United States General Accounting Office

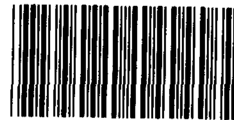
GAO

Report to Designated Congressional Committees

May 1992

TAX POLICY AND ADMINISTRATION

1991 Annual Report on GAO's Tax-Related Work



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

General Government Division

B-242620

May 21, 1992

The Honorable Dan Rostenkowski
Chairman, Committee on
Ways and Means
House of Representatives

The Honorable Lloyd Bentsen
Chairman, Committee on
Finance
U.S. Senate

The Honorable Lloyd Bentsen
Chairman, Joint Committee on
Taxation
Congress of the United States

The Honorable John Conyers, Jr.
Chairman, Committee on
Government Operations
House of Representatives

The Honorable John Glenn
Chairman, Committee on
Governmental Affairs
United States Senate

This report is submitted in compliance with 31 U.S.C. 719(d) and summarizes our work on tax policy and administration during fiscal year 1991. It contains appendixes that include information on actions taken on our recommendations as of December 31, 1991, recommendations we made to Congress before fiscal year 1991 that remain open, and assignments for which we were authorized access to tax information under 26 U.S.C. 6103(i)(7)(A)(i).

Key Recommendations for Tax Policy and Administration

In recommendations to Congress and the administration, we suggested actions that could be taken to improve compliance, increase accounts receivable collections, simplify the tax system, improve the Tax Systems Modernization Program, strengthen management practices, and enhance the effectiveness of tax incentives.

Improve Compliance With Tax Laws

Compliance with the tax laws remains a serious problem that results in billions of dollars in lost revenues. The Internal Revenue Service (IRS) estimated that the annual tax gap—the difference between taxes owed and taxes voluntarily paid—would reach over $113 billion in 1992 and about one-quarter of that amount would ultimately be collected. Corporate compliance has declined to an alarming degree. IRS data made available in 1991 showed that small corporations, which make up about 80 percent of all corporations, voluntarily paid about 61 percent of taxes they owed in 1987 compared to 81 percent in 1980—a 25-percent decrease. We identified several legislative and administrative actions that could help improve compliance.

- **Business Information Returns Program.** Matching information returns to individual tax returns has proven to be a cost-effective way to increase collections and boost voluntary compliance by individuals. We recommended a similar matching program for corporations. Matching information returns on just five types of corporate income—interest, dividends, rents, royalties, and capital gains—could generate about $1 billion in additional revenue annually. We recognized that corporate taxpayers and payors submitting information returns would experience some additional burden and might have to change their accounting records and other information systems. These problems could be mitigated by a phased implementation of the program (GAO/GGD-91-118, Sept. 27, 1991). (See p. 47.)
- **Seller-Financed Mortgages.** When the seller finances all or part of the buyer's purchase of property, IRS requires the seller to report the interest received and the buyer's name. The buyer is required to report the seller's name and address. IRS does not have authority to require buyers to provide sellers' Social Security numbers. As much as $200 million in 1989 taxes may not have been paid because improper amounts of seller-financed mortgage interest income and deductions were reported. If buyers were required to report sellers' Social Security numbers, we believe that most of the taxes would be paid because of increased voluntary compliance. We recommended that Congress enact legislation to require such reporting (GAO/GGD-91-38, Mar. 29, 1991). (See p. 39.)
- **High-Income Nonfilers.** IRS identifies potential nonfilers when a tax return cannot be located for income reported on information returns. IRS assigns cases a priority—based on estimated tax collections—that determines the degree of IRS scrutiny. We estimated that half the high-income nonfilers—those whose incomes exceeded $100,000—were not assessed a tax in earlier stages and were not pursued by revenue officers because IRS underestimated potential collections from such cases.

On the basis of our recommendations, IRS changed its procedures to more effectively investigate high-income nonfilers (GAO/GGD-91-36, Mar. 13, 1991). (See p. 35.)

The tax gap for large corporate taxpayers has also been a concern. IRS programs to audit large corporations may not be as effective as they should in promoting voluntary compliance. According to IRS data, large corporations were appealing 80 percent of the taxes IRS examiners recommended and were winning 75 percent of the amounts appealed. We are considering these issues in a review of IRS' large corporation examination program. We are also reviewing compliance levels by payors in filing information returns for payments to independent contractors as well as ways to increase compliance levels.

Increase Accounts Receivable Collections

We have identified the continuing high level of tax debt—$107 billion at the end of fiscal year 1991—as one of 16 federal programs particularly vulnerable to mismanagement, fraud, abuse, and major losses of funds due to poor internal controls and financial management systems. We suggested several ways to increase collection of IRS accounts receivable.

- **Debts Written Off.** Over the past 5 years, IRS had to continually write off higher amounts of tax debts because the statute of limitations had expired. Write-offs, including interest and penalties, of $2.3 billion in 1986 had increased to $4.6 billion in 1990. Following our August 1990 testimony on the growth in accounts receivable, Congress extended the statute of limitations from 6 to 10 years to allow IRS more time to collect these debts. Using the new 10-year period, we estimated that of $93 billion owed by businesses and individual taxpayers as of September 30, 1990, about $46 billion would eventually be written off if IRS made no changes to its collection practices. Of the remaining amount, we estimated IRS would collect $23 billion and abate or otherwise resolve $24 billion. We recommended that IRS develop more specific information on accounts written off, systematically analyze local decisions to classify accounts uncollectible, and follow through on plans to send certain taxpayers reminder notices (GAO/GGD-91-89, Sept. 30, 1991). (See p. 63.)
- **Employment Tax Delinquencies.** At the end of fiscal year 1990, delinquent employment taxes totaled nearly $30 billion, or 31 percent of the accounts receivable balance. These taxes included unemployment taxes, employees' Social Security taxes, and employees' income taxes withheld by employers. IRS efforts to prevent, identify, and collect delinquent employment taxes were fragmented. IRS had not developed all

the information necessary to target efforts on likely delinquent employers or evaluate the effectiveness of its employment tax delinquency programs. We recommended that IRS develop a comprehensive plan to prevent, identify, and collect employment tax delinquencies. We suggested designation of an official to oversee the plan, and we identified certain management information that should be developed (GAO/GGD-91-94, Aug. 28, 1991). (See p. 58.)

We are continuing to focus on ways to increase collections of accounts receivable. We expect to report on innovative collection approaches, pioneered by states and other federal agencies, that IRS could adopt. We are also reviewing IRS methods to allocate collection cases among its staff, and we are looking at IRS management of inactive accounts.

Simplify the Tax System

Simplification is a key to controlling taxpayer burden and maintaining high levels of voluntary compliance. We identified some changes that would improve compliance and tax administration.

- **Tax Treatment of Intangible Assets.** A continuing controversy between taxpayers and IRS is the extent to which taxpayers can deduct the costs of purchased intangible assets, such as customer or subscription lists. Reported values of intangible assets grew from about $45 billion to $262 billion between 1980 and 1987. At issue in the cases reviewed were 175 types of intangible assets valued at over $23 billion by the taxpayer with IRS proposed adjustments of over $8 billion. In general, an intangible asset may be amortized over its useful life. But purchased goodwill and intangible assets with lives that cannot be determined are not amortizable. Upon audit, IRS frequently contends that intangible assets amortized by a taxpayer are in fact purchased goodwill. To reduce the controversy, we suggested that Congress consider specifying statutory cost recovery periods for amortization of purchased intangible assets, including goodwill. The Chairman of the House Committee on Ways and Means has introduced legislation that would require most intangible assets, including goodwill, to be amortized over 14 years (GAO/GGD-91-88, Aug. 9, 1991). (See p. 116.)
- **Earned Income Credit Schedule.** Responding to 1991 changes in the earned income tax credit, IRS decided to require taxpayers to file a separate schedule to receive the credit. Despite IRS' special efforts to test the clarity of the form and instructions, we believe the form is too complex and will confuse some taxpayers. For most eligible taxpayers, information currently on the tax return is sufficient for IRS to determine their eligibility

for the basic credit and two of three supplemental credits without the additional schedule. Following our testimony, IRS decided to revert to its previous processing rules and calculate the credit for as many taxpayers as possible using information reported on the return (GAO/T-GGD-91-68, Sept. 9, 1991). (See p. 118.)

- **Payroll Tax Deposit Rules**. Payroll tax deposit rules are complex and make it difficult for employers to predict when to make their deposits. About one-third of the nation's employers were being penalized annually because they did not comply with the complex rules. Two bills were under consideration that would simplify the rules by requiring employers to deposit payroll taxes on the Tuesday or Friday following their paydays. GAO testified that changes to the deposit rules were urgently needed and that both bills would make it easier for employers to comply with the rules (GAO/T-GGD-91-65, Sept. 12, 1991). (See p. 114.)

We are studying other areas that offer the potential for simplification. As required by the Omnibus Budget Reconciliation Act of 1990, we are studying how the advance payment system of the earned income tax credit could be implemented to lessen administrative complexity. We also expect to report soon on problems IRS had with applying transfer pricing rules to U.S. subsidiaries of foreign corporations.

Improve the Tax Systems Modernization Program

By replacing IRS' antiquated computer systems with new technology, Tax Systems Modernization (TSM) will fundamentally change almost all of IRS' business functions. As such, TSM is critical to the long-term improvement of tax administration. We continued monitoring TSM progress in 1991 and identified several key issues.

- **TSM Progress**. We reviewed the TSM draft Design Master Plan and concluded that the plan was a useful, high-level guide for developing and implementing TSM. We said, however, that a number of issues vital to TSM's success, such as fixing accountability for modernization, managing technology risks, and protecting taxpayer privacy, were not included in the plan (GAO/IMTEC-91-53BR, June 25, 1991). In later testimony, we discussed how the modernization offered opportunities for IRS to reorganize the way it does business, including how it is organized to process returns and deal with taxpayers (GAO/T/GGD-91-54, July 9, 1991). (See pp. 20 and 83.)

At the request of several congressional committees, we are continuing to monitor IRS' modernization program. We are also assessing the extent to

which the TSM design can be adapted to organizational and program changes resulting from revisions in IRS' business processes.

Strengthen Management Practices

We suggested several actions IRS and the Bureau of Alcohol, Tobacco and Firearms (BATF) could take to strengthen agency management.

- **General Management**. We reported on actions IRS had taken to implement recommendations made in our 1988 general management review. We said that IRS had developed an agencywide strategic planning process and had established the important leadership positions of Chief Financial Officer and Chief Information Officer. But, we also said that IRS was years away from developing the human resources management plan we had recommended in 1988. Because human resource planning is critical as IRS implements TSM, we recommended that IRS bring a greater sense of urgency to that effort (GAO/GGD-91-74, Apr. 29, 1991). (See p. 73.)
- **Integrity and Ethics**. Our survey of IRS employees showed that almost 67 percent believed that the level of integrity in IRS was high or very high; 40 percent believed that at least some upper-level managers engaged in various forms of misconduct; and although 76 percent said they would be generally willing to report misconduct, only 23 percent strongly believed IRS would protect them from retaliation for reporting. We recommended that IRS improve the perception that its employee sanctions were fair by publicizing summary information about disciplinary actions taken, periodically reviewing disciplinary actions for equity, and maintaining National Office oversight while processing all Inspector General findings (GAO/T-GGD-91-58, July 24, 1991 and GAO/GGD-91-112FS, July 24, 1991). (See p. 87.)
- BATF **Compliance Inspections**. Because of increasing compliance responsibilities and a growing law enforcement effort, BATF has had to make resource trade-offs. One result was a reduction in tax compliance inspections of alcohol producers, which was exacerbated by inspections that were done by inspectors who were not required to have any accounting expertise. We recommended that BATF increase the availability of accounting expertise for use on tax compliance inspections. We also recommended that BATF enhance its operational efficiency by using standard work plans for compliance inspections and developing better data on compliance (GAO/GGD-91-67, Mar. 3, 1991 and GAO/T-GGD-91-19, Mar. 20, 1991). (See p. 68.)

We are pursuing other management issues important to the long-term improvement of tax administration. We are evaluating the annual review process through which IRS assesses its progress in meeting business objectives. We are also monitoring IRS' tracking of congressionally authorized enforcement initiatives to see if the intended results are being realized.

Enhance Effectiveness of Tax Incentives

Congress often adopts tax preferences and incentives to foster certain policy goals, such as improving access to housing or promoting employment for lower income workers. In 1991, over 128 tax preference items accounting for over $332 billion in revenue forgone remained in the tax code, despite continuing concerns that they frequently are not well targeted at intended beneficiaries and that the subsidized activities would have been undertaken anyway. Our work contributed to congressional debate on the costs and benefits associated with various incentives.

- **Targeted Jobs Tax Credit Program.** This program is intended to induce employers to favor disadvantaged individuals facing barriers to employment. We found that little information was available on employer or worker participation in the program. Only about half of the 60 employers we interviewed had made some special effort to hire target group members. If Congress wants more employers in the program to take special actions to benefit target group members, we suggested that it impose new requirements that might involve requiring employer outreach efforts, eligibility screening before hiring, and additional training and supervision (GAO/HRD-91-33, Feb. 20, 1991). (See p. 97.)
- **Retirement Center Bonds.** Nonprofit charitable organizations have increasingly used tax-exempt bonds to finance housing for the elderly. We identified 271 tax-exempt bonds totaling $2.8 billion that were issued from 1980 through July 1990 on behalf of charitable organizations to finance 221 housing facilities for the elderly. Weak financial structures, developer inexperience, and overestimated market projections made the facilities particularly vulnerable to default. The subsidy may serve a public purpose by encouraging housing for elderly persons unable to afford private for-profit units (GAO/GGD-91-50, Mar. 29, 1991). (See p. 97.)

We are assessing other tax expenditure programs. We are studying work incentive and income targeting issues involved with the design and administration of the Earned Income Tax Credit Program. We expect to report soon on an overview of tax subsidies provided for fringe benefits

with a focus on tax policy issues presented by the treatment of pensions, health and life insurance, and cafeteria plans.

We do our work on tax policy and administration matters pursuant to 31 U.S.C. 713, which authorizes the Comptroller General to audit IRS and BATF. GAO Order 0135.1, as amended, prescribes the procedures and requirements that must be followed in protecting the confidentiality of tax returns and return information made available to us when doing tax-related work. This order is available upon request.

Copies of this report are being sent to the Director of the Office of Management and Budget, the Secretary of the Treasury, and the Commissioner of Internal Revenue. Copies will also be sent to interested congressional committees and to others upon request.

Major contributors to this report are listed in appendix VII. If you or your colleagues would like to discuss any of the matters in the report, please call me on (202) 275-6407.

Jennie S. Stathis

Jennie S. Stathis
Director, Tax Policy and
Administration Issues

Contents

Letter

Appendix I Summaries of Tax-Related Products Issued in Fiscal Year 1991 by Subject Matter 1[illegible]

Appendix II Summaries of Tax-Related Products Issued Before Fiscal Year 1991 With Open Recommendations to Congress as of December 31, 1991 12[illegible]

Appendix III Listing of Open Recommendations to Congress 141

Appendix IV
Listing of Recommendations Made in Fiscal Year 1991 to the Commissioner of Internal Revenue and to Other Agency Heads 143

Appendix V
Chronological Listing of GAO Products on Tax Matters Issued in Fiscal Year 1991 145

Appendix VI
Listing of Assignments for Which GAO Was Authorized Access to Tax Data in Fiscal Year 1991 Under 26 U.S.C. 6103 147

Appendix VII
Major Contributors to This Report 148

Abbreviations

ADP	automated data processing
ACS	Automatic Collection System
BATF	Bureau of Alcohol, Tobacco and Firearms
CFO	Chief Financial Officer
ERISA	Employee Retirement Income Security Act
FMFIA	Federal Managers' Financial Integrity Act
HUD	U.S. Department of Housing and Urban Development
IRS	Internal Revenue Service
SSA	Social Security Administration
TSM	Tax Systems Modernization

Summaries of Tax-Related Products Issued in Fiscal Year 1991 by Subject Matter

ADP and Information Technology

Treasury ADP Procurement: Contracting and Market Share Information 1
Status of IRS' Input Processing Initiative 1
Tax System Modernization: An Assessment of IRS' Design Master Plan 2
Tax System Modernization Issues Facing IRS 2
Tax System Modernization: Status of On-line Files Initiative and Telecommunications Planning 2

Budget Issues

IRS' Budget Request for Fiscal Year 1992 2
Uncertainties Surrounding IRS' Fiscal Year 1992 Budget Request for Tax System Modernization 2

Compliance

IRS' Accounts Receivable Inventory 2
Extent and Causes of Erroneous Levies 2
Effectiveness of IRS' Return Preparer Penalty Program Is Questionable 3
IRS' Compliance Programs to Reduce the Tax Gap 3
IRS Does Not Investigate Most High-Income Nonfilers 3
IRS Can Improve Its Program to Find Taxpayers Who Underreport Their Income 3
Expanded Reporting on Seller-Financed Mortgages Can Spur Tax Compliance 4
IRS' Efforts to Ensure Corporate Tax Compliance 4
Refund Offset Program Benefits Appear to Exceed Costs 4
Money Laundering: The U.S. Government is Responding to the Problem 4
IRS Needs to Implement a Corporate Document Matching Program 4
Collecting Back Taxes: IRS Phone Operations Must Do Better 5
Negligence and Substantial Understatement Penalties Poorly Administered 5
IRS Experience Using Undercover Operations' Proceeds to Offset Operational Expenses 5
Efforts to Prevent, Identify, and Collect Employment Tax Delinquencies 5
Money Laundering: The Use of Cash Transaction Reports by Federal Law Enforcement Agencies 6
Opportunities to Increase Revenue Before Expiration of the Statutory Collection Period 6

General Management

IRS' 1990 Filing Season Performance Continued Recent Positive Trends 66
BATF: Management Improvements Needed to Handle Increasing Responsibilities 68
IRS Needs to Improve Certain Measures of Service Center Quality 71
Managing IRS: Important Strides Forward Since 1988 but More Needs to Be Done 73
Public Service: How Effective and Responsive Is the Government? 76
Information on Revenue Agent Attrition 78
Management Challenges Facing IRS 80
A Generally Successful Filing Season in 1991 81
Identifying Options for Organizational and Business Changes at IRS 83
IRS' Administration of the International Boycott Tax Code Provisions 85
IRS' Efforts to Deal With Integrity and Ethics Issues 87
Administrative Aspects of the Health Insurance Tax Credit 89

Pension Issues

Employee Benefits: Improvements Needed in Enforcing Health Insurance Continuation Requirements 90
Private Pensions: 1986 Law Will Improve Benefit Equity in Many Small Employers' Plans 92
Pension Plans: IRS Needs to Strengthen Its Enforcement Program 93

Tax Policy

Funding Options for the Resolution Trust Corporation 95
Targeted Jobs Tax Credit: Employer Actions to Recruit, Hire, and Retain Eligible Workers Vary 97
Tax-Exempt Bonds: Retirement Center Bonds Were Risky and Benefited Moderate-Income Elderly 99
Tax Incentives and Enhanced Oil Recovery Techniques 101
GAO Plans for Evaluating Luxury Excise Taxes 103
Nonprofit Hospitals: Better Standards Needed for Tax Exemption 104
Public Utilities: Disposition of Excess Deferred Taxes 106
Internal Revenue Code Provisions Related to Tax-Exempt Bonds 108

Taxpayer Service

Better Training Needed for IRS' New Telephone Assistors 109
Further Testing of IRS' Automated Taxpayer Service Systems Is Needed 111

Opportunities to Improve IRS Correspondence on Withholding Allowances 11

Tax Simplification

Simplifying Payroll Tax Deposit Rules 11
Issues and Policy Proposals Regarding Tax Treatment of Intangible Assets 11
The New Earned Income Credit Form Is Complex and May Not Be Needed 11

Other

1990 Annual Report on GAO's Tax-Related Work 12
Social Security: Information About the Accuracy of Earnings Records 12
Credit Unions: Reforms for Ensuring Future Soundness 12
Asset Management: Governmentwide Asset Disposition Activities 12

ADP and Information Technology

Treasury ADP Procurement: Contracting and Market Share Information

GAO/IMTEC-91-8FS, 11/13/90

In a report to the Chairman and Ranking Minority Member of the House Committee on Government Operations, GAO provided information on the Department of the Treasury's procurements of mainframe computers and mainframe peripheral equipment. GAO focused on the extent to which the procurements required compatibility with International Business Machines or any other computer manufacturer.

Information GAO obtained from Treasury showed that during the 3-1/2 fiscal years ending in March 1989, Treasury had a total of 323 procurements for mainframes and mainframe peripherals and that 85 percent of these (275) required some type of compatibility. Treasury required International Business Machine compatibility 68 percent of the time (188 of its 275 compatible procurements). Treasury also required that 73 procurements have Unisys compatibility and that 7 have Honeywell-Bull compatibility. The remaining seven small procurements had various other compatible requirements.

Treasury obligated $270.9 million for the 323 mainframe and mainframe peripheral procurements. When GAO used dollars for comparison—as opposed to the number of procurements—it found that overall Treasury obligated more dollars (72 percent of the total) for International Business Machine equipment than for any other manufacturer's equipment ($195.2 million versus $75.7 million for all others), including both compatible and other procurements where no compatibility was required.

IRS accounted for 83 percent of total Treasury procurements (270 of the 323 procurements) and 74 percent of the obligated dollars ($200.9 million of the $270.9 million).

GAO also provided information on the procurement methods Treasury used, including its use of contractors that participate in the Small Business Administration's program for small disadvantaged businesses—known as 8(a) contractors.

Status of IRS' Input Processing Initiative

GAO/IMTEC-91-9, 12/12/90

In a report to the Subcommittee on Oversight of the House Committee on Ways and Means, GAO provided information on IRS' input processing initiative that is intended to speed the way in which tax information is fed into computer systems for processing.

GAO said that (1) the input processing initiative would allow IRS to drastically reduce the manual processes associated with handling paper income tax returns, tax payments, and other tax information and (2) the initiative had three major components, or modules, designed to automate the labor intensive aspects of entering tax return data and other tax information into IRS' computer system. The three modules were (1) the Electronic Filing System, in which tax returns are transmitted over communication lines directly to one of three service centers; (2) the Document Processing System, which will convert tax returns, correspondence, and other tax information submitted on paper to electronic images for subsequent processing, storage, and retrieval; and (3) the Cash Management System, in which IRS is exploring various option for processing tax payments.

At the time of GAO's work, development of the input processing modules, collectively, was expected to cost over $390 million. Although IRS expecte to begin reducing the current manual processes in 1992, GAO said that it would be nearer to year 2000 before IRS fully implements and integrates al of its input processing initiatives to have a dramatic impact on IRS' operations.

The Electronic Filing System is available nationwide. GAO said that it had cost about $7 million to develop and was expected to handle about 13 million returns, about 7 percent of all returns received annually. GAO note that continued technical difficulties with printing copies of electronically filed tax returns could limit the system's usefulness and that the problem, if not resolved, would be amplified as the number of electronically filed returns increases.

As for the Document Processing System, GAO said that (1) research and design had begun, (2) IRS expected to spend $378.8 million to develop this capability, and (3) the system should be fully operational by 1998. IRS believed that nearly 97 percent of all paper returns would be converted to electronic images by this system and that the system would also use character recognition to automatically read data from tax returns. GAO

noted that problems might be caused by the fact that tax returns did not come into IRS on standard forms with easy-to-read, uniformly printed characters, for which character recognition technology was best suited.

In cash management, GAO said that IRS intends to use electronic funds transfer technologies for faster receipt of tax payments from employers and individual taxpayers. IRS had planned several multimillion dollar projects, targeted primarily at employers making federal tax deposits, to achieve this goal. However, IRS had to deal with the fact that there was little or no incentive for the individual taxpayer to pay taxes electronically as opposed to paying with a paper check.

Related GAO Product(s)

GAO/IMTEC-90-13, 02/08/90; GAO/T-IMTEC-90-5, 03/22/90; GAO/IMTEC-90-51, 07/10/90; GAO/T-IMTEC-91-4, 03/20/91; and GAO/T-IMTEC-91-8, 06/25/91

Tax System Modernization: An Assessment of IRS' Design Master Plan

GAO/IMTEC-91-53BR, 06/25/91

In a report to the Chairman of the Senate Committee on Governmental Affairs, GAO discussed its evaluation of IRS' draft Design Master Plan for th Tax Systems Modernization (TSM) program.

TSM is a comprehensive $8 billion effort to acquire the technology needed to upgrade IRS' information systems. By September 1990, IRS expected to have issued a Design Master Plan that would be the road map for guiding the agency through TSM's development and implementation. The plan was to identify tax processing needs and the projects and schedule necessary to meet those needs. At the time of GAO's review, however, IRS had yet to issue the plan in final. GAO's report, therefore, was based on an assessmen of a draft plan that IRS had issued in the interim.

