United States General Accounting Office

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Report to the Chairman, Subcommittee on Oversight, Committee on Ways and Means, House of Representatives

September 1991

TAX ADMINISTRATION

Opportunities to Increase Revenue Before Expiration of the Statutory Collection Period

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GAO

United States
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General Government Division

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September 30, 1991

The Honorable J. J. Pickle
Chairman, Subcommittee on Oversight
Committee on Ways and Means
House of Representatives

Dear Mr. Chairman:

This report, one of a series of documents responding to your March 28, 1990, request, addresses Internal Revenue Service accounts receivable that are written off because the collection statute of limitations[1] has expired. Specifically, this report provides information on (1) the amount of the accounts receivable that has been or possibly will be written off and (2) preliminary data on the potential impact of the November 1990 extension of the collection period from 6 to 10 years. This report also discusses IRS' procedures for managing accounts receivable that are nearing the end of their collection periods.

Using disposition rates we calculated on the basis of unaudited disposition information, by age of account, for the September 30, 1989, accounts receivable balance, we estimated the amounts of the September 30, 1990, accounts receivable balance that would be disposed of through collection, abatement, or expiration of the collection statute of limitations. We did not assess the reliability of IRS' disposition information for the September 30, 1989, balance. However, we reviewed the information for apparent reasonableness and consistency by comparing it with amounts IRS had reported as total collections, abatements, and expiration write-offs for past fiscal years. Currently, there is much uncertainty about the reported accounts receivable balances. As part of the financial audit of IRS that we are now doing,[2] we will verify IRS' accounts receivable balance and provide an audit opinion on the collectibility of the accounts receivable through detailed audit work.

Part of our intent in this report is to provide a preliminary sense of what may be collected if IRS' past experience is reported correctly and indicative of the future. Given the heightened congressional interest in

[1]The collection statute of limitations—Section 6502 of the Internal Revenue Code—provides a specific period of time for IRS to collect delinquent taxes after assessment. Until November 1990, the collection period was 6 years. The Omnibus Budget Reconciliation Act of 1990 extended the collection period to 10 years.

[2]Pursuant to the Chief Financial Officers Act of 1990, IRS is part of a pilot project that requires it to prepare auditable financial statements for fiscal year 1992. We have elected, as authorized by the act, to audit IRS' fiscal year 1992 financial statements.

the growing accounts receivable balance, our initial projection of collections and write-offs could help Congress gain a better perspective on IRS' collection effort.

This report does not address the portion of your request that deals with an allowance for doubtful accounts. Our analysis of future dispositions represents a preliminary view of what would be expected to happen to the September 30, 1990, accounts receivable inventory on the basis of historical information provided by IRS. This analysis is based solely on the projection of IRS' past reported collection experience to the future. Our projections do not consider such factors as taxpayers' ability to pay their taxes, anticipated economic conditions, and changes in IRS' collection procedures, which would need to be considered in establishing a formal allowance of doubtful accounts. In addition, IRS' past collection experience may not necessarily be representative of the collection experience for the September 30, 1990, balance because of possible changes in the mix of accounts receivable and errors in the reported historical data. We plan to do further work to help IRS determine an allowance for doubtful accounts for financial reporting purposes in our financial audit of IRS.

Accounts receivable that are written off because the collection statute of limitations has expired should provide an accurate indication of lost revenue. However, as we testified before your Subcommittee in February 1990, the dollar value of the accounts receivable inventory contains significant amounts that are invalid because of errors or duplication and therefore would not become revenue regardless of the effect of the statute of limitations.[3] While many of the invalid amounts will be removed from the accounts receivable inventory through abatements,[4] it is likely that an undeterminable amount will not be removed and thus will be written off with the valid amounts when the collection period expires. Consequently, IRS' statute expiration write-offs overstate the potential tax revenue lost.

Results in Brief

Although IRS establishes and resolves billions of dollars of accounts receivable each year, a substantial portion remains outstanding at the end of each year. The dollar amount of receivables that remains uncollected and is subsequently written off because the collection statute of

[3]IRS' Accounts Receivable Inventory, Statement before the Subcommittee on Oversight, Committee on Ways and Means, House of Representatives (GAO/T-GGD-90-19, Feb. 20, 1990)

[4]IRS can reduce or cancel any unpaid tax assessment that is excessive, erroneous, or illegal.

limitations expired has grown steadily over the past 5 years. We estimate that annual write-offs of assessed taxes and assessed and/or accrued interest and penalties from IRS' two major master files—individual and business—grew from $2.3 billion to $4.6 billion between fiscal years 1986 and 1990.[5]

We expect future write-offs to be significant, reflecting the prior growth in the accounts receivable inventory. According to our projection of future dispositions based solely from IRS' most recent track record in collecting accounts, about $46 billion, or 49 percent, of IRS' $93 billion individual and business accounts receivable inventory at September 30, 1990, could be uncollected and ultimately written off because of the expiration of the collection statute of limitations. Of the remaining $47 billion, projections show that IRS could collect about $23 billion and could abate or otherwise resolve about $24 billion. These projections do not reflect IRS' overall collection effectiveness because they do not include the accounts receivable that IRS collects in the year they are established.

These estimates are tentative and could change as more specific information becomes available from our financial audit and improvements in IRS' management information systems. The estimates assume that IRS' future collection success rates and practices will follow those of past years and that the historical information provided by IRS is accurate. Nevertheless, in testing the projections using the first full year of actual IRS data available, the disposition predicted by our approach came within 1 percent of the actual reported disposition. Further, IRS agreed that our approach was a reasonable way to project collections from prior experience to provide a preliminary sense of what may be collected.

Because specific information is not currently available about the validity of accounts that are written off or the characteristics of the taxpayers whose accounts expire, we were not able to estimate how much of these write-offs would be potentially collectible if additional or revised collection measures were instituted. The collectibility, as opposed to the projected amount of collections, of the accounts in the

[5] As of September 30, 1990, the individual and business master files included $92.6 billion, or 96 percent, of the $96.3 billion total IRS accounts receivable inventory, which consists of all assessed or accrued taxes, penalties, and interest that IRS is responsible for collecting. The remaining $3.7 billion of accounts receivable is included in the individual retirement account master file and the nonmaster file. IRS does not maintain complete disposition information on these accounts, and therefore we have excluded them from our estimates and analysis of statute expiration write-offs in this report.

receivables inventory will be addressed in the financial audit. However, extension of the collection period to 10 years now provides IRS with the opportunity to increase collections. Our projection of IRS information indicates that existing collection procedures could possibly result in IRS collecting an additional $1.7 billion from the September 30, 1990, inventory as a result of the extension. This projection is based on analysis of unaudited age and disposition information from IRS' accounts receivable management information system.

Although we did not evaluate the effectiveness of IRS' collection policies and procedures, we noted two areas where IRS could improve its oversight and possibly reduce the amounts written off because of statute expiration. First, while IRS requires local reviews of decisions to suspend collection activities, it does not centrally analyze the local results to identify systemic problems. Second, although reminder notices are sent to taxpayers whose accounts were suspended early in the collection process, all taxpayers whose accounts were suspended later in the collection process are not sent these reminder notices. However, IRS has plans, which we believe should be implemented as scheduled, to send reminder notices to those taxpayers who do not currently receive them.

Background

IRS is responsible for resolving tens of billions of dollars of new and existing accounts receivable each year through its three-stage collection process. First, a service center attempts to collect unpaid taxes by sending a series of computer-generated notices, or bills, to the taxpayer. If IRS does not resolve the account and the liability is under a predetermined dollar threshold, IRS suspends active collection efforts. These accounts are classified as "deferred," and IRS takes no further collection action except for sending the taxpayer annual reminder notices and offsetting the delinquency against future refunds.

Second, IRS classifies unresolved accounts over the dollar threshold as "Taxpayer Delinquent Accounts" (TDA), prioritizes them, and generally sends these accounts to the Automated Collection System (ACS). At this stage, IRS employees can begin taking collection enforcement actions to resolve delinquent accounts. These actions include seizing taxpayers' liquid assets that are being held by third parties and/or telephoning the taxpayer to arrange payment. IRS sends unresolved, prioritized TDAS to a computerized workload management holding file called "the queue" to await assignment to revenue officers in its district offices.

Third, revenue officers attempt collection on assigned, generally higher priority, accounts through personal contact with the taxpayer and additional collection enforcement actions. Lower priority cases can remain in the queue until the statutory collection period expires with no additional collection action; in essence, collection action has been suspended.

At any time during the collection process, IRS can officially suspend active collection efforts by classifying accounts as currently not collectible (CNC) for a variety of reasons. The most common reasons are that (1) collection of the tax would cause the individual taxpayer undue financial hardship, (2) IRS is unable to locate the taxpayer or the taxpayer's assets, or (3) a business taxpayer is defunct or bankrupt and has no assets.

Accounts in suspended status—deferred, CNC, and queue accounts—are included in IRS' accounts receivable inventory until they are resolved or the collection statute of limitations expires. Generally, no further active collection efforts occur unless the account is reactivated. Queue accounts are reactivated as the accounts are assigned to revenue officers. Reactivation of a deferred account occurs when a computer match finds that the taxpayer's delinquency has increased and now represents a higher collection priority. Reactivation of CNC accounts occurs when a manual follow-up or a computer match reveals that (1) the taxpayer's income exceeds the threshold level selected by a revenue officer indicating that payment of the delinquent balance may no longer present an undue financial hardship, (2) the taxpayer now has assets that can be used to pay the tax delinquency, or (3) a new address can be used to locate the taxpayer.

Until the statutory collection period expires, IRS can use a number of less resource-intensive collection tools to resolve suspended accounts. For example, under the Internal Revenue Code, IRS can offset taxpayers' future tax refunds against unpaid account balances. In addition, federal tax liens are imposed after taxpayers fail to pay the delinquent amounts owed, and unsatisfied liens remain in effect until the statute of limitations expires. IRS files notices of tax liens to provide public notification of the tax debt and secure IRS' claim to taxpayers' property. According to IRS officials, offsets and payments to remove tax liens are most of the revenue IRS receives from taxpayers on older accounts.

The Revenue Act of 1926 established a 6-year period for the collection of assessed taxes through enforced collection action or initiation of a lawsuit. In November 1990, the Omnibus Budget Reconciliation Act of

1990 lengthened the collection period to 10 years. The Internal Revenue Code also provides for various automatic extensions of the collection period. For example, the collection statute of limitations is extended when a taxpayer's assets are in the control or custody of a court or when a taxpayer is outside the United States for at least 6 months.

The taxpayer can also agree to extend the collection statute of limitations. This agreement normally occurs when the taxpayer (1) elects to pay estate taxes in installments, (2) enters into an installment agreement to pay delinquent taxes over a period that extends beyond the statutory period, or (3) formally attempts to negotiate a settlement for less than the full amount owed.

In addition, IRS can obtain a federal court judgment against the taxpayer for the delinquent taxes. Such federal judgments—which are collected by U.S. attorneys—have no limitations on the collection period from personal property and are valid for up to 40 years against real property.

Objectives, Scope, and Methodology

The objectives of this assignment were to develop preliminary information on (1) the dollar amount of accounts receivable that has been or will be written off because of the expiration of the collection statute of limitations and (2) the potential impact of the November 1990 extension of the collection statute of limitations. We also reviewed IRS' procedures for ensuring that appropriate resolution actions are taken on accounts receivable nearing the end of their collection periods.

To estimate the amount written off in past years, we started with the amount of statute expiration write-offs of assessed accounts receivable, as developed by IRS' Collection Division, and added an estimate of the interest that had accrued on these receivables over the prior 6-year collection period. We used an IRS computer program to calculate the accrued interest. Some interest and penalties are usually assessed when the accounts receivable are established and, therefore, would be included in IRS' statute expiration write-off amounts. However, the actual amount of interest and penalties is unknown. To avoid the possibility of overstating total accrued interest and penalties, we did not estimate the additional penalties that could have accrued after the taxes were assessed.

To project possible future write-offs, we used information from IRS' accounts receivable management information system databases on the disposition of fiscal year 1988 and 1989 ending accounts receivable inventories. Earlier data were not available. Using the resolution data for the fiscal year 1989 ending inventory and regression and other analyses, we projected future write-offs, because of the expiration of the collection statute of limitations, for the September 30, 1990, accounts receivable inventory.

IRS' Research Division reviewed our methodology and believed that our approach for projecting IRS' information was reasonable. Our projections and methodology were not developed for determining an allowance for doubtful accounts for financial reporting purposes and should not be used as such. (See app. I for a detailed discussion of our methodology for estimating future write-offs.)

To determine the potential impact of the 1990 law that extended the statute of limitations, we interviewed IRS officials and obtained relevant documents. We also used the same IRS databases used to project future statute expirations to project possible future collections. The additional collections resulting from extending the statute of limitations are the difference between the future collections that we projected for the 6-year and 10-year collection periods. (See app. I for a detailed discussion on our methodology for projecting future collections.)

We interviewed IRS officials and reviewed IRS reports and documents to develop information on IRS' procedures to ensure that appropriate resolution action is taken on accounts prior to expiration of the collection statute of limitations.

We did our work from August 1990 to January 1991 in accordance with generally accepted government auditing standards. Our work was done at IRS' headquarters in Washington, D.C., and the Midwest Regional and Chicago District offices in Chicago. IRS provided written comments on a draft of this report. These comments are incorporated where appropriate and are included in appendix II.

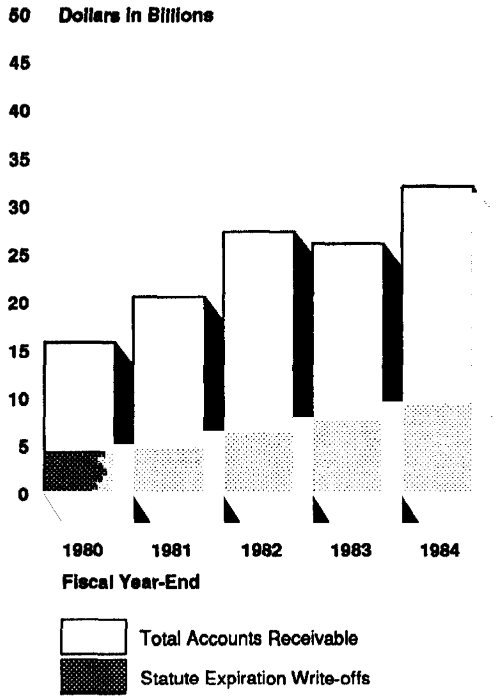
Write-Offs Due to the Expiration of the Collection Statute of Limitations Have Been Significant

We estimate that IRS wrote off over $4.6 billion in individual and business accounts receivable, including accrued interest and penalties, during fiscal year 1990 because the collection statute of limitations had expired. IRS reported that its write-offs for the same time period, however, were $2.5 billion. IRS' reported write-offs are lower than our estimate because IRS includes assessed taxes, interest, and penalties but not accrued interest and penalties. Because additional interest and some penalties accrue after the taxes are assessed, IRS' amount is significantly understated. IRS is developing a report that will show the total amount—assessments plus interest and penalties accrued after assessment—written off in each fiscal year because the collection statute of limitations expired.

