

GAO

Testimony

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TAX ADMINISTRATION:

IRS' Management of Seized  
Assets

Statement of  
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IRS' MANAGEMENT OF SEIZED ASSETS  
SUMMARY OF STATEMENT BY  
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GAO believes that IRS should seek another agency or contractor to handle the property management functions that two of its divisions--Collection and Criminal Investigation--now carry out in disposing of seized property. Neither division has adequate controls to protect the property it seizes--such as vehicles, office equipment, business inventory, and real estate--from theft, waste, or misuse. And the practices used to dispose of the property do not always provide the best return for the taxpayer.

IRS depends heavily on the integrity of its staff to protect the property it seizes. To their credit, GAO found few instances of stolen or missing property. However, GAO found several very basic internal control weaknesses. IRS does not know the total amount of property in its possession because it lacks an adequate management information system. Physical inventories are not conducted and documentation problems include failure to report seizures in a timely manner, to obtain receipts showing where the property was stored, and to note the physical condition of the property when it was seized.

GAO believes that storage and sales costs could be reduced and revenue increased if the seized property were consolidated. Each Collection Division revenue officer who seizes property is expected to find a place to store the property and to sell it. Consequently, GAO found instances where storage costs for similar property varied within the same metropolitan area. For example, in Fort Lauderdale, IRS was paying \$10 per day to store vehicles at one location, \$5 per day at another, and \$3 per day at a third location. Similarly, IRS does not generally reap the benefits that would come from combined sales. Instead, each revenue officer independently decides when to sell property, how to advertise it, and the time and place of the sale.

The Criminal Investigation Division's problem is less complex, as the division makes fewer seizures and has to dispose of only a portion of the property. Although seizures begin with the individual special agents, a coordinator within the district provides a degree of specialization and the Marshals Service manages much of its property. But the division has an unreliable information system and has not established effective sales procedures. As a result, valuable property is being held for long periods awaiting sale.

Mr. Chairman, Mr. Schulze, and Members of the Subcommittee:

We are pleased to be here today to give you the results of our review of IRS' management of assets that are seized from individuals and businesses. Mr. Schulze originally requested this review and was later joined in his request by the Chairman.

Our basic conclusion is that there is vast room for improvement. Controls over this property are weak. They are inadequate to protect against theft, waste, or misuse. And the practices used do not necessarily lead to the highest sales price at the lowest cost. As a result, the return is low compared to the taxes owed. Another concern is that the practices used could easily lead to disparate treatment of taxpayers.

### BACKGROUND

The types of seized assets we are talking about today are cars, machinery, furniture, real estate, and the like. Two IRS divisions--Collection and Criminal Investigation--seize such assets. The Collection Division's goal is to collect delinquent taxes owed the government--first by encouraging payment and only as a last resort actually taking property. Much of the property is released back to the taxpayer; the property kept has to be sold and the proceeds applied to the tax debt.<sup>1</sup> The Criminal Investigation Division, on the other hand, takes assets bought with illegal money or used in criminal activities; this division is far more likely than Collection to seize cash. And, once the property is administratively or judicially forfeited, it may be used or shared with other law enforcement agencies; only the remaining property is sold.

Both divisions have problems with asset management.

### LACK OF CONTROLS OVER SEIZED ASSETS

Neither we nor IRS managers know the total amount, value, or types of property in IRS' possession; where it is located; how long it has been there; what it costs to store it; or whether its condition has deteriorated. Such information is at best only available in individual case files. Without summary records, it would be very difficult to periodically check to see that all this property is where it is supposed to be. And no one does. Without records and physical inventories, thefts can go unnoticed.

Thus, IRS relies heavily on the integrity of its staff to protect this property. And to the staff's credit, we found few instances of stolen or missing property.

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<sup>1</sup>The Collection Division also levies liquid assets such as bank accounts but does not take physical possession of the money. Such levies were not included in our review.

