United States General Accounting Office

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Report to the Chairman, Committee on the Budget, U.S. Senate

December 1987

TAX ADMINISTRATION

IRS' Implementation of the 1987 Revenue Initiative

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United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-227715

December 2, 1987

The Honorable Lawton Chiles
Chairman, Committee on the Budget
United States Senate

Dear Mr. Chairman:

Through a supplemental appropriation for fiscal year 1986 and a continuing resolution for fiscal year 1987, Congress provided the Internal Revenue Service (IRS) with funds to increase its examination staff by 2,500 positions—1,618 of which were designated for revenue agents, 175 for tax auditors, and 707 for support personnel. IRS projected that this increased staffing would enable it to examine 113,000 additional tax returns and would generate $593 million in additional tax collections during fiscal year 1987. The staffing increase for 1987 represented the first installment of a 3-year revenue initiative that calls for increasing IRS' examination staff by 2,500 positions a year through fiscal year 1989. In response to your February 4, 1987, request, this report provides information on administrative actions taken by IRS to implement the fiscal year 1987 phase of that initiative.

IRS did not achieve the gain in revenue agent staffing anticipated by the fiscal year 1987 phase of the revenue initiative until late in that fiscal year. A primary reason was that many of the agents hired through the initiative actually filled attrition vacancies that had gone unfilled because of a management decision to divert resources from enforcement to returns processing in 1986. Despite the staffing shortfall, IRS officials still expect to meet the revenue projections for 1987.

Objective, Scope, and Methodology

In your February letter, you asked us to investigate, in two phases, the revenue potential of enhanced compliance and enforcement programs in IRS. First, you requested a brief review of administrative actions taken by IRS to hire the new enforcement personnel and asked us to make some preliminary assessments as to whether IRS will be able to train and station these new employees. Second, you requested that we establish a mechanism to measure additional revenue brought in by enhanced enforcement efforts.

This report addresses the first phase of your request. As agreed with your office, we focused our work on IRS actions to hire, train, and otherwise assimilate the new revenue agents whose positions were made possible by the fiscal year 1987 revenue initiative. We began work on the second phase of your request in September 1987.

Our objective in reviewing the 1987 revenue initiative was to provide an overview of how IRS was implementing the initiative. To do this, we obtained (1) statistics from IRS headquarters on the revenue and staffing impact of the initiative and (2) information from three regional and seven district offices on how new revenue agents were recruited and assimilated into the workforce. We did our work at IRS headquarters in Washington, D.C.; its regional offices in Cincinnati, Ohio; Dallas, Texas; and San Francisco, California; and its district offices in Cincinnati and Cleveland, Ohio; Dallas, Texas; Detroit, Michigan; Indianapolis, Indiana; Laguna Niguel, California; and Phoenix, Arizona. These regions and districts were selected to provide a balanced perspective of how IRS field offices were affected by the initiative. The Western (San Francisco) and Southwestern (Dallas) regions and the districts in those regions were chosen because they were greatly affected by the initiative in terms of the number of revenue agents hired to meet projected examination workload. The Central Region (Cincinnati) and its districts were less affected and therefore provided balance on how the hiring and assimilation of fewer new revenue agents affected operations. We interviewed the Regional Commissioner or Assistant Regional Commissioner for Examination in each of the three regions. In the seven districts, we interviewed the chief or assistant chief of the Examination Division, certain group managers and branch chiefs, and a nonrandom sample of revenue agents who had been hired in the last quarter of fiscal year 1986.

We did most of our work in February 1987, in accordance with generally accepted government auditing standards, and briefed your staff on February 26, 1987. In May, your office requested that we provide a written report. In preparing this report, we obtained some additional information from IRS that was not presented at the February briefing.

The results of the four major areas of our study—staffing levels, additional revenue, hiring, and assimilation—are highlighted below.

Staffing Levels

IRS received a supplemental appropriation in July 1986 which, according to IRS budget documents, was to "insure the full revenue potential" of the fiscal year 1987 phase of the initiative by allowing IRS to hire and start training new revenue agents during the final quarter of fiscal year 1986. The new agents were to be net additions to IRS' revenue agent workforce and, according to IRS officials, were to be on board before, or at least shortly after, the start of fiscal year 1987. As discussed below, IRS' revenue agent staffing levels did not increase to the extent envisioned by the revenue initiative and the supplemental appropriation.

As shown in appendix I, IRS had 14,507 revenue agents on board as of October 1, 1986, compared to 13,807 on January 1, 1986—an increase of 700. That increase was 918 less than the 1,618 increase authorized by the fiscal year 1987 phase of the revenue initiative. We used January 1, 1986, as the starting point for our comparison to illustrate the size of IRS' agent workforce before the peak recruiting season and the fiscal year 1986 supplemental appropriation.

A primary reason for the shortfall in net additions to the agent workforce, according to IRS officials, was a decision by the former Commissioner to move resources from enforcement to returns processing in 1986 to avoid processing delays and problems similar to those experienced during the 1985 filing season. The decision restricted examination officials from hiring new agents to fill openings created by attrition before the final quarter of fiscal year 1986. That decision, along with an estimated attrition rate, according to IRS officials, of about 100 agents a month caused IRS' on-board strength of revenue agents to decrease by 436 between January 1 and June 21, 1986. Therefore, once the supplemental was approved and IRS began hiring new agents in July 1986, a number of those hired actually filled vacancies created by attrition, which kept IRS from realizing the gains in staff anticipated through the revenue initiative.

Changing the starting point for our staffing analysis to June 21, 1986, just before IRS started hiring agents again, and comparing it to October 1, 1986, at which time the new agents authorized by the 1986 supplemental should have been on board, still shows that IRS fell short of achieving the staffing gains anticipated by the revenue initiative. On June 21, 1986, IRS had 13,371 revenue agents on board. If it had increased staffing by the 1,618 agents called for by the initiative, IRS would have had 14,989 agents on board as of October 1, 1986. Instead, 14,507 agents were on board at that date—482 less than anticipated.

In its technical comments on a draft of this report, IRS provided additional statistics, in terms of staff years realized rather than persons on board, to demonstrate that it did not achieve the goal of the revenue initiative.

"In July, 1986, Congress provided funds for 404 Examination staff-years as the beginning of a three year revenue initiative. From July through September, 1986, Examination hired 3,800 employees including 2,080 revenue agents. This equates to 399 staff-years, fully utilizing all the supplemental funds. However, because of previous attrition and internal management actions, 13,619 staff-years of a total annual authorization of 14,671 revenue agent staff-years were realized.

For Fiscal Year 1987, the budget authorized 15,806 revenue agent staff-years including 1,618 revenue initiative revenue agents. During Fiscal Year 1987, Examination will have hired 3,195 revenue agents. However, because of attrition and internal management actions including budget adjustments, 14,995 revenue agent staff-years will be realized."

Additional Revenue

IRS originally projected that the 1,618 additional revenue agents hired through the revenue initiative, and brought on board as of October 1, 1986, would help to generate additional tax revenues of $593 million in fiscal year 1987. Although IRS did not realize the revenue agent staff years authorized by the revenue initiative, officials believe, on the basis of their management information, that IRS will meet its revenue projections for fiscal year 1987. If this is true, it would indicate that IRS' estimates of additional tax to be generated through the revenue initiative are conservative.

IRS' estimate of $593 million in additional tax revenues was based on a planning model that uses marginal yield analysis to project the additional revenue generated from each additional staff person. According to IRS officials, the model accounts for such factors as training time for new revenue agents and the loss of direct examination time by experienced agents who provide the training. To measure the first year's impact of the 1987 revenue initiative, IRS officials said they will subtract from the additional tax actually recommended for 1987, an estimate, using the model, of what additional taxes would have been recommended if additional staff had not been provided through the revenue initiative. The difference, according to IRS officials, should reflect the revenue impact of the initiative in terms of recommended additional tax.

To clarify, recommended tax does not represent what is actually collected from the taxpayer but, rather, the amount of additional tax a revenue agent has determined, through an audit, the taxpayer should pay. There are several reasons why IRS might actually collect less than the recommended amount. The taxpayer might appeal the agent's decision, for example, and, as a result, get the recommended amount reduced. Also, the taxpayer may go bankrupt or for some other reason be unable to pay the full amount due. According to Examination officials, IRS, in estimating the yield from examinations, assumes that about 73 percent of the additional tax recommended is assessed and that 95 percent of the assessed amount plus interest is actually collected.