GAO concluded that the draft Design Master Plan was a reasonable, useful, high-level guide for developing and implementing TSM. The plan, however, did not address certain key issues vital to the success of the modernization. These issues included

- articulating a clear, comprehensive vision of how IRS expected to conduct business in the future;
- completing plans that describe how IRS will handle the transition of its business functions from slow, largely manual business methods to the modernization's more rapid electronic methods;
- establishing and assessing progress against measurable goals;
- fixing accountability for major modernization activities;
- protecting taxpayer privacy;
- evaluating and managing technology risks; and
- developing a comprehensive human resources strategy that would include recruiting, training, and retaining staff with highly technical skills.

Related GAO Product(s)

GAO/IMTEC-91-13, 02/08/90; GAO/IMTEC-91-51, 07/10/90; and GAO/IMTEC-91-9, 12/12/90

Tax System Modernization Issues Facing IRS

GAO/T-IMTEC-91-8, 06/25/91 and GAO/T-IMTEC-91-18, 07/09/91

In testimonies before the Senate Governmental Affairs Committee and the Subcommittee on Commerce, Consumer, and Monetary Affairs of the House Committee on Government Operations, GAO highlighted some key prerequisites to moving forward with Tax Systems Modernization and identified issues the committees and IRS needed to focus on as the modernization project moved from planning to implementation.

GAO said that IRS' first prerequisite was to formally communicate, in a clear comprehensive way, its vision of how it wants to do business in the future and how technology will be used to achieve this vision. A clearly defined, well-communicated vision of the future way of using technology to do business can serve as a rallying point, a core concept on which Congress, agency leaders, employees, and outside customers can focus. It is also a standard against which Congress and IRS may measure progress.

A second prerequisite discussed was the need to finalize the Design Master Plan, intended as a road map or baseline for the modernization. In this regard, more than half a billion dollars had been budgeted for the modernization through fiscal year 1991, and IRS had requested $427 million more in fiscal year 1992 for modernization initiatives without a final plan.

GAO also identified other important issues IRS faced as it implemented the modernization program. Specifically, GAO said that IRS needed to strengthen both its procurement and its systems development policies and practices and ensure that it has people with the necessary technical expertise to carry out the program.

Related GAO Product(s)

GAO/IMTEC-89-54, 06/22/89; GAO/IMTEC-90-24, 01/12/90; GAO/IMTEC-90-13, 02/08/90; GAO/IMTEC-90-51, 07/10/90; GAO/IMTEC-91-9; 12/12/90; GAO/IMTEC-91-39, 06/18/91; GAO/IMTEC-91-42, 06/20/91; and GAO/IMTEC-91-53BR, 06/25/91

Tax System Modernization: Status of On-Line Files Initiative and Telecommunications Planning

GAO/IMTEC-91-41FS, 08/14/91

In a fact sheet to the Chairman, Subcommittee on Oversight, House Committee on Ways and Means, GAO provided information on the status of IRS' Corporate Files On-Line, a series of projects intended to give IRS immediate access to tax information and telecommunications plans.

The On-Line files project is a short-term initiative that will be replaced in phases, by fiscal year 1996, as part of IRS' Tax System Modernization (TSM) program. It consists of 14 systems and 1 prototype project, which will enable IRS employees to search for and retrieve taxpayer information—such as names and Social Security numbers—faster than before. This information helps locate taxpayers' accounts and reduce errors. Currently four of the On-Line files systems have been fully implemented, and most of the others are scheduled to be completed by April 1993.

IRS originally planned for a second version of the On-Line files project to add advanced data management and retrieval capabilities. GAO told IRS that this version would be expensive and would provide few additional benefits. As a result, in January 1991, IRS canceled it, saving an estimated $125 million.

TSM will require telecommunications that permit the new computer systems to work together. In October 1990, IRS reorganized its Telecommunications Division within the agency so it would be easier to coordinate telecommunications planning and implementation. IRS has also assigned telecommunications a high priority in planning for TSM.

Budget Issues

IRS' Budget Request for Fiscal Year 1992

GAO/T-GGD-91-17, 03/20/91

In testimony before the Subcommittee on Oversight of the House Committee on Ways and Means, GAO noted that IRS' fiscal condition in 1991 appeared to be more stable than it was in the previous 2 fiscal years. During those years IRS encountered budget shortfalls of $360 and $465 million, respectively. GAO said that IRS might have to absorb about $74 million in cost increases for fiscal year 1991 but that IRS would apparently be able to cover most of these costs without having to take the drastic kind of actions it took in 1989 and 1990 when it froze hiring, curtailed promotions, and reduced support services. Because of the more stable fiscal condition in 1991, it appeared that IRS would be able to more fully implement congressionally authorized compliance initiatives—something it was unable to do in fiscal year 1990.

The administration's fiscal year 1992 budget request for IRS totaled $6.73 billion, a net increase of $622 million over the authorized level for fiscal year 1991. IRS' first budget priority for fiscal year 1992 was full funding for existing staff and related support costs. That priority accounted for the largest portion of the requested $622 million increase. GAO pointed out that, compared to previous years' budgets, the administration's fiscal year 1992 budget request for IRS appeared to have been formulated to more accurately reflect on-board labor costs, thus improving the likelihood that new program initiatives would be implemented.

The most significant compliance initiative proposed in the budget request for fiscal year 1992 provided an additional $34 million for IRS to collect delinquent accounts. GAO expressed the belief that this request was reasonable in light of staffing reductions that resulted from past hiring freezes. Another initiative provided for $5.5 million to increase the number of examinations of high-dollar tax returns. This increase, however, would expand audit coverage by only .01 percentage point over the fiscal year 1991 level, thus doing little to reverse the steady decline in audit coverage.

As part of this testimony, GAO provided an interim assessment of IRS' performance during the 1991 tax return filing season. GAO's final assessment of that filing season can be found on page 63.

Summary of Related Action(s)

On October 28, 1991, the President signed Public Law 102-141 appropriating $6.67 billion to IRS—about $55 million less than requested. The biggest difference was in the tax law enforcement area in which IRS was appropriated $3.58 billion compared to the $3.63 billion requested.

Related GAO Product(s)

GAO/T-GGD-89-16, 04/04/89; GAO/GGD-89-116, 08/18/89; GAO/T-GGD-90-26, 03/22/90; and GAO/GGD-90-101FS, 07/30/90

Uncertainties Surrounding IRS' Fiscal Year 1992 Budget Request for Tax System Modernization

GAO/T-IMTEC-91-4, 03/20/91

In testimony before the Subcommittee on Oversight of the House Committee on Ways and Means, GAO discussed (1) IRS' fiscal year 1992 budget request for Tax Systems Modernization and (2) the effects of fiscal year 1991 reductions to IRS' data processing budget on its operations.

GAO cited two major concerns about the $451 million budgeted for the modernization program in fiscal year 1992. First, the amount might have been more than was needed because about $55 million related to projects that were not identified as modernization projects in IRS' Design Master Plan. The plan was still in draft at the time of GAO's testimony. Second, IRS had no system to track modernization projects against cost, schedule, and performance goals.

GAO also said that the $49 million cut in IRS' data processing budget for fiscal year 1991 had not adversely affected IRS' computer operations. GAO's work indicated that the reduction was achieved by eliminating planned increases for ongoing projects and delaying the start of others. None of the projects affected was among those identified as being part of Tax Systems Modernization, and IRS budget officials did not expect the cuts to adversely affect ongoing data processing operations.

Related GAO Product(s)

GAO/T-IMTEC-90-5, 03/22/90 and GAO/IMTEC-91-9, 12/12/90

Compliance

IRS' Accounts Receivable Inventory

GAO/T-GGD-91-2, 10/18/90 and GAO/GGD-91-45, 04/16/91

As part of its continuing work on IRS' accounts receivable inventory, GAO examined the composition and disposition of two groups of accounts comprising 10 percent of the first quarter 1990 accounts receivable inventory of $67.7 billion. Those two groups were (1) the 98 largest receivables, which accounted for $6.2 billion; and (2) accounts receivable from federal agencies for employment taxes, which accounted for $185 million.

In 1990 testimony before the Subcommittee on Oversight, House Committee on Ways and Means, GAO said that for both groups of accounts the amount owed declined substantially from the first quarter of 1990 through August 1990; but very little of this decrease could be attributed to collections from these taxpayers. Rather, nearly all of the decrease was the result of amounts written off by adjusting taxpayers' accounts due to taxpayer or IRS errors. GAO said that erroneous receivables could be reduced through improvements to (1) the complex and confusing federal tax deposit system and (2) IRS' accounting and information processing systems.

GAO followed up that testimony with an April 1991 report to the Secretary of the Treasury dealing with federal agency tax compliance. In the report, GAO concluded that IRS' master file transcript records contained many errors that showed up as accounts receivable on IRS' books and gave the appearance that federal agencies had not paid their employment taxes.

GAO found, instead, that most agencies had paid their taxes on time and that most of the errors in the records were a result of the cumbersome paper-based process being used to make payments. This process, which required federal agencies to make payments to IRS through Treasury, was outdated and prone to errors, often resulting in payment processing and posting errors that showed up as accounts receivable. GAO said that electronic interagency funds transfer, with the requirement that the funds transfer information be provided to IRS, should help reduce the numerous errors responsible for federal agency receivables.

GAO also found that federal managers appeared to place insufficient priority on reporting their federal tax liability and that late filing of tax returns was widespread. GAO said that enhanced attention to tax deposit issues by high-level agency officials should help foster greater agency accountability. GAO also cited the need for improved communications between IRS and other federal agencies. For example, GAO said that (1) the notices IRS sends to agencies when tax data do not reconcile and when returns have not been filed should be clarified to apply to the unique tax situation faced by federal agencies, (2) IRS needed to inform agencies of adjustments it makes to their accounts, and (3) IRS needed to provide assistance to agencies through training programs.

Recommendation(s)

Treasury, in close coordination with IRS and the Financial Management Service, should undertake a governmentwide program to improve federal agency tax processing. That program should include

- streamlining agency tax payment processing through electronic interagency funds transfer and requiring that the funds transfer information be provided to IRS;
- enhancing the clarity of IRS communications with agencies in such ways as developing notices tailored to the unique tax situation of federal agencies and informing agencies of adjustments to their accounts; and
- providing for an IRS training program for agencies' staff involved in making tax payments and filing tax returns.

Treasury should also develop methods to promote greater accountability by top agency management for compliance with tax laws and regulations by working with the agencies and the Office of Management and Budget. Treasury should consider, among other methods, enhancing agency tax compliance by (1) ensuring that agencies' Federal Managers' Financial Integrity Act reviews adequately cover tax compliance and include management follow-up and (2) developing a process for top managers to certify their agencies' tax compliance.

Action(s) Taken and/or Pending

Treasury generally agreed with our recommendations. Although no recommendations have been fully implemented, actions that have been taken or planned include the following:

- IRS in conjunction with the Federal Management Service, plans to implement in 1992 an electronic Federal Tax Deposit payment process for

federal agencies, which would also allow them to file their employment tax returns electronically;

- IRS has assigned a federal agency coordinator to specifically deal with agencies about notices, account adjustments, and other tax-related matters;
- IRS plans to implement in 1992 a training program for agency staffs involved in making tax payments and filing tax returns; and
- IRS, in coordination with Treasury and the Office of Management and Budget, is considering using the fiscal year 1992 integrity act reviews as a vehicle for implementing methods for greater accountability by top agenc managers for compliance with the tax laws.

Related GAO Product(s)

GAO/GGD-90-102, 07/31/90 and GAO/GGD-91-94, 08/28/91

Extent and Causes of Erroneous Levies

GAO/GGD-91-9, 12/21/90

This report, prepared in response to a request from the Joint Committee on Taxation, discusses (1) the extent and causes of erroneous levies and (2) IRS' controls to prevent erroneous levies or mitigate their effects. Erroneous levies occur when IRS levies the assets of taxpayers who do not owe taxes, levies for an amount greater than the taxes owed, or levies when the taxpayer has an installment agreement to pay the delinquency or is in bankruptcy.

IRS did not maintain statistics on erroneous levies. Therefore, to determine the extent and causes of erroneous levies, GAO analyzed IRS' use of levies for a stratified nationwide sample of 787 delinquent taxpayers whose accounts were sent to IRS' Automated Collection System (ACS)[1] in fiscal year 1986. (The sample contained levies on 404 individuals and 383 businesses.) GAO projected the sample results to the universe of 448,200 delinquent taxpayers who had assets levied as result of accounts sent to ACS during fiscal year 1986.

As a result of its work, GAO estimated that IRS (1) had initiated 16,100 erroneous levies on the assets of 12,400, or 2.8 percent, of the 448,200 taxpayers and (2) had erroneously levied the assets of businesses to a much greater extent than those of individuals—5.7 percent for businesses and 1.5 percent for individuals. GAO cited delays and errors in recording taxpayers' payments as the two primary causes of the erroneous levies.

GAO said that IRS could improve its controls and significantly reduce the number of erroneous levies by instituting a levy verification program nationwide. As of March 1990, when GAO completed its work, 3 of IRS' 10 service centers were using a manual levy verification program before issuing levies. This program helped ensure that the amount of each levy was correct by searching for changes in the taxpayer's delinquency status, unrecorded payments received from the taxpayer that could affect the amount of the levy, and overpayments in the taxpayer's other accounts that would reduce the taxpayer's liability. This type of verification program, if properly implemented, could have eliminated at least one-third, and possibly as many as two-thirds, of the erroneous levies GAO identified.

[1]ACS, which was phased in during 1983 and 1984, is an automated system that IRS employees at 23 call sites use to telephone delinquent taxpayers, receive calls from taxpayers, and retrieve information from the taxpayers' accounts.

Recommendation(s)

The Commissioner of Internal Revenue should establish a nationwide levy verification program that would determine whether there are (1) overpayments in the taxpayer's other accounts, (2) pending payments, and (3) changes in the status of the taxpayer's account.

Action(s) Taken and/or Pending

In February 1991, IRS said that, in addition to implementing a nationwide manual verification program at the service centers, it had issued instructions to its collection field staff requiring them to check taxpayer account information on the Integrated Data Retrieval System before mailing levies to determine whether there are (1) overpayments in the taxpayer's other accounts, (2) pending payments, and (3) changes in the status of the taxpayer's account. IRS also said that as part of its modernization efforts, it intends to explore developing an automated levy verification process.

Related GAO Product(s)

GAO/GGD-89-97FS, 07/17/89 and GAO/GGD-91-20, 06/25/91

Effectiveness of IRS' Return Preparer Penalty Program Is Questionable

GAO/GGD-91-12, 01/07/91

In 1989, almost half of the individual income tax returns filed were prepared by paid return preparers. IRS has experienced problems with what it calls incompetent and unscrupulous preparers who understate their clients' tax liabilities. Civil penalties are a principal tool IRS can use to punish and deter noncompliant behavior by preparers. In response to a request from the Chairman of the Senate Finance Subcommittee on Private Retirement Plans and Oversight of IRS, GAO reviewed whether IRS administers preparer penalties appropriately and consistently.

IRS assesses penalties on return preparers when its examination of tax returns reveals that the preparer understated the taxpayer's taxes due to (1) negligent or intentional disregard of rules and regulations or (2) willful understatement. The Omnibus Budget Reconciliation Act of 1989 raised the penalties for these actions to $250 and $1,000 respectively and revised the definitions. In addition to assessing penalties, IRS can also refer preparers to Treasury's Director of Practice or the local district director for further disciplinary action, which could involve prohibiting the preparers from representing taxpayers before IRS.

GAO found that IRS needed to better ensure that preparers engaged in negligent or abusive tax practices are penalized. Although IRS generally assessed the right penalty when it decided to penalize a preparer, penalty cases were often not opened when potential preparer misconduct was evident on returns with at least $5,000 in taxes owed.

IRS examiners and their supervisors indicated they were reluctant to pursue return preparer penalties because of the low dollar amounts of the penalties. Even though preparer penalties may not yield significant revenues, GAO believed that their potential long-term effect in encouraging voluntary compliance by preparers and their client taxpayers should also be considered in determining the value of penalty actions.

GAO noted that IRS district offices might assess different penalties and penalty amounts for similar misconduct. These differences were partly due to difficulties in clearly distinguishing between the two penalties (for "intentional disregard" and for "willful understatement") and ambiguities that were only partly addressed by the 1989 legislation. Additionally, due to different interpretations of the code, some districts were collecting more than Congress intended when both the negligence or intentional disregard and the willful understatement penalties were assessed.

GAO also found that referrals were often not made when required. This inconsistency was due to examiners' lack of familiarity with the referral process, unclear guidance explaining referral procedures, and the lack of internal controls to ensure that required referrals were made.

Recommendation(s)

GAO made several recommendations directed at helping to ensure that (1) IRS opens warranted preparer penalty cases, (2) preparer penalties are assessed appropriately and consistently, and (3) referrals are made when required. Included were recommendations that the Commissioner do the following:

- Take actions to ensure that examiners consider the penalties and document their decisions regarding the opening of preparer penalty cases These actions could include a memorandum to examiners and group managers emphasizing existing penalty requirements as well as other communications.
- Develop National Office guidance that to the greatest extent possible clearly defines and differentiates between the preparer penalties as defined in section 6694(a) for taking an unrealistic position, section 6694(b) for willful or reckless conduct, and section 6701 for aiding and abetting an understatement of tax liability.
- Adopt procedures to ensure that no more than the maximum amount allowable under the Internal Revenue Code is collected for these penaltie If IRS determines that the problem cannot be eliminated administratively, i should ask Congress to modify the statute to limit the total amount IRS ca assess, rather than collect, for these penalties.
- Clarify the Internal Revenue Manual to clearly state that referrals are required when preparer penalties are assessed and designate responsibility for making them.
- Ensure that examiners receive training that clearly communicates the referral requirements.

Action(s) Taken and/or Pending

IRS agreed to most of GAO's recommendations and said that it would take actions to improve examiner awareness, guidance, and training on the return preparer penalties and related referrals. For example, IRS is draftin a penalty handbook, which it expects to complete in 1992. When the handbook is completed, IRS intends to include a preparer penalty module in its continuing education course.

IRS has issued guidance on differentiating preparer penalties in regulations implementing the 1989 Omnibus Budget Reconciliation Act.

To ensure that no more than the maximum amount allowable under the Internal Revenue Code is collected for these penalties, the Assistant Commissioner for Examination requested a computer change to reject an assessment if it exceeds the maximum amount allowable. If this action does not work, IRS intends to seek a legislative change.

IRS also revised the Internal Revenue Manual to clarify that the examining official is responsible for preparing the referral of the preparer to the District Director or the Director of Practice as appropriate. The manual also requires that the referral be transmitted through the Return Preparer Coordinator.

IRS has also revised examination Form 4318, Examination Workpapers, to include among the list of "Reminders" appearing on the form one that directs the examiner to the relevant Internal Revenue Manual provision for referrals.

Related GAO Product(s)

GAO/GGD-90-92, 08/15/90 and GAO/GGD-91-91, 07/03/91

IRS' Compliance Programs to Reduce the Tax Gap

GAO/T-GGD-91-11, 03/13/91

In testimony before the Subcommittee on Commerce, Consumer, and Monetary Affairs of the House Committee on Government Operations, GAO said that IRS could better use information returns to pursue people who do not file a tax return (nonfilers) or who file a return but do not report income (underreporters). Doing so could allow IRS to narrow the income tax gap—which is the difference between the amount of income tax that taxpayers owe and the amount they voluntarily pay for a tax year. In 1988, IRS estimated the gross tax gap to be $85 billion for 1987 and projected it would reach over $113 billion by 1992. IRS' estimates show that nonfilers and underreporters accounted for about $7 billion and $48 billion, respectively, of the 1987 tax gap.

GAO found that IRS could improve its use of information returns to identify and pursue nonfilers and underreporters. For example, IRS' nonfiler program had an ironic imbalance that allowed high-income nonfilers—or those who make over $100,000—to more easily escape scrutiny than nonfilers with lower incomes. At three service centers that GAO reviewed, IRS did not fully pursue about half of the high-income nonfilers primarily because of a flaw in setting work load priorities and a decision to exclude high-income nonfilers from a program that creates a tax assessment for other nonfilers. Also, when IRS eventually received a delinquent return from a high-income nonfiler, it did not use the information returns, along with other data, to ensure that the nonfiler paid all taxes owed. Had IRS set priorities correctly, GAO estimated that these three service centers could have recommended up to $10 million more in taxes.

GAO also found that IRS could improve its computer matching of information returns with tax returns to reduce the millions of underreporter cases that do not result in the recommendation of additional taxes. Pursuing such unproductive cases wastes IRS' resources and burdens taxpayers who respond to IRS' inquiries. IRS could have avoided up to 40 percent of the unproductive cases in one service center by better using information returns, among other data, in its computer match. Had IRS done so and used the savings to pursue unworked cases, GAO estimated that the service center could have recommended over $18 million in additional taxes.

Related GAO Product(s)

GAO/GGD-89-81, 09/06/89; GAO/GGD-91-36, 03/13/91; and GAO/GGD-91-49, 03/13/91

IRS Does Not Investigate Most High-Income Nonfilers

GAO/GGD-91-36, 03/13/91

In response to a request from the Chairman of the Subcommittee on Commerce, Consumer, and Monetary Affairs, House Committee on Government Operations, GAO determined whether IRS could investigate more high-income nonfilers and do so more effectively.

IRS identifies potential nonfilers when a tax return cannot be found for income reported on information returns, such as wage statements (Form W-2). IRS assigns cases a priority—based on the estimated tax yield—that determines the degree of IRS scrutiny.

IRS uses three stages to investigate nonfilers. First, IRS sends as many as four notices that ask nonfilers to file a return. Second, IRS sends unresolved cases—depending on amounts and types of income—to either (1) an automated call site, where a tax examiner tries to obtain a tax return; or (2) the Substitute for Returns Program, where IRS estimates taxes owed, prepares a "substitute" return for the delinquent one, and recommends a tax assessment. In the third stage, cases unresolved at automated call sites are referred to an IRS district. Cases with a low priority may not be pursued at the automated call sites or the district offices. Rather, IRS may investigate other cases, such as those involving delinquent taxes owed by businesses or individuals, that have higher priorities.

To determine whether changing IRS' three-stage process would produce more returns and taxes, GAO randomly selected 1,200 of 3,600 high-income nonfiler cases at three IRS service centers. The 3,600 cases were those still unresolved after 2 notices had been sent to a universe of about 12,000 cases. Of the 1,200 sample cases, GAO asked IRS to experiment by sending about

- 300 directly to district revenue officers,
- 300 to automated collection system sites, and
- 300 to the Substitute for Returns Program.

The final group of 300 was used as a control and investigated using the normal three-stage process.

GAO found that IRS did not fully investigate high-income nonfilers, which created an ironic imbalance. Unlike lower income nonfilers in the Substitute for Returns Program, high-income nonfilers who did not

respond to IRS' notices were not investigated or assessed taxes. Even if high-income nonfilers eventually filed tax returns, their returns received less scrutiny than those returns filed on time.

GAO estimated that half of the high-income nonfilers at the three service centers were not investigated by district revenue officers or assessed a tax in earlier stages. Revenue officers did not pursue them because IRS understated the estimated yields from investigating them. Even if IRS correctly estimated these yields, it had too few revenue officers to investigate many more cases.

IRS could investigate more high-income nonfilers by using the Substitute for Returns Program. GAO's test showed that this method produced more yield at the lowest cost and created a tax assessment that otherwise was unlikely. GAO believes an assessment, even if understated, is better than letting the nonfiler escape a revenue officer's scrutiny.

Although IRS checked returns filed on time for noncompliance, it did not have a systematic way to check for underreported income or overstated deductions on delinquent returns that high-income nonfilers eventually filed. GAO found that none of these delinquent returns were computer matched with information returns, and few returns were referred to the Examination Division to be checked. However, nearly half of the delinquent returns that GAO asked IRS to check had evidence of noncompliance.

Recommendation(s)

To improve IRS' pursuit of high-income nonfiler cases, the Commissioner of Internal Revenue should

- separately estimate tax yields for high-income nonfiler cases so more of these cases will be investigated by revenue officers,
- modify the Substitute for Returns Program to include high-income nonfiler cases that would otherwise escape IRS action, and
- develop a system to check delinquent returns from high-income nonfilers for noncompliance.