During the past 5 years, we estimate that annual write-offs have steadily increased from $2.3 billion to $4.6 billion. This increase in statute expiration write-offs reflects earlier growth in IRS' accounts receivable inventory. IRS' assessed accounts receivable, excluding accrued interest and penalties, increased from $15.8 billion to $31.9 billion between the ends of fiscal years 1980 and 1984. (IRS did not begin reporting accrued interest and penalties until fiscal year 1989.)

While the data cited above reflect the amount of assessed and accrued receivables expiring in a given year, figure 1 shows the portion of a given year's assessed inventory that IRS reported as being written off over the following 6 years as the statutory collection period expired.

Figure 1: Portion of Year-End Assessed Accounts Receivable Balance for Fiscal Years 1980-1984 Written Off During the Following 6 Years



Source: GAO analysis.

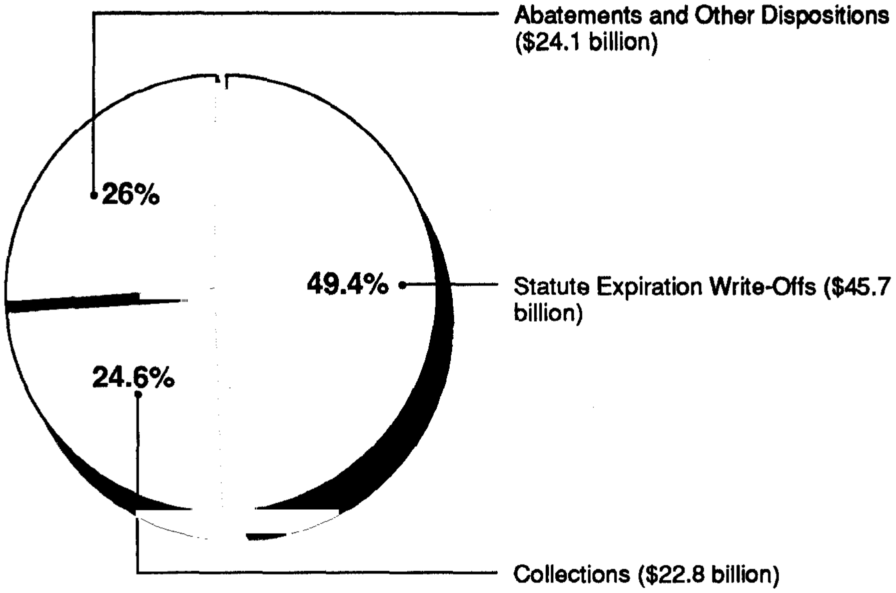
For the fiscal year-end 1980 to 1984 assessed accounts receivable inventories, the percentage of each year's inventory written off over the 6-year period grew from 27 percent for 1980 to 30 percent for 1984.

Because IRS did not calculate accrued interest and penalties on accounts receivable inventory balances at that time, and reliable information on the age of accounts in these inventories was not available, we were not able to estimate the amounts of accrued interest and penalties for those years. However, if accrued interest and penalties were included, the accounts receivable inventory and statute expiration write-offs would both be higher. The proportion of amounts written off would be greater because accruals represented a greater proportion of the total amount owed on older accounts subject to statute expiration write-off than on total accounts receivable. For example, while accruals represented about 26 percent of the amount of individual and business accounts receivable outstanding at the end of fiscal year 1990, they represented about 51 percent of the amount of the receivables that had been outstanding for 5 years or longer.

Almost One Half of IRS' Accounts Receivable Inventory Will Probably Be Written Off Because the Collection Statute Expired

On the basis of our projection of IRS information, about $46 billion, almost one-half of the fiscal year-end 1990 individual and business accounts receivable inventory of $93 billion, could be written off as the 10-year statutory collection period expires, assuming that IRS' collection procedures do not change. As shown in figure 2, the projections indicate that about $24 billion could be abated or otherwise disposed of, and about $23 billion could ultimately be collected.

Figure 2: Projected Disposition of IRS' September 30, 1990, Accounts Receivable



Source: GAO analysis.

Although these estimates reflect what could happen to the 1990 year-end inventory if the reported experience in 1989 is representative, they are not indicative of IRS' overall collection effectiveness. IRS resolves billions of dollars of accounts receivable in the year they are established, and these resolved accounts are not reflected in information that is based on IRS' year-end accounts receivable inventory. IRS is developing information that will help analyze the overall effectiveness of its collection efforts.

Extension of the Statutory Collection Period Provides Additional Collection Potential

The recent statutory extension of the collection period from 6 to 10 years provides IRS with the opportunity to increase collections through continued application of existing collection practices and the development and application of new practices. If collection procedures do not change, the projections show that IRS could collect an additional $1.7 billion from its September 30, 1990, accounts receivable inventory as a result of extending the collection period.[6] Historically, IRS had already suspended active collection efforts on the vast majority of accounts that

[6] In our analyses we estimated the ultimate disposition of IRS' fiscal year-end 1990 accounts receivable under both the 10-year and 6-year statute of limitations. We estimated that collections would increase from about $21.1 billion to about $22.8 billion—8 percent—as the statutory collection period increased.

were written off because the statute of limitations had expired. Prior to expiration, these accounts were subject to passive collection practices and possible reactivation. Additional collections should occur as these collection tools are continued throughout the extended collection period.

We believe that additional amounts may also be collected if IRS improves the effectiveness of its collection efforts through the modification of existing, or the development and application of additional collection tools that can take advantage of the extended collection period. However, because specific information on the validity of accounts written off, the characteristics of taxpayers whose accounts have expired, and the effectiveness of the collection actions applied to those accounts is not currently available,[7] it is unclear how much additional revenue could be realized or what types of modified or additional procedures would be cost-effective.

When we completed our review in January 1991, IRS had not fully evaluated the effects of extending the collection statute of limitations and therefore had not officially estimated additional collections that might occur.

Other Effects of Extending the Statute

Extending the statutory collection period will affect IRS' operations. For example, IRS had to alter computer programs to recognize the 10-year period. To protect the government's interest, IRS will also have to refile existing liens to allow for the extension. According to an IRS Collection Division official, IRS will pay about $35 million to refile the 3.5 million liens outstanding when the statutory collection period was extended.

Increasing the statutory collection period will also increase the size and dollar amount of accounts receivable inventories over the next 4 years because fewer accounts will be written off, and accounts will have an additional 4 years for interest and penalties to accrue. As a result, the number of accounts that must be maintained in IRS' computer files will increase.

