

December 1998

# TAX ADMINISTRATION

## IRS' Audit and Criminal Enforcement Rates for Individual Taxpayers Across the Country



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**General Government Division**

B-280369

December 23, 1998

The Honorable Harold E. Ford, Jr.  
House of RepresentativesThe Honorable Henry A. Waxman  
House of Representatives

Recently, some observers have raised questions about whether the Internal Revenue Service (IRS) disproportionately audits or pursues criminal investigations of taxpayers in some locations compared to other locations. An April 1997 study<sup>1</sup> concluded that enforcement of the tax laws occurred at higher rates among taxpayers living in the South compared to enforcement in the rest of the country. Moreover, congressional hearings in 1998 pointed to concerns about whether IRS' audits and criminal investigations were always justified.

Given concerns about alleged disproportionate treatment, at your request this report provides information about (1) factors that might explain why IRS' audit, criminal investigation initiation, and prosecution referral rates for individual taxpayers differ across the country; (2) rates at which individual taxpayers were audited in IRS' Tennessee-Kentucky district and the South<sup>2</sup> during fiscal years 1992 through 1997 compared to the national average rates; (3) rates at which individual taxpayers were investigated for alleged criminal tax and nontax violations and referred for prosecution in IRS' Tennessee-Kentucky district and the South during fiscal years 1992 through 1997 compared to the national average rates; and (4) controls that IRS has established for its audits, criminal investigations, and prosecution referrals for individual taxpayers and whether these controls were used.<sup>3</sup>

IRS' 33 districts and 10 service centers audit tax returns to determine whether taxpayers have complied with tax laws and paid the correct taxes. The Criminal Investigation Division (CID) through district and regional

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<sup>1</sup>The Transactional Records Access Clearinghouse (TRAC)—a data-gathering and research organization associated with Syracuse University—did the study. The study focused on criminal prosecutions, convictions, and sentencings. It did not draw the same conclusions about IRS data on its audits, criminal investigations, or prosecution referrals.

<sup>2</sup>IRS' Southeast Region includes the districts for Tennessee, Kentucky, Alabama, Florida, Georgia, Louisiana, Mississippi, North Carolina, South Carolina, Virginia, West Virginia, Indiana, Maryland, and Delaware. We included all but three of these districts in our analyses of the South. We excluded Indiana, Maryland and Delaware because they are generally not considered part of the South.

<sup>3</sup>As agreed with your offices, we did not test the effectiveness of IRS' controls over audits, criminal investigations, and prosecution referrals.

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offices investigates alleged criminal tax violations and makes referrals to U.S. Attorneys for prosecution. IRS has four regional offices to oversee these and other activities in the field.

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## Results in Brief

IRS officials identified several factors to explain variation across the country in audit, criminal investigation initiation, and prosecution referral rates for individual taxpayers. The main factor was that the rates for civil and criminal tax noncompliance vary geographically. That is, neither the types of taxpayers nor their tax behaviors are homogeneous across districts. IRS officials also identified other factors that might affect geographic variation, such as the location of available audit and criminal investigation staff.

Because a variety of factors can affect the geographic variations in IRS audit, criminal investigation initiation, and prosecution referral rates, comparisons of these rates must be interpreted with caution. Some factors fall outside IRS' direct control, such as the location of taxpayers' noncompliant behaviors. Other factors are more subject to IRS' control, such as how many auditors and criminal investigators it assigns to a location. We were not able to adjust for all such factors in comparing audit, criminal investigation initiation, and prosecution referral rates across locations. Had we been able to make these adjustments, the results of our comparisons of rates across locations could have been different.

For the years 1992 through 1997 combined, the unadjusted audit rate for the Tennessee-Kentucky district was below the national average rate, and the South's rate was approximately at the national average. The annual rates for the Tennessee-Kentucky district were approximately at or below the national average, and the South's annual rate was approximately at the national average.

The 6-year combined criminal investigation initiation and prosecution referral rates for the Tennessee-Kentucky district were below the national averages, and the South's rates were approximately at the national averages. Although not every annual rate for the Tennessee-Kentucky district or the South was at or below the national average, the rates generally were.

IRS has established controls for its audits, criminal investigations, and prosecution referrals. These controls generally consist of standards to guide audit and investigation behavior, such as how auditors are to gather and document evidence and how criminal investigators are to conduct

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investigations of alleged criminal tax and nontax violations. The controls also include a series of reviews to check adherence to the standards.

We could not determine the extent to which IRS has used most of its controls over audits, criminal investigations, and prosecution referrals. Statistics on how often the controls were used are not maintained in any database except for the reviews done at the close of audits to measure adherence to the audit standards. However, both Examination and CID officials said that they believe that the controls to initiate audits and criminal investigations are always used.

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## Background

IRS believes that taxpayers are more likely to voluntarily comply with the tax laws if they believe that their returns may be audited and unpaid taxes identified. IRS audits 1 to 2 percent of the more than 100 million income tax returns filed annually by individuals to check for voluntary compliance in reporting income, deductions, and other tax issues as well as in paying the correct tax liability. IRS relies on the taxpayer to provