



*The Private Debt Collection  
Request for Quotation Outlines  
Adequate Procedures and Controls*

**September 2005**

**Reference Number: 2005-10-156**

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.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

September 19, 2005

**MEMORANDUM FOR** COMMISSIONER, WAGE AND INVESTMENT DIVISION  
CHIEF, AGENCY-WIDE SHARED SERVICES

*Pamela J. Gardiner*

**FROM:** Pamela J. Gardiner  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – The Private Debt Collection Request for  
Quotation Outlines Adequate Procedures and Controls  
(Audit # 200510021)

This report presents the results of our review to determine whether the Internal Revenue Service (IRS) had established adequate procedures and controls, through the provisions stipulated in the Request for Quotation (RFQ), to facilitate its management oversight of the Private Debt Collection (PDC) program. We did not review the procurement approach or bid evaluation process for this program.

This was a special, limited-scope audit that, together with companion audits being conducted by the Office of Audit Small Business and Corporate Programs and Information Systems Programs Business Units, provides coverage of a key initiative for which the Treasury Inspector General for Tax Administration committed resources as a high priority.

*Synopsis*

On October 22, 2004, the President signed the American Jobs Creation Act of 2004<sup>1</sup> to permit private collection agencies (PCA) to help collect Federal tax debts. The purpose of the PDC program is to help reduce the significant and growing number of uncollectible cases and enable the IRS to better focus existing resources on more difficult cases. The IRS intends to initially contract for debt collection services with three PCAs; it issued a detailed RFQ in support of this proposed procurement on April 25, 2005. However, this RFQ was cancelled after the United

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<sup>1</sup> Pub. L. No. 108-357, 118 Stat. 1418 (2004).



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States Court of Federal Claims filed an order on July 25, 2005, informing the IRS it intended to enjoin the solicitation. The order ruled that the IRS' restriction of the solicitation to vendors with current Federal Government debt collection task orders was arbitrary and capricious. The IRS tentatively plans to issue a new RFQ, absent the contested restriction, in September 2005 and begin delivering cases to the selected PCAs in mid-2006.

Our limited-scope review of the April 25, 2005, RFQ and subsequent amendment did not identify any material omissions that would, in our opinion, adversely affect the IRS' ability to effectively manage this effort. The RFQ contains detailed information regarding the award fee, performance incentive structure, and nonperformance penalty process. In addition, the RFQ adequately addresses PDC program oversight, management information, and data security requirements. For example, the RFQ specifies an onsite security review by the IRS of PCA facilities and stipulates that tax compliance checks and background investigations be performed for all PCA managers and employees. The RFQ also contains taxpayer rights provisions mandating PCA adherence to applicable Federal laws, including the Fair Debt Collection Practices Act,<sup>2</sup> the Privacy Act of 1974,<sup>3</sup> and the IRS Restructuring and Reform Act of 1998.<sup>4</sup> Finally, the IRS developed a comprehensive taxpayer complaint resolution process to investigate and address potential violations of taxpayers' rights by PCAs. We will be evaluating the implementation of these procedures, as well as associated systems development controls, as part of a series of companion audits being conducted by the Office of Audit Small Business and Corporate Programs and Information Systems Programs Business Units.

The IRS plans to implement the PDC program in two phases, beginning with a limited implementation phase. This two-phase approach should allow the IRS to evaluate program performance and identify/address any areas needing improvement before full-scale implementation. We also found that the IRS is currently in the process of developing both a detailed procedures guide and an operational handbook to assist in guiding the implementation and day-to-day operation of the PDC program.

While our review of the PDC RFQ indicated it established adequate general procedures and controls to facilitate the management of the PDC effort, we did identify four areas we believe warrant additional consideration and emphasis as the IRS develops the detailed procedures in support of the PDC program.

- Development of a methodology to ensure PCA employee compensation is not based on collection statistics, such as dollars collected per taxpayer contact.

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<sup>2</sup> 15 U.S.C. §§ 1601 note, 1692-1692o (2000).

<sup>3</sup> 5 U.S.C. § 552a (2000).

<sup>4</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).



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- Development of detailed requirements regarding the review of PCA telephone activity reports and specification of expected PCA turnaround times on IRS requests for these reports.
- Further clarification as to what constitutes a “computer desktop” as defined in the security requirements of the RFQ and development of a specific requirement that account access for separated PCA employees, or employees no longer needing access to Federal tax data, be immediately disabled.
- Development of specific time periods PCAs should allow a taxpayer who disputes the amount of a liability being collected to forward documentation to support his or her position.