Action(s) Taken and/or Pending

IRS generally agreed with GAO's recommendations and is taking or plans to take action to implement them. For example, IRS is changing its procedures so that all high-income nonfiler cases that are unresolved after a collection action will be referred to the Examination Division for further

review. IRS said this process would be more effective in determining the correct amount of unreported income than the Substitute for Returns Program, which computes income on the basis of wage and information returns. In addition, IRS has issued instructions to require all delinquent returns to be checked for both unreported income and overstated deductions and referred to the Examination Division where appropriate.

Related GAO Product(s)

GAO/T-GGD-91-11, 03/13/91

IRS Can Improve Its Program to Find Taxpayers Who Underreport Their Income

GAO/GGD-91-49, 03/13/91

IRS primarily identifies underreporters by computer matching income reported on information returns (e.g., Form W-2) with income reported on individual tax returns. In response to a request from the Chairman of the Subcommittee on Commerce, Consumer, and Monetary Affairs, House Committee on Government Operations, GAO determined whether IRS (1) could improve computer matching to avoid unproductive underreporter cases and (2) was notifying the Social Security Administration (SSA) when its underreporter work disclosed errors in wages that were previously reported to SSA.

GAO reported that IRS' underreporter program had been cost effective but could be more so. From 1982 to 1988, the percent of nationwide underreporter cases that were unproductive had increased from 54 percent to an estimated 66 percent. Unproductive cases (1) cost IRS money that could have been spent pursuing taxpayers who owed additional taxes and (2) imposed a burden on compliant taxpayers who had to respond to IRS' inquiries.

To identify ways that IRS' computer matching could be made more productive, GAO analyzed 514 randomly selected cases from a group of 61,000 unproductive cases at the Fresno Service Center for 1987, the most recent year data were available. These 61,000 cases involved two types of income—wages paid to employees and payments to self-employed persons—and represented 27 percent of the 229,000 unproductive cases closed as of January 1990 at Fresno. In projecting the results of its sample, GAO said that many of Fresno's 61,000 unproductive cases occurred because of three computer match problems: (1) taxpayers reported income on tax return lines not included in the match, (2) payers submitted duplicate or multiple information returns for the same taxpayer, and (3) the match did not count specific changes to income that were reported on amended tax returns. Other unproductive cases were caused by individuals who organized their businesses as corporations or partnerships. These individuals provided their Social Security numbers—rather than business identification numbers—to payers of income to the business. When payers used Social Security numbers to report the income payments, IRS' match looked for that income on the recipient's individual tax return. The match would thus identify the individual as an underreporter, even though the income was properly reported on the recipient's business tax return.

GAO concluded that by eliminating unproductive cases through more effective computer matching, Fresno could have pursued more productive underreporter cases and possibly recommended up to $19 million in additional taxes for 1987. GAO suggested that further reductions in unproductive cases might be identified if IRS captured specific reasons for such cases on its management information system.

GAO also found that IRS did not notify SSA when IRS' underreporter work identified persons who did not receive wages that employers reported to SSA. As a result, almost half of the SSA accounts that GAO reviewed continued to overstate an estimated $44 million in wages. Unless corrected, such overstatements could result in SSA paying people more benefits than they are entitled to receive.

Recommendation(s)

To reduce the number of unproductive underreporter cases, the Commissioner of Internal Revenue should modify the computer match to

- search for income on as many tax return lines as possible without inadvertently screening out productive cases,
- use SSA's corrected wage data to identify when employers submit multiple information returns for the same taxpayer, and
- count changes to specific amounts of income that taxpayers report on amended tax returns.

The Commissioner should (1) notify taxpayers who provide their Social Security numbers to payers of business income to begin providing their businesses' tax identification numbers and (2) modify the management information system for the underreporter program to provide specific reasons why cases were unproductive. This information, when available, should be used to monitor results and further improve the matching process.

The Commissioner should also provide SSA with corrected wage data for taxpayers found to have wages that were incorrectly reported to SSA.

Action(s) Taken and/or Pending

IRS generally agreed with GAO's recommendations and has taken or plans to take action to implement them. For example, IRS (1) has identified additional matching requirements and has enhanced computer screening of wage discrepancies to search for income without inadvertently screening out productive cases; (2) intends to use duplicate documents

that are available—especially Form W-2s—to eliminate unproductive cases; (3) expects to complete action in 1992 to remind taxpayers to submit a new Form W-9 informing the payer of the correct taxpayer identification number when income belongs to a corporation or partnership; and (4) plans, within the framework of the disclosure provisions of section 6103 of the Internal Revenue Code, to work closely with SSA in providing the information SSA needs for taxpayers having wages that were incorrectly reported to SSA.

Related GAO Product(s)

GAO/IMTEC-90-51, 07/10/90 and GAO/T-GGD-91-11, 03/13/91

Expanded Reporting on Seller-Financed Mortgages Can Spur Tax Compliance

GAO/GGD-91-38, 03/29/91

This report responded to a request from the Chairman, Subcommittee on Private Retirement Plans and Oversight of the Internal Revenue Service, Senate Committee on Finance. It discussed how third-party information reports might help increase taxpayer compliance with the requirements for reporting interest payments made under seller-financed mortgages.

Under this mortgage arrangement, the individual seller finances all or part of the buyer's purchase of the property. The Internal Revenue Code requires that the seller pay tax on the interest income received from the buyer. IRS requires sellers to report on Schedule B (Interest and Dividend Income) of their Form 1040 the amount of interest income received from the buyer and the buyer's name.

The Internal Revenue Code stipulates that buyers who itemize deductions can deduct their mortgage interest payments to sellers. IRS requires that buyers report sellers' names and addresses on Schedule A (Itemized Deductions) of their Form 1040. Federal law does not give IRS the authority to require buyers to provide sellers' Social Security numbers nor does IRS require buyers to send sellers a notice that IRS is aware of the interest payment made to them.

On the basis of its analysis, GAO concluded that as much as $200 million in 1989 federal taxes may not have been paid because of noncompliance in reporting seller-financed mortgage interest income and deductions. GAO believed that if legislation was enacted to require buyers to report sellers' Social Security numbers, most of this tax revenue would have been paid due to increased voluntary compliance. To pursue any remaining unpaid taxes, IRS could use the numbers as part of an enforcement program to identify sellers who fail to report mortgage interest as well as buyers who overstate mortgage deductions.

Recommendation(s) to Congress

Congress should enact legislation to

- require buyers who deduct seller-financed mortgage interest to report on their tax returns the name and Social Security number of the seller and
- authorize IRS to penalize (1) buyers who fail to provide the sellers' identification number and cannot show that they made reasonable efforts to obtain it and (2) sellers who refuse to provide their numbers to buyers.

Recommendation(s) to the Commissioner of Internal Revenue

If Congress enacts legislation to require buyers to report sellers' Social Security numbers, the Commissioner of Internal Revenue should use the sellers' and buyers' numbers to study the extent of taxpayer noncompliance and, on the basis of the study's results, implement an enforcement program, such as computer matching, to pursue cases of potential noncompliance.

Action(s) Taken and/or Pending

No legislative action had been taken as of December 31, 1991.

IRS' Efforts to Ensure Corporate Tax Compliance

GAO/T-GGD-91-21, 04/17/91

In testimony before the Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs, GAO discussed IRS' efforts to ensure corporate tax compliance.

GAO said that (1) the nation's tax gap—the difference between the amount of income tax owed for 1 tax year and the amount paid voluntarily—was over $100 billion and growing rapidly, (2) IRS had estimated the gap to be $85 billion for 1987 and had projected that it would reach about $114 billion by 1992, (3) IRS had estimated that it would ultimately collect about one-quarter of each year's tax gap, and (4) IRS had estimated that corporations accounted for $31 billion of the $114 billion gap.

GAO testified that the corporate tax gap had grown three times faster than the gap for individuals, and new evidence indicated that the gap for small corporations might be even greater than the estimates suggested. New IRS audit results showed that 2.3 million small corporations (about 80 percent of all corporations) voluntarily paid 61 percent of the tax they owed in 1987. For 1980, just 7 years earlier, IRS audit results showed this voluntary compliance to be 81 percent. This dramatic drop in compliance contrasted sharply with much higher compliance levels for individual taxpayers during this period—about 82 percent.

GAO said it was reviewing corporate tax compliance and IRS' program to audit the largest corporations in the country. It appeared that IRS might be losing its ability to promote voluntary compliance among the largest corporations because of various IRS management problems that have persisted since the late 1970s. GAO noted, for example, that IRS did not know how much of the additional taxes it recommends from an audit are ultimately billed to the corporation after the appeals process. Also, IRS training for revenue agents had not kept pace with changes in the economy and in laws that are very difficult to administer (such as those relating to transfer pricing and intangible assets). In GAO's opinion, these problems helped explain why, according to IRS data, large corporations (1) were appealing 80 percent of the taxes IRS recommended and (2) were winning 75 percent of the appealed amounts.

Summary of Related Action(s)

IRS is continuing to revise its Coordinated Examination Program to corre these and other related problems. GAO plans to continue to track these improvements to see whether they are addressing the problems GAO uncovered.

Related GAO Product(s)

GAO/GGD-90-53BR, 04/04/90; GAO/T-GGD-90-32, 04/19/90 and GAO/GGD-90-85, 06/20/90

Refund Offset Program Benefits Appear to Exceed Costs

GAO/GGD-91-64, 05/14/91

IRS offsets federal tax refunds due taxpayers who have certain nontax delinquent debts. IRS offset about $4 billion in taxpayer refunds during calendar years 1982 through 1990 for the nonpayment of child and spousal support payments and since 1986 for the nonpayment of federal nontax debts, such as education loans. In this report to the Joint Committee on Taxation, GAO (1) evaluated the effects of the Refund Offset Program on the filing behavior of guaranteed student loan defaulters and (2) compared the program's estimated benefits resulting from increased debt collections with the program's estimated costs resulting from increased noncompliance.

Because of concerns that offsets might reduce taxpayer compliance, Congress required the Department of the Treasury to examine the Refund Offset Program's effect on compliance and how it aids in collecting federal debts. In that regard, IRS has issued four refund offset reports. Each report showed a pattern of more nonfiling and more tax returns filed with taxes due in years after an offset. GAO has issued two reports on IRS' study methodology. GAO's main concern in those reports was whether IRS' study groups were comparable. IRS matched taxpayers by their taxable income and filing status but did not consider other potentially relevant nontax differences such as a debtor's predisposition toward nonpayment of debt.

To address study group comparability, GAO developed a study approach that used a sample of guaranteed student loan defaulters. Since each guaranty agency did not refer all student loan defaulters for offset in the first 2 years of the program, GAO separated the defaulters into two groups: defaulters who were offset and those who were not. Thus, GAO's study groups were more equivalent on a key nontax characteristic that might relate to noncompliance with tax laws—all were defaulters. GAO used an analytic technique that isolated the effects of different tax and nontax characteristics on filing behavior.

GAO's study showed that the Refund Offset Program had less of an adverse effect on tax compliance overall than suggested by IRS studies. While both agencies' studies showed that offsetting federal tax refunds for nontax debts increased nonfiling the next year, GAO's study showed that the offset had virtually no effect 2 years later. GAO also found no evidence that an offset taxpayer was more likely not to pay taxes due when filing a tax return the year after an offset. IRS' studies showed an increase in these balance-due returns.

GAO also made a limited estimate of the potential tax revenues lost due to nonfiling by student loan defaulters in the year after an offset. The debt recovered from the offset was at least four times greater than the potentia revenue loss. IRS' studies had not estimated the overall costs and benefits of the program.

Recommendation(s)

Congress will need information on the overall costs and benefits of the Refund Offset Program when it considers the 1994 expiring provision. Thus, IRS should carry out its plans for future studies and specifically ensure that those studies (1) control as many meaningful tax and nontax characteristics as possible; (2) include an estimate of the potential revenu loss due to any noncompliant filing behavior; and (3) include a compariso of this loss with the program's benefits.

Action(s) Taken and/or Pending

IRS agreed that further refinements to its study methodology are needed to ensure study group comparability. Thus, IRS has included additional nontax characteristics, such as age and geographic region, in its analyses. IRS has also developed a methodology for estimating the benefits and costs associated with offsetting taxpayers' refunds for nonpayment of nontax federal debts. IRS expects to report on the results of its analyses in August 1992.

Related GAO Product(s)

GAO/GGD-88-117, 09/01/87 and GAO/GGD-89-60, 04/25/89

Money Laundering: the U.S. Government Is Responding to the Problem

GAO/NSIAD-91-130, 05/16/91

In a report to the Chairman of the Subcommittee on Narcotics, Terrorism and International Operations, Senate Committee on Foreign Relations, GAO discussed the federal government's antimoney laundering effort, including collection, analysis, and use of currency transaction data; federal agency staffing, resources, and coordination; additional steps underway or improvements needed in combating money laundering; and negotiations with foreign governments concerning the exchange of financial transactions data. IRS is one of many federal agencies involved in the antimoney laundering effort. During fiscal year 1989, for example, IRS initiated 1,132 criminal money laundering cases.

GAO concluded that progress had apparently been made in the evolving federal effort to fight money laundering, although there was a lack of "hard" data to demonstrate this conclusively. GAO said that (1) awareness of the problem had increased and important legislation had been enacted, (2) currency transaction reporting had increased, (3) greater resources appear to have been allocated to antimoney laundering activities in certain areas and efforts were being made to improve coordination, and (4) international negotiations were leading to significant agreements.

GAO also cited some problems. First, questions persisted about the usefulness of currency transaction data in initiating criminal cases, and problems had occurred in data processing. Second, resources were not always adequate to support antimoney laundering activities, especially in Treasury's Office of Financial Enforcement. That office is responsible for governmentwide monitoring and coordination of antimoney laundering functions and negotiating international agreements regarding record keeping for large U.S. currency transactions and disclosure of such records to U.S. law enforcement officials. A final problem cited by GAO involved coordination among the many federal agencies involved. GAO said that coordination problems and related jurisdictional issues had affected such areas as information exchange among agencies. In that regard, GAO noted how Internal Revenue Code provisions relating to confidentiality and disclosure of tax information restricted IRS' ability to share such data.

Recommendation(s)

The Secretary of the Treasury should direct that all permanent positions allocated to the Office of Financial Enforcement be filled as quickly as possible.

Action(s) Taken and/or Pending

Treasury generally agreed with GAO's recommendation and is planning to implement it.

Related GAO Product(s)

GAO/GGD-91-53, 03/18/91 and GAO/GGD-91-125, 09/25/91

IRS Needs to Implement a Corporate Document Matching Program

GAO/T-GGD-91-40, 06/10/91 and GAO/GGD-91-118, 09/27/91

In testimony before the Subcommittee on Commerce, Consumer, and Monetary Affairs of the House Committee on Government Operations, GAO discussed the need for a corporate document matching program, stating, among other things, that the benefits accruing to the federal government from such a program would exceed corresponding costs.

At the time GAO testified, the latest IRS data available showed that corporate compliance with the tax laws had declined to an alarming degree. In 1980, small corporations that IRS studied (about 80 percent of all corporations) voluntarily reported 81 percent of the taxes owed. Seven years later, in 1987, these corporations voluntarily reported only 61 percent—a 25-percent decrease from 1980. The only way IRS could detect this noncompliance was by auditing corporate tax returns. But audit coverage had also declined. In 1990, IRS audited about 2.6 percent of all corporations, which was substantially less than the 6.5 percent corporate audit coverage it had in 1980. Further, audits are costly and IRS research studies have shown that without information returns, an audit will detect only about one-third of the income that taxpayers fail to report. However, unlike individuals, the law does not require that information returns be submitted on income earned by corporations.

Matching information returns to individual tax returns has proven to be a highly cost-effective way of bringing in billions of dollars in tax revenues to the Treasury while at the same time boosting voluntary compliance by individuals. GAO expressed the belief that similar results would occur if the law required information returns on income earned by corporations and if IRS developed a program to match these documents to corporate tax returns. Recognizing start-up costs of $70 million plus annual operating costs of $70 million, GAO estimated that a limited corporate document matching program involving interest, dividends, rents, royalties, and capital gains would generate about $1 billion in additional revenue. An expanded program that included more types of unreported corporate income could generate even more revenue. Given IRS' experience with the growth of the individual document matching program, the ratio of revenues to costs should only improve.

GAO recognized that corporate taxpayers and payors submitting information returns would experience some additional burden and might have to make changes to their accounting records and other information systems. A key to obtaining the cooperation and the compliance of these

two groups is to see that they have adequate lead time to make an orderly conversion from their existing systems.

In a September 1991 report to the Subcommittee Chairman, GAO provided an analysis of steps needed to make the program a reality. First, Congress needs to pass legislation that would require payments to corporations be reported on information returns and appropriate the necessary funds for IRS to implement the program. Because such a reporting requirement can create burdens on the business community, it is important for IRS to take steps to ease these burdens and facilitate the reporting and matching of payments. For example, IRS could phase in the reporting requirement and document match over several years and slowly expand the program as IRS and the business community learn from their initial experiences. The report contained an appendix that provided more detail on these options along with analyses of other related issues of interest to the Subcommittee.

Summary of Related Action(s)

Since July 1991, IRS has been doing follow-up work on a pilot program involving corporate information returns. As part of that effort, IRS has talked to payors about implementation problems and tried to identify Payor Master File data on payors who voluntarily sent in information returns on payments to corporations.

Related GAO Product(s)

GAO/T-GGD-87-4, 03/17/87; GAO/GGD-88-102, 07/22/88; GAO/GGD-88-110, 09/06/88; GAO/GGD-90-38, 05/29/90; GAO/GGD-90-90, 06/05/90; GAO/T-GGD-91-40, 06/10/91; and GAO/T-GGD-91-20, 06/25/91

Collecting Back Taxes: IRS Phone Operations Must Do Better

GAO/IMTEC-91-39, 06/18/91

In a report to the Chairman of the Senate Committee on Governmental Affairs, GAO discussed IRS' Automated Collection System (ACS). This system, which was phased in during 1983 and 1984, is an automated one that IRS employees at 23 call sites use to telephone delinquent taxpayers, receive calls from taxpayers, and retrieve information from the taxpayers' accounts.

GAO concluded that while ACS was working better than the manual system it replaced, it had not shown any significant improvement since 1985 and was not working as well as it should. For example, calls were not being made to taxpayers when they were likely to be home because most call sites were not open evenings and weekends. Also, call site staff spent too much time doing things other than working on tax cases. During fiscal year 1990, call site employees spent 52 percent of their time on leave, in training, working on administrative matters, or managing rather than working on collecting delinquent taxes.

GAO said that IRS' organization made it hard for IRS headquarters to fix these problems. Its organization had led to different ways of operating the call sites and to limited communication between the sites and headquarters, including basic and consistent ways to measure call site performance.

GAO pointed out that (1) more automation could help ACS by dialing numbers automatically and forwarding answered calls to call site employees or by screening and routing incoming calls and (2) ACS staffing had increased in fiscal year 1991 and another increase was expected in fiscal year 1992. GAO cautioned, however, that adding more people or more automation would not solve all the problems facing the call sites. These problems can be solved only by IRS analyzing call site operations, developing the right kind of data to measure and compare performance, and recognizing that it may need to fundamentally change its operation.

Recommendation(s)

The Commissioner of Internal Revenue should implement at all ACS call sites (1) automation for making outgoing calls and for receiving and directing incoming calls and (2) standard hours of operation.

The Commissioner should also expeditiously establish measurements, such as a target overhead rate, to evaluate the performance of call sites. Private collection agencies should be used to help do this and to look at

call site operations and identify specific management, technological, operational, and organizational changes that would improve the collection of back taxes.

Action(s) Taken and/or Pending

IRS agreed with GAO's recommendations. IRS has been working on a new system to receive and direct incoming calls more efficiently, which will include the improvements recommended. A test will be conducted and completed by September 30, 1992. If it is successful, a Request for Proposal will be prepared and the system will be implemented by March 1994.

The monitoring of standard hours of operation at ACS call sites has been completed. All call sites will be in compliance with the extended work week in fiscal year 1992.

IRS plans to continue its effort to establish meaningful measurements of ACS productivity and levels of service. IRS is developing baselines to measure inventory turnover, percentage of productive hours, and time to close a case. In addition, IRS has agreed to explore the feasibility of conducting a joint study of its ACS operation with private firms as a further way to improve its collection of delinquent taxes. The feasibility of this study will be determined in fiscal year 1992.

Related GAO Product(s)

GAO/T-IMTEC-91-8, 06/25/91

Negligence and Substantial Understatement Penalties Poorly Administered

GAO/GGD-91-91, 07/03/91

IRS may assess a negligence penalty if a taxpayer demonstrates disregard of rules and regulations, including failure to make a reasonable attempt to comply with the provisions of the Internal Revenue Code and failure to exercise the level of care that a reasonable and ordinarily prudent taxpayer would use under the circumstances. A substantial understatement penalty can be assessed against individual taxpayers if the understatement of tax exceeds the greater of $5,000 or 10 percent of the corrected tax.

At the request of the Chairman of the Subcommittee on Private Retirement Plans and Oversight of IRS, Senate Committee on Finance, GAO reviewed IRS' administration of the negligence and substantial understatement penalties. On the basis of a sample of audit case files from three IRS districts, GAO evaluated (1) whether the negligence and substantial understatement penalties had been assessed in accordance with IRS policies and procedures, (2) whether IRS' internal controls were adequate to ensure proper assessment of these penalties, and (3) how IRS might better improve its administration of these penalties.

GAO said that the purpose of the negligence and substantial understatement penalties in enhancing compliance was being undermined by errors IRS was making during its administration of these penalties. In the districts reviewed, GAO estimated that about one-third of the cases contained erroneous penalty determinations because IRS generally was too lenient and either did not assess penalties that were warranted or assessed penalties that were too small. GAO's findings mirrored those contained in two earlier IRS internal audit reports.

The high error rate was puzzling because GAO found IRS guidance to examiners adequate, and the cases generally did not involve complex tax law issues. In addition, IRS had in place a system of internal controls that, if properly implemented, should have identified and corrected the problems GAO identified. However, GAO estimated that over 60 percent of the cases in the universe were reviewed within IRS at least once without the errors being corrected.

IRS officials cited various factors that could have caused the problems GAO found, including emphasis on other parts of the examination, work load pressures, and staff turnover and inexperience. Although these factors may have contributed to the problem, GAO believed the fundamental cause

might have been the attitude of examination personnel about the value of pursuing penalties in relation to other examination issues. GAO concluded, therefore, that an effective solution to the problem should include a change in staff attitude regarding penalty administration overall. GAO pointed to IRS' Quality Improvement Program as an appropriate vehicle for achieving that change because of the program's premise that employee involvement in problem analysis is more likely to result in the determination of root cause and successful solutions.

GAO also found that, in an estimated 76 percent of the cases in GAO's universe, IRS examiners did not provide taxpayers with adequate written explanations of the particular facts, circumstances, and criteria that warranted penalties in their case.

Recommendation(s)

The Commissioner of Internal Revenue should do the following:

- Establish a National Quality Improvement Project in the examination function to clarify the root causes of the problems GAO found and to identify and implement effective solutions.
- Determine the effectiveness of the solutions through a subsequent review of selected examination cases, both with and without penalty assessments. These reviews should focus on the documentation and appropriateness of the penalty decisions so as to determine how well penalties are being administered by the district and the effectiveness of existing internal controls.
- Take actions to ensure that the negligence and substantial understatement penalty explanations in IRS' examination reports provide taxpayers with the specific facts, circumstances, and criteria that warrant assessment of the penalty.

Action(s) Taken and/or Pending

IRS has assigned responsibility for determining the root causes of the problems GAO identified to its Civil Penalties Task Force. IRS plans to review the effectiveness of the solutions through an organization it expects to establish in the examination function in fiscal year 1992. This organization will handle cross-functional national penalty administration, including negligence and substantial understatement penalties. In addition, IRS plans to (1) revise its penalty explanations in the examination reports provided to taxpayers and (2) complete this action in 1992.

Related GAO Product(s)

GAO/GGD-90-32, 12/22/89 and GAO/GGD-91-12, 01/07/91

IRS Experience Using Undercover Operations' Proceeds to Offset Operational Expenses

GAO/GGD-91-106, 07/03/91

This report responded to section 3301 of the Crime Control Act of 1990. Section 3301 required that GAO study IRS undercover investigative operations that were done using the authority provided in section 7608(c) of the Internal Revenue Code of 1986. This authority exempts IRS undercover operations from certain laws and allows IRS to use the proceeds from the undercover operation to offset necessary and reasonable expenses incurred in the operation. The Crime Control Act required that GAO evaluate (1) IRS' use of the proceeds in these operations (2) the operations' results, and (3) IRS' financial audits of the operations.