We selected a sample of 70 pending individual case files and asked to see the property and records.<sup>2</sup> While we could account for the property we inventoried in all but two cases, it was sometimes not where the records said it would be. We also reviewed 278 closed cases.<sup>3</sup> Five of them had documents indicating property had been stolen. One file indicated property was missing. In most cases, the records did not reflect the value of these assets described below.

- Televisions, video cassette recorders, telephones, scuba equipment and other personal items were stolen in Atlanta.
- Mobile telephones, beepers, and an answering machine were stolen, but later recovered, in Tucson.
- A grocery inventory valued at \$10,000 was stolen in Miami.
- Three television remote controls were stolen in Xenia, Ohio.
- Four hubcaps were stolen from a Cadillac in Columbus, Ohio.
- A 1980 gold Krugerrand was missing in Phoenix. This was the only Criminal Division case in this group.

In 9 other Criminal Division cases, records did not reflect what happened to the property. So we could not tell whether IRS had, or was supposed to have, the property in its possession. We have no evidence that the property was stolen; the records appeared to be out of date. Two examples of this problem follow.

- An agent in Miami seized a \$13,000 Mazda in March 1991. As of April 1992, the file did not show what happened to the car. IRS has since told us that the car was placed into official IRS use.
- An agent in Fort Lauderdale seized 30 pieces of gold and diamond jewelry worth \$17,000 in January 1991. When we reviewed the file in April, it did not show what happened to the jewelry. IRS has since told us that the jewelry is in storage.

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<sup>2</sup>The 70 cases--43 Collection Division and 27 Criminal Investigation Division--were selected at random from open seizure cases in which property was stored within 1 hour's distance of five district offices. In 50 cases, our review started with the case file; in 20 we started with property found at the storage site.

<sup>3</sup>In six district offices, we reviewed a random sample of 180 Collection Division cases closed in 1991 as well as all 98 Criminal Investigation Division cases closed that year.

IRS has reconciled 5 other cases. In the remaining 2 cases, IRS has not yet found a movie camera, digital diary, and two beepers.

We found a plethora of other control weaknesses. About one-third of the time, seizures were not reported within 5 days, as expected; sometimes they were not reported for weeks. In 80 percent of Collection cases and 34 percent of Criminal Investigation cases, no receipts were obtained showing who had the property. In 64 percent of Collection cases, no one noted the physical condition of the assets, leaving IRS open to complaints of damage. In one instance, we observed property in an unsecured location--two cars and a boat on a trailer in an unsecured, unfenced parking lot.

The recordkeeping problems combined with the cases of stolen or missing items illustrate that property is vulnerable to loss.

#### WASTEFUL PRACTICES

Taxpayers are also subject to another kind of loss. If property is handled poorly or sold too cheaply, delinquent taxpayers are credited with paying less of their debts--because the debtor must bear all seizure and property disposal costs. And, of course, when the government collects less money than it could, all taxpayers bear the burden.

And these properties are often not sold for top dollar. In the cases we reviewed, IRS got 43 percent of what revenue officers thought the property was worth. Property taken from each taxpayer was advertised and sold alone rather than consolidated in a larger sale. Property management professionals tell us that larger sales bring more buyers and higher bids.

The costs deducted from the proceeds are sometimes higher than they have to be. Storage costs, for example, vary even within the same metropolitan area.

IRS loses money on many of the assets it seizes. In fact, in 23 percent of the cases we reviewed--42 of 180--IRS collected no money at all but incurred labor and overhead costs. In half of these cases, taxpayers' accounts were charged for such out-of-pocket expenses as towing and storing. In 13 cases, property had to be returned to the taxpayer when the revenue officer learned that the taxpayer had insufficient equity to make a sale worthwhile.

The examples that follow demonstrate the problems.

- No money was collected when a revenue officer in Richmond seized a \$4,500 vehicle from a taxpayer who owed \$53,000. After paying towing and storage costs of \$200, the officer learned the taxpayer's equity in the vehicle was less than the

expected sale proceeds. He released the property back to the taxpayer.