[7] IRS' only information on expired accounts is (1) the collection stage the account was in if it was active when it expired or the type of suspension (deferred or CNC, for example) if the account was suspended when it expired and (2) the IRS office responsible for the account when it expired.

IRS Procedures to Manage Active and Suspended Accounts Receivable Prior to Expiration of the Statute of Limitations

IRS procedures for managing active accounts approaching statute expiration are designed to provide managerial oversight to ensure that the collection statute of limitations does not expire on accounts while collection is still being pursued by ACS or field collection employees. IRS' procedures do not require special reviews for suspended accounts that have gone through at least part of IRS' active collection process.

Controls Over Active Accounts

IRS' procedures for ensuring that the statutory collection period does not expire on active accounts rely heavily on managerial reviews of accounts nearing the end of their collection period. According to IRS information, less than 2 percent of the accounts written off during fiscal year 1990 were in active status.

IRS collection managers at ACS call sites receive weekly reports that identify active accounts that will expire within 1 year. While these collection managers are responsible for ensuring that these accounts receive appropriate collection action before they expire, the Internal Revenue Manual states that accounts nearing the end of the collection period should not be worked ahead of higher priority accounts. Thus, under IRS' priority system, some low priority active accounts may be lost because of the expiration of the statutory collection period. During fiscal year 1990, according to IRS information, only $567,000 in active accounts receivable expired in the ACS stage. We did not determine the priority of these accounts.

IRS collection managers in district offices receive monthly reports identifying all accounts assigned to revenue officers that will expire within 14 months. According to the Internal Revenue Manual, collection managers are required to review the accounts and ensure that revenue officers collect, abate, or suspend collection on all accounts prior to the end of the collection period. Revenue officers and collection managers responsible for active accounts that expire may be subject to disciplinary action. IRS procedures state that whenever the collection period for an active account expires there should be a district office investigation to determine whether the revenue officer or collection manager was negligent or if there were systemic problems that allowed the collection period to expire. IRS does not maintain information on the number of revenue officers or collection managers who have been disciplined for allowing the collection statute of limitations to expire.

According to IRS information, during fiscal year 1990 $30.7 million in active accounts assigned to revenue officers expired. We did not review these accounts to determine the appropriateness of IRS' collection efforts prior to expiration.

Controls Over Suspended Accounts

Almost 99 percent of the $2.5 billion written off in fiscal year 1990 were in suspended accounts. About 92 percent of these amounts were classified as CNC. Another 3 percent were low-priority accounts for which collection action had been suspended either after the service center notice stage (deferred accounts) or after ACS processing (queue accounts). Finally, 5 percent were accounts on which collection action had been suspended for a variety of other reasons, such as bankruptcy and litigation. IRS is studying some of the areas involved in the latter category, and thus we did not include them in our review.

During fiscal year 1990, about $2.2 billion in CNC accounts receivable were written off because the collection period expired. At our request, IRS conducted a special analysis of a sample of individual and business accounts that were classified as CNC in 1983 and 1984 and for which the statute of limitations had expired. Most of the individual accounts had been classified as CNC either because IRS had determined that repayment would cause the taxpayer undue financial hardship, or IRS was unable to contact or locate the taxpayer. Most business accounts had been classified as CNC because the business was bankrupt or defunct. In addition, 65 percent of both the individual and business accounts had been classified as CNC more than 4 years before the statute expired.

IRS' primary controls to ensure that all possible collection steps have been followed on CNC accounts consist primarily of (1) requirements for managerial and quality reviews of the initial decisions to suspend the accounts and (2) computerized checks of subsequently obtained information to determine whether the circumstances that caused the suspension have changed. IRS procedures require that collection managers review most employee decisions to classify an account as CNC. In addition, regional teams are to review all CNC accounts over $100,000 and a random sample of smaller dollar accounts to determine the appropriateness of the initial decisions. According to IRS officials, collection managers sometimes reject the initial decision to classify an account as CNC and send the account back to the responsible employee for additional collection action or case documentation. However, no information is maintained on the results of the initial manager's review, and the results of regional reviews are maintained only in the regional offices. IRS' national office does not receive information on the results of either review.

IRS' Midwest Region conducted about 11 percent of the approximately 25,500 regional CNC reviews done nationwide in fiscal year 1990. Available summary information for this region's reviews identified case processing or documentation deficiencies in at least 447 cases and showed that reviewers rejected 126 cases, 5 percent of the total reviewed, and sent them back for additional collection action. The reviews cited, among other things, continuing problems in (1) taking all necessary enforcement actions prior to classifying an account as CNC, (2) properly setting the income thresholds used to systematically monitor accounts for possible reactivation, and (3) using liens to protect the government's interests. According to some IRS national office officials, nationwide information on regional review results would be useful for identifying and correcting systemic problems and developing or modifying training programs.

After an account is classified as CNC, IRS generally makes no further active collection efforts unless previously scheduled manual or annual automated follow-ups reveal changes in the potential collectibility of the accounts. According to IRS information, in fiscal year 1990 CNC accounts worth $1.3 billion were reactivated on the basis of these monitoring activities. IRS does not routinely capture information on the total amount it collects from reactivated accounts. However, a 1990 IRS study, which was based on a sample of accounts classified as CNC in 1983, estimated that 35 percent of the individual taxpayer accounts were subsequently reactivated, and over 52 percent of the reactivated amounts were collected. For business cases, only an estimated 4 percent were reactivated, and 29 percent of these amounts were collected. In addition to the case monitoring discussed above, IRS sends periodic reminder notices to taxpayers whose accounts were classified as CNC because of financial hardship or IRS' inability to contact the taxpayer.

IRS has no procedures for looking at deferred accounts that are nearing the end of their statutory collection period. IRS procedures require reactivation of deferred accounts when additional taxpayer delinquencies increase the liability over the predetermined deferral dollar threshold. The procedures also require that while accounts are in deferred status, taxpayers should be sent annual reminder notices and subjected to future refund offsets. The statutory period expired on about $29 million of deferred accounts in fiscal year 1990, according to IRS information.

During fiscal year 1990, the collection period expired on about $44.7 million of queue accounts, according to IRS information. Although taxpayers' accounts in the queue are to be subjected to future refund offsets, IRS, under its procedures, does not send taxpayers periodic reminder notices. IRS plans to start sending semiannual reminder notices on queue accounts in February 1992.

Conclusions

The amount of money written off of accounts receivable because of the expiration of the statutory collection period has been steadily increasing. With the caveats and limitations discussed earlier, we project that the statute could ultimately expire on about $46 billion of IRS' $93 billion of accounts receivable reported as outstanding at September 30, 1990.

The lack of currently available information on the validity of accounts written off or on the characteristics of the taxpayers whose accounts expire precludes us from estimating how much of these write-offs would be potentially collectible if additional or revised collection measures were instituted. However, projections also indicate that continuation of existing collection practices could result in IRS collecting about $23 billion of the September 30, 1990, inventory—$1.7 billion, or 8 percent more than it would have collected if the statute had not been extended.