GAO reported that IRS had made limited use of the offset authority, which was due to expire on December 31, 1991. From November 1988 through May 1, 1991, IRS had approved the use of the offset authority in only 19 of its undercover operations—less than 5 percent of the total undercover operations initiated for the same period.

The 19 undercover operations using the offset provision had produced about $545,000 in income. Of the income earned, approximately $121,000 was used to offset operational expenditures; $269,000 had not yet been offset against expenditures; and about $155,000 had been returned to the general fund. IRS reported that as of May 1, 1991, undercover operations using the offset provision had resulted in the seizure of over $207 million in cash and significant amounts of drugs, including cocaine and heroin, and 75 convictions.

GAO noted that identifying a direct cause and effect relationship between the financing mechanism provided by the offset authority and the results of a given investigation was difficult, if not impossible, because many variables came into play. However, GAO concluded that the additional funds made available through the use of the offset provision allowed IRS to either undertake more investigations than it could without those funds or to expand the range of activities for each investigation.

GAO raised questions about IRS' control over funds. None of the operations involving the offset provision had met the statutory criteria requiring a detailed financial audit. In some cases, IRS Internal Audit might not have sufficient access to all the information needed to do a thorough audit because it did not have complete access to information on investigations done under the control of a grand jury. Thirteen of the 19 operations using the offset authority were grand jury cases.

Further, GAO believed that IRS' use of Internal Audit to audit undercover operations using the offset provision should not be limited to those operations meeting a specific dollar threshold. IRS' use of Criminal Investigation Division employees to do audits of offset operations in which activity fell below the prescribed dollar thresholds raised questions of organizational independence, a general standard for government auditing. GAO said that such questions could be avoided by having Internal Audit do all the audits. In addition, the sensitivity of the activities being undertaken and the exemption of the expenditures from normal controls over appropriated funds increased the need for the audits to be done by an independent entity.

GAO also said that Congress' understanding of the use and results of undercover operations involving the offset provision could be enhanced if IRS' reports to Congress contained additional details and were more timely.

Matter for Congressional Consideration

Should Congress decide to extend the offset authority, it might also wish to revise the current IRS reporting requirements. GAO said that (1) expanding the information IRS is required to include in its annual reports to Congress and (2) requiring IRS to report the results of its detailed financial audits after the covert phase of the operation instead of when the operation is closed could provide Congress with more timely and complete information on undercover operations involving offsetting. Such reporting should not jeopardize undercover agents' safety or the success of criminal proceedings.

Recommendation(s)

The Commissioner of Internal Revenue should direct the Chief Inspector to ensure that Internal Audit expands its financial audits to include all undercover operations involving offsetting, regardless of the amount of expenditures or proceeds.

Action(s) Taken and/or Pending

The offset authority expired on December 31, 1991, thereby rendering our recommendations moot.

Efforts to Prevent, Identify, and Collect Employment Tax Delinquencies

GAO/GGD-91-94, 08/28/91

This report is one in a series responding to a request from the Chairman, Subcommittee on Oversight, House Committee on Ways and Means, dealing with IRS' accounts receivable inventory. This report addresses IRS' efforts to prevent, identify, and collect employment tax delinquencies.

Federal employment taxes include Social Security and unemployment taxes owed by employers and employees' Social Security and income taxes withheld for the government by employers. At the end of fiscal year 1990, delinquent employment taxes accounted for about $29.7 billion, or 3 percent, of the $96.3 billion accounts receivable balance. Over two-thirds of all federal tax revenue is collected through employment taxes. In fiscal year 1989, employment taxes accounted for $707 billion, or about 70 percent, of the $1 trillion in federal gross tax receipts. Each year, howeve businesses fail to pay billions of dollars in employment taxes. Nonpaymei of employment taxes poses significant problems for IRS and is costly to th government.

Failing businesses have used nonpayment of employment taxes as a mear to avoid or delay going out of business. As a result, financially troubled businesses with large payrolls can quickly accumulate large delinquencie that are difficult, if not impossible, for IRS to collect. In addition, not only does the government lose the money it is owed, but it also provides full credit and benefits to the employees just as if the taxes had been paid. In some cases, money is refunded to employees for withheld income taxes that were never paid.

Considering the significance of employment tax delinquencies and the quickness with which large employment tax delinquencies can accumulate, the prevention, early identification, and collection of these delinquencies are critical. At the time of GAO's review, however, IRS did no have a centralized effort for preventing, identifying, or collecting delinquent employment taxes. Efforts were scattered throughout the various functional areas of the agency with no central focus or assigned responsibility. Thus, IRS could not ensure that its resources were effectively allocated to address employment tax delinquencies.

Moreover, IRS had not developed all the information necessary to (1) targe its efforts at employers most likely to be delinquent or (2) evaluate the effectiveness of its employment tax delinquency efforts. GAO found that, because of these conditions, IRS' efforts to prevent, identify, or collect

employment tax delinquencies might not have been as effective as they could have been. IRS had not done enough to prevent employment tax delinquencies. One reason is that IRS had insufficient information on the characteristics of delinquent taxpayers to determine the reasons for the delinquencies. GAO also found that one of IRS' two primary prevention programs—the Federal Tax Deposit Alert Program—(1) was not targeted at those most likely to be delinquent, (2) produced numerous unproductive alerts, and (3) might not have had any significant effect on promoting employment tax compliance for the period the alert had been issued or subsequent periods.

GAO said that limited staff resources constrained the effectiveness of IRS' efforts to identify employment tax delinquencies through audit and information matching. This constraint also prevented IRS from investigating many of the leads and cases brought to its attention. In addition, the number of employment tax audits done by IRS' examination function fell from 109,000 in 1979 to a low of about 24,000 in 1988 before rising to 42,000 in 1990.

Programs to collect employment tax delinquencies were not effective because they were generally untimely or used infrequently. For example, one collection program typically assessed taxpayers 2-1/2 years after the delinquency occurred. Another program was rarely used because, according to IRS officials, it was extremely labor intensive and taxpayers who did not comply with the program's requirements were rarely prosecuted.

GAO believes that IRS needs to develop a comprehensive plan to deal with employment tax delinquencies. GAO said the plan should designate an official to coordinate the activities of the various functional areas and develop the information needed to better target employment tax efforts and evaluate and improve effectiveness.

Recommendation(s)

The Commissioner of Internal Revenue should develop a comprehensive plan to prevent, identify, and collect employment tax delinquencies. The plan should coordinate efforts among all IRS functions. The Commissioner should designate an official to oversee execution of the plan and the various programs involved. The plan should include development of the information necessary to (1) define the characteristics of employers who are delinquent in paying employment taxes; and (2) measure the effectiveness of IRS' programs to prevent, identify, and collect employment

tax delinquencies. Specifically, the plan should address how IRS will find answers for the following questions raised in our review:

- What are the major characteristics of employment tax delinquents and th reasons for delinquencies? What prevention programs are needed to deal with them?
- What specific changes are needed to improve the effectiveness of the Federal Tax Deposit Alert Program?
- What is the reason for the large number of unproductive cases generated through the Combined Annual Wage Reporting Program, and how can thi program be made more effective?
- Are the employment tax adjustment and examination programs more effective than other employment tax identification programs and, if so, how should resources be reallocated to take advantage of this?
- How can IRS improve the timeliness and effectiveness of its monthly filing special trust accounts, and 100-percent penalty procedures to more effectively resolve employment tax delinquencies?
- If the current procedures and programs are not effective and cannot be improved, what alternatives are needed?

Action(s) Taken and/or Pending

IRS agreed that (1) improving employment tax compliance is one of the most important challenges it faces in administering the tax system and (2) a comprehensive strategy is needed to improve compliance with employment tax laws. IRS said that it is responding to GAO's recommendations through its Compliance 2000 Program and related studies, which are under the jurisdiction of the Chief Operations Officer, and which IRS believes will provide the comprehensive oversight recommended in GAO's report.

Related GAO Product(s)

GAO/GGD-78-14, 02/21/78; GAO/GGD-89-21, 12/14/88; GAO/GGD-89-94, 08/21/89; GAO/GGD-89-107, 09/25/89; GAO/GGD-90-102, 07/31/90; GAO/T-GGD-91-2, 10/18/90; and GAO/T-GGD-91-59, 07/24/91

Money Laundering: The Use of Cash Transaction Reports by Federal Law Enforcement Agencies

GAO/GGD-91-125, 09/25/91

In a report to the Chairmen of the Senate Committee on Finance and the House Committee on Ways and Means, GAO discussed the issue of large cash transactions reported on IRS Form 8300, Report of Cash Payments Over $10,000 Received in a Trade or Business. Any person engaged in a trade or business who receives over $10,000 in cash payments in one transaction or two or more related transactions is required to report the transaction to IRS on Form 8300. The information is used in investigations of tax evasion and in investigations of other criminal activity, such as money laundering.

Sections 3302 and 3303 of the Crime Control Act of 1990 require GAO to report on (1) the use of the reports by federal agencies for law enforcement purposes, (2) the number of cases in which a criminal penalty has been sought for willful failure to file these reports, and (3) any change in the effectiveness of the penalty by reason of legislation enacted in 1990 that reclassified the offense from misdemeanor to felony. This report complies with these requirements.

During the 1-year period ending April 1991, federal law enforcement agencies accessed more than 15,000 Forms 8300 that had been filed with IRS. Federal law enforcement agencies use the information contained in the reports to (1) identify suspicious transactions that might involve money laundering and (2) support ongoing investigations of other criminal activity. Law enforcement agencies may also use the reports when investigating the possibility of seizing goods purchased with the proceeds of illegal activity. In some cases, the reports can help identify and locate such goods.

In the 18-month period ending March 1991, IRS recommended 3,880 penalties for failure to file the report or for providing false or incomplete information on the report. All but 80 of these were civil penalties. IRS officials said that all of the 80 criminal penalties were for willful failure to file a report.

In November 1990, willful failure was reclassified as a felony rather than a misdemeanor. The maximum sentences for the offense, however, were not affected by the reclassification. GAO could not determine what impact, if any, the reclassification had on the penalty's effectiveness. Information on whether the reclassification might have created an additional incentive for compliance with the reporting requirement was not available. IRS officials

said that it is possible that the penalty might have been recommended more often had the offense been a felony. However, information was not available to confirm this perception.

The number of reports filed each month increased at a faster rate after th offense was classified a felony. IRS attributed the increase to a number of factors but primarily to substantial increases in enforcement activity. IRS officials said that they did not believe the reclassification had any significant effect on improving compliance with the reporting requiremer

Related GAO Product(s)

GAO/GGD-91-53, 03/18/91 and GAO/NSIAD-91-130, 05/16/91

Opportunities to Increase Revenue Before Expiration of the Statutory Collection Period

GAO/GGD-91-89, 09/30/91

This is another in a series of reports requested by the Chairman, Subcommittee on Oversight, House Committee on Ways and Means, relating to IRS' accounts receivable. This report deals with the accounts receivable that are written off because the statute of limitations[2] has expired. Specifically, the report provides information on (1) the amount of 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. The report also discusses IRS' procedures for managing accounts receivable that are nearing the end of their collection periods.

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 limitations expired has grown steadily over the past 5 years. GAO estimated 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.

Using disposition rates calculated on the basis of unaudited disposition information, by age of account, for the September 30, 1989, accounts receivable balance, GAO 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. GAO did not assess the reliability of IRS' disposition information. However, GAO 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. GAO said that there is much uncertainty about the reported accounts receivable balances. As part of another job it is doing,[3] GAO will verify IRS' accounts receivable balance and provide an audit opinion on the collectibility of the accounts receivable through detailed audit work.

[2]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.

[3]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.

One of the purposes of the report was 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 th growing accounts receivable balance, GAO's initial projection of collection and write-offs would help Congress gain a better perspective on IRS' collection effort.

Although it did not evaluate the effectiveness of IRS' collection policies an procedures, GAO noted two areas where IRS could improve its oversight an 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 systemi 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.

Recommendation(s)

The Commissioner of Internal Revenue should

- 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 currently not collectible 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 (those awaiting assignment to revenue officers) to increase collections of these accounts receivable.

Action(s) Taken and/or Pending

IRS agreed with two of GAO's recommendations. IRS did not agree with GAO' recommendation to develop more specific information about accounts written off because IRS believes that its current management information and recent special studies provided significant and useful information about these accounts, and IRS is using this information to perfect the validity of the accounts receivable inventory.

In 1992, IRS is planning to issue procedures to send reminder notices on cases assigned to the collection queue. In addition, IRS (1) began collecting data for a centralized National Office review system of currently not collectible decisions and (2) completed an extensive study of the entire currently not collectible inventory and began implementing program changes recommended by that study. IRS said that these changes, which included conducting delinquency checks on employment tax returns sooner and developing a scoring system to predict collectibility, were aimed at reducing the currently not collectible inventory by reducing invalid assessments. IRS believes that preventing invalid assessments from entering the inventory will have a greater impact over the long run than identifying and removing invalid assessments already in the inventory.

Related GAO Product(s)

GAO/GGD-90-19, 02/20/90; GAO/T-GGD-91-17, 03/20/91; and GAO/T-GGD-91-20, 06/25/91

General Management

IRS' 1990 Filing Season Performance Continued Recent Positive Trends

GAO/GGD-91-23, 12/27/90

In response to a request from the Chairman, Subcommittee on Oversight, House Committee on Ways and Means, GAO reviewed IRS' performance in processing returns and related refunds during the 1990 tax return filing season. GAO also assessed IRS' performance in helping taxpayers file their returns by (1) supplying them with tax forms, instructions, and publications; and (2) providing toll-free telephone assistance to answer their tax law questions.

GAO concluded that IRS generally enjoyed a successful 1990 filing season. First, IRS offices visited by GAO usually had tax materials on hand, and, in most instances, IRS accurately filled GAO's phone and mail orders for tax materials. Second, IRS' and GAO's tests showed that the accuracy rate for answering taxpayer questions about the tax law improved substantially over 1989. Finally, returns processing improved over 1989, continuing a strong showing dating back to 1988.

Although the 1990 filing season went well for IRS overall, there were some minor trouble spots. Delivery time for some of the tax materials GAO ordered by mail took longer than IRS told taxpayers to expect, and more taxpayers received busy signals in 1990 than in 1989 when they telephoned to order materials or ask tax law questions. GAO noted that any improvement in those areas in 1991 would likely depend on the availability of additional staff.

GAO also noted that the test IRS made in 1990 to assess its ability to fill taxpayers' phone and mail orders for tax materials was methodologically flawed, preventing it from setting goals for 1991 based on its 1990 performance.

Recommendation(s)

To provide a measure of quality in supplying taxpayers with tax materials, IRS should develop and implement a statistically valid survey of its ability to fill phone and mail orders. The survey should (1) correct the problems that GAO identified with IRS' 1990 test; (2) include measures that are consistent from year to year, thus allowing measurement of performance over time; and (3) provide the basis for establishing annual goals.

Action(s) Taken and/or Pending

IRS revised its testing procedures and GAO tested these procedures as part of its review of the 1991 tax return filing season (see p. 76). GAO found that the new methodology provided an accurate assessment of the tax material distribution program's performance.

Related GAO Product(s)

GAO/GGD-89-2, 11/14/88; GAO/T-GGD-89-12, 03/16/89; GAO/GGD-90-37, 01/04/90; GAO/GGD-90-34, 01/10/90; GAO/T-GGD-90-26, 03/22/90; GAO/GGD-90-120, 08/31/90; GAO/GGD-91-66, 03/20/91; GAO/T-GGD-91-17, 03/20/91; GAO/IMTEC-91-42, 06/20/91; and GAO/GGD-91-98, 06/28/91

BATF: Management Improvements Needed to Handle Increasing Responsibilities

GAO/GGD-91-67, 03/19/91 and GAO/T-GGD-91-19, 03/20/91

In a report to and testimony before the Subcommittee on Oversight, Hous Committee on Ways and Means, GAO (1) discussed how the duties of the Bureau of Alcohol, Tobacco and Firearms (BATF) had changed and (2) provided its views on steps BATF could take to use resources more efficiently.

BATF operates on an annual appropriation of about $300 million and has about 4,000 staff years divided between its two major components—Compliance Operations and Law Enforcement. Complianc Operations regulates the alcohol, tobacco, firearms, and explosives industries and collects related excise taxes. One way it regulates the alcohol industry, for example, is by testing samples of products on the market. In fiscal year 1990, BATF collected $5.8 billion in alcohol excise taxes; $4.3 billion in tobacco excise taxes; and $130 million in special occupational taxes imposed on businesses that sold alcohol, tobacco, and firearms. Law Enforcement is responsible for enforcing federal firearms and explosives laws. It investigates such things as firearms trafficking, large-scale thefts of firearms, and terrorism, and it helps local law enforcement agencies investigate arson involving interstate commerce.

GAO reported that BATF's duties had increased over the past few years. Its law enforcement efforts in the firearms area had grown, for example, as it expertise became critical to the government's antidrug effort. BATF had also assumed several new compliance duties, including (1) the collection of special occupational taxes, which it assumed from IRS in July 1987; (2) the testing of alcoholic beverages in response to consumer complaints, which it assumed from the Food and Drug Administration in November 1987; and (3) the collection of firearms and excise taxes, which it assume from IRS in January 1991.

With its additional duties, BATF had to make trade-offs in deciding how best to use its staff. One result of those trade-offs was a reduction in tax compliance inspections of alcohol producers. GAO expressed concern about the effect of BATF's reduced compliance presence. That concern wa heightened by the fact that compliance inspections were being done by inspectors who were not required to have any accounting expertise. BATF recognized the need for such expertise and said it was considering requiring inspectors to have 6 credit hours of college-level accounting before being promoted to the journeyman level. Considering the nature of compliance inspections and the findings of other groups, such as a BATF

task force and consultant who commented on the issue, GAO believed that 12 hours might be more appropriate.

GAO identified other steps that BATF could take to enhance its operational efficiency.

- The use of standard work plans for compliance inspections would help ensure that a minimum amount of work is done at each inspection, work tasks are clearly set forth, and inspections are done on the basis of current policy. BATF acknowledged the need for standard work plans in response to a 1984 consultant's report but had not finished developing them at the time of GAO's study.

—In deciding what to include in its sample test of alcohol products on the market, BATF could target its resources more effectively by analyzing data not only from recent tests but also from those done over a period of several years. The use of several years of test results would enable BATF to better analyze trends.

- BATF would also be better able to handle its work load and make necessary trade-offs if it had better data with which to assess its performance and to provide a basis for determining future directions. Information on compliance, such as the number of facilities inspected, is an example of data that would be useful. Also helpful would be data on the efficiency, quality, and timeliness of BATF's law enforcement efforts.

Recommendation(s)

The Director of BATF should ensure that the following actions are taken:

- Increase the availability of accounting expertise for use on tax compliance inspections. Options BATF might consider include requiring that inspectors have 12 hours of college level accounting credits before being eligible for promotion to journeyman level or changing the inspector/auditor staffing mix by hiring auditors to fill vacated inspector positions.
- Develop a series of standard work plans for the various types of compliance inspections.
- Correct problems that impede the use of laboratory data in the market basket sampling program and, once this database is available, develop a management information system to target products for inclusion in the test samples.

- Develop more comprehensive performance measurement systems for Compliance Operations and Law Enforcement that include measures of quality, timeliness, and efficiency.
- Periodically measure the extent of compliance with the excise taxes for which BATF is responsible.

Action(s) Taken and/or Pending

BATF generally agreed with GAO's recommendations. BATF said that 61 percent of its inspectors (1) had at least 6 credit hours of college accounting and (2) took two internal training courses, which BATF said were equivalent to another 6 credit hours of accounting. Thus, BATF felt that its inspectors had sufficient accounting experience.

BATF also said that it (1) expected to have all standard work plans issued by June 1992; (2) was working on correcting problems that impeded the use of laboratory data in the market basket sampling program; and (3) agreed with the need for better management information systems and the need to periodically measure the level of taxpayer compliance.

Related GAO Product(s)

GAO/GGD-86-49, 06/05/86; GAO/GGD-89-52, 05/09/89; and GAO/GGD-90-123, 09/27/90

IRS Needs to Improve Certain Measures of Service Center Quality

GAO/GGD-91-66, 03/20/91

In response to a request from the Chairman, Subcommittee on Oversight, House Committee on Ways and Means, GAO provided information on steps that IRS was taking to monitor and improve the quality of various service center activities. GAO focused on three specific activities: (1) the quality of correspondence with taxpayers about adjustments to their accounts, (2) the extent to which IRS errs in processing tax returns, and (3) the accuracy of notices sent to taxpayers informing them about changes made to their returns during processing.

GAO said that IRS appeared to have improved the quality of correspondence it sends taxpayers to tell them about adjustments to their accounts. IRS statistics showed that the percentage of IRS letters with critical errors decreased from 38 percent in February 1989 to 14 percent in August 1990.

IRS' progress in improving the accuracy with which it processes tax returns was less clear. The data IRS used to monitor its progress in improving processing quality showed a decrease in error rates from 23 percent in 1988 to 18 percent in 1990. This error rate was not a valid indicator of IRS' processing quality, however, because it (1) included errors made by taxpayers and (2) counted as errors things that were not errors. IRS' progress in improving the quality of its processing performance was further clouded by the fact that service centers had been making the same types of processing errors year after year. IRS had begun studying ways to reduce some of those recurring errors in the hopes of having solutions in place for the 1991 filing season. Reports on those projects had not been finalized as of January 1991.

IRS lacked an effective measure of the accuracy of notices it sends taxpayers. Output review—the service center unit that reviews notices for accuracy—selected notices for review primarily on the basis of the historical probability of that type of notice having an error. While that strategy helped target limited resources toward the most error-prone notices, it did not provide IRS with a valid measure of the accuracy of all notices. Moreover, the opportunity to reduce errors on notices was hampered at the two service centers GAO visited. Output review units at the centers were not following IRS procedures directing them to report identified errors to the managers of units originating the notices.

Recommendation(s)

To better assess its returns processing performance, IRS should (1) use an indicator to measure returns processing quality that identifies the extent t which returns are being sent to error resolution specifically because of errors made by service center staff in processing returns and (2) measure the overall quality of returns processing notices rather than just those that are referred to output review. To help fund the development of such indicators, IRS should reconsider how it spends the money currently available for service center quality control efforts and assess how the quality data it now collects might be used to help build the needed indicators.

IRS should also (1) compile data on output review results in a way that enables management to identify specific problems that need to be addressed and (2) ensure that the results are so used.

Action(s) Taken and/or Pending

IRS has begun reporting information on returns processing errors in a way that segregates IRS errors from taxpayer/preparer errors and more specifically identifies the source of IRS errors. IRS said that (1) it would be developing quality standards for taxpayer notices by the end of fiscal year 1992 and (2) budgetary constraints prevented it from expanding its review of notices in fiscal year 1991. IRS also said that it had redesigned its notice disposition reporting system and expected full implementation in 1992.

Related GAO Product(s)

GAO/GGD-88-101, 07/13/88; GAO/T-GGD-91-17, 03/20/91; and GAO/GGD-91-98, 06/28/91

Managing IRS: Important Strides Forward Since 1988 but More Needs to Be Done

GAO/GGD-91-74, 04/29/91

IRS faces many challenges including (1) a burgeoning work load that threatens the capacity of its antiquated computer systems, (2) increasing demands to do more at a time of fiscal austerity, and (3) a quest for solutions to a tax gap of over $100 billion in taxes owed but not paid and a growing accounts receivable inventory. In October 1988, GAO recommended steps to help IRS meet those challenges. In this April 1991 report, GAO discussed IRS' progress in implementing those recommendations that GAO believed would have the greatest impact on improving efficiency, managerial accountability, and quality.

GAO reported that since 1988, IRS had taken steps to establish a leadership framework that would better enable it to address the challenges it faces. Some of the more important steps were establishing the positions of Chief Financial Officer (CFO), Controller, and Chief Information Officer and establishing a business review process. By taking these important steps, IRS had mechanisms in place that provided a solid foundation for future advances. A CFO and Controller gave IRS the leadership to meet long-standing financial management challenges. A Chief Information Officer provided the leadership to guide IRS through a major modernization of its information systems. And business reviews would help IRS measure performance in its field offices and hold managers accountable for meeting IRS-wide goals.

GAO identified actions that IRS needed to take to better ensure that those mechanisms are effective. For example, if IRS' new financial leadership was to successfully deal with the financial challenges facing IRS, it had to be responsible for all of IRS' financial matters. Such was not the case when GAO issued its report in April 1991. At that time the CFO and Controller were primarily responsible for administrative accounting matters. Responsibility for accounting activities relating to about $1 trillion in annual tax revenues rested elsewhere in IRS. GAO also said that (1) if the Chief Information Officer was to successfully guide modernization, IRS needed to support him by enhancing the technical expertise of its senior managers and executives; and (2) before IRS could effectively measure performance and hold managers accountable, it had to develop measurable performance goals—an end to which IRS is working.

