

20.3.1.3
(04-11-2018)
**Sample Selection
Process**

- (1) On a semi-annual basis, as requested by the program manager or project lead, SB/SE Research identifies the sample of tax modules to be included in each review cycle.
- (2) The tax modules must include at least one penalty assessment. In some cases, one tax module may include multiple penalty assessments for a variety of penalties. The sample is delivered directly to the program manager or project lead by SB/SE Research.
- (3) The sample should include tax modules that proportionately reflect the total population in the Unpaid Assessments inventory. The sample should be selected proportionately across the four financial classifications (tax receivables, compliance assessments, write-offs and memos) and include the following:
 - a. representative sample from Individual Master File (IMF) and Business Master File (BMF),
 - b. representative sample of systemic assessments and manual assessments, and
 - c. tax modules where the sum of the assessed penalty and accrued penalty is greater than \$0.
- (4) The project lead maintains a listing of tax modules included in the sample. This listing is referred to as the Civil Penalty Review Master Listing.

20.3.1.4
(04-11-2018)
**Scope of Civil Penalty
Reviews**

- (1) Prior to assignment to the reviewers, the SMEs complete IDRS research and analyze the sample to identify the types of civil penalties included in the review cycle. Generally, the penalties include:
 - a. failure to file (FTF) penalty under IRC 6651(a)(1),
 - b. failure to pay (FTP) penalty under IRC 6651(a)(2),
 - c. estimated tax (EST) penalty under IRC 6654,
 - d. failure to deposit (FTD) penalty under IRC 6656,
 - e. bad check penalty under IRC 6657, and
 - f. the accuracy-related penalty under IRC 6662.
- (2) The list above is not all-inclusive (Over 170 civil penalties are administered by IRS). The sample may include tax modules with other civil penalties that must be verified for accuracy during the review process.
- (3) In instances where multiple penalties are assessed against the same taxpayer, all civil penalties identified on the tax module must be verified for accuracy.
- (4) Penalty abatements should be reviewed to the extent possible, based on information available on the Integrated Data Retrieval System (IDRS) and on Accounts Management Services (AMS).

20.3.1.5
(04-11-2018)
**Documenting Civil
Penalty Reviews**

- (1) Reviewers should document their audit trail so subsequent reviewers can follow steps taken, information and documents reviewed and conclusions reached.
- (2) Each module reviewed is controlled using a unique control number designated on assignment to the reviewers. Control numbers are generated using the following naming convention: YYYYLNNN

- YYYY = the calendar year when the review was conducted (i.e. 2016)
- L = a letter to correspond with the review cycle for the year (i.e. A - first cycle, B - second cycle, etc.)
- NNN = the control number assigned to the taxpayer module (i.e. 001...100...etc.)

Example: 2016A050 is module 50 from the first review conducted in 2016

- (3) Each electronic file folder should contain the following for all penalty assessments and/or abatements reviewed:
 - a. Data Collection Instrument (DCI),
 - b. Copies of IDRS research including: TXMODA, IMFOL/BMFOL, PIFTF (for failure to file (FTF) penalties), INTSTD (for failure to pay (FTP) penalties), FTDPN (for failure to deposit (FTD) penalties), and COMPAS and PIEST (for estimated tax (EST) penalties),
 - c. Copies of lead and computation sheets used for recalculation of the penalty,
 - d. Additional workpapers and spreadsheets used for manual computations and to document findings, and
 - e. Supporting penalty abatement documentation reviewed, if applicable.
- (4) Documentation will be uploaded to an enterprise shared folder and retained for five years from the date of issuance of the final report of findings, based on IRM 1.15.2 and Document 12990, *Records Control Schedules*.