Although IRS places significant emphasis on managerial monitoring of active accounts near the end of their collection period to ensure resolution, it does not place similar emphasis on suspended accounts. Reviews of the initial decisions to suspend collection actions and automated monitoring of these accounts for changes are the primary controls IRS uses to ensure that appropriate collection action occurs before the statutory collection period expires. However, we did not do a detailed evaluation of these reviews, IRS' monitoring activities, or the accounts IRS wrote off. As a result, we cannot determine whether IRS' current efforts are adequate with respect to suspended accounts. We did note, however, that IRS' national office does not receive information on the results of regional reviews and is therefore not using all available information, especially the evaluation of the initial decision to classify an account as CNC, for effective systemic oversight of the collection process. We also noted that IRS does not send reminder notices to taxpayers whose accounts are indefinitely suspended in the queue.

Recommendations to the Commissioner of Internal Revenue

We recommend that the Commissioner of Internal Revenue

- develop more specific information on the validity and characteristics of accounts written off to determine whether additional cost-effective collection measures can be developed and applied;
- systematically collect and analyze local review results on the decisions to classify accounts as CNC to help identify potential systemic problems that may need correction; and
- ensure timely completion of IRS' plans to send reminder notices to taxpayers with accounts suspended in the queue to increase collections of these accounts receivable.

IRS Comments and Our Evaluation

IRS reviewed a draft of this report and provided written comments on August 7, 1991 (see app. III). IRS agreed with our recommendations to centrally analyze the results of regional currently not collectible reviews and to periodically send reminder notices to taxpayers with accounts suspended in the queue. However, IRS did not agree with our recommendation to develop more specific information on the validity and characteristics of accounts written off to determine whether additional cost effective measures can be developed and applied.

IRS believed that it had sufficient information on the accounts likely to be written off and that the potential revenue from these accounts was minimal. IRS acknowledged that there are inaccurate assessments in the accounts receivable inventory that will eventually expire and that these invalid assessments should be removed so that IRS can accurately report the amounts due the government. However, IRS stated that it would be more effective to concentrate its efforts on (1) preventing new invalid receivables and (2) identifying and correcting invalid assessments already in the active inventory.

We do not believe IRS has sufficient information on accounts that have been written off due to the expiration of the statutory collection period. As we stated earlier, IRS' information on expired accounts is limited to (1) the collection stage the account was in if it was active when it expired or the type of suspension (deferred or CNC, for example) if the account was suspended when it expired and (2) the IRS office responsible for the account when it expired. This information does not address the source or validity of the expired accounts or the effectiveness of the collection actions IRS applied to the accounts. We believe such information is essential in determining whether modified or additional collection procedures would be cost effective.

The information IRS has on accounts likely to be written off is primarily based upon its inventory of CNC accounts. IRS' information on this inventory is limited to the distribution of CNC accounts by type (hardship or bankrupt taxpayers, for example). IRS stated that it has used this information to develop new programs and procedures. Although IRS may have used this information on the distribution of CNC accounts to help it revise some of its procedures for handling CNC accounts, the information does not address the underlying reasons for noncollection. The underlying reasons, such as lack of validity, characteristics of delinquent taxpayers, or inadequacies in IRS' collection actions must be understood to design cost-effective collection measures to develop.

We agree that IRS should work toward preventing new invalid receivables and identifying and correcting invalid assessments in the active inventory and are not proposing that IRS drop these efforts to develop information on the validity and collectibility of accounts that are lost due to the expiration of the statutory collection period. However, because almost one-half of the September 30, 1990, inventory—$45.7 billion—is expected to be lost due to expiration of the statutory collection period over the next 10 years, we do not think this segment of the inventory can be ignored. In fact, we believe that information developed on the validity of accounts written off would also be useful in IRS' efforts to eliminate the invalid accounts still in the accounts receivable inventory. For instance, IRS could use this information to identify programs or conditions that lead to invalid accounts receivable.

Further, we do not believe IRS has developed the information necessary to estimate potential revenue from CNC accounts. Although IRS believes this amount is small, it could not provide us with any data or analyses to substantiate that belief.

Our specific responses to IRS' comments are contained in appendix II of this report.

As arranged with the Subcommittee, we are sending copies of this report to the Commissioner of Internal Revenue and other interested parties. We will make copies available to others upon request.

Major contributors to this report are listed in appendix III. If you have any questions about this report, please call me on (202) 272-7904.

Sincerely yours,

Paul L. Posner

Paul L. Posner
Associate Director, Tax Policy and
Administration Issues

Contents

Abbreviations

ACS	Automated Collection System
CNC	currently not collectible
IRS	Internal Revenue Service
TDA	Taxpayer Delinquent Account

Methodology for Estimating Accounts Receivable Dispositions, Statute Expirations, and the Impact of Extending the Statute of Limitations

We developed a model to estimate the (1) future disposition of IRS' September 30, 1990, individual and business master file accounts receivable balances and (2) potential impact of extending the statutory collection period. We constructed the model using age-based account disposition information from IRS' accounts receivable management information system. The individual and business master file accounts contained in this system totaled $92.6 billion and represented over 96 percent of the $96.3 billion accounts receivable balance at the end of fiscal year 1990. The system does not contain information on the $3.7 billion of accounts receivable that are not maintained on these master files, and therefore our methodology understates IRS' estimated total future collections, abatements, and statute expiration write-offs.

Accounts Receivable Disposition Information

IRS' accounts receivable management information system, which began operation in fiscal year 1989, reports the annual disposition of the year-end's individual and business master file accounts receivable balances. The disposition information is reported in detail by age of the accounts at the beginning of the year. Using this information, we calculated the fiscal year 1990 accounts receivable disposition (collection, abatement, statute expiration, and other) rates by age of account for individual and business accounts that were outstanding at the end of fiscal year 1989. We calculated these rates for seven age groups of accounts—ranging from those that were less than 1 year old at the end of fiscal year 1989 to those that were more than 6 years old at the end of the fiscal year.

IRS' accounts receivable management information system follows accounts over the statutory collection period that was in effect at the time the system was designed—6 years. Because the statute was only recently extended to 10 years, information was not available that would allow the direct calculation of detailed age-based disposition rates for accounts more than 6 years old. To impute disposition rates for the additional 4 years, we performed separate regression and other analyses for each of the individual disposition components—collections, statute expirations, and abatements and other dispositions. We used the age-based disposition component rates that we calculated from the accounts receivable management information system to develop the regression equations. In all cases where we used the regression analyses, the proportion of total variation explained by our regression equations ranged from 81 to 99 percent. In one case we used a weighted average constant value because we believe it provided a better estimate. We used a summation of the actual and/or imputed component disposition rates to calculate the total disposition rate for each age category. Although these analyses were based on the limited accounts receivable disposition data available in IRS' management information system, the results provided a reasonable basis for our estimates of disposition results that would occur during the additional 4 years.

Methodological Assumptions

In developing and applying our estimation methodology, we made a number of assumptions. These assumptions relate to the use of the age of accounts receivable as an indicator of future disposition results, the stability of collection results over time, and the relationship between dispositions of assessed account balances and the interest and penalties that have accrued on these balances since assessment.

Age of Accounts Considered the Most Significant Indicator of How Accounts Are Resolved

We assumed that the age of accounts receivable is the most significant indicator of how the accounts will be resolved. IRS' accounts receivable management information system allows analysis of account dispositions by age and/or collection status (i.e., notice, CNC, TDA) of accounts at the beginning of the initial year. While the age of unresolved accounts is readily determinable at the beginning of each subsequent year, the system did not contain information that would allow us to accurately estimate the subsequent collection status of accounts as they moved through the collection cycle. Thus, a combined age and collection status analysis, which we believe would provide more precise estimates, was not feasible at the time but might become feasible as IRS collects more information over time.