During the second phase of our work, we will be looking at IRS' yield from examinations. In so doing, we expect to evaluate the factors IRS considers and the assumptions it uses to estimate yield and the methods it uses to measure actual results.

Hiring

According to IRS officials, efforts to hire the additional revenue agents authorized by the 1987 initiative were adversely affected by the timing of the supplemental appropriation and by IRS' inability to offer competitive salaries to college graduates.

The fiscal year 1986 supplemental appropriation, which provided funds to enable IRS to hire the additional revenue agents before the start of fiscal year 1987, was enacted in July 1986. Therefore, even though IRS recruited for revenue agents early in 1986, it could not make firm job commitments and thus hire those agents until July—after the supplemental was approved. IRS officials said that potential job applicants with accounting degrees often receive commitments and accept job offers before June graduation, thus limiting the pool of applicants available to IRS. Although IRS officials said they were pleased with their new recruits, they also told us they would like the opportunity to recruit from a greater number of graduates. Consequently, the officials would like to have funds available to make firm hiring commitments to June graduates prior to graduation.

IRS officials said that the ability to make firm offers before graduation is even more important because IRS cannot offer accounting graduates salaries that are competitive with those offered in most of the private sector. Officials say this is especially true in certain large metropolitan areas, such as New York City. Starting salaries for college graduates with accounting degrees are compared in table 1.

Table 1: Starting Salaries for Accounting Graduates (February 1987)

IRS revenue agents	"Big 8" accounting firms	Other private sector accounting jobs
$14,822-18,358	$22,000–25,000	$17,000–20,000

Sources: General Schedule salary scale, personnel departments at two "Big 8" firms, and the American Institute of Certified Public Accountants.

Staff Assimilation

IRS was able to assimilate (train, equip, and house) the over 2,000 new revenue agents hired during the final quarter of fiscal year 1986. Although a few districts we visited experienced some logistical problems related to office space and the location of particular examination groups, IRS officials said that the problems were overcome and the districts were able to provide recruits with the necessary facilities and normal training. Interviews with management staff and newly hired agents in February 1987 indicated that in the districts we visited, IRS' multiyear training program for new agents (see app. II), which uses experienced agents as instructors, was proceeding in accordance with established guidelines and schedules, even with the large influx of staff.

Because the revenue agent training program spans several years, IRS' ability to effectively assimilate the new agents associated with the fiscal year 1988 phase of the revenue initiative could be complicated. During fiscal year 1988, districts will have to train revenue agents hired during the first 2 years of the revenue initiative. This could put a greater strain on the availability of experienced agents because those agents are used as training instructors and are assigned to provide daily oversight and guidance to new staff. The strain will be further exacerbated by the fact that the experienced agents themselves will have to be trained on the tax law changes generated by the Tax Reform Act of 1986. To help ease the strain on individual districts, IRS' implementation of the fiscal year 1988 phase of the revenue initiative will include a 20 percent cap on revenue agent growth in some districts. The objective of the cap is to assure orderly growth in the districts without compromising their ability to train and support new staff and perform planned examination work.

The hiring of new revenue agents is also reflected in IRS' plan to automate the examination function. For example, IRS officials told us that they have budgeted funds to provide an additional 3,000 lap-top computers. The 3,000 will increase the total number of lap-top computers to 18,000, which should be enough to equip all the additional agents to be hired through the 3-year initiative.

Agency Comments and Our Evaluation

IRS commented on a draft of this report by letter dated October 21, 1987 (see app. III). IRS stated that our use of June 20, 1987, to calculate an on-board strength of 14,850 revenue agents did not present a complete picture of IRS' hiring achievements. IRS pointed out that between June 20, 1987, and August 29, 1987, an additional 1,359 revenue agents were hired and brought on board, reflecting the usual July and August reporting dates of June hires. This brought the number of revenue agents on board to 16,209.

We used June 20, 1987, as the last date for our staffing comparisons because that was the most current data available when we prepared our report. Although the chart in appendix I still reflects the staffing level at that date, we no longer highlight that figure. Because the intent of the revenue initiative and the supplemental appropriation was to increase revenue agent staffing by the start of the fiscal year, the number of agents on board as of October 1, 1986, is the more important number.