### *Response*

We discussed these issues with the IRS during our fieldwork, and management informed us they plan to address the areas we identified in the PDC procedures guide and operational handbook, which are currently being developed. Accordingly, we made no further recommendations in this report; however, we plan to continue assessing the implementation of the PDC program and will evaluate actions taken as a result of this audit. Management’s complete response to the discussion draft report is included as Appendix IV.

Copies of this report are also being sent to the IRS managers affected by the report findings. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.



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## *Background*

In 1996, the Internal Revenue Service (IRS) conducted a pilot project to use private collection agencies (PCA) to help collect Federal tax debts. However, reviews of this pilot identified legal and administrative barriers. In June 1997, Congress directed the IRS to stop using PCAs for Federal tax debt collection. With the continued rise in tax debt receivables between Fiscal Years 1996 and 2000, we issued a Management Advisory Report in July 2001<sup>1</sup> suggesting the IRS reconsider the use of PCAs to assist in the collection of Federal tax debts.

On October 22, 2004, the President signed the American Jobs Creation Act of 2004<sup>2</sup> to permit PCAs to help collect Federal tax debts. The purpose of the IRS Private Debt Collection (PDC) program (formerly the Collection Contract Support program) is to help reduce the significant and growing number of uncollectible cases and enable the IRS to better focus existing resources on more difficult cases.

The total individual income tax debt designated as uncollectible has grown from approximately \$7 billion 3 years ago to more than \$13 billion at present. Department of the Treasury officials estimate that, over the next several years, the PDC program will result in approximately \$1 billion more in revenue.

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The current PDC program was initiated in October 2001, when the IRS began studying the feasibility of using PCAs within a modernized collection environment, then subsequently solicited information regarding policies and practices from the private debt collection industry. The IRS determined the use of PCAs to collect a portion of its delinquent receivables was feasible, with proper oversight and guidance. Selected PCAs would focus on taxpayers who were likely to pay their outstanding tax liabilities if they were located and contacted. The IRS would not refer to PCAs cases with indications that IRS expertise or discretion may be necessary or that enforcement action would be required to resolve the liability.

The IRS intends to contract for debt collection services with three PCAs from the General Services Administration Federal Supply Schedule in an initial limited implementation. On April 25, 2005, the IRS issued a Request for Quotation (RFQ) that includes a description of the work to be performed. The Statement of Work and the general terms and conditions are located

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<sup>1</sup> *Management Advisory Report: Additional Options to Collect Tax Debts Need to Be Explored* (Reference Number 2001-40-122, dated July 2001).

<sup>2</sup> Pub. L. No. 108-357, 118 Stat. 1418 (2004).



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within the RFQ and its attachments. The IRS planned to begin issuing cases to the three selected PCAs in early 2006.

However, this RFQ was cancelled after the United States Court of Federal Claims filed an order on July 25, 2005, informing the IRS it intended to enjoin the solicitation. The order ruled that the IRS' restriction of the solicitation to vendors with current Federal Government debt collection task orders was arbitrary and capricious. The IRS tentatively plans to issue a new RFQ, absent the contested restriction, in September 2005 and begin delivering cases to the selected PCAs in mid-2006. The second phase will be the full-scale implementation involving up to 12 PCAs. The IRS plans to issue another RFQ after evaluating the results of the initial phase.

This review was performed at the Wage and Investment Division in New Carrollton, Maryland, in the Office of Filing and Payment Compliance, and at the Agency-Wide Shared Services Division in Oxon Hill, Maryland, in the Office of Procurement Business Operations, during the period March through July 2005. The audit was conducted in accordance with *Government Auditing Standards*. This was a special, limited-scope audit that, together with companion audits being conducted by the Office of Audit Small Business and Corporate Programs and Information Systems Programs Business Units, provides coverage of a key initiative for which the Treasury Inspector General for Tax Administration committed resources as a high priority. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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*Results of Review*

***The Private Debt Collection Request for Quotation Adequately  
Addresses the Award Fee, Performance Incentive Structure, and  
Nonperformance Penalty Process***

On April 25, 2005, the IRS issued an RFQ in connection with the PDC program. The RFQ contains the general terms and conditions of the PDC program procurement as well as a detailed description of the work to be performed. On May 26, 2005, the IRS amended the RFQ to include additional information concerning the qualifications of PCAs submitting proposals for PDC work, data security requirements, and employee background investigations in response to inquiries from PCAs.