Analysis of the detailed disposition rates shows that the age of accounts receivable is significantly related to the amount and type of annual disposition activity that takes place. For example, collection rates on accounts owed by individuals decreased from 34.2 percent of the outstanding balance for accounts less than 1 year old to an estimated 1.5 percent of the remaining balance for accounts that would be over 10 years old at the beginning of the year. Statute expiration rates—the percent of each age category's balance that is written off because of the expiration of the statute of limitations—start out at an extremely low level and increase significantly as accounts reach the end of the statutory collection period.

Collection Results Assumed to Be Stable

The model assumes that there will be no significant changes in the level or success of IRS collection efforts in the future. For example, we assume that IRS will continue to collect 4.4 percent of individuals' accounts receivable balances when they are in their fifth year of existence. This assumption is necessary to provide a baseline for estimated future disposition activity. Although changes in collection policies, procedures, practices, applicable legislation, or economic conditions may occur over the next 10 years, it was not possible to forecast the changes or their impacts on the disposition of accounts receivable at the time of our review.

We tested this assumption for 1 year by comparing our total estimated fiscal year 1990 dispositions of fiscal year-end 1989 assessed accounts receivable with the actual fiscal year 1990 dispositions of these accounts. Our total estimated dispositions of these balances were within 1 percent of the total IRS recorded dispositions for both individual and business accounts.

Resolution of Accrued Interest and Penalties

IRS' accounts receivable management information system does not report specific information on the dispositions of accrued interest and penalties information. Thus, the model assumes that reduction of accrued interest and penalties from accounts receivable balances when abatements or other write-offs take place is proportional to the reduction of the assessed balance. This assumption allowed us to estimate dispositions on the basis of the September 30, 1990, accounts receivable balances that include both assessed and accrued amounts. We made this assumption to recognize the difference in the way IRS records accrued interest and penalties resolved through payment versus those resolved through abatement and write-off. IRS records the collection of accrued interest and penalties, to the extent paid, at the time of payment. However, for accounts abated or written off IRS did not record the disposition of the related interest and penalty accruals.

Estimated Activity of Accounts Receivable

We applied the age-based fiscal year 1990 accounts receivable total disposition rates to fiscal year-end 1990 accounts receivable balances by age group to estimate the total disposition of accounts receivable that would take place in each age category over both the 10-year and 6-year collection periods and the residual unresolved balance that would remain. This process was carried over the stated collection period plus an additional year. We added the extra year to our analysis period because IRS' accounting system, the basis for the management information system, does not recognize expiration of the statute of limitations on some accounts until the subsequent fiscal year. The residual unresolved balance that remained after this process reflects accounts on which the statute of limitations would have been extended. Our methodology estimated the ultimate disposition of all such extended accounts so that total dispositions would equal total accounts receivable as of September 30, 1990.

Our estimates of specific disposition components were computed similarly. We applied specific component disposition rates to the total unresolved balance in each age category—beginning balance in an age category plus the residual balance from the preceding age category—to estimate the amount of each disposition component. Table I.1 shows how we used the actual and imputed age category collection rates to estimate total collections from individual and business accounts over the 10-year collection period. The percentage in the residual balance column represents the proportion of the final year collection rate to the final year total disposition rate.

Table I.1: GAO's Estimates of Collections From IRS' September 30, 1990, Accounts Receivable (Dollars in Millions)

	Individual Master File			
	Less than 1 year	**1-2 years**	**2-3 years**	**3-4 years**
Balance in age category	$14,022	$8,252	$6,428	$5,313
Prior year residual balance		7,869	12,858	16,446
Total in age category	$14,022	$16,121	$19,285	$21,758
Collection percentage	34.17%	12.93%	7.73%	5.49%
Net collections	$4,791	$2,084	$1,491	$1,194
	Business Master File			
	Less than 1 year	**1-2 years**	**2-3 years**	**3-4 years**
Balance in age category	$15,153	$5,662	$5,589	$4,725
Prior year residual balance		5,870	8,906	13,001
Total in age category	$15,153	$11,532	$14,496	$17,726
Collection percentage	29.08%	9.69%	3.61%	2.86%
Net collections	$4,407	$1,118	$524	$508

[a]The beginning balance in the 6-7 year old age category includes all accounts over 6 years old. IRS' information system did not provide more detailed information on the actual age of these accounts.

[b]Totals may not add due to rounding.

Source: GAO analysis.

Individual Master File								
4-5 years	**5-6 years**	**6-7 years[a]**	**7-8 years**	**8-9 years**	**9-10 years**	**Over 10 years**	**Residual**	**Total[b]**
$4,716	$3,840	$4,524						**$47,094**
19,465	21,616	23,530	$26,002	$24,320	$22,837	$11,976	$8,581	
$24,181	$25,457	$28,055	$26,002	$24,320	$22,837	$11,976	$8,581	
4.40%	2.94%	3.00%	2.24%	1.93%	1.68%	1.49%	5.26%	
$1,065	$748	$842	$581	$468	$385	$179	$451	**$14,279**
Business Master File								
4-5 years	**5-6 years**	**6-7 years[a]**	**7-8 years**	**8-9 years**	**9-10 years**	**Over 10 years**	**Residual**	**Total[b]**
$4,255	$4,085	$6,087						**$45,556**
16,451	19,853	23,323	$28,393	$27,786	$27,291	$23,301	$12,614	
$20,706	$23,938	$29,410	$28,393	$27,786	$27,291	$23,301	$12,614	
2.20%	1.25%	1.23%	0.89%	0.73%	0.61%	0.52%	1.14%	
$455	$299	$363	$252	$203	$167	$122	$144	**$8,560**

Table I.2 shows how we estimated future individual and business statute expiration write-offs by applying the actual and imputed age-based statute expiration rates to the unresolved balance in each age category. The percentage in the residual balance column represents the proportion of the final year statute expiration rate to the final year total disposition rate. Statute expirations are shown in all age categories primarily because IRS' accounts receivable management information system assigns age categories on the basis of the age of the most recent assessment in the account. Earlier assessments will generally expire 10 years from the date of their assessment and will be removed from the account at that time, thus showing up in age categories of less than 10 years.

Table I.2: GAO's Estimates of Statute Expiration Write-Offs From IRS' September 30, 1990, Accounts Receivable (Dollars in Millions)

	Individual Master File		
	Less than 1 year	1-2 years	2-3 years
Balance in age category	$14,022	$8,252	$6,428
Prior year residual balance		7,869	12,858
Total in age category	$14,022	$16,121	$19,285
Statute expiration percentage	0.09%	0.11%	0.13%
Net statute expirations	$13	$17	$25
	Business Master File		
	Less than 1 year	**1-2 years**	**2-3 years**
Balance in age category	$15,153	$5,662	$5,589
Prior year residual balance		5,870	8,906
Total in age category	$15,153	$11,532	$14,496
Statute expiration percentage	0.03%	0.13%	0.13%
Net statute expirations	$5	$15	$19

[a]The beginning balance in the 6-7 year old age category includes all accounts over 6 years old. IRS' information system did not provide more detailed information on the actual age of these accounts.