- An officer in Cincinnati seized a vehicle worth \$300 from someone who owed \$40,000. Sold for \$280, after expenses of \$150, the vehicle brought only \$130 to apply to the tax debt--less than 1 percent of what the taxpayer owed. Considering the revenue officer's time and IRS' overhead, the government undoubtedly lost money.
- A revenue officer who seized highway construction equipment admitted having no idea of its value. She asked the taxpayer its worth, set the "fair market value" at half the taxpayer's estimate, and set the minimum selling price at 60 percent of "fair market value". The property was eventually released back to the taxpayer because he filed bankruptcy before a sale was arranged.
- Properties from 11 Atlanta seizures were stored in 10 locations. The two storage vendors we contacted said they would negotiate discounts to store more IRS property.
- Vehicles were stored in three places in Fort Lauderdale. One charged \$10 a day, one \$5 a day, and one \$3 a day.
- Vehicles were stored in two places in Richmond, one costing almost 3 times the other.
- A vehicle seized in November 1990 was still in storage in Fort Lauderdale in April 1992. Storage costs, which by then totaled \$4,500, were increasing \$10 a day.

In part because of inefficiencies such as these, the Collection Division collects less and less of the taxes owed. In 1989, proceeds satisfied 13 percent of the associated tax debts. In 1990, the proceeds satisfied 9 percent, and in 1991, only 8 percent of the tax debts owed. And these returns do not account for IRS' salaries or overhead costs to seize and sell the properties.

The government also loses when property that is seized in criminal cases is not disposed of efficiently. Some property has been left to depreciate for many months without a sale being arranged, as the examples below show.

- The Cleveland office was paying \$150 a month to store a \$30,000 Corvette and a \$25,000 Jaguar and did not know when a sale would be arranged. (IRS now says it will transfer the Jaguar to the Marshals Service for disposal and give the Corvette to another law enforcement agency.)

- The Cincinnati office has stored a \$200,000 Ferrari Testarossa and \$50,000 worth of jewelry for over a year. The car is in IRS' own parking lot and the jewelry in an IRS safe; so IRS has not incurred storage costs.
- The Detroit office owes \$5,000--and is accruing \$600 a month--to store a \$225,000, 42-foot boat seized in February 1992.

#### FLAWED PROCESS CAUSES WASTE AND DISPARITIES

Inefficiencies are to be expected as long as IRS continues doing business the same way. The process is too dependent on too many people of whom too much is expected.

In the Collection Division, the process is dependent on the skills and good judgment of 8,000 revenue officers. Their job is to collect delinquent taxes, which they usually do by asking for payments, negotiating installment agreements, garnishing wages, or identifying bank accounts or other cash assets that can be levied. A revenue officer who decides to seize property needs far more skills than the day-to-day job demands. The officer becomes the lien searcher, appraiser, person who takes the property, contracting officer for storage, custodian, advertiser, seller, and perhaps auctioneer. This is a lot to ask of any one person. And these skills are used infrequently. Total seizures in 1991 numbered 10,000--or little more than one per officer on average.

The risk of doing business this way is obvious--8,000 different ways of doing things and none of the added control that comes from segregating duties. All 8,000 officers are expected to appraise the value of property that ranges from bulldozers to antiques. But they are not trained appraisers and largely use their own judgments. The officers use their appraisals to set the minimum bids IRS is willing to accept.

With few exceptions, the officers are also on their own in finding a place to store the property. Some may be aware of, or search for, more economical storage facilities than others. Assets from 116 seizures that we reviewed were stored at 89 different locations. Most of the seizures--111--were in 18 metropolitan areas. Storage costs varied even within the same metropolitan area and did not reflect potential discounts. We found exceptions.

- One of several offices in Cincinnati made arrangements to use a government storage facility at no cost.
- The Phoenix District had a purchase agreement with one vendor where two offices stored almost all their seized vehicles.

More such arrangements would save time and money.