Our limited-scope review of the April 25, 2005, RFQ and subsequent amendment did not identify any material omissions that would, in our opinion, adversely affect the IRS' ability to effectively manage this effort. The RFQ contains adequate information regarding the award fee, performance incentive structure, and nonperformance penalty process. In addition, the RFQ adequately addresses PDC program oversight, management information, and data security requirements. For example, the RFQ specifies an onsite security review by the IRS of PCA facilities and stipulates that tax compliance checks and background investigations will be performed for all PCA managers and employees. The RFQ also contains taxpayer rights provisions mandating PCA adherence to applicable Federal laws, including the Fair Debt Collection Practices Act,<sup>3</sup> the Privacy Act of 1974,<sup>4</sup> and the IRS Restructuring and Reform Act of 1998.<sup>5</sup> Finally, the IRS developed a comprehensive taxpayer complaint resolution process to investigate and address potential violations of taxpayers' rights by PCAs. We will be evaluating the implementation of these procedures, as well as associated systems development controls, as part of a series of companion audits being conducted by the Office of Audit Small Business and Corporate Programs and Information Systems Programs Business Units.

The IRS plans to implement the PDC program in two phases, beginning with a limited implementation phase. This two-phase approach should allow the IRS to evaluate program performance and identify/address any areas needing improvement before full-scale implementation. The first phase is scheduled not to exceed 30 months and includes up to

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<sup>3</sup> 15 U.S.C. §§ 1601 note, 1692-1692o (2000).

<sup>4</sup> 5 U.S.C. § 552a (2000).

<sup>5</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).



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3 PCAs. The second phase will be the full-scale implementation of the PDC program involving up to 12 PCAs. The IRS plans to issue another RFQ after evaluating the results of the limited implementation phase.

Finally, the IRS is currently in the process of developing both a detailed procedures guide and an operational handbook to assist in guiding the implementation and day-to-day execution of the PDC program. While our review did not identify any material omissions in the RFQ, we did identify several areas we believe warrant further clarification as the IRS develops detailed procedures in support of the PDC program.

***Additional Clarification Regarding Oversight, Security Requirements,  
and Case Processing Would Further Help Ensure Effective  
Implementation of the Private Debt Collection Program***

The day-to-day operation of the PDC program will be governed by a detailed policy and procedures guide and an operational handbook, which the IRS expects to have developed by September 30, 2005. These documents will outline the general requirements of the program, prohibited practices, and specific steps PCAs are required to follow when collecting Federal tax debt, as well as the actions the IRS plans to take to ensure PCAs comply with the terms of the contract.

While our review of the PDC RFQ indicated it established adequate general procedures and controls to facilitate the management of the PDC effort, we did identify four areas we believe warrant consideration and further emphasis as the IRS develops detailed procedures in support of the PDC program. Specifically:

- Although the RFQ prohibits PCA employee compensation based on collection statistics and requires PCAs to provide an employee compensation plan, it does not address how the IRS will monitor PCAs to ensure ongoing compliance with these requirements. Public confidence in the IRS PDC program would be severely undermined if, for example, PCA employees were compensated based on tax dollars collected per telephone contact or tax dollars collected per hour.
- While the RFQ does require PCAs to provide telephone reports to the IRS as needed, it does not specify how frequently the IRS will review the reports or the review criteria. The RFQ also does not specify an expected turnaround time by PCAs on IRS requests for telephone reports. Review of telephone reports is critical to identifying abusive collection practices such as calls made to taxpayers very late at night and/or very early in the morning.
- Although the RFQ prohibits the storage of IRS systems applications or data on a computer desktop owned by the PCA, it does not specify whether “computer desktop”



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includes or extends to hard drive memory space, shared network drives, or email folders. The RFQ also does not specifically state that account access for separated PCA employees, or employees no longer needing access to Federal tax data, be immediately disabled. Explicit definition of critical computer security terms and requirements would further help ensure each PCA's understanding of IRS requirements.

- The RFQ states that, when a taxpayer disputes the amount of a liability being collected, the PCA will collect supporting documentation from the taxpayer before referral of the account to the IRS. However, the RFQ does not specify a time period during which PCAs should allow a taxpayer to forward this documentation to support his or her position. Requiring PCAs to give taxpayers a predetermined amount of time to forward promised documentation, such as cancelled checks, would further help ensure the fair and equal treatment of all taxpayers by PCAs.