[b]Totals may not add due to rounding.

Source: GAO analysis.

Individual Master File

4-5 years	5-6 years	6-7 years[a]	7-8 years	8-9 years	9-10 years	Over 10 years	Residual	Total[b]
$4,716	$3,840	$4,524						**$47,094**
19,465	21,616	23,530	$26,002	$24,320	$22,837	$11,976	$8,581	
$24,181	$25,457	$28,055	$26,002	$24,320	$22,837	$11,976	$8,581	
1.63%	0.30%	0.34%	0.38%	0.41%	42.18%	20.60%	72.66%	
$395	$76	$95	$98	$100	$9,633	$2,467	$6,235	**$19,190**

Business Master File

4-5 years	5-6 years	6-7 years[a]	7-8 years	8-9 years	9-10 years	Over 10 years	Residual	Total[b]
$4,255	$4,085	$6,087						**$45,556**
16,451	19,853	23,323	$28,393	$27,786	$27,291	$23,301	$12,614	
$20,706	$23,938	$29,410	$28,393	$27,786	$27,291	$23,301	$12,614	
0.13%	0.13%	0.13%	0.13%	0.13%	13.24%	44.68%	97.43%	
$27	$31	$39	$37	$36	$3,612	$10,412	$12,290	**$26,548**

Comments From the Internal Revenue Service

Note: GAO comments supplementing those in the report text appear at the end of this appendix.

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

COMMISSIONER

AUG 07 1991

Mr. Paul Posner
Associate Director, Tax Policy
and Administration Issues
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Posner:

We have reviewed your draft report to Chairman Pickle, Subcommittee on Oversight, House Ways and Means Committee on IRS accounts receivable written off because of expiration of the collection statute.

We agree with the two recommendations in the draft report dealing with a centralized review of Currently-Not-Collectible (CNC) decisions and sending reminder notices on cases assigned to the Collection Queue. New procedures to send reminder notices will be operational in February, 1992.

Current management information and recent special studies provide us with significant and useful information about accounts that are likely to be written off. We are using this information to develop new programs and procedures. For example, we already have detailed information about accounts in CNC status which comprise over 90 percent of the accounts on which the statute expires. Using that information, we have revised our procedures for following up on suspended accounts to ensure that we reactivate those accounts with the greatest collection potential. We do not agree with the recommendation to develop more information about the validity of these accounts at this time.

We agree with GAO that there are inaccurate assessments in the inventory which will eventually expire and that those invalid assessments should be removed so that we can accurately report on the amount of taxes owed the government. At this time, however, we are concentrating our efforts on preventing invalid assessments as well as identifying them in the current inventory. Efforts to clean up the current inventory by identifying and correcting invalid assessments will result in a more accurate description of the amounts owed in all categories, including suspended accounts.

Based on our management information, we believe that potential revenue from uncollectible accounts is small. For the most part, only those accounts that were classified as uncollectible because we were unable to locate or contact the taxpayer have any potential revenue. Our efforts to reduce the number of these cases are detailed in the enclosure.

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Mr. Paul Posner

Our Collection procedures are designed to ensure that every cost-effective action is taken before we suspend active collection. But we do not completely write the case off at this point. Passive collection efforts on suspended accounts result in additional collections. In addition, we reactivate over 30 percent of individual accounts as taxpayers' income changes or we identify available assets. Our priorities, however, are to remove invalid assessments from the inventory increasing collections from current accounts, before they get too old and difficult to collect. Our studies indicate that timely collection action is a critical factor in collecting amounts owed.

Detailed comments about the recommendations and general comments about the report text are enclosed.

Best regards.

Sincerely,

Fred T. Goldberg, Jr.

Enclosure

IRS COMMENTS ON RECOMMENDATIONS
CONTAINED IN DRAFT GAO LETTER ON
CONTROLS OVER ACCOUNTS RECEIVABLE
(STATUTE EXPIRATION CASES)

RECOMMENDATION:

We recommend that the Commissioner of Internal Revenue:

-- **Develop more specific information on the validity and characteristics of accounts written off to determine whether additional cost effective collection measures can be developed and applied;**

Programs to perfect the validity of our accounts receivable inventory as well as research aimed at evaluating taxpayers and programs are ongoing. As a result we are making major strides in perfecting the validity of the accounts receivable inventory. A major undertaking has been factoring out the effect of multiple assessments resulting from use of the 100 percent penalty. Also, we are changing our criteria for determining ability to pay based on total positive income rather than adjusted gross income.

We currently have a substantial amount of management information about Currently-Not-Collectible accounts, which comprise 90% of the accounts for which the statute expires without collection. Current management information is also used in our Resource Workload Management System (RWMS) to prioritize cases based on ability to pay. While RWMS has been successful in focusing our resources on the most productive cases, we are reviewing it to determine if improvements can be made. Special studies are also conducted to gather in-depth information about segments of the accounts receivable inventory.

-- **systemically collect and analyze local review results on the decisions to classify accounts as currently not collectible to help identify potential systemic problems that may need correction;**

See comment 1.

We agree to analyze Currently-Not-Collectible post review findings at the national level. The Collection Quality Measurement System (CQMS) will review specific "vital few" critical actions prior to placing a case in suspense status as Currently-Not-Collectible. Data gathering for this measurement system began in June, 1991. Results will be available at the district, region and national levels.

This analysis will supplement other actions we have taken to identify systemic problems. For example, local post review results are analyzed in each region. National Office ensures the success of this program via regional reviews. In addition, regional offices can use Form 5391, Systems Change Request, to surface problem areas to National Office. A yearly analysis of

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the NO-5000-149 report, Recap of Accounts Currently not Collectible, further assures problem areas will be identified.

-- **ensure timely completion of IRS' plans to send reminder notices to taxpayers with accounts suspended in the queue to increase collections of these accounts receivable.**

We appreciate your support of this initiative which is on schedule. Commencing February 1992, semiannual reminder notices will be sent on accounts assigned to the queue.

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GENERAL COMMENTS

Pages 4 and 18 - "Because little is known about the validity of accounts written off or the characteristics of the taxpayers whose accounts expire, neither we nor IRS is in a position to estimate how much of these write-offs would be potentially collectible if additional or revised collection measures were instituted."

Comment: IRS is making major strides in improving the validity of its accounts receivable inventory. For instance, a major component of duplicate accounts is 100 percent penalty assessments. We recently modified our crediting system to allow for cross credits when dual 100 percent penalty assessments have been made. By February 1992, we will be able to partially abate the underlying corporate assessment to reflect trust fund amounts paid by any of the responsible persons.

A great deal is known about the characteristics of taxpayers placed in Currently-Not-Collectible status and this information is used to continually refine our programs. For instance, the income criterion on which we base the decision to reactivate CNC accounts was changed from adjusted gross income to taxpayer positive income. This new formula recognizes certain losses to better define ability to pay. Our Resource Workload Management System (RWMS), which profiles each taxpayer account and assigns a score based on projected ability to pay, is currently the subject of extensive review as we attempt to validate and refine the system. We also conduct special studies such as the 1990 Collection Research File Analysis Report and the nationally supported Currently Not Collectible (CNC) Task Force which provide us with more information about suspended accounts.