We believe that IRS' hiring of 1,359 revenue agents toward the end of fiscal year 1987 should be considered separately from what was done around the beginning of that fiscal year to achieve the objective of the supplemental appropriation and revenue initiative. Several hundred agents hired toward the end of a fiscal year cannot have the same impact on that year's examination program as they would if hired near the beginning of the year, as intended by the revenue initiative. Those hired at the beginning have a full year to train and start examining returns unlike those hired at the end. That point was illustrated by IRS' technical comments on page 4, which show that although 3,195 agents were hired during fiscal year 1987, IRS still ended the year with 811 unrealized staff years.

IRS also expressed the belief that we should place greater emphasis on the uncertainty faced by IRS because of delays inherent in the appropriations process. IRS explained that the uncertainty presents a major impediment to the careful planning and managing of resources and is a continuing problem for all IRS programs. We believe that our comments on page 5 and IRS' comments in appendix III provide the emphasis IRS is seeking.

As agreed with your office, we are sending copies of this report to IRS. Unless you publicly announce its contents earlier, we plan no further distribution until 20 days from the date of the report. At that time, we

will send copies to interested parties and make copies available to others upon request.

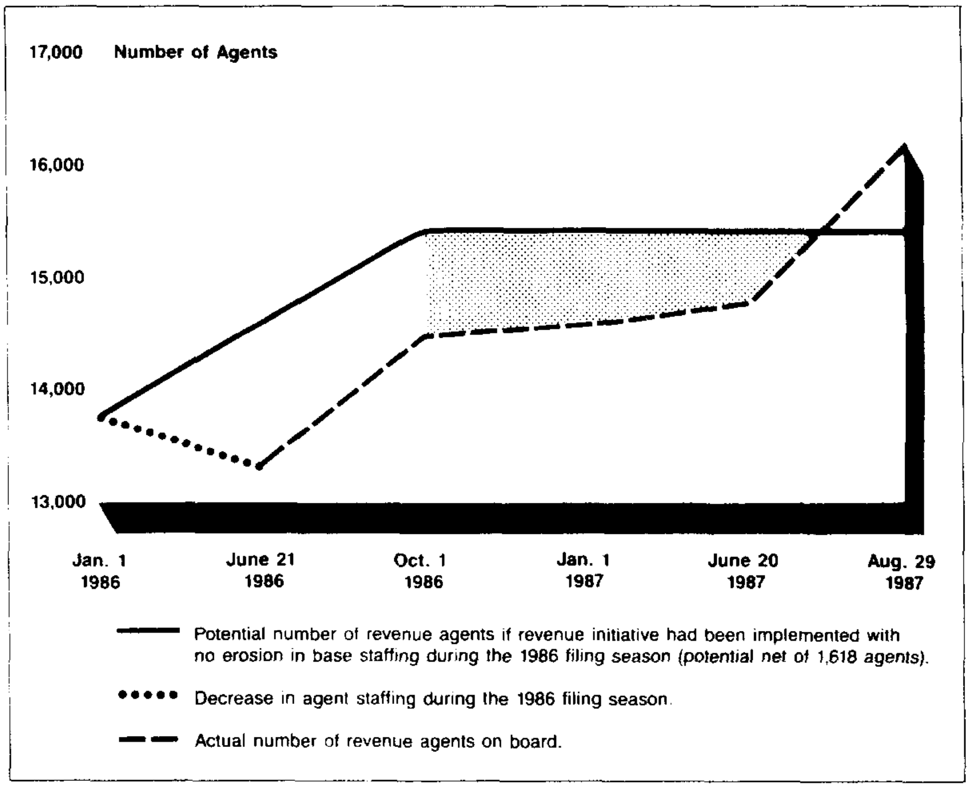
Sincerely yours,

Jennie S. Stathis

Jennie S. Stathis
Associate Director

mpact of Revenue Initiative on Agent Staffing

gure I.1: Number of Revenue Agents on
ard—Actual Versus Potential



Shaded area represents gap between potential staffing level and actual on-board strength when using January 1, 1986 as the baseline.

ble I.1: Number of Revenue Agents on
ard—Actual Versus Potential

Date	Number of agents on board	Potential agents on board under revenue initiative[a]	Number of on-board agents above or (below) potential
Jan. 1, 1986	13,807	•	•
June 21, 1986	13,371	b	b
Oct 1, 1986	14 507	15,425	(918)
Jan. 1, 1987	14,606	15,425	(819)
June 20, 1987	14,850	15,425	(575)
Aug. 29, 1987	16,209	15,425	784

[a]Computed using the January 1, 1986, on-board figure as a base.

[b]Not applicable because June 21, 1986, was before the initiative's effective date.

Training Schedule for Revenue Agents

Training Schedule for Revenue Agents

Phase	Type	Length of time		Subject matter
I	Preclassroom	0.5	weeks	Orientation
	Classroom	5	weeks	Nonbusiness tax returns and Schedule E
	On-the-job	5	weeks	Audits conducted at IRS office
		2	weeks	Complete auditing returns
	Total	**12.5**	**weeks**	
II	Classroom	7	weeks	1040 - Schedules C,D,E,F, auditing training
	On-the-job	8	weeks	1040 business returns
	Field experience	6	months	1040 business returns, Schedules C,D,E,F
	Total	**41**	**weeks**	
III	Classroom	3	weeks	Corporations (Forms 1120), S-Corporations (Forms 1120S), computer training
	On-the-job	10	weeks	1120, 1120S returns
	Field experience	6	months	1120, 1120S, and 1040 business returns
	Total	**39**	**weeks**	
IV	Classroom	4	weeks	Partnerships (Forms 1065), tax shelter concepts
	On-the-job	16	weeks	1065 returns, related returns, partnership procedures
	Field experience	1	year	1065, 1120. 1120S, and 1040 business returns
	Total	**72**	**weeks**	
V	Preclassroom	2	weeks	Introduction to advanced corporate auditing
	Classroom	4	weeks	In-depth advanced corporate auditing with additional international emphasis
	On-the-job	8	weeks	1120 returns
	Total	**14**	**weeks**	

Notes: The totals for each phase are approximations of weeks.

On-the-job training is conducted under the guidance of an on-the-job instructor, while field experience normally means the agent is conducting the audit in the field without an on-the-job instructor.

Comments From the Internal Revenue Service

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

COMMISSIONER

OCT 21 1987

Ms. Jennie S. Stathis
Associate Director
General Government Division
United States General Accounting Office
Washington, DC 20548

Dear Ms. Stathis:

We appreciate the opportunity to review and comment on your draft report entitled "Tax Administration: IRS' Implementation of the FY 1987 Revenue Initiative." Certain technical comments on the draft report have already been provided directly to your staff for inclusion in the final report.

We believe that the June 20, 1987 date used in the report to calculate on board strength of 14,850 revenue agents and a resulting shortfall of 575 revenue agents does not present a complete picture of our hiring achievements. Between that date and August 29, 1987, an additional 1,359 revenue agents were hired and brought on board, reflecting the usual July and August reporting dates of June recruits. Thus, there were 16,209 revenue agents in total on board as of August 29, more than the 15,425 GAO said were needed for FY 1987 to meet the revenue initiative's hiring goals.

Additionally, we believe the report should place greater emphasis on the uncertainty faced by the IRS because of delays inherent in the appropriations process. This uncertainty presents a major impediment to the careful planning and managing of resources, and is a continuing problem for all Service programs.

For example, as noted in the report, hiring for the revenue initiative was funded through a supplemental appropriation for FY 1986. This supplemental appropriation provided funds to recruit and hire June graduates, but was not enacted until July of 1986. Thus, the chance to hire June graduates was essentially lost for that year.

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Ms. Jennie S. Stathis

For FY 1987, the revenue initiative was funded through a continuing resolution. Although enacted in October, 1986, the resolution followed several months of uncertainty over the exact funding levels likely to be included: the House wanted to add additional resources to the original request while the Senate sought to reduce the original request. The important fact here is that planning under these circumstances was difficult at best. As GAO noted, and as the Senate Appropriations Committee recently reminded us, firm job commitments cannot be made until funding is enacted. Therefore, hiring under the FY 1987 continuing resolution was basically delayed until June, 1987. As stated earlier, this June hiring did not manifest itself until July of this year, after GAO had completed its research for the report.

I trust these comments will be useful in preparing the final report.

With kind regards,

Sincerely,

Larry G. Gibbs

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