We discussed these issues with the IRS during our fieldwork, and management informed us they plan to address the areas we identified in the PDC procedures guide and operational handbook, which are currently being developed. Accordingly, we have no further recommendations to offer at this time; however, we plan to continue assessing the implementation of the PDC program and will evaluate actions taken as a result of this audit. Management's complete comments regarding the issues we identified are included as Appendix IV.



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## **Appendix I**

### *Detailed Objective, Scope, and Methodology*

The overall objective of this review was to determine whether the Internal Revenue Service (IRS) had established effective procedures and controls, through the provisions stipulated in the Request for Quotation (RFQ), to facilitate its management oversight of the Private Debt Collection (PDC) program. We did not review the procurement approach or bid evaluation process for this program. To accomplish our objective, we:

- I. Determined whether the RFQ effectively addressed the award fee, performance incentive structure, and nonperformance penalty process.
  - A. Reviewed the process used to establish the Pricing and Commission schedule.
  - B. Analyzed the nonperformance penalty process and evaluated the penalties stipulated for taxpayer rights, privacy, and disclosure violations.
- II. Ascertained whether the RFQ effectively addressed oversight of the private collection agencies (PCA), program success measures, and management information required from the PCAs.
  - A. Evaluated oversight requirements incorporated into the RFQ relating to case processing actions including call monitoring (by the contractor, IRS, and Treasury Inspector General for Tax Administration) and the taxpayer complaint investigation process.
  - B. Reviewed requirements incorporated into the RFQ relating to data security, including security specifications and periodic onsite security reviews.
- III. Determined whether the IRS had taken effective actions to address prior audit findings related to the PDC program.<sup>1</sup>

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<sup>1</sup> *Efforts to Develop a Successful Collection Contract Support Program Could Be Enhanced* (Reference Number 2003-30-075, dated March 2003).



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**Appendix II**

*Major Contributors to This Report*

Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)  
John R. Wright, Director  
Anthony J. Choma, Audit Manager  
Gerald Horn, Audit Manager  
Philip Smith, Lead Auditor  
Stasha Smith, Senior Auditor  
Chinita Coates, Auditor  
Rashme Sawhney, Auditor  
Seth Siegel, Auditor



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**Appendix III**

*Report Distribution List*

Commissioner C  
Office of the Commissioner – Attn: Chief of Staff C  
Deputy Commissioner for Operations Support OS  
Deputy Commissioner for Services and Enforcement SE  
Deputy Commissioner, Wage and Investment Division SE:W  
Director, Procurement OS:A:P  
Director, Filing and Payment Compliance SE:W:CP:FPC  
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National Taxpayer Advocate TA  
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Office of Management Controls OS:CFO:AR:M  
Audit Liaisons:  
    Director, Procurement OS:A:P  
    Acting Senior Operations Advisor, Wage and Investment Division SE:W:S



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**Appendix IV**

*Management's Response to the Draft Report*



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
ATLANTA, GA 30308

RECEIVED  
SEP 01 2005

AUG 31 2005

MEMORANDUM FOR PAMELA J. GARDINER  
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: *for* Richard J. Morgante *Pamela D. Watson*  
Commissioner, Wage and Investment Division

SUBJECT: Discussion Draft Audit Report: The Private Debt Collection  
Request for Quotation Outlines Adequate Procedures and  
Controls (Audit # 200510021)

Thank you for the opportunity to respond to your discussion draft report entitled "*The Private Debt Collection Request for Quotation Outlines Adequate Procedures and Controls.*" I am pleased your review acknowledged the significant accomplishments of the Internal Revenue Service team to develop a comprehensive document for administration of the Private Debt Collection (PDC) initiative. The Policy and Operations guide, which is additional supporting information to the Statement of Work currently being developed, will include information and clarification regarding:

- the methodology for IRS reviews to ensure that Private Collection Agency (PCA) employee compensation is not based on collection statistics;
- requirements regarding the review of PCA telephone activity reports and expected turnaround times for receipt of these reports;
- what constitutes a computer desktop, as defined in the security requirements of the Request for Quotation (RFQ), and the requirement that account access for separated PCA employees, or employees no longer needing access to Federal tax data, be immediately disabled; and
- specific timeframes PCAs should allow taxpayers to forward documentation in support of their position when disputing the amount owed.

We would also like to recognize the audit team's efforts during this audit. The IRS staff that worked with your audit team provided positive feedback regarding observations your team shared regarding our PDC procurement documents. As a result, we have strengthened certain RFQ criteria and operational guidelines.

If you have any questions, please call me at (404) 338-7060, or members of your staff may contact Jim Grimes, Director, Compliance, at (404) 338-9904.