20.3.1.6
(04-11-2018)
Conducting Civil Penalty Reviews

- (1) In general, the reviewers analyze IDRS research and utilize verification tools (i.e. lead and computation sheets) to review the penalty assessments. (See *Civil Penalty Review Job Aid* for a detailed explanation of steps taken to conduct the reviews.) Using IDRS research and the verification tools, the reviewers recompute each penalty and compare the results to the assessed amount. The reviewers document the computation of each penalty and maintain electronic copies of all IDRS research used to complete the reviews.
- (2) For penalties found to **match** the assessed amount, the reviewers communicate findings to the project lead and the civil penalty review master listing is updated to reflect **match**.
- (3) In instances where the penalties do not match the assessment shown on Master File, the reviewers communicate findings to the project lead and the civil penalty review master listing is updated to reflect **mismatch**. The reviewers consult with the specific penalty SME to determine if the penalty is a true **mismatch**. The SME conducts additional research and analysis to verify the mismatch (i.e. amount and type), determines the cause of the mismatch and identifies corrective actions needed.

20.3.1.7
(04-11-2018)
Identifying Potential Inconsistencies and Errors

- (1) The types of mismatches (or errors) found may include:
 - a. manual data entry errors specific to one taxpayer,
 - b. systemic computational errors affecting many taxpayers,
 - c. processing or procedural errors, and
 - d. use of incorrect information in systemic reference/explanation tools available on IDRS.

Note: This list is not all-inclusive. Other types of mismatches may be identified through this review process.

- (2) The Civil Penalty Review Master Listing is updated by the project lead to document the findings.
- (3) Depending on the type of mismatch, the SMEs identify the actions needed to resolve both the systemic root cause and computational errors on the specific case. Where required, the SMEs input Knowledge Incident/Problem Service Asset Management (KISAM) tickets to report the issue to Information Technology (IT) for further analysis. Based on their findings, IT may initiate programming changes affecting systemic computations as necessary.
- (4) The SMEs contact affected functions (e.g. Automated Substitute for Return (ASFR), Automated Underreporter (AUR), etc.) to request adjustments to correct the errors, as needed. The SMEs keep the program manager and project lead apprised of the status of the mismatches and corrective actions. After corrective actions are requested, the SMEs and/or project lead continue to take actions to verify corrections were implemented.
- (5) The SMEs conduct testing to ensure corrective actions are functioning properly. The SMEs document the results of the testing and provide the results of testing to the project lead for inclusion as an addendum to the finalized report of findings (see IRM 20.3.1.8). As needed, affected tax modules may be included in subsequent review cycles and rechecked to determine if corrections and adjustments were made properly.
- (6) The SMEs maintain control of the mismatches from identification through resolution.

20.3.1.8
(04-11-2018)
**Reporting Civil Penalty
Review Results**

- (1) This section covers the report preparation and dissemination.

20.3.1.8.1
(04-11-2018)
**Civil Penalty Accuracy
Review Report
Preparation**

- (1) When the reviews are complete, the reviewers must provide the project lead with a completed copy of their civil penalty review master listing and all associated files (included in their electronic file folders) for review. The project lead compiles the results into a spreadsheet that encompasses all reviewed tax modules. A report of findings will be prepared that conveys actions taken, errors identified (if any) and corrective actions completed (if any).

20.3.1.8.2
(04-11-2018)
**Civil Penalty Accuracy
Review Report
Distribution**

- (1) The report of findings is reviewed by the review team members before being presented to the program manager for a final review of the document. The program manager reviews and assesses the documented review process, results and corrective actions to ensure the report of findings is accurate and complete. The report of findings is considered final when signed by the program manager.
- (2) The finalized report of findings is shared with Director, Business Support Office and other leadership, as needed. In addition, the report of findings will be shared with the CFO, specifically ROS and CPIC. The finalized report of findings will be uploaded to an enterprise shared folder and retained for five

years from the date of issuance of the final report of findings, based on IRM 1.15.2, and Document 12990, *Records Control Schedules*.

20.3.1.8.3
(04-11-2018)

**Resolution of Corrective
Actions Identified in the
Civil Penalty Accuracy
Review Report**

- (1) On finalization of the report of findings, if unresolved corrective actions exist, the program manager ensures corrective actions are properly implemented, tested and documented as an addendum to the finalized report of findings.