While citing IRS' progress in developing an agencywide strategic planning process, GAO was not as positive about IRS' progress in developing a plan for identifying and meeting its future human resource needs. According to

milestones in IRS' Strategic Business Plan, IRS was several years away from developing the data needed to construct a human resource management plan. The Strategic Business Plan called for redefining, by September 1994 the required occupations and skills needed to carry out IRS' mission. Until then, IRS will be unable to develop a plan that lays out specific steps to recruit, train, and retain the right kinds of people.

Recommendation(s)

The Commissioner of Internal Revenue should ensure that IRS (1) reconsiders the milestones it has established for the human resource related strategies in its Strategic Business Plan with a view toward bringing a greater sense of urgency to that effort; (2) revises its internal reports on the status of GAO's October 1988 recommendations to accurately reflect its lack of progress in developing a human resource management plan; and (3) develops and implements, as a priority, a strategy for providing additional technical expertise at senior decisionmaking levels—a strategy that should include an assessment of IRS' needs for additional technical experience and a program to satisfy those needs.

GAO also recommended that the Commissioner of Internal Revenue (1) transfer responsibility for revenue accounting activities to the CFO and the Controller and (2) ensure that the Assistant Commissioner for Procurement Services adopts as one of his priorities the development of software to manage ADP contract obligations.

Action(s) Taken and/or Pending

IRS revised its internal reports to more accurately show the status of its efforts toward developing a human resource management plan. IRS (1) still believed that the September 1994 target date was reasonable considering the task's complexity and the resources available; and (2) was considering options for improving the technical expertise of its managers and executives, including a program involving the Maxwell School at Syracuse University. IRS did not transfer revenue accounting responsibilities to the CFO and the Controller. Instead, IRS (1) established and staffed an Account Receivable Executive position reporting directly to the CFO; and (2) said that person would, at least initially, focus on establishing better management information and would implement strategies to limit growth of uncollectible receivables. IRS also said it (1) was assigning priority attention to software development and (2) was bringing in a contractor to help.

Related GAO Product(s)

GAO/GGD-89-1, 10/14/88; GAO/IMTEC-90-13, 02/08/90; GAO/GGD-90-45, 03/08/90; and GAO/T-GGD-91-20, 06/25/91

Public Service: How Effective and Responsive Is the Government?

GAO/T-HRD-91-26, 05/08/91

In testimony before the House Committee on Ways and Means, GAO presented its views on the effectiveness of government programs. GAO wa responding to one of the Committee's major concerns: whether the American people were getting their money's worth from the federal government. GAO said that a lot will be required of the government and its managers to operate more efficiently and effectively in the years ahead, but positive signs are on the horizon. In general, GAO said that the problems of the government are its management, and not its people.

To improve management, GAO said agencies (1) need to develop strategie such as long-range plans and sound financial systems, to overcome disruptive effects of leadership changes; and (2) must become accustome to operating with the customer's needs in mind and to measure performance accordingly.

As an example of improving the quality of serving the public, GAO cited IR as having improved the accuracy rate of its telephone responses to taxpayer questions from 66 to 81 percent in fiscal years 1989 to 1990. Unfortunately, the trade-off was that the likelihood of a taxpayer successfully contacting a tax assistor decreased from 61 to 42 percent. From a taxpayer's standpoint, the definition of acceptable public service would be a successful contact and a correct answer every time. Thus, recent improvements in one dimension were offset by the deterioration i another service, and both are still in need of improvement.

GAO said that IRS has also taken steps to improve the quality of its correspondence and begun to monitor that quality more closely. IRS reports the rate of serious errors dropped from 38 percent in fiscal year 1989 to 14 percent in fiscal year 1990. While that improvement is noteworthy, millions of taxpayers still received erroneous information la year.

GAO also said that the taxpayers' ability to comply and IRS' ability to carry out its responsibilities are greatly affected by the complexities of the law. Areas GAO recently examined include

- the federal tax deposit requirements for withheld income and Social Security taxes, in which complexity makes it difficult for employers to comply with the requirements and for IRS to administer the deposit penalty; and

- other sections of the Internal Revenue Code that are particularly troublesome for IRS and corporations, such as those relating to amortizing the price of intangible assets purchased in a corporate acquisition or merger and reallocating income between foreign and domestic corporate subsidiaries.

GAO said that Congress has a long interest in service to the public, although frequently its focus is on the problems of individual constituents. While acknowledging that this perspective should continue, GAO sees a broader view as being equally important. For example, GAO said that tax simplification needs to be a major consideration in every review of the tax code because simplification is critical to improving compliance with the nation's tax laws.

GAO noted that oversight activities, such as congressional hearings, provide a vehicle for focusing on broader service questions. Through such efforts, Congress can help executive branch agencies (1) focus on these broader questions, (2) reach an understanding with Congress on the definition of what high-quality service is, (3) debate the means and strategies for achieving that quality of service, and (4) determine the resource commitments necessary for quality improvements.

Related GAO Product(s)

GAO/HRD-91-112, 09/13/91

Information on Revenue Agent Attrition

GAO/GGD-91-81, 06/10/91

This report, issued in response to a request from the Chairman of the Senate Committee on the Budget, provides information on revenue agent attrition. The Committee was interested in the extent to which revenue agents were leaving IRS, especially early in their careers, because of the potential impact of attrition on the amount of revenue that can be expected from an increase in examination staff.

GAO's analysis of IRS data showed that between March 1987 and April 1990 revenue agents left IRS at a rate of 6.5 percent a year. Data compiled by the Office of Personnel Management showed that the attrition rate for all white-collar federal employees in professional and administrative jobs was lower—about 4 percent a year during fiscal years 1987 through 1990.

GAO's analysis also showed that revenue agents hired during the study period were more apt to leave IRS during their early years of employment and that attrition was more prevalent in some of IRS' larger metropolitan field offices. Neither of those results was surprising. For example, IRS had often pointed to its inability to pay the kinds of salaries paid by the private sector as a reason for its problems in recruiting and retaining revenue agents in the more competitive metropolitan markets. The Federal Employees Pay Comparability Act of 1990, enacted in November 1990, could help alleviate this situation in some areas of the country. The act provided for, among other things, a locality-based pay system that reflects geographical variations in pay.

IRS' revised methodology for estimating the additional revenues to be derived from an increase in examination staff, which it used in conjunction with a staffing increase authorized for fiscal year 1991, did not include an offset to recognize the impact of attrition. IRS' rationale was that the amount of attrition was minimal when spread over its 63 district offices. Because GAO's results showed that certain districts were affected by attrition much more than others, IRS, at GAO's request, introduced an attrition factor into its methodology and recomputed its estimate. That adjustment did not significantly affect the revenue estimate. Using its methodology, IRS had originally estimated that the 750 revenue agent increase requested for fiscal year 1991 would generate $8.3 billion in additional revenue over 15 years. After a factor for attrition was included, that estimate was reduced by 1.6 percent, or $137.2 million.

Related GAO Product(s)

GAO/GGD-88-119, 08/08/88; GAO/GGD-90-32, 12/22/89; GAO/GGD-90-77, . 04/06/90; and GAO/GGD-90-119, 09/05/90

Management Challenges Facing IRS

GAO/T-GGD-91-20, 06/25/91

In testimony before the Senate Committee on Governmental Affairs, GAO said that IRS was at a major crossroads that demanded strong visionary leadership supported by effective information systems, state-of-the-art technology, and quality staff to ensure it could address the challenges posed as it approached the 21st century. GAO pointed to a burgeoning IRS work load that included providing assistance to over 70 million taxpayers processing over 200 million tax returns and related documents, collecting and accounting for over $1 trillion in revenues, narrowing a $100 billion a year tax gap, and dealing with a growing accounts receivable inventory o its books that was pushing $100 billion.

GAO discussed the promise posed by new management strategies emergin at IRS while noting that many issues warranted Congress' attention to ensure that IRS positioned itself to effectively address the many challenge it faced. These issues included the following:

- Strategic planning—How well do the performance objectives and measures chosen by IRS reflect and adequately measure the key dimensions of performance?
- Financial management—How adequately is the recently developed management framework supported by qualified staff, and how well does the current organizational structure promote effective financial management?
- Compliance initiatives—How could a new balance be struck between traditional compliance activities, including additional staffing, and more preventative approaches, such as tax law simplification and expanded information reporting, to improve compliance in a more cost-effective manner?
- Tax systems modernization—How well is IRS realizing the full potential o new technology to achieve management's vision of where the agency should be in the 21st century, and does Congress endorse that vision?

Related GAO Product(s)

GAO/GGD-89-1, 10/14/88; GAO/GGD-91-74, 04/29/91; and GAO/T-GGD-91-54, 07/09/91

A Generally Successful Filing Season in 1991

GAO/GGD-91-98, 06/28/91

In response to a request from the Chairman, Subcommittee on Oversight, House Committee on Ways and Means, GAO assessed IRS' performance during the 1991 filing season. Specifically, GAO looked at the accuracy and accessibility of IRS' toll-free telephone assistance, the availability of tax materials at IRS' distribution centers and walk-in offices, and the processing of returns by IRS' 10 service centers.

When compared with IRS' expectations and using indicators that GAO and IRS have historically pointed to as measures of performance, the 1991 filing season was generally successful.

- The accuracy of IRS' answers to taxpayers' tax law questions through the toll-free telephone assistance program improved from 77 percent in 1990 to 84 percent in 1991, just 1 percentage point less than IRS' goal for 1991.
- Tests by GAO and IRS indicated that taxpayers should have found tax forms and publications readily available.
- Seven service center inventories of things "gone wrong" or needing special attention during returns processing were at levels that IRS considered manageable. Also, receipts of returns, correspondence, and remittances into six of the inventories during the 1991 filing season were down from 1990.
- The percent of processing errors made by service center staff continued a downward trend that began in 1988, although certain types of errors continued to predominate.
- Returns were filed electronically by 7.5 million taxpayers, 79 percent more than in 1990 and 21 percent more than IRS had expected.
- More taxpayers filed the simpler Form 1040A than in 1990.

One area of concern was the indication from IRS' data that taxpayers continued to have difficulty reaching an IRS telephone assistor. Using information from IRS' telephone data report on the number of calls received and answered between January 1 and April 27, 1991, GAO computed an accessibility rate of 40.3 percent in 1991—up from 34.1 percent for the same period in 1990 but still considerably less than the 1989 rate of 58 percent. IRS officials said that they expect accessibility to increase as assistors become more experienced with some relatively new tools that have been made available to help them do their jobs. One such tool, for example, is a guide that IRS developed to help assistors probe for all the facts needed about a taxpayer's situation before attempting to answer the taxpayer's question. One way IRS hopes to enhance experience

is by minimizing assistor attrition and thus stabilizing the work force fror
year to year.

Related GAO Product(s)

GAO/GGD-89-2, 11/14/88; GAO/T-GGD-89-12, 03/16/89; GAO/GGD-90-37, 01/04/90; GAO/GGD-90-34, 01/10/90; GAO/T-GGD-90-26, 03/22/90; GAO/GGD-90-120, 08/31/90; GAO/GGD-91-23, 12/27/90; GAO/T-GGD-91-17 03/20/91; GAO/GGD-91-66, 03/20/91; and GAO/IMTEC-91-42, 06/20/91

Identifying Options for Organizational and Business Changes at IRS

GAO/T-GGD-91-54, 07/09/91 and GAO/GGD-91-133FS, 09/24/91

In testimony before the Subcommittee on Commerce, Consumer, and Monetary Affairs of the House Committee on Government Operations, GAO discussed the organizational and business implications of Tax Systems Modernization (TSM).

GAO expressed its strong support for IRS' modernization program and said that TSM offers the potential for great improvements in tax administration. GAO also said that IRS' Design Master Plan (1) outlined a solid technical blueprint and (2) suggested how automation of current business operations would greatly enhance service to taxpayers and promote more efficient processing of tax returns and compliance program administration. GAO noted, however, that the plan did not provide a corresponding vision of how the new technology could enable IRS to transform its future organizational structures and business operations. GAO said that although automation of current business processes should clearly provide benefits, IRS' current organizational structure and business operations—premised on outdated technology—would constrain the agency from becoming all it could be with the new tools. For example, IRS had not recognized the opportunities presented by new technology to consolidate its field office structure.

Many of these changes are actually made possible by the technical architecture selected for TSM. Several changes, however, such as consolidating or changing the functions of the existing 10 service centers, may be constrained as IRS implements its current TSM design plans. GAO expressed the belief that IRS needed to systematically examine options for major changes in business operations and be unconstrained by assumptions that limit organizational change.

As a follow-up to that testimony, GAO issued to the Subcommittee Chairman a September 1991 fact sheet, which discussed private sector modernization efforts that IRS might want to consider as part of its TSM efforts. The fact sheet provided information on the experiences of 26 private companies that had implemented computer modernizations and/or undergone organizational change. It included appendixes that (1) described the methodology GAO used to obtain information on the 26 companies it surveyed; (2) provided summary data that showed how many of these companies implemented new technologies, underwent organizational change, and underwent organizational changes that were

linked to technological changes; and (3) provided details on several of the companies GAO identified as falling into each of these categories.

Summary of Related Action(s)

In November 1991, the House Committee on Government Operations issued House Report 102-388 on the progress of IRS' modernization effort. That report included information from GAO's testimony and fact sheet.

Related GAO Product(s)

GAO/NSIAD-91-190, 05/02/91; GAO/IMTEC-91-53BR, 06/25/91; and GAO/T-GGD-91-20, 06/25/91

IRS' Administration of the International Boycott Tax Code Provisions

GAO/GGD-91-105, 07/11/91

This report responded to a request of the late Senator John Heinz for information on the administration of section 999 of the Internal Revenue Code. Section 999 was enacted in 1976 primarily to discourage participation in the Arab League's economic embargo of Israel. Section 999 required U.S. taxpayers to report their business activities with boycotting countries and denied several tax benefits to those who participated in unsanctioned international boycotts.

All taxpayers with operations in or with boycotting countries must file IRS Form 5713 to report their business activities in those countries. A fine of up to $25,000 and/or imprisonment of up to 1 year can be imposed for the willful failure to report boycott-related activities. The number of Forms 5713 filed was 1,462 in 1976; the number reached a peak of 3,738 in 1981 and then decreased in 4 of the 5 years between 1982 and 1986.

GAO reported that IRS' international examiners had audited the returns of some taxpayers who had operations in boycotting countries. According to a 1991 Treasury boycott report, tax audits of boycott issues involved an average of 350 taxpayers in 1983 and 1984. GAO estimated that the audited returns accounted for approximately 11 percent of the Forms 5713 filed in those 2 years. GAO found no evidence of a taxpayer ever being fined or prosecuted for filing late or not filing a Form 5713.

GAO noted that IRS examiners were provided boycott-related data by the Department of Commerce, which administers the antiboycott amendments of the Export Administration Act of 1979. GAO also noted, however, that the results of Commerce's boycott investigations could not be used as conclusive evidence of boycott participation in tax audits because of differences between the definitions of boycott participation in section 999 and the act of 1979. GAO also noted that IRS was prohibited by law from providing confidential tax information to Commerce officials.

Some of the taxpayers who filed Form 5713 received one or more requests to engage in boycott activities as prerequisites of doing business in the boycotting countries. The boycott activities included agreements to refrain from doing business with (1) boycotted countries, such as Israel; (2) blacklisted U.S. companies engaged in trade with Israel; or (3) companies whose owners or managers are of a particular nationality, race, or religion. There were 6,335 reported boycott requests in 1976, 17,439 in 1978, and 11,246 in 1986. Requests to refrain from doing business with or employing

individuals of a particular nationality, race, or religion increased in every year since 1976, more than doubling from 498 in 1976 to 1,076 in 1986. Treasury statistics showed that Iraq, Jordan, Kuwait, Saudi Arabia, Syria, and the United Arab Emirates were responsible for more than 60 percent of total boycott requests and agreements. Of the taxpayers who received boycott requests, only a small proportion actually reported agreeing to engage or engaging in boycotting activities. In 1986, 44 taxpayers reported participating in a total of 1,450 boycott agreements.

Boycott participants can lose certain types of tax benefits, including the foreign tax credit on income taxes paid to boycotting countries and the ta deferral on the earnings of U.S. foreign subsidiaries. Treasury estimated that in 1986, due to section 999, 40 corporate boycott participants paid an average of $71,250 more in taxes. Treasury reports, however, did not provide a detailed description of the tax benefit losses of boycott participants by asset size and industry. GAO found that most boycott participants were manufacturing companies and that 26 of the 40 penalized corporations in 1986 had $1 billion or more in assets.

IRS' Efforts to Deal With Integrity and Ethics Issues

GAO/T-GGD-91-58, 07/24/91 and GAO/GGD-91-112FS, 07/24/91

In testimony before and a fact sheet to the Subcommittee on Commerce, Consumer, and Monetary Affairs of the House Committee on Government Operations, GAO provided information on IRS' efforts to deal with integrity and ethics issues. GAO said that IRS, in conjunction with Treasury's Inspector General, had made substantial progress in responding to concerns about integrity and ethics at IRS. GAO cautioned, however, that (1) the actions IRS had taken so far were initial steps in a major long-term effort and (2) IRS would need to maintain a high level of effort for several years to successfully carry out its plan to reshape IRS' culture.

A critical step IRS took to demonstrate that senior employee misconduct would be independently investigated was to transfer 21 staff years and $1.9 million to the Inspector General. GAO said that this action strengthened the Inspector General's role at IRS because, when misconduct is now alleged on the part of senior IRS managers or IRS Inspection employees, the Inspector General can conduct any investigation he believes is warranted. GAO concluded that the Inspector General effectively handled 127 such allegations. After its investigations, the Inspector General's findings were referred to IRS for deciding what sanctions, if any, to impose. While GAO did not take issue with the actions IRS took in the cases GAO reviewed, it believed that IRS could improve the perception that its decisions on sanctions were fair by (1) publicizing summary information about disciplinary actions taken against employees at all levels, (2) periodically reviewing disciplinary actions by type of infraction and level of employee to ensure they were equitably applied, and (3) maintaining National Office oversight while processing all Inspector General findings.

As part of its work in this area, GAO mailed 2,700 questionnaires to a random sample of IRS employees. The results of that survey were discussed during GAO's testimony and documented in detail in its fact sheet. The survey results indicated the importance for IRS to continue its emphasis on integrity and ethics. Almost 67 percent of IRS employees believed that the level of integrity in IRS was generally high or very high, and 34 percent believed that at least some upper level managers engaged in various forms of misconduct. GAO's survey also showed that 40 percent of IRS employees were not aware of IRS' Inspection Hotline and 74 percent were unaware of Treasury's Hotline as proper places to report misconduct. Although 76 percent of the employees said they would be generally willing to report misconduct if they were aware of it, only 23 percent of all employees believed that IRS would protect them (to a great

or very great extent) from retaliation for reporting. Similarly, when asked the extent to which senior management fosters a climate for taking actior against employees who breach ethical standards, only 23 percent believec such a climate was fostered to a great or very great extent. Further, 20 percent believed senior managers received preferential treatment when IF acted to correct misconduct.

Summary of Related Action(s)

Since GAO's July 1991 testimony and report, IRS has devoted substantial attention to initiatives intended to change the organization's integrity climate. For example, IRS is (1) planning to communicate with its employees about channels for reporting misconduct and the various protections afforded employees when they report and (2) developing an IRS-wide ethics awareness training course. IRS' Office of the Chief Inspecto is also (1) working on ways to enhance its image of independence and commitment of quality audits and investigations and (2) taking steps to encourage employee cooperation with inspection. In addition, IRS has (1) instituted procedures to monitor disciplinary actions involving senior officials at IRS' National Office and (2) developed plans to publish summary information about sanctions involving employees at all organizational levels.

Related GAO Product(s)

GAO/GGD-92-16, 12/31/91

Administrative Aspects of the Health Insurance Tax Credit

GAO/GGD-91-110FS, 09/12/91

The Omnibus Budget Reconciliation Act of 1990 provided taxpayers who qualify for the Earned Income Credit and contribute toward the purchase of health insurance for a qualifying child an additional credit to offset taxes owed. In a fact sheet to the Chairman and Ranking Minority Member of the Subcommittee on Health of the House Committee on Ways and Means, GAO provided information on how this health insurance tax credit would work administratively. Because IRS was still in the process of putting together forms and instructions, the information in this fact sheet was based on preliminary information obtained in discussions with IRS officials.

GAO said that taxpayers would be required to keep proof of payments of or contributions toward health insurance. If employers do not provide information to taxpayers concerning the amount of taxpayers' contributions toward health insurance premiums, taxpayers might not know how much the premiums cost. Taxpayers then might not take the credit or they might not report the correct information to IRS.

GAO noted that self-employed persons who claim both the health insurance credit and the self-employed health insurance deduction are required to reduce their deductible health insurance premiums by the amount of the credit. GAO said that calculating both the deduction and the credit was a problem because both numbers are dependent on each other. Specifically, the deduction is used to calculate adjusted gross income, which is then used to determine eligibility for the credit. This credit is then used to reduce the premium used to compute the deduction, which will increase the adjusted gross income—thereby potentially affecting eligibility of the credit once again.

GAO cited a number of steps that could be taken to solve this administrative problem and simplify procedures for the self-employed taxpayer. One way would require that taxpayers either claim the deduction or take the credit, but not both. A second alternative, which would probably be more expensive to the Department of the Treasury, would disregard the health insurance credit offset to the self-employed deduction in calculating adjusted gross income.

Related GAO Product(s)

GAO/GGD-T-91-68, 09/17/91

Pension Issues

Employee Benefits: Improvements Needed in Enforcing Health Insurance Continuation Requirements

GAO/HRD-91-37, 12/18/90

In a report to Senator John Glenn, GAO discussed IRS' and the Departmen of Labor's enforcement of the health insurance continuation requiremen of the Consolidated Omnibus Budget Reconciliation Act of 1985. GAO focused on the agencies' (1) efforts to help private individuals who bring cases of alleged noncompliance by employers to their attention, (2) procedures for investigating these allegations, and (3) enforcement history.

GAO reported that IRS and Labor provided limited help to individuals claiming noncompliance with the act's health insurance continuation requirements. With respect to IRS, GAO said that the agency sent informational material to persons inquiring about continued insurance benefits. This material stated that while there were sanctions in the Internal Revenue Code for employers who violate the act, the code provided no remedy for individuals denied benefits. They were told that violations of the code might also violate laws administered by Labor and to contact Labor if they needed additional information. The informationa material did not suggest that persons who believed they had been improperly denied benefits notify IRS so it could consider imposing tax penalties.

GAO said also that IRS referred allegations of noncompliance to its district offices and that these offices decided whether to pursue the case to determine whether tax penalties should be imposed. IRS headquarters ha received over 100 allegations of violations. In most cases, IRS had not decided whether it would take action on the allegations. In the five cases in which IRS had begun action, only one examination was completed. In that case, IRS found no violation.

GAO concluded that the extent of violations of the act was unknown and that IRS' method of dealing with potential beneficiaries of the act discouraged the reporting of violations. In GAO's opinion, it was unlikely that people denied the act's benefits would take the additional effort to notify IRS of violations after reading IRS material that says IRS cannot help them get benefits and refers them to Labor.

Recommendation(s)

The Commissioner of Internal Revenue and the Secretary of Labor should act to encourage people who believe they are improperly denied benefits under the 1985 act to report these denials to IRS. In addition to the informational materials being provided, these actions should include (1) a discussion of the tax consequences of violating the act, (2) a statement that IRS wants to be made aware of possible act violations, and (3) a description of the information that IRS needs to pursue a case. Similar information should be provided to callers, who may not be sent this material. The information should make clear that the Internal Revenue Code provides no remedy for individuals who are denied the act's benefits and that people will need to pursue remedies on their own, such as through lawsuits, to obtain the act's benefits.

IRS should also provide people inquiring about the act's benefits with the telephone number as well as the address of Labor's Division of Technical Assistance and Inquiries so that those needing further assistance can promptly contact Labor. Inquirers should be advised that there may be difficulty reaching Labor by telephone because of the number of calls, and they should write if their situation is not urgent.

Action(s) Taken and/or Pending

Labor has installed in its new automated answering system a recorded message encouraging the reporting of violations of the act to IRS and describing the data IRS needs to pursue such violations. A similar message is included in letters that Labor uses to respond to inquiries about the act.

IRS has modified its response letters to people inquiring about the act. The letters now state that IRS wants to know about possible violations of the act and describe the information IRS needs and where to send it. IRS has also modified its recorded message to callers about the act to provide Labor's telephone number. Because of Labor's new automated answering system, it will not be necessary to advise people that there may be difficulty in reaching Labor by phone.

Related GAO Product(s)

GAO/HRD-86-12, 10/21/85

Private Pensions: 1986 Law Will Improve Benefit Equity in Many Small Employers' Plans

GAO/HRD-91-58, 03/29/91

In a report to congressional committees required by the Retirement Equ
Act of 1984, GAO presented the results of its study on the effect of federa
pension rules on women. The Tax Reform Act of 1986 made major chan
to federal pension rules in part to address perceived inequities in the
benefits men and women earn. The report discussed specific pension ru
that affect benefit equity between men and women and the likely effect
that act's changes to these rules will have on benefit equity.

Before the 1986 act, many participants in small employers' plans—fewe
than 100 employees—were treated inequitably under GAO's criteria. GAO
assumed that a plan was equitable if every participant earned a benefit t
was the same percentage of pay per year of service. To adjust for roundi
and plan year differences, GAO considered inequitable any plan in which
men earned more than $1.10 in benefits as a percentage of pay per year
service for every $1 women earned.

GAO found that most small employer-sponsored defined benefit plans,
those which prescribed specific retirement benefits through a formula,
favored the higher paid, who were predominantly men. GAO also found t
the integration changes and proposed IRS nondiscrimination rules in the
1986 act will substantially limit the extent to which a plan may favor the
higher paid in the allocation of benefits. Consequently, the extent of
benefit inequity should decrease in many small employers' defined bene
plans. GAO supported IRS' new rules and believed that they would result i
substantial gains in benefit equity.

Related GAO Product(s)

GAO/HRD-89-105BR, 09/26/89

Pension Plans: IRS Needs to Strengthen Its Enforcement Program

GAO/HRD-91-10, 07/02/91

In a report to the Chairman of the Subcommittee on Oversight, House Committee on Ways and Means, GAO discussed IRS' efforts to enforce standards in the Employee Retirement Income Security Act of 1974 (ERISA).

GAO said that (1) IRS had increased the resources it devoted to examining pension plan operations, a key element of its ERISA enforcement strategy, but (2) IRS' program had not been as effective as IRS expected in identifying plans with ERISA violations. In discussing reasons for the unexpected effect, GAO said that (1) IRS' criteria for targeting plans with a high potential for ERISA violations were outdated because they were based on plan characteristics that had changed since the criteria were developed, (2) most plans IRS examined in the past 3 years were selected to train inexperienced staff rather than because the plan was likely to have a violation, and (3) IRS had not maintained an adequate oversight program to ensure that examinations were sufficiently thorough to identify ERISA violations.

While noting that IRS was taking action to address these issues, GAO said that IRS intended to spend much of its enforcement resources on examining small, overfunded plans with sponsoring employers who might have received excessive tax deductions for plan contributions. While this initiative might raise significant revenues, it would shift IRS' limited enforcement resources away from examining underfunded plans in which participants' benefits and the government's insurance program may be at risk. GAO also pointed out that a quality assurance program implemented in February 1990 did not provide for reviewing enough employee plan examinations to draw statistically valid conclusions about the quality of a district office's examination program.

GAO reported further that (1) IRS expected a large increase in the number of requests to approve plan design changes to comply with the Tax Reform Act of 1986, (2) IRS made several changes to reduce the time spent reviewing plan designs in order to meet this increased demand, and (3) these changes could diminish IRS' ability to ensure that plan designs comply with ERISA.

Recommendation(s)

The Commissioner of Internal Revenue should direct the Assistant Commissioner (Employee Plans and Exempt Organizations) to

- include plan underfunding among the criteria for targeting plans for examination,
- revise quality assurance procedures so that enough examinations are reviewed to draw statistically valid conclusions about examination quality and
- develop a strategy to determine whether approving plans without detailed review adversely affects plan participants and compliance with ERISA.

Action(s) Taken and/or Pending

IRS agreed to use underfunding as a criteria in identifying returns for examination and advised GAO that its fiscal year 1992 work plan calls for each office to direct examination time to returns with minimum funding issues. IRS expected to review enough examinations to draw statistically valid results about examination quality. In addition, IRS planned to establish a post-review program in fiscal year 1992 to assess the technical quality of its reviews of plan designs.

Related GAO Product(s)

GAO/T-HRD-90-37, 06/13/90 and GAO/HRD-89-32, 01/23/91

Tax Policy

Funding Options for the Resolution Trust Corporation

GAO/T-GGD-91-3, 10/24/90

GAO provided a statement for the record in conjunction with hearings before the Resolution Trust Corporation Task Force of the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban Affairs.

The statement dealt with the issue of how best to finance the corporation's bailout of the savings and loan industry. GAO provided some perspective on the following questions:

- Should the resolution of failed thrifts be debt or tax financed?
- If tax financing is chosen, should the revenues come from the general fund or from some special tax earmarked for this particular issue?
- If an earmarked tax is chosen, what kind of tax makes the most sense from a tax and financial policy perspective?

GAO concluded that while debt financing did not reduce national savings in the context of the bailout, tax financing did allow for a replenishment of the capital stock. As a result, tax financing might actually help to restore some of the losses that resulted from the thrift crisis. While not favoring any particular approach to raising general revenues, GAO did note that general fund financing had certain advantages compared to a special earmarked tax to fund the bailout effort. GAO said that the primary advantage of general fund financing for the Resolution Trust Corporation was that it allowed consideration of those equity, efficiency, and ease of administration principles that underlie good tax policy without resorting to taxes that were artificially tied to the corporation's problem.

Looking ahead, GAO saw that all depository institutions, depositors, and the public at large would have a stake in making sure that the deposit insurance system was able to perform its role in protecting deposits, stabilizing markets, and maintaining confidence in the nation's banking system. As such, decisions about who should contribute to the funding solution and the amounts of their respective contributions depended fundamentally on (1) judgments about what is fair and (2) assessments of who is best able to bear the additional tax or financial burden.

Related GAO Product(s)

GAO/T-AFMD-89-47, 02/21/89; GAO/AFMD-90-8FS, 01/19/90; GAO/T-AFMD-90-15, 04/06/90; and GAO/T-AFMD-90-32, 09/19/90

Targeted Jobs Tax Credit: Employer Actions to Recruit, Hire, and Retain Eligible Workers Vary

GAO/HRD-91-33, 02/20/91

In 1977, Congress established the Targeted Jobs Tax Credit Program to induce employers to favor certain disadvantaged individuals facing barriers to employment. Over the past 10 years, employers had claimed an estimated $4.5 billion in tax credits under the program. Yet, little information was available on the employers using the program or the workers hired under it.

In a report to two subcommittees of the House Committee on Education and Labor, GAO provided descriptive information on employers using the program and the individuals for whom the tax credits were claimed. GAO discussed (1) the extent to which employers made specific efforts to identify, hire, or retain eligible workers and (2) differences in participants' earnings before and after their involvement in the program.

This tax credit program is intended to increase employment opportunities for members of the targeted groups by providing a financial incentive to employers to recruit, hire, and retain target group members. GAO found that nearly half of the 60 employers it interviewed had made some special effort to do so. The other half had taken advantage of the tax credit without making special efforts to hire members of the targeted groups.

GAO also determined that work experiences had a positive impact on participants' earnings. GAO did not find any substantial differences, however, in earnings changes resulting from participants' work experience when compared with the experience of other workers who were eligible for the program but did not participate.

GAO's analysis of data from 13 states indicated that (1) retail stores and restaurants were the primary users of the tax credit program in 1988 and (2) most of the hirings under the program that year involved youths who were hired to fill entry-level jobs requiring minimal skills and paying low wages.

Matter(s) for Congressional Consideration

If Congress wishes that a higher proportion of employers using the Targeted Jobs Tax Credit Program would take special actions that benefit members of the targeted groups, it could modify the program by imposing new requirements. For example, program requirements might involve employer outreach efforts to eligible populations, prescreening to determine eligibility before the hiring decision, or providing additional

training or supervision to eligible workers to increase the likelihood of retention.

Action(s) Taken and/or Pending

No legislative action had been taken as of December 31, 1991.

Tax-Exempt Bonds: Retirement Center Bonds Were Risky and Benefited Moderate-Income Elderly

GAO/GGD-91-50, 03/29/91

Nonprofit charitable organizations have increasingly used tax-exempt bonds to obtain lower interest rates to finance housing for the elderly. In response to a request from Senator David Pryor and Congressman Brian Donnelly, GAO (1) reviewed the extent to which charitable organizations use tax-exempt bonds for housing the elderly; (2) identified the characteristics of the housing facilities, including the type of services provided and related fees and residents' incomes; and (3) determined the extent to which and reasons why housing facilities default on their tax-exempt bonds.

GAO identified 271 tax-exempt bonds totaling $2.8 billion that were issued from 1980 through July 1990 on behalf of charitable organizations to finance 221 housing facilities for the elderly. In about half of the facilities' most recent bond issues, bond proceeds provided 90 percent or more of the total funds used to finance the project. Facilities used the bond proceeds and other related funds primarily to finance construction; expansion; and furniture, fixtures, and equipment.

The facilities GAO identified offered the elderly residents a range of living arrangements, health care and assistance, and amenities. Entrance and monthly fees varied depending on unit size and services offered. The fees must support both the specialized services and the relatively high debt payments these highly debt-financed projects must pay.

Accordingly, GAO found that 75 percent of the facilities housed residents with average incomes greater than $15,000—making the facilities primarily affordable to 27 percent of the nation's elderly. Due to the expense of these housing projects for the elderly, it is unrealistic to expect similar projects financed solely by bonds to be available to the vast majority of elderly with incomes below $15,000. Additional subsidies would have to be provided. However, the bond subsidy may still serve a public purpose by encouraging charitable organizations to provide housing for elderly persons who may not be able to afford private, for-profit units.

As of the end of 1989, GAO estimated that the overall default rate for bonds issued for retirement centers between 1980 and 1989 was about 20 percent. In comparison, GAO estimated an overall default rate of about 1 percent for selected revenue bonds, such as bonds for industrial development projects and hospitals. GAO's case studies of defaulted projects showed that the facilities were highly debt financed and the

bonds' interest rates were higher than average rates charged on revenue bonds issued during the same period. This weak financial structure combined with the inexperience of some developers and their overestimated market projections of occupancy made the facilities particularly vulnerable to default.

Various industry officials described to GAO potential safeguards against default. However, policies that might reduce the possibility of default, such as requiring a certain level of equity, might also preclude successful projects from being undertaken if the organization does not have equity.

Tax Incentives and Enhanced Oil Recovery Techniques

GAO/T-GGD-91-36, 05/21/91

In testimony before the Subcommittee on Energy and the Environment of the House Committee on Interior and Insular Affairs, GAO discussed the use of tax expenditures to provide incentives for oil production and, in particular, to provide incentives for enhanced oil recovery.

Tax expenditures—reductions in income tax liability resulting from special tax provisions—are often used to achieve economic and social objectives. Their use, although legitimate, raises concerns because they are not explicitly considered as part of the standard budget process. As a result, they may not receive the frequent and careful attention they deserve. In addition, there are not good controls on the overall amount spent for and the budgetary impact of tax expenditures.

The arguments for petroleum production tax incentives usually encompass some combination of enhancing energy security, rewarding risk taking, or generating additional investment in new technologies. However, the drawbacks of such incentives are (1) some portion of any tax expenditure is spent on activities that would have occurred anyway and (2) there are alternative ways to achieve energy security and reduce risk that may achieve the goals at lower cost. In a previous report (GAO/GGD-90-75, 07/23/90), GAO reviewed a selected group of tax incentives for petroleum production and indicated that some were of questionable merit. Other tax incentives, including tax preferences for enhanced oil recovery methods, offered the potential for giving better returns on the tax dollar.

Since there is not much oil produced using enhanced oil recovery techniques, there is less chance of spending a lot of tax revenue on something that would have occurred anyway. If new production responds to incentives to a sufficient extent, the tax revenue cost per barrel could be lower than other petroleum-related tax expenditures. To the extent that the techniques are new and relatively untested, the spillover benefits could be significant.

Another issue of interest in evaluating the costs and benefits of the increased use of enhanced oil recovery techniques is their environmental effects. Brines from wells used to inject fluids into oil fields to enhance oil recovery can enter drinking water supplies. While the Environmental Protection Agency has a program to prevent contamination, these safeguards did not always protect against a leading source—improperly

plugged abandoned wells. Increased use of enhanced oil recovery techniques could lead to additional environmental costs that need to be included in any cost-benefit calculation.

Related GAO Product(s)

GAO/RCED-89-97, 07/05/89 and GAO/GGD-90-75, 07/23/90

GAO Plans for Evaluating Luxury Excise Taxes

GAO/T-GGD-91-44, 06/12/91

In a statement for the record prepared in conjunction with hearings by the Subcommittee on Taxation and Debt Management of the Senate Committee on Finance, GAO provided information on its plans for evaluating policy and administrative issues associated with luxury excise taxes.

GAO said that its objectives in examining these new taxes were to

- evaluate IRS' current efforts and future plans to collect luxury excise taxes,
- identify compliance and policy issues arising from the design of the tax, and
- examine the impact on the boating industry.

Nonprofit Hospitals: Better Standards Needed for Tax Exemption

GAO/T-HRD-91-43, 07/10/91

In July 1991 testimony before the House Committee on Ways and Means, GAO discussed the contents of a May 30, 1990, report on tax exemption standards for nonprofit hospitals. In the wake of increasing pressure on hospitals to contain costs, there are concerns that some hospitals are reducing their provision of indigent care and other charitable activities. Changes in the market affect all types of hospitals, but nonprofit hospitals are under more scrutiny because of their treatment as charities under the tax code.

GAO found that the link between tax-exempt status and the provision of charitable activities for the poor or underserved was weak for many nonprofit hospitals. Typically, in the states GAO reviewed, large urban teaching and public hospitals provided a disproportionate share of charity and other unreimbursed care. The nonprofit hospitals providing the lowest levels of such care served the fewest Medicaid patients and often had the highest profits. These were among the hospitals most financially able to provide additional care to the medically indigent and the hospitals that profited most from their tax exemptions.

Furthermore, in the communities GAO reviewed it was not uncommon for nonprofit hospitals' strategic goals to resemble those of for-profit institutions. For example, both focus on increasing market share rather than targeting underserved populations or addressing particular health problems of this segment of their communities. For the most part, the nonprofits' admission policies effectively limited charity care to emergency room and admissions resulting from emergencies.

In addition to providing care to those unable to pay, nonprofit hospitals were providing such community services as health education and screening, clinic services, and immunizations. However, these activities did not distinguish nonprofits from for-profit hospitals. Nonprofit hospitals were just as likely as for-profits to charge a fee for these services and more likely to recover the costs of providing them.

GAO noted that IRS had no requirements relating hospitals' tax-exempt status to the charitable activities they provide to the poor or underserved residents of their communities. GAO concluded that if Congress wanted to encourage nonprofit hospitals to provide charity care to the poor and underserved and other community services, it should revise the criteria for tax exemption.

Related GAO Product(s)

GAO/HRD-90-84, 05/30/90

Public Utilities: Disposition of Excess Deferred Taxes

GAO/GGD-91-51, 09/27/91

In response to a request from Congressman Robert T. Matsui, GAO provided information about the treatment of privately owned[4] public utilities' excess deferred tax reserves created by the Tax Reform Act of 1986. Excess deferred taxes were created when this act reduced the maximum corporate income tax rate from 46 percent to 34 percent and thereby cancelled some future expected income tax payments of privately owned utilities. Section 203(e) of the Tax Reform Act of 1986 requires that the return of excess deferred taxes to ratepayers be normalized. Under normalization accounting rules,[5] utilities transfer excess deferred taxes to ratepayers through reductions in utility service rates over a period at least as long as the remaining life of the capital assets that gave rise to them. Congress chose normalization rather than flow-through treatment, which permits a more rapid return of the excess deferred taxes to ratepayers. Under flow-through accounting for the return of excess deferred taxes, public utility commissions would determine how rapidly the taxes would be returned, which could range from an immediate, one-time flow through to flow through over several years.

The report (1) describes the origin of excess deferred taxes and how utilities may and may not use them, including any restrictions on utilities' use of excess deferred taxes to diversify into nonutility activities; (2) provides data on excess deferred tax balances and estimates how fast they can be passed on to utility customers under normalization; (3) discusses policy issues involving normalization treatment for deferred and excess deferred taxes; (4) describes the benefits and costs of the normalization requirement for utilities and utility customers; and (5) describes the likely reaction of state public utility commissions if section 203(e) was repealed. The report also contains several appendixes that provide additional detail on certain related topics.

GAO calculated public utilities' excess deferred taxes for 1987 to be about $17.9 billion, which represented about 6 percent of these utilities' aggregate gross revenues from their utility-related businesses for that year. The speed with which these taxes should be returned to ratepayers has prompted robust debate, but an objective resolution is not attainable

[4]Privately owned public utility companies, like other privately owned enterprises, are owned by investors and pay corporate income taxes. In contrast, publicly owned public utility companies, including federal, state, and municipally owned utilities and some mutual or cooperative companies producing utility services, do not pay income taxes.

[5]In setting its rates, a utility is required to follow certain normalization rules for deferred and excess deferred taxes in order to be eligible to use accelerated depreciation for its utility-related property.

because differing criteria can be applied to judge the desirability of results. However, many normal state regulatory practices would tend to offset any adverse impacts on utilities that might result from a more rapid flow through of the taxes to ratepayers following a repeal of section 203(e).

Internal Revenue Code Provisions Related to Tax-Exempt Bonds

GAO/GGD-91-124FS, 09-27-91

In response to a request from the Chairman, Subcommittee on Human Resources and Intergovernmental Relations, House Committee on Government Operations, GAO provided information on the tax-exempt bond provisions that are contained in the Internal Revenue Code. The fa sheet was intended to be useful (1) to those in Congress interested in reviewing the cumulative array of statutory conditions and requirements affecting tax-exempt bond issues; and (2) as a guide for public and priva tax-exempt bond issuers, bond counsels, and other participants in the marketing or oversight of bonds. It also provides a brief perspective on how the use of tax-exempt bonds has changed over the years and how Congress has reacted to these changes by adding legislative restrictions.

Taxpayer Service

Better Training Needed for IRS' New Telephone Assistors

GAO/GGD-91-83, 06/12/91

The telephone assistance program is IRS' primary method of answering taxpayers' questions. In a report to the Chairmen of the Subcommittee on Oversight, House Committee on Ways and Means, and the Subcommittee on Commerce, Consumer, and Monetary Affairs, House Committee on Government Operations, GAO assessed the development and delivery of IRS' training program for the approximately 1,000 new telephone assistors hired each year and identified changes that could improve training effectiveness.

At the time of GAO's review, training for new assistors (Phase 1 training) consisted of 6 weeks of classroom instruction and 2 to 4 weeks of on-the-job training. The classroom curriculum covered tax law, research techniques, communication skills, and related subjects. At the end of on-the-job training, trainees had the opportunity to answer taxpayer questions and receive any needed remedial training. Instructors determined whether trainees could be certified as job-ready assistors.

GAO identified areas needing improvement that could better ensure that trainees completing the program are adequately prepared for the job. GAO said that the (1) course materials were not sufficiently evaluated for effectiveness; (2) task forces that developed these materials lacked experience and training in writing course materials; (3) classroom written tests, which were primarily relied on to evaluate trainees, did not adequately measure knowledge and skills; and (4) certification process, which was intended to verify that trainees were ready to work independently, provided little assurance that trainees were ready to answer taxpayers' questions. GAO said that problems with the training program might have been further heightened by IRS' policy for selecting instructors, which did not ensure that only capable instructors taught the course. In that regard, the Taxpayer Service Division policy required that all assistors, as a condition for promotion to grade 9, become instructors.

Recommendation(s)

GAO made several recommendations to the Commissioner of Internal Revenue. Key ones were recommendations designed to bring greater expertise to bear in preparing, evaluating, and delivering course materials

and to strengthen trainee testing, on-the-job training, and related procedures leading to certification for job readiness.

Action(s) Taken and/or Pending

IRS generally agreed with GAO's recommendations and identified actions it has taken or plans to take to implement them. For example, IRS has taken steps to eliminate teaching as a requirement for the Taxpayer Service Specialist position and, instead, will fill instructor positions by competitiv selection.

In addition, IRS has developed a detailed checklist that outlines the tasks and expectations needed to update task force training. IRS is planning a longer training program for task force members and will provide clerical assistance for these training sessions. IRS has also expanded its training fc on-the-job-training instructors and adopted the Training Development Quality Assurance System to enhance the level and quality of course development projects.

Related GAO Product(s)

GAO/GGD-88-17, 12/03/87; GAO/GGD-89-30, 02/02/89; and GAO/GGD-90-37 01/04/90

Further Testing of IRS' Automated Taxpayer Service Systems Is Needed

GAO/IMTEC-91-42, 06/20/91

In a report to the Chairman of the Senate Committee on Governmental Affairs, GAO discussed the results of its review of IRS' Taxpayer Service Integrated System. IRS developed that system to help employees find the correct answers to taxpayer questions, electronically order requested forms, set up an automated process to research taxpayer questions and call them back later, and access other systems containing information on taxpayers for research purposes.

GAO's basic objective was to determine whether tests to measure the system's effectiveness provided the information necessary to justify its installation at all of IRS' 32 telephone call sites. GAO concluded that IRS did not have the basic information it needed to decide whether to install the system at all 32 sites. Tests to determine whether the system would improve service to taxpayers were inconclusive because they included tests that IRS ran during the 1991 tax return filing season, which were too limited or otherwise flawed. GAO further noted that even if the system could improve service, IRS might be able to realize improvements of equal magnitude through management changes.

In December 1990, the Office of Management and Budget denied IRS' 1992 Taxpayer Service Integrated System budget request for $41 million. Because of this denial and GAO's concerns, IRS decided to continue testing the system rather than begin installing it during fiscal year 1992, as originally planned. GAO agreed with this approach and said that further testing, if properly constructed and carried out, should yield the information IRS needs to decide whether to install the system at additional sites.

Recommendation(s)

To ensure that the Taxpayer Service Integrated System is not installed nationwide until its benefits have been clearly demonstrated, the Commissioner of Internal Revenue should make sure that IRS develops a test methodology that will allow it to conclusively determine the system's impact on call site operations. This methodology should (1) identify specific, measurable benefits of the system and (2) distinguish to what extent benefits are due to automation and to what extent they are due to other operational changes. Finally, if IRS decides to install the system nationwide, it should consider how it can be most effectively combined with ongoing management improvement initiatives to enhance the accuracy and productivity of taxpayer service call sites.

Action(s) Taken and/or Pending

IRS agreed that the benefits of the Taxpayer Service Integrated System should be clearly demonstrated before nationwide installation. After further analysis and testing, IRS cancelled the project because (1) test results were inconclusive due to poor test methodology and (2) a busines case could not be made for going ahead with the project. IRS current plan call for initiating a new system, called Telephone Response Integrated System, to meet its call site needs.

Related GAO Products

GAO/IMTEC-89-33, 05/05/89; GAO/GGD-90-37, 01/04/90; GAO/IMTEC-90-5 07/10/90; GAO/GGD-91-23, 12/27/90; and GAO/T-IMTEC-91-8, 06/25/91

Opportunities to Improve IRS Correspondence on Withholding Allowances

GAO/GGD-91-122, 09/27/91

In a report to the Assistant to the Commissioner (Taxpayer Ombudsman), GAO presented its views on how certain IRS correspondence to taxpayers might be made easier to understand. The correspondence involved letters IRS sends taxpayers when it questions either the number of withholding allowances being claimed on Form W-4 or the taxpayer's claim of exemption from withholding. GAO pointed to several problems with this correspondence that, if corrected, would make the letters easier to understand.

The correspondence discussed in this report is generated by the collection branch in IRS' service centers. GAO observed that some of the problems noted with the withholding allowance correspondence seemed to evolve from the same flawed process that GAO identified in a July 1988 report (GAO/GGD-88-101, 07/13/88) on correspondence prepared by a different service center unit called the adjustments/correspondence branch. In that report, GAO said that employees in the adjustments/correspondence branch (1) were composing letters by selecting paragraphs from an array of standard paragraphs and (2) were not able to review completed letters to make sure that they were understandable.

As noted in GAO's September 1991 report, since 1988, IRS has introduced technology to help employees compose and review completed letters. Budget limitations, however, had precluded all service center functions that correspond with taxpayers, such as the collection branch, from implementing that technology.

Related GAO Product(s)

GAO/GGD-88-101, 07/13/88

Tax Simplification

Simplifying Payroll Tax Deposit Rules

GAO/T-GGD-91-59, 07/24/91 and GAO/T-GGD-91-65, 09/12/91

In testimony before the House Committee on Ways and Means in July an[d] before the Subcommittee on Taxation, Senate Committee on Finance, in September, GAO discussed the need to simplify payroll tax deposit rules. Those rules are complex and make it difficult for employers to predict with certainty when to make their payroll tax deposits. About one-third o[f] the nation's employers were being penalized annually because they did n[ot] comply with these complex rules. H.R. 2775 and S. 1610, which were und[er] consideration when GAO testified, would simplify these rules by requiring employers to deposit their payroll taxes on the Tuesday or Friday following their paydays. The bill would exempt small employers with quarterly tax liabilities of $3,500 or less from this Tuesday/Friday rule an[d] instead allow them to make quarterly deposits.

GAO believes that changes to the deposit rules are urgently needed and sa[id] that these bills would make it easier for employers to understand the deposit requirements and to comply with the deposit rules. Both bills contain a look back provision, which for the first time would permit employers to know with certainty what their deposit requirement would be for the forthcoming quarter. The bills substantially fulfilled the recommendation GAO made in a 1990 report on the subject (GAO/GGD-90-102, 07/31/90).

However, S. 1610 differed in several respects from H.R. 2775, and GAO preferred the provisions of S. 1610 over those of H.R. 2775. S. 1610 has a higher deposit threshold at which small employers would be exempted from the Tuesday/Friday deposit rule. H.R. 2775 exempts employers with $3,500 or less in quarterly liability from making deposits on Tuesday or Friday. The S. 1610 exemption level is $18,000. This higher exemption lev[el] would reduce by 1.4 million the number of small employers who would b[e] required to make deposits on Tuesday or Friday. Furthermore, even though the Senate bill increases the exemption, it would nevertheless hav[e] a positive effect on federal revenues because many employers' deposits would be made faster under the Tuesday/Friday rule than they are now.

S. 1610 also had a different look back provision. Under H.R. 2775, employers qualified for the exemption if they were below the $3,500

threshold for eight consecutive quarters. Therefore, all employers would have to review eight quarters of deposit history each and every quarter—those who exceeded the threshold in one quarter would have to wait at least 2 years before again qualifying for the exemption. The S. 1610 provision looks back for only four quarters. GAO believes that the shorter look back provision would (1) be less burdensome, (2) enable small employers to return to the slower deposit, and (3) still achieve certainty in advance about which deposit rules apply during a given quarter.

Related GAO Product(s)

GAO/GGD-90-102, 07/31/90 and GGD-91-94, 08/28/91

Issues and Policy Proposals Regarding Tax Treatment of Intangible Assets

GAO/GGD-91-88, 08/09/91

One of the oldest controversies between taxpayers and IRS is the extent to which taxpayers can deduct the price they pay for intangible assets, such as customer or subscription lists. The general rule is that the cost of an intangible asset can be amortized over its useful life. Purchased goodwill and other intangible assets without determinable useful lives, however, a not amortizable. Taxpayers are supposed to determine the specific useful life for each intangible asset separately. The taxpayer's determination of useful life is only questioned when IRS performs an audit. IRS frequently contends that many intangible assets are in fact purchased goodwill and not amortizable. However, taxpayers assert that the assets are not goodwill, the determined useful lives are accurate, and the intangible assets are eligible for amortization.

The opportunities for disputes between taxpayers and IRS intensified during the 1980s, when business acquisition activity increased and led to growth in the reported value of intangible assets from about $45 billion in 1980 to $262 billion in 1987. As a result, billions of dollars of potential tax deductions and, therefore, tax revenues are affected by decisions on whether tax deductions for intangible asset costs are permitted.

In response to a request from the Joint Committee on Taxation, GAO provided information on the types of deductible intangible assets, the asset values and useful lives claimed, and the industries affected. GAO also explored various proposals for revising intangible asset tax rules, which had not significantly changed since 1927.

GAO analyzed tax data IRS gathered in 1989 on all of its unresolved, or ope purchased intangible asset cases. Taxpayers in 9 industry groups had claimed deductions for 175 types of purchased intangible assets that they identified as different from goodwill and valued at $23.5 billion. In 70 percent of the cases in which taxpayers claimed that intangible assets ha a determinable useful life, IRS claimed that the assets were in fact goodwil and not amortizable. In total, IRS proposed adjustments of about $8 billion on the basis of its evaluation of the value, useful life, or classification of intangible assets. The final outcome of these cases will depend on IRS' or the courts' interpretation of facts related to each asset.

GAO concluded that disagreements between taxpayers and IRS over which intangible assets may be amortized would continue unless changes were made in the current rules. GAO said that the current tax treatment of

goodwill and similar intangible assets failed to recognize the economic benefits that wasting intangible assets contribute over time. These assets are consumed over time even if a precise period cannot be determined. Denying amortization deductions does not result in an accurate determination of taxable income since expenses are not properly matched to income generated. Recognition of these economic benefits over time for tax purposes could be accomplished, according to GAO, by establishing specific statutory cost recovery periods for purchased intangible assets similar to those used for tangible assets.

Matter(s) for Congressional Consideration

Congress should consider revising the current tax law to provide for amortization of purchased intangible assets, including goodwill, over specific statutory cost recovery periods.

Action(s) Taken and/or Pending

On July 25, 1991, the Chairman of the House Committee on Ways and Means introduced H.R. 3035. The bill would revise the tax rules to require that most purchased intangible assets, including goodwill, be amortized over 14 years. In October 1991, the Committee held hearings on the bill; as of December 31, 1991, no further action had been taken.

Related GAO Product(s)

GAO/NSIAD-88-56BR, 12/28/87 and GAO/T-GGD-92-1, 10/02/91

The New Earned Income Credit Form Is Complex and May Not Be Needed

GAO/T-GGD-91-68, 09/17/91

In testimony before the Subcommittee on Information and Regulation of the Senate Committee on Governmental Affairs, GAO said that the new earned income credit form is complex and may not be needed.

GAO reported that about 12 million low-income households with children received over $6 billion in earned income tax credit payments in 1990. Until 1991, taxpayers who qualified could get one refundable credit based on their earned income regardless of the number of children they had. Th Omnibus Budget Reconciliation Act of 1990 simplified the credit by eliminating some of the complicated eligibility requirements. The act also increased the credit for households with more than one child and added two supplemental credits for households (1) with children under 1 year old and (2) that purchase health insurance for a qualifying child. To claim the credit, the act required that taxpayers include the name and age of each qualifying child, along with the Social Security number of any child older than 1. The conference report to the act specified that taxpayers should file a separate schedule with this information in order to get the credit.

IRS went beyond its normal processes in developing the new form by (1) setting up a special task force to develop the form, (2) soliciting comment from outside the usual channels, and (3) using focus groups to test the clarity and simplicity of the form and instructions. IRS made a number of changes to the initial version of the form based on the comments it received from the public and from focus groups. The focus groups, however, were composed entirely of people who filled out their own tax returns and, generally, had experience with the credit.

IRS also developed new processing procedures to handle the new form an expanded its outreach efforts to inform people about both the credit and the form. Because the procedures are premised on receiving the new forn correctly filled out, they are likely to limit the number of taxpayers who will receive the credit and result in taxpayers who qualify for the basic credit either not receiving it or receiving it late.

GAO believes that, even with the extra efforts IRS put into developing the form, it is still too complex and will confuse some taxpayers. The complexity could dissuade some eligible taxpayers from completing the form and getting the credit. Under previous rules, IRS could have calculated the credit for these taxpayers using information reported on th

tax return. GAO believes that, for most eligible taxpayers, the information currently on the tax return is sufficient for IRS to determine a taxpayer's eligibility for the basic credit. As a result, GAO believes that a separate form is not really necessary. If a taxpayer does not enclose an earned income credit form in the 1992 filing season, IRS should attempt to determine eligibility using information from the income tax return.

Summary of Related Action(s)

For the 1992 filing season, IRS has agreed to use the information contained on the tax return to determine earned income credit eligibility for most taxpayers.

Other

1990 Annual Report on GAO'S Tax-Related Work

GAO/GGD-91-46, 04/16/91

This report was prepared in compliance with a legislative requirement an contains information on GAO's tax policy and administration-related work during fiscal year 1990. It includes (1) summaries of tax-related products issued in fiscal year 1990; (2) summaries of tax-related products issued before fiscal year 1990 with open recommendations to Congress; (3) descriptions of legislative actions taken in fiscal year 1990 in response to GAO recommendations; (4) a list of recommendations to Congress that were open as of September 30, 1990; (5) a list of recommendations GAO made in fiscal year 1990 to the Commissioner of Internal Revenue; and (6 brief descriptions of assignments for which GAO was authorized access to tax data in fiscal year 1990.

GAO reported that (1) IRS had taken, or planned to take, action on most of the tax-related recommendations GAO made during fiscal year 1990; and (: congressional committees and Members of Congress used GAO products i overseeing tax administration operations, considering tax policy issues, and enacting legislation.

Social Security: Information About the Accuracy of Earnings Records

GAO/HRD-91-89FS, 04/19/91

In a fact sheet issued to the Chairman of the House Committee on Ways and Means, GAO summarized information in Social Security Administration (SSA) studies relating to two questions that had been raised by the Chairman:

- How accurate are the earnings records that SSA maintains?
- Are certain workers more likely to have errors in their earnings records than others?

With respect to accuracy, GAO cited (1) SSA studies that indicated that if SSA received and processed a wage report, the chances of it recording the report to the wrong account, or in an amount different from that reported, were very small; (2) a 1987 SSA study that found, in a nationwide sample of 1,744 persons receiving their first retirement benefit check in June 1985, that about 6.5 percent had 1 or more errors in their earnings records; and (3) a payment accuracy study issued in 1989 that found a similar error rate. GAO also pointed out various limitations in the studies that affected interpretation of the study results.

GAO said that there were no published studies directly related to the issue raised by the Chairman's second question. However, an unpublished internal study of SSA's 1978 suspense file of uncredited earnings provided information on the proportion of employees in the SSA file by broad industrial groups. The data showed, for example, that for 1978 almost 20 percent of the wage reports filed by businesses involved in agricultural production and services was not credited to valid workers' Social Security accounts.

Summary of Related Action(s)

On May 20, 1991, the House Committee on Ways and Means issued a report entitled "Report Card on the Social Security Administration." The Committee evaluated SSA's performance in six critical areas on the basis of SSA studies, GAO reports, and congressional surveys. The information contained in GAO's fact sheet was used as the basis for the Committee evaluation of SSA's earnings records—one of the six critical areas that the Committee checked. On the basis of this information, the Committee advised covered workers to obtain from SSA a copy of their "Personal Earnings and Benefit Estimate Statement." This statement details a worker's lifetime earnings that SSA records annually, thereby enabling the

person to identify any discrepancies in SSA's records and have them corrected.

Credit Unions: Reforms for Ensuring Future Soundness

GAO/GGD-91-85, 07/10/91

This report to Congress was prepared pursuant to section 1201 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. It discusses issues related to the (1) financial condition of credit unions and their federal insurance fund, (2) regulation and supervision of credit unions, (3) structure of the credit union industry, and (4) evolving role of credit unions in the financial marketplace.

GAO found that today's federally insured credit unions are in better shape than banks and thrifts due in part to changes in the types of loans and accounts credit unions offer, relaxed membership restrictions, and tax treatment. Unlike other federally insured depository institutions, credit unions are exempt from federal income taxation. GAO discussed the historical basis for the tax-exempt status and described how IRS administers the tax-exempt status of credit unions. GAO also summarized arguments for and against the tax exemption of credit unions and described how taxation would effect credit unions.

Recommendation(s)

GAO made over 50 recommendations related to organization, regulation, supervision, and insurance that would help ensure continued safe and sound operations and also protect the National Credit Union Share Insurance Fund. No recommendations, however, pertained to the tax-exempt status of credit unions.

Related GAO Product(s)

GAO/GGD-82-26, 02/19/82; GAO/GGD-83-13, 10/06/82; GAO/GGD-86-122BR, 09/09/86; GAO/GGD-89-47, 02/21/89; GAO/AFMD-89-25, 05/31/89; GAO/GGD-90-93, 07/19/90; GAO/GGD-90-97, 08/15/90; GAO/AFMD-90-18, 09/13/90; and GAO/GGD-91-26, 03/04/91

Asset Management: Governmentwide Asset Disposition Activities

GAO/GGD-91-139FS, 09/27/91

In a fact sheet to the Ranking Minority Member of the Subcommittee on Oversight, House Committee on Ways and Means, GAO provided information on the asset disposition activities of 22 agencies, including II that dispose of (1) financial assets, (2) real property, and (3) personal property.

GAO said that the federal government has a fragmented approach to managing and disposing of assets targeted for disposition. Over time, authority for managing and disposing of these assets has been given to many agencies, and congressional oversight has been spread among numerous committees. The result of such fragmentation has been the absence of a governmentwide asset disposition policy and the lack of an central control over asset disposition activities, illustrated by the absenc of a governmentwide inventory of these assets.

The fact sheet provides a governmentwide inventory of assets and describes the extent of federal government involvement in asset disposition activities. In an accompanying appendix, GAO presented an overview of the 22 agencies involved in asset disposition, including the types and value of their assets. These agencies reported having assets targeted for disposition that were valued at $193 billion at the end of fisc year 1990. IRS accounted for $76 million of this amount.

Summaries of Tax-Related Products Issued Before Fiscal Year 1991 With Open Recommendations to Congress as of December 31, 1991

Congress Should Require IRS to Include in Its Annual Budget Submission Information on Actual Revenues Derived From Audits 12

Congress Should Revise the Reporting Requirements to Better Assess the Effects of Section 127 of the Internal Revenue Code Dealing With Employer-Provided Education Assistance 12

Congress Should Repeal Legislation That Restricts IRS' Authority to Prospectively Reclassify Employees Who Have Been Misclassified as Independent Contractors 12

Congress Should Repeal Internal Revenue Code Section 809 Dealing With Policyholder Dividends Paid by Life Insurance Companies and Designate What Portion of These Dividends Consists of Distributed Earnings 13

Congress May Wish to Periodically Reconsider the Preferential Tax Treatment Given to Interest That Is Earned on Life Insurance and Deferred Annuity Contracts, Weighing Social Benefits Against Revenue Forgone 13

Congress Should Consider Restricting the Use of Low-Income Housing Tax Credits Generally to Areas Where Vacancy Rates Are Low for Suitable Units Renting at or Below the Area's Fair Market Rents 13

Congress Should Make Several Tax-Related Changes to the Debt Collection Act to Help Alleviate the Government's Credit Management Problems 13

Congress Should Consider Revising the Criteria for Tax Exemption If It Wishes to Encourage Nonprofit Hospitals to Provide Charity Care and Other Community Services 13

Congress Should Require IRS to Include in Its Annual Budget Submission Information on Actual Revenues Derived From Audits

GAO/GGD-88-119, 08/08/88

In response to a request from the Chairman of the Senate Committee on the Budget, GAO addressed the following two questions: (1) Can Congress rely on IRS' estimates of examination yield? and (2) Were the expected results of an increase in examination staff in 1987 realized? For fiscal year 1987, Congress had provided IRS with funds to add 2,500 examination staff—an increase that IRS said would enable it to audit 120,000 more returns and assess, as a result of those audits, $829 million in additional taxes, penalties, and interest.

GAO said that future estimates of revenues to be gained from audits would be more reliable if IRS used more realistic assumptions. For example, GAO cited as unrealistic IRS' assumption that data on the results of audits closed in 1972 were still reliable. IRS used that same outdated data to compute the "actual" assessed amounts shown in its budgets but did not disclose in those budgets that the "actuals" were only estimates.

With respect to the yield realized as a result of the staffing increase authorized for fiscal year 1987, GAO noted that (1) IRS estimated the yield to be $847.5 million in assessed taxes, penalties, and interest even though it did not achieve the examination staffing levels authorized for fiscal year 1987 and did fewer audits than anticipated; and (2) IRS' estimate was significantly overstated because, among other things, IRS failed to take into account the amount of potential revenue lost because experienced examination staff were used to train and coach new staff and thus were unavailable to audit returns.

Recommendation(s)

Congress should consider requiring IRS to include in its annual budget submission information on the actual amount of revenues derived from its audits.

Action(s) Taken and/or Pending

This recommendation cannot be implemented until IRS has information on the actual amount of revenues derived from its audits. IRS is developing an integrated enforcement management information system that will eventually provide data on the actual revenues generated by its enforcement efforts. IRS expects to implement that system in phases, with the final phase scheduled to be operational by October 1, 1993.

Congress Should Revise the Reporting Requirements to Better Assess the Effects of Section 127 of the Internal Revenue Code Dealing With Employer-Provided Education Assistance

GAO/GGD-89-76, 06/23/89

In a report to Congressman Frank Guarini, GAO (1) evaluated data that the Department of the Treasury used to assess the effect of section 127 of the Internal Revenue Code and (2) assessed the availability and reliability of certain information relating to section 127. This section allows individuals to exclude from their gross income the value of educational assistance provided by an employer through an employee educational assistance program.

In June 1988, Treasury concluded that section 127, which was due to expire on December 31, 1988, should not be extended. GAO reported that the information on which Treasury relied, although the best available, was insufficient to support its conclusion. GAO explained that the information came from surveys that were not specifically focused on gathering information to evaluate the success of section 127, had low response rates or were not representative of the population being surveyed. GAO said that (1) in 1984 Congress enacted a reporting requirement (section 6039D of the Internal Revenue Code) to provide a basis for assessing section 127, but the information required of employers was not sufficiently specific; and (2) information that would be useful in assessing section 127, such as the average income of participants and the average benefit at each salary level, was unavailable from reliable sources.

Recommendation(s)

When GAO issued its report, section 127 had expired. GAO recommended that if Congress decided to reinstate the provision, it might want to revise the reporting requirement to better assess the provision's effects. This revision could be done by requiring information on the salary level of participants and the average benefit at each salary level. To help make any further assessment of section 127, Congress could also specify that the data be reported for a sufficient length of time to adequately measure any effects.

Action(s) Taken and/or Pending

Section 127 has been extended three times since GAO issued its report—most recently in the Tax Extension Act the President signed into law on December 11, 1991. That act extended section 127 through June 30 1992, but like the other extensions did not revise the employer reporting requirement.

Congress Should Repeal Legislation That Restricts IRS' Authority to Prospectively Reclassify Employees Who Have Been Misclassified as Independent Contractors

GAO/GGD-89-107, 09/25/89

In response to a request from the Chairman of the Subcommittee on Commerce, Consumer and Monetary Affairs, House Committee on Government Operations, GAO assessed whether matching independent contractors' information returns with their tax returns would provide IRS with a systematic method for identifying employers who misclassify employees as independent contractors.

From information returns, GAO identified about 191,000 independent contractors who had received all of their income from 1 of about 32,000 employers. IRS revenue officers (1) interviewed a sample of 408 of those employers and determined that 157 may have misclassified their employees as independent contractors; (2) completed detailed examinations of 95 of those 157 employers and confirmed that 92 had misclassified 17,347 employees; and (3) recommended, for those 92 employers, taxes and penalties of $16.7 million in 1986 and 1987.

GAO noted that (1) IRS would not have to create a new matching process to identify misclassifications because it already matched information returns and income tax returns to identify unreported income; and (2) although IRS could use information returns to better identify misclassified employees, section 530 of the Revenue Act of 1978 prohibits IRS from assessing back taxes that should have been withheld and paid and restricts IRS' authority to require certain employers to reclassify workers, even for future years.

Recommendation(s)

In view of the equity issues and tax revenues involved, Congress may want to consider repealing the restriction against requiring employers to prospectively reclassify employees who have been misclassified as independent contractors.

Action(s) Taken and/or Pending

In a November 1990 report, Tax Administration Problems Involving Independent Contractors, the House Committee on Government Operations made several recommendations regarding the misclassification of workers. For example, the Committee recommended that the tax-writing committees consider eliminating the previous audit "safe harbor" protection of section 530 as a reasonable basis for not requiring an employer to reclassify workers. Under that provision, an employer is protected from reclassification if there had been a previous IRS audit that did not successfully challenge the employer's classification practices. No

congressional action with respect to section 530 had been taken as of December 31, 1991.

The Committee also recommended that IRS establish a matching program to systematically identify employers who are most likely to be misclassifying workers as independent contractors along the lines suggested by GAO. IRS implemented such a program in 1991 and is studying its results.

Congress Should Repeal Internal Revenue Code Section 809 Dealing With Policyholder Dividends Paid by Life Insurance Companies and Designate What Portion of These Dividends Consists of Distributed Earnings

GAO/GGD-90-19, 10/19/89 and GAO/T-GGD-90-03, 10/19/89

In a report to the Chairmen of the Subcommittees on Health and on Select Revenue Measures, House Committee on Ways and Means, and in testimony before the Select Revenue Measures Subcommittee, GAO discussed (1) the effect of section 809 of the Internal Revenue Code on the income tax split between stock and mutual life insurance companies and within the mutual segment itself and (2) alternative methods of taxing mutual life insurance companies. Congress enacted section 809 to make the taxation of mutual companies more parallel to that of stock companies.

GAO found that section 809 imposed taxes that (1) were higher for the mutual companies as a whole in years when their earnings were low and vice versa, (2) were regressive on the basis of company income because averages for all mutual companies dictated each firm's taxes, and (3) depended disproportionately on the behavior and performance of the larger mutual companies. GAO also found that for 1984 through 1987, the mutual stock split in taxes produced by the section 809 approach was consistent with the mutual stock split in income.

After examining various alternatives, GAO concluded that the most equitable approach would be to repeal section 809, allow mutual life insurance companies to deduct all policyholder dividends in determining corporate taxable income, and tax policyholders on the earnings part of certain dividends.

Recommendation(s)

Congress should repeal section 809 and designate what portion of policyholder dividends paid by life insurance companies consists of distributed earnings. For administrative reasons, companies would pay the tax as a proxy for individual policyholders.

Action(s) Taken and/or Pending

GAO's proposal and a number of others have been part of the ongoing discussion about the tax treatment of mutual life insurance companies. However, as of December 31, 1991, no legislative action had been taken.

Congress May Wish to Periodically Reconsider the Preferential Tax Treatment Given to Interest That Is Earned on Life Insurance and Deferred Annuity Contracts, Weighing Social Benefits Against Revenue Forgone

GAO/GGD-90-31, 01/29/90

In a report to the Chairmen of the Senate Committee on Finance and the House Committee on Ways and Means, GAO responded to section 5014 of the Technical and Miscellaneous Revenue Act of 1988. Section 5014 calle for GAO to report on (1) the effectiveness of the revised tax treatment of life insurance products in preventing the sale of life insurance primarily for investment purposes; and (2) the policy justification for, and the practical implications of, the current tax treatment of earnings accruing c the cash surrender value of life insurance and annuity contracts in light o the Tax Reform Act of 1986.

Under current law, interest earned on life insurance and deferred annuity contracts, commonly referred to as "inside buildup," is not taxed as long as it accumulates within the contract. By choosing not to tax the interest as it is earned, the federal government forgoes an estimated $5 billion in tax revenue each year. Also, as a result of this preferential tax treatment, there are incentives to design life insurance and annuity products that ar targeted more toward generating investment income than toward providing insurance protection.

GAO found that recent changes in the definition of life insurance had reduced the sales of single-premium policies but said it was more difficul to evaluate the effect on other investment-oriented life insurance product

GAO noted that the most convincing policy justification for the current tax treatment of accrued interest is that it lowers the cost of providing insurance and retirement income protection. Even if more is spent on life insurance and annuity protection as a result of this tax preference, it is nc clear that the revenue loss is justified. In addition, although borrowing against the cash value of life insurance is not taxed, it reduces the protection afforded beneficiaries. As a result, the current tax treatment, which allows the borrowing of life insurance accrued interest without tax appears inconsistent with (1) the goal of fostering increased protection and (2) the tax treatment of similar products, such as Individual Retirement Accounts and 401(k) plans.

Recommendation(s) to Congress

Because the pattern of policy usage as well as the type of products offere can change, Congress may wish to periodically reconsider its policy decision to grant preferential tax treatment to inside buildup, weighing th social benefits against the revenue forgone. If Congress decides not to tax

inside buildup, it should eliminate tax-free borrowing of life insurance proceeds. Any borrowing of those proceeds should be considered a distribution of interest income. To offset the advantages of accruing interest income without tax, a penalty provision needs to be added to the regular tax. Since repayment of the amount borrowed restores the death benefits, any amount that is taxed when it is borrowed should be tax deductible if subsequently repaid.

Action(s) Taken and/or Pending

As of December 31, 1991, no legislative action had been taken.

Congress Should Consider Restricting the Use of Low-Income Housing Tax Credits Generally to Areas Where Vacancy Rates Are Low for Suitable Units Renting at or Below the Area's Fair Market Rents

GAO/T-RCED-90-34, 02/27/90 and GAO/RCED-90-168, 06/19/90

In response to a request from the Chairman of the Subcommittee on HUD/Moderate Rehabilitation Investigation, Senate Committee on Banking Housing and Urban Affairs, GAO provided information on the financial implications of combining subsidies under the Department of Housing and Urban Development's (HUD) Section 8 Moderate Rehabilitation Program and the Department of the Treasury's Low-Income Housing Tax Credit Program. In February 1990, GAO testified on one of those projects. In June 1990, GAO reported on eight specific housing projects.

GAO reported that (1) developers for the eight projects realized cash proceeds that exceeded their costs for acquiring and rehabilitating the properties by 11 to 34 percent; and (2) developers generated the proceeds by selling their ownership interests in the projects, along with the related tax credits, and combining them with mortgage loans secured by moderat rehabilitation rental subsidies.

GAO said that (1) by combining rehabilitation subsidies and tax credits, developers received more assistance than needed to ensure the projects' financial viability or to compensate them for their limited financial risk; (2) the use of both programs was questionable because the projects were located in areas with ample vacant units and with rents generally well below the established rents for the eight projects; and (3) it would have been more economical to rely on existing rental housing subsidized by certificates and/or vouchers under HUD's Certificate and Voucher Program rather than developing the eight projects GAO reviewed.

GAO noted that Congress and HUD had taken steps to better control subsidies under the Moderate Rehabilitation and Tax Credit Programs. Those changes (1) limited the amount of subsidies allowable and the way they could be used, (2) placed greater responsibility on state credit-allocation agencies, and (3) prohibited the use of tax credits in conjunction with the Section 8 program.

Recommendation(s)

Congress may wish to consider restricting the use of tax credits generally to areas where vacancy rates are low for suitable units renting at or below the area's fair market rents. Congress could further require that any deviation from this policy by a state credit allocation agency be documented and subject to review by an authorized representative of the federal or state government.

Action(s) Taken and/or Pending

The Omnibus Budget Reconciliation Act of 1990 requires the Secretary of the Treasury and HUD's Inspector General to jointly conduct a study on the combined use of the low-income credit and the Section 8 Moderate Rehabilitation Program funds and to submit the results to Congress no later than January 1, 1993. No further action had been taken as of December 31, 1991.

Summary of Related Action(s)

HUD revised its program policies and guidelines to require that when projects are to receive tax credits in conjunction with HUD subsidies, HUD must consider the value of the tax credit and adjust accordingly the amount of other subsidies awarded to the project. In addition, HUD revised its program policies to target housing subsidies to geographic areas with low unit vacancies.

Congress Should Make Several Tax-Related Changes to the Debt Collection Act to Help Alleviate the Government's Credit Management Problems

GAO/AFMD-90-12, 04/16/90

At the request of Congressman John R. Kasich, GAO reviewed the efforts o selected federal agencies, including IRS, to implement the Office of Management and Budget's nine-point credit management program. That program's nine points include such things as (1) screening loan applicant (2) reporting to consumer reporting agencies, (3) using collection firms, (4) offsetting federal income tax refunds, and (5) writing off delinquent debts. GAO focused on selected programs at the five primary credit agencies—the Small Business Administration and the Departments of Agriculture, Housing and Urban Development, Education, and Veterans Affairs.

GAO noted the progress agencies had made over the past several years in certain credit management areas. GAO also cited a number of problems. For example, agencies were not always (1) checking if loan applicants were delinquent in paying taxes or (2) reporting closed-out debts to IRS as income to the debtor.

Recommendation(s) to Congress

Because of the magnitude of the government's credit management problems, Congress should amend the Debt Collection Act in a number o ways. The tax-related changes would involve (1) screening loan applicant to determine credit worthiness and ability to repay and to determine if th applicants owe delinquent debts to the federal government, including IRS; (2) denying credit to applicants who owe delinquent debts to the federal government; (3) referring all appropriate debts to IRS for the purpose of offsetting delinquent debtors' tax refunds; and (4) reporting closed-out debts to IRS as income to the debtor.

Congress should legislatively direct the Secretaries of Housing and Urban Development and Veterans Affairs and the Administrators of the Farmers Home and Small Business Administrations, in coordination with IRS, to tes the use of consent forms for obtaining and using tax information in the loan making process. The affected agencies could designate selected programs, including those with guaranteed loans, for participation in the test. Congress should also require IRS to disclose address information to agencies pursuing debt collection activities under authorities in addition t the Federal Claims Collection Act.

Action(s) Taken and/or Pending

Although Congress has not yet acted on each of GAO's recommendations, the Unemployment Compensation Act of 1991 provides permanent

authority for collecting nontax debts by reducing debtors' tax refunds. Also, the Senate Committee on Governmental Affairs and the House Committee on Governmental Operations are interested in pursuing legislation to improve management and oversight of the government's lending programs. The need for credit management legislation was addressed during hearings before the Senate Committee on Governmental Affairs on September 18, 1990, and the House Committee on the Budget's Urgent Fiscal Issues Task Force in October 1991. In addition, the administration submitted a legislative package to Congress that addresses many of GAO's recommendations relating to IRS.

Congress Should Consider Revising the Criteria for Tax Exemption If It Wishes to Encourage Nonprofit Hospitals to Provide Charity Care and Other Community Services

GAO/HRD-90-84, 05/30/90 and GAO/T-HRD-90-45, 06/28/90

In a report to and testimony before the House Select Committee on Aging GAO discussed the role of nonprofit hospitals in providing (1) acute medical care to indigents and (2) other community services, such as healt education and screening. Private nonprofit hospitals, which account for about one-half of the nation's hospitals, are exempt from federal taxation if they meet certain tests established by IRS. Until 1969, the test for tax-exempt status included specific reference to providing services to those unable to pay. Since then, IRS has not required such care as long as the hospital provides benefits to the community in other ways.

GAO analyzed the distribution of uncompensated care among hospitals in five states to assess the role of nonprofit hospitals in supplying such care. GAO found that (1) nonprofit hospitals provided a smaller share of their states' uncompensated care than they provided of general hospital services; (2) uncompensated care expenses were not distributed equally among the nonprofit hospitals but were disproportionately concentrated in large urban teaching hospitals; (3) among the rest of the nonprofit hospitals, the tendency was for those hospitals with the greatest ability to finance charity care to have the lowest rates of uncompensated care; and (4) about 57 percent of the nonprofit hospitals in the five states incurred charity care costs that amounted to less than GAO's estimate of the value o the hospitals' tax exemptions.

GAO noted that (1) some hospitals' goals did not focus on the health needs of the poor or underserved in their community, (2) physician staffing and charity admissions policies discouraged indigent admissions except in emergency cases, and (3) nonprofit hospitals were more likely than investor-owned hospitals to offer community services but were equally likely to charge patients for them and more likely to recover their costs.

Recommendation(s)

Currently, there are no requirements relating hospitals' charitable activities for the poor to tax-exempt status. If Congress wishes to encourage nonprofit hospitals to provide charity care to the poor and underserved and other community services, it should consider revising th criteria for tax exemption. Criteria for exemption could be directly linked to a certain level of (1) care provided to Medicaid patients, (2) free care provided to the poor, or (3) efforts to improve the health status of underserved portions of the community.

Action(s) Taken and/or Pending

On February 4, 1991, the Chairman of the House Select Committee on Aging introduced H.R. 790, The Charity Care and Hospital Tax-Exempt Status Reform Act of 1991. On March 12, 1991, a similar bill, H.R. 1374 was introduced. Both bills would establish standards of charity care for tax-exempt hospitals. In July 1991, hearings were held on both bills by the House Committee on Ways and Means. No further action had been taken as of December 31, 1991.

Listing of Open Recommendations to Congress

Congress Should Enact Legislation to (1) Require Buyers Who Deduct Seller-Financed Mortgage Interest to Report on Their Tax Returns the Name and Social Security Number of the Seller and (2) Authorize IRS to Penalize Buyers Who Fail to Provide the Seller's Identification Number Without Showing Reasonable Efforts to Obtain It and Penalize Sellers Who Refuse to Provide Their Numbers to Buyers 41

Congress May Wish to Extend the Offset Authority for Expenses IRS Incurred in Undercover Operations, That Expired on December 31, 1991, and Revise Current IRS Reporting Requirements 57

Congress Should Consider Modifying the Targeted Jobs Tax Credit Program by Imposing New Eligibility Requirements If It Wishes to Encourage Employers Using the Program to Take Special Actions That Benefit Members of the Targeted Group 97

Congress Should Consider Revising the Current Tax Law to Provide for Amortization of Purchased Intangible Assets, Including Goodwill, Over Specific Statutory Cost Recovery Periods 117

Congress Should Require IRS to Include in Its Annual Budget Submission Information on Actual Revenues Derived From Audits 127

Congress Should Revise the Reporting Requirements to Better Assess the Effects of Section 127 of the Internal Revenue Code Dealing With Employer-Provided Education Assistance 128

Congress Should Repeal Legislation That Restricts IRS' Authority to Prospectively Reclassify Employees Who Have Been Misclassified as Independent Contractors 129

Congress Should Repeal Internal Revenue Code Section 809 Dealing With Policyholder Dividends Paid by Life Insurance Companies and Designate What Portion of These Dividends Consists of Distributed Earnings 131

Congress May Wish to Periodically Reconsider the Preferential Tax Treatment Given to Interest That Is Earned on Life Insurance and Deferred Annuity Contracts, Weighing Social Benefits Against Revenue Forgone. If Congress Decides Not to Tax That Interest, It Should Eliminate Tax-Free Borrowing of Life Insurance Proceeds 132

Congress Should Consider Restricting the Use of Low-Income Housing Tax Credits Generally to Areas Where Vacancy Rates Are Low for Suitable Units Renting at or Below the Area's Fair Market Rents 134

Congress Should Make Several Tax-Related Changes to the Debt Collection Act to Help Alleviate the Government's Credit Management Problems 1[illegible]
Congress Should Consider Revising the Criteria for Tax Exemption If It Wishes to Encourage Nonprofit Hospitals to Provide Charity Care and Other Community Services 1[illegible]

Listing of Recommendations Made in Fiscal Year 1991 to the Commissioner of Internal Revenue and to Other Agency Heads

Compliance

The Department of the Treasury Should Take Steps, in Coordination With IRS and the Financial Management Service, to Improve Federal Agency Tax Compliance 27

Establish a Nationwide Levy Verification Program 29

Take Specific Actions to Ensure That (1) Warranted Preparer Penalty Cases Are Opened, (2) Preparer Penalties Are Assessed Appropriately and Consistently, and (3) Preparer Penalty Referrals Are Made When Required 31

Take Various Steps to Improve IRS' Pursuit of High-Income Nonfiler Cases 35

Modify the Computer Match to Reduce the Number of Unproductive Underreporter Cases 38

If Congress Enacts the Legislation Recommended by GAO, IRS Should Use (1) Sellers' and Buyers' Social Security Numbers to Study the Extent of Noncompliance With the Reporting Requirements Related to Seller-Financed Mortgages and (2) the Study Results to Implement an Enforcement Program 41

Ensure That Future Studies of IRS Refund Offset Program (1) Control as Many Meaningful Tax and Nontax Characteristics as Possible, (2) Include an Estimate of the Potential Revenue Loss Due to Any Noncompliant Filing Behavior, and (3) Include a Comparison of This Loss With the Progam's Benefits 45

The Secretary of the Treasury Should Direct That all Permanent Positions Allocated to the Office of Financial Enforcement Be Filled a as Quickly as Possible 47

Implement at all ACS Call Sites Automation for Making Outgoing Calls and for Receiving and Directing Incoming Calls 51

Establish a National Quality Improvement Project to (1) Clarify the Root Causes of the Problems GAO Found in IRS' Administration of the Negligence and Substantial Understatement Penalties and (2) Identify and Implement Effective Solutions 53

Direct IRS' Chief Inspector to Ensure That Internal Audit Expands Its Financial Audits to Include all Undercover Operations Involving Offsetting, Regardless of the Amount of Expenditures or Proceeds 56

Develop a Comprehensive Plan to Prevent, Identify, and Collect Employment Tax Delinquencies 58

Take Steps to Increase the Potential of Collecting More Accounts Receivable Before the Statutory Collection Period Expires 63

General Management

- Develop and Implement a Statistically Valid Survey of IRS' Ability to Fill Taxpayer's Phone and Mail Orders for Tax Materials
- The Bureau of Alcohol, Tobacco and Firearms Should Increase the Availability of Accounting Expertise for Use on Tax Compliance Inspections and Take Various Steps to Enhance Its Operational Efficiency
- Improve Certain Measures of Service Center Quality and Take Steps to Better Use the Results
- Improve the Management of IRS by, Among Other Things, (1) Transferring Revenue Accounting Responsibility to the Chief Financial Officer, (2) Developing and Implementing a Strategy for Providing Additional Technical Expertise at Senior Decisionmaking Levels, and (3) Bringing a Greater Sense of Urgency to the Human Resource Related Strategies in IRS' Strategic Business Plan

Pension Issues

- Work With the Secretary of Labor to Encourage People Who Believe They Are Improperly Denied Benefits Under the Consolidated Omnibus Budget Reconciliation Act of 1985 to Report These Denials to IRS
- Improve IRS' Program for Identifying Pension Plans in Violation of the Employee Retirement Income Security Act

Taxpayer Service

- Improve IRS' Training Program for New Telephone Assistors
- Make Sure That IRS Develops a Test Methodology That Will Allow It to Conclusively Determine the Impact of IRS' Taxpayer Service Integrated System

Chronological Listing of GAO Products on Tax Matters Issued in Fiscal Year 1991

Testimony on IRS' Accounts Receivable Inventory (GAO/T-GGD-91-2)	10/18/90
Testimony on Funding Options for the Resolution Trust Corporation (GAO/T-GGD-91-3)	10/24/90
Treasury ADP Procurement: Contracting and Market Share Information (GAO/IMTEC-91-8FS)	11/13/90
Status of IRS' Input Processing Initiative (GAO/IMTEC-91-9)	12/12/90
Employee Benefits: Improvements Needed in Enforcing Health Insurance Continuation Requirements (GAO/HRD-91-37)	12/18/90
Extent and Causes of Erroneous Levies (GAO/GGD-91-9)	12/21/90
IRS' 1990 Filing Season Performance Continued Recent Positive Trends (GAO/GGD-91-23)	12/27/90
Effectiveness of IRS' Return Preparer Penalty Program Is Questionable (GAO/GGD-91-12)	01/07/91
Targeted Jobs Tax Credit: Employer Actions to Recruit, Hire, and Retain Eligible Workers Vary (GAO/HRD-91-33)	02/20/91
Testimony on IRS' Compliance Programs to Reduce the Tax Gap (GAO/T-GGD-91-11)	03/13/91
IRS Does Not Investigate Most High-Income Nonfilers (GAO/GGD-91-36)	03/13/91
IRS Can Improve Its Program to Find Taxpayers Who Underreport Their Income (GAO/GGD-91-49)	03/13/91
BATF: Management Improvements Needed to Handle Increasing Responsibilities (GAO/GGD-91-67)	03/19/91
Testimony on the Activities of BATF (GAO/T-GGD-91-19)	03/20/91
Testimony on IRS' Budget Request for Fiscal Year 1992 and Status of the 1991 Tax Return Filing Season (GAO/T-GGD-91-17)	03/20/91
IRS Needs to Improve Certain Measures of Service Center Quality (GAO/GGD-91-66)	03/20/91
Testimony on Uncertainties Surrounding IRS' Fiscal Year 1992 Budget Request for Tax System Modernization (GAO/T-IMTEC-91-4)	03/20/91
Tax Exempt Bonds: Retirement Center Bonds Were Risky and Benefited Moderate-Income Elderly (GAO/GGD-91-50)	03/29/91
Expanded Reporting on Seller-Financed Mortgages Can Spur Tax Compliance (GAO/GGD-91-38)	03/29/91
Private Pensions: 1986 Law Will Improve Benefit Equity in Many Small Employers' Plans (GAO/HRD-91-58)	03/29/91
Changes Are Needed to Improve Federal Agency Tax Compliance (GAO/GGD-91-45)	04/16/91
1990 Annual Report on GAO's Tax-Related Work (GAO/GGD-91-46)	04/16/91
Testimony on IRS' Efforts to Ensure Corporate Tax Compliance (GAO/T-GGD-91-21)	04/17/91
Social Security: Information About the Accuracy of Earnings Records (GAO/HRD-91-89FS)	04/19/91
Managing IRS: Important Strides Forward Since 1988 but More Needs to Be Done (GAO/GGD-91-74)	04/29/91
Testimony on Public Service: How Effective and Responsive Is the Government? (GAO/T-HRD-91-26)	05/08/91
Refund Offset Program Benefits Appear to Exceed Costs (GAO/GGD-91-64)	05/14/91
Money Laundering: The U.S. Government Is Responding to the Problem (GAO/NSIAD-91-130)	05/16/91
Testimony on Tax Incentives and Enhanced Oil Recovery Techniques (GAO/T-GGD-91-36)	05/21/91
Information on Revenue Agent Attrition (GAO/GGD-91-81)	06/10/91
Testimony on the Need for IRS to Implement a Corporate Document Matching Program (GAO/T-GGD-91-40)	06/10/91
Statement for the Record on the Status of a GAO Assignment Examining Luxury Excise Taxes (GAO/T-GGD-91-44)	06/12/91
Better Training Needed for IRS' New Telephone Assistors (GAO/GGD-91-83)	06/12/91
Collecting Back Taxes: IRS Phone Operations Must Do Better (GAO/IMTEC-91-39)	06/18/91
Further Testing of IRS' Automated Taxpayer Service Systems Is Needed (GAO/IMTEC-91-42)	06/20/91

(continued)

Tax System Modernization: An Assessment of IRS' Design Master Plan (GAO/IMTEC-91-53BR)	06/25/
Testimony on Management Challenges Facing IRS (GAO/T-GGD-91-20)	06/25/
Tax System Modernization: Attention to Critical Issues Can Bring Success (GAO/IMTEC-91-8)	06/25/
A Generally Successful Filing Season in 1991 (GAO/GGD-91-98)	06/28/
Pension Plans: IRS Needs to Strengthen Its Enforcement Program (GAO/HRD-91-10)	07/02/
Negligence and Substantial Understatement Penalties Poorly Administered (GAO/GGD-91-91)	07/03/
IRS Experience Using Undercover Operations' Proceeds to Offset Operational Expenses (GAO/GGD-91-106)	07/03/
Testimony on Identifying Options for Organizational and Business Changes at IRS (GAO/T-GGD-91-54)	07/09/
Testimony on Tax System Modernization Issues Facing IRS (GAO/T-IMTEC-91-18)	07/09/
Testimony on Nonprofit Hospitals: Better Standards Needed for Tax Exemption (GAO/T-HRD-91-43)	07/10/
Credit Unions: Reforms for Ensuring Future Soundness (GAO/GGD-91-85)	07/10/
IRS' Administration of the International Boycott Tax Code Provisions (GAO/GGD-91-105)	07/11/
Testimony on IRS' Efforts to Deal With Integrity and Ethics Issues (GAO/T-GGD-91-58)	07/24/
Testimony on Simplifying Payroll Tax Deposit Rules (GAO/T-GGD-91-59)	07/24/
Internal Revenue Service: Employee Views on Integrity and Willingness to Report Misconduct (GAO/GGD-91-112FS)	07/24/
Issues and Policy Proposals Regarding Tax Treatment of Intangible Assets (GAO/GGD-91-88)	08/09/
Tax System Modernization: Status of On-line Files Initiative and Telecommunications Planning (GAO/IMTEC-91-41FS)	08/14/
Efforts to Prevent, Identify, and Collect Employment Tax Delinquencies (GAO/GGD-91-94)	08/28/
Testimony on Simplifying Payroll Tax Deposit Rules (GAO/T-GGD-91-65)	09/12/
Administrative Aspects of the Health Insurance Tax Credit (GAO/GGD-91-110FS)	09/12/
The New Earned Income Credit Form Is Complex and May Not Be Needed (GAO/T-GGD-91-68)	09/17/
Tax Systems Modernization: Private Sector Modernization Efforts IRS May Want to Examine (GAO/GGD-91-133FS)	09/24/
Money Laundering: The Use of Cash Transaction Reports by Federal Law Enforcement Agencies (GAO/GGD-91-125)	09/25/
Benefits of a Corporate Document Matching Program Exceed the Costs (GAO/GGD-91-118)	09/27/
Public Utilities: Disposition of Excess Deferred Taxes (GAO/GGD-91-51)	09/27/
Opportunities to Improve IRS Correspondence on Withholding Allowances (GAO/GGD-91-122)	09/27/
Internal Revenue Code Provisions Related to Tax-Exempt Bonds (GAO/GGD-91-124FS)	09/27/
Asset Management: Governmentwide Asset Disposition Activities (GAO/GGD-91-139FS)	09/27/
Opportunities to Increase Revenue Before Expiration of the Statutory Collection Period (GAO/GGD-91-89)	09/30/

Listing of Assignments for Which GAO Was Authorized Access to Tax Data in Fiscal Year 1991 Under 26 U.S.C. 6103 (I)(7)(a)(i)

Subject matter	Objectives
IRS' Efforts to Address Integrity Problems Among Its Senior Managers	To examine the (1) handling of senior employee misconduct cases by IRS and the Treasury Inspector General, (2) Inspector General's efforts to obtain prosecutions, and (3) willingness of IRS employees to report wrongdoing and IRS' efforts to facilitate such reporting without fear of retribution.
IRS' Management of Work Force Integrity	To examine IRS' approach to managing its ethics and integrity program with specific emphasis on determining (1) the adequacy of internal controls over conflict of interest for employees; (2) the policies, procedures, and practices for administering the ethics program; (3) the management and administration of internal security programs, particularly in the prevention, detection, investigation, and adjudication of instances of employee misconduct; and (4) the policies, procedures, and practices regarding whistle-blowers.
IRS' Efforts to Increase Electronic Filing of Returns	To (1) determine whether IRS is doing all it can do to promote electronic filing and make it accessible to the general public; and (2) assess whether electronic filing makes it easier to create, and more difficult to detect, fraudulent refund schemes given the absence of a paper trail.
Department of Veterans Affairs' Use of Tax Information	To monitor collection, use, protection, and verification of tax information the Department of Veterans Affairs received from IRS.
IRS' Consolidated Financial Statements	To (1) determine the extent of financial management and internal control problems that need to be corrected in order to prepare financial statements in accordance with generally accepted accounting principles; (2) identify necessary audit procedures to opine on fiscal year 1992 financial statements, including opening balances; (3) assist IRS in preparation of financial statements in accordance with generally accepted accounting principles, including the development of pro forma statements; and (4) analyze available data maintained on its operations to determine the adequacy of such data.
IRS' Undercover Investigative Operations	To evaluate (1) the use of proceeds of undercover investigative operations, (2) the results of such operations, and (3) the financial audits IRS did under the Crime Control Act of 1990.
Violations of the Employee Retirement Income Security Act	To determine (1) whether IRS had identified breaches and ERISA violations in underfunded defined benefit pension plans for which the Pension Benefit Guaranty Corporation had assumed responsibility and (2) what actions IRS took.
IRS' Consolidated Examination Program	To (1) assess the reasons for the declining audit coverage of large corporations and (2) identify the major factors that cause the amount of tax assessments that are recommended from examinations of large corporations to be reduced by IRS' Appeals Division or by tax litigation.
IRS' Use of Taxpayer Compliance Measurement Program Data	To determine whether the taxpayer compliance measurement process (1) is managed effectively and (2) achieves the purposes intended by IRS.

Major Contributors to This Report

General Government Division, Washington, D.C.

David J. Attianese, Assistant Director, Tax Policy and Administration Issues
Robert J. McArter, Assistant Director, Tax Policy and Administration Issues
Joseph T. Valonis, Senior Evaluator-in-Charge

Ordering Information

The first copy of each GAO report and testimony is free. Additional copies are $2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

U.S. General Accounting Office
P.O. Box 6015
Gaithersburg, MD 20877

Orders may also be placed by calling (202)275-6241.

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

Official Business
Penalty for Private Use $300

First-Class Mail
Postage & Fees Pai
GAO
Permit No. G100