Similarly, IRS does not generally reap the benefits that would come from combined sales. Advertising costs could be reduced and more buyers attracted if property were consolidated for larger sales. Instead, each officer may independently sell the property seized, deciding the specific advertising to be used and the time and location of the sale. Thus, we found sales advertised in the same newspaper within 4 days of each other; and two sales within a 2-week period in the same city were common. Again, we found an exception. In Columbus, Ohio, revenue officers combined property from several seizures and held larger sales. Columbus officers reported that property sold for amounts exceeding their expectations--some at or close to the values they had set as "fair market". They attributed the higher prices to more bidders attracted by larger sales.

IRS needs to find a way to make its sales more effective.

The Criminal Investigation Division problem is less complex. This division makes fewer seizures--IRS estimated 2,000 last year--and has to dispose of only a portion of the property. Some property is converted to official use, and the Marshals Service sells assets the division takes in judicial proceedings. Although seizures begin with individual special agents, a coordinator within each district provides a degree of specialization. But the division has an unreliable tracking system and before this year did not have sales procedures. When procedures were developed this year, they were not coordinated with IRS' Facilities Management Branch. Yet agents were told that the Facilities Management Branch would dispose of assets for them. Because Facilities Management personnel had not been forewarned, some refused. The division, which has yet to work out the glitch with Facilities Management, needs to resolve how sales should occur. The longer the delay, the longer valuable property will be allowed to deteriorate awaiting sale.

#### OPTIONS TO IMPROVE ASSET MANAGEMENT

We believe any one of a number of changes would help IRS improve the management of seized assets.

Perhaps the simplest change in the Collection Division would be staff specialization. Either allow some revenue officers to specialize in managing seized property or convert some officer positions to asset management positions. This would confine the task to fewer, more experienced people. It should offer more visibility and therefore more control over all Collection Division property a district has in its possession. Someone would have the ongoing job of arranging storage at the least cost and sales at the highest price.

A more ambitious approach, still within the purview of IRS, would be to consolidate storage and sales--either on a districtwide or



regionwide basis. This, too, would require asset management professionals but also the cooperation of both divisions.

Another approach would be to turn the job of asset management over to someone else--a contractor or one of the other agencies that has a sizable asset management function, such as the Customs Service, the Marshals Service, or the General Services Administration (GSA). The Customs Service, also in the Treasury Department, has a contract for the nationwide management of seized property and a network of bonded warehouses for storage. The Justice Department's Marshals Service, which already manages judicial forfeitures seized by the Criminal Investigation Division, has property management specialists and nationwide and regional contracts and agreements for storage and sale of seized property. While GSA does not have storage facilities, it has well-established sales programs--especially for vehicles. The Collection Division has an agreement with GSA to sell seized real estate, but none of the districts we visited had used it.

Last year, we reported that administration costs could be reduced 11 percent a year if Customs and the Marshals Service consolidated their management and disposition of noncash property. Even more savings are likely from lower vendor costs due to economies-of-scale. The two agencies have agreed to a pilot test to begin next month.

#### CONCLUSIONS AND RECOMMENDATIONS

While any of the options should improve the situation, we believe it makes the most sense to give the asset management job to an agency or contractor that specializes in it. The solution for the Criminal Division seems obvious. As I noted earlier, it already has an arrangement with the Marshals Service to sell some property. We see no reason why a similar arrangement could not be made for the remaining property. IRS needs to make the same kind of decision for Collection Division property.

It is also clear that IRS needs far better information than it now has. But it makes no sense for IRS to embark upon a redundant effort to develop the same kind of information system which the Marshals Service and Customs have already paid for and are now upgrading. IRS does need to inventory its property in order to know what it has to turn over to another agency.

Regardless of the asset management option selected, IRS needs to improve controls over the seizure process. Revenue officers need better guidance on what is a cost-effective seizure. They also need to adhere to such already established procedures as checking the taxpayer's equity before taking property, reporting seizures timely, and noting the property's condition.

But the major issue is that the current IRS process is inherently flawed and detracts from IRS' main mission. The process is so haphazard that it could easily lead to disparate treatment of taxpayers. Thus, it is important that IRS assess how well each of the agency or contractor options fits its operational requirements, choose one, and follow through to implement the change.

This concludes my statement. My colleagues and I will be pleased to respond to any questions.