See comment 2.

The last part of the sentence states "...neither we nor IRS is in a position to estimate how much of these write-offs would be potentially collectible if additional or revised collection measures were instituted." We disagree. While a precise estimate may be difficult to determine, available information indicates that the amount is not likely to be significant.

An analysis of the Collection Activity Report NC-5000-149, titled "Recap of Accounts Currently not Collectible Report", for CNC accounts posted during FY 1990 reveals that only two categories of cases (Unable to Locate and Unable to Contact) hold any promise of increases in revenues. These two categories comprise only 17.5% of the amount reported as uncollectible. (All categories shown below)

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Category	Portion of Dollars reported CNC
Unable to Locate	12.0%
Statute or Suit	.4%
Bankrupt	9.8%
Decedent	2.6%
Tolerance	<.1%
Defunct Corp	26.0%
Unable to Contact	5.5%
In Business	.6%
Hardship	43.0%

The largest category of dollars reported CNC is hardship. All avenues of payment are explored before we make a determination of hardship. Generally, taxpayers in this category have insufficient income or assets to meet their tax obligations.

The next largest category is defunct corporation. In these cases, investigation has determined that there are no assets or there is insufficient equity in remaining assets to justify taking enforcement action.

In the Unable to Locate and Unable to Contact cases, we are directing our efforts to improving access to all sources of information that could help us locate the taxpayer. We are developing the use of universal computerized locator services early in the collection process. For instance, Corporate Files On Line is a major Tax Systems Modernization project that will make Master File and information return data available to field personnel instantly. Coupled with expansion of ACS hours to contact taxpayers, these initiatives should result in earlier taxpayer contact and fewer cases being suspended.

See comment 3.

Page 4 - GAO estimates that IRS will collect an additional $1.7 billion from the September 30, 1990 inventory as a result of statute extension.

Comment: This figure is misleading since the computation does not factor costs of collection such as the costs of lien refiling noted on page 16.

See comment 4.
Now on p. 4

Page 5 - "While IRS requires local reviews of decisions to suspend collection activities, it does not centrally analyze the local results to identify systemic problems."

Comment: It's important to note that cases returned for additional investigation as a result of post-reviews are a small fraction of those processed, less than 5 percent. Current and planned efforts to use post-review information are detailed above.

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See comment 5
Now on p. 5
and 14

Pages 7 and 24-25 While discussing accounts in suspended status, the report comments, "Generally, no further active collection efforts occur unless the account is reactivated."

Comment: The report fails to note the scope of our monitoring and follow-up procedures. Thirty-two percent of IMF accounts reported uncollectible are reactivated as the result of monitoring actions that indicate a possible improvement of collection potential. These activities include screening incoming tax returns for changes of address or increases in Taxpayer Positive Income. In addition, information returns (Forms W-2, 1099) are reviewed for new information. Most states participate with IRS in a state refund offset program which affects suspended and active accounts. Reminder notices are sent to taxpayers in currently not collectible status that were closed due to hardship or inability to contact as well as all deferred accounts.

See comment 6
Now on p. 6

Page 9 The description of the period to collect a judgment is inaccurate. Administrative action to collect on the judgment can be taken during the life of the judgment. Judgments last twenty years against real property and can be renewed for twenty years; there is no limit against personal property.

See comment 7
Now on p. 8 and 9

Pages 13 and 14 - The graph and written explanation of Figure 1 need clarification. It appears accrued interest has been added to the statute expired amounts, but not to the total accounts receivable inventory to which the write offs were compared.

See comment 8
Now on p. 11

Page 15 - "We believe that additional amounts may also be collected if IRS improves the effectiveness of its collection efforts through the development and application of additional collection tools that take advantage of the extended collection period."

Comment: As we noted, the amount of revenue available from suspended accounts is quite low. We would agree, however, that collections should increase, and fewer cases would expire if we continue our ongoing efforts to improve the quality of our collection operation. We would be happy to explore any specific suggestions.

Page 20 - "Under IRS' priority system, some low priority active accounts [in ACS] may be lost due to the expiration of the statutory collection period."

Comment: This is correct. However, an analysis of statute expirations in ACS confirms the accuracy of our prioritizing system. Although the number of ACS modules that expired in FY 1990 remained unchanged, dollars lost dropped 21%. During the year, the average dollar value per module expired fell 20%.

The following are GAO's comments on the Internal Revenue Service's letter dated August 7, 1991.

GAO Comments

1. IRS agreed to analyze currently not collectible post review findings at the national level and stated that such an analysis will supplement other actions it has taken to identify systemic problems. We are currently conducting a detailed review of IRS' internal controls over determinations to place accounts in suspended status. In this review, we are evaluating the adequacy and effectiveness of IRS' actions discussed in its response and its oversight of accounts placed in currently not collectible status.

2. IRS stated that (1) available information indicates that the amount of write-offs due to statute expiration that would be potentially collectible if additional or revised collection measures were instituted is not likely to be significant and (2) only two categories of CNC cases (Unable to Locate and Unable to Contact) hold any promise of increases in revenue. We do not believe that IRS has developed sufficient information to make such a conclusion. In fact, IRS' Currently Not Collectible Study Group Report issued in February 1991 discusses in detail IRS' lack of information on the validity and collectibility of all types of CNC accounts.

3. IRS stated that our $1.7 billion estimate of additional collections due to extension of the statute of limitations is misleading because it does not take into account additional costs of collection. At the time we did our review, IRS had only identified the additional $35 million cost due to lien refiling, about 2 percent of the estimated additional revenue. While both we and IRS have recognized that additional costs would probably be incurred as a result of the statute extension, IRS has provided no additional cost estimates.

4. IRS pointed out that less than 5 percent of currently not collectible cases subject to post review were returned for additional investigation. While we agree that only about 5 percent of the cases reviewed in one region were returned for additional investigation, as stated in the report, we found that the region's reviewers identified problems in about 15 percent of the cases reviewed. Although only cases for which reviewers feel additional action may lead to subsequent revenue collection are sent back to revenue officers, reviewers identify all errors found in the work conducted to collect the delinquent tax. In addition, it is important to note that most of the cases that were returned for additional investigation or that had errors identified were larger dollar cases- those over IRS' mandatory review threshold of $100,000.

5. IRS pointed out that we fail to note the full scope of IRS' follow-up and monitoring of suspended cases. Our discussion of IRS' follow-up and monitoring activities was not intended to be an exhaustive description of IRS' efforts. Rather, it was intended to identify what we felt were the primary controls and monitoring activities. We are currently conducting a detailed review of the adequacy and effectiveness of these activities. In addition, we have modified the report to recognize IRS' periodic reminder notices to certain taxpayers whose delinquent accounts are placed in currently not collectible status.

6. IRS pointed out the specific limits applicable to collection of federal court judgments. We have modified the report to explicitly state these limitations.

7. IRS stated that both figure 1 and its explanation were unclear. We have clarified the figure and its explanation.

8. IRS agreed that collections would increase and fewer accounts would expire if it continued its efforts to improve the quality of its collection operation and indicated it would be happy to explore specific suggestions. We expect that our ongoing reviews of the Resource and Workload Management System, IRS' management of its suspended accounts inventory, and other planned reviews will result in additional recommendations to improve the effectiveness of IRS' collection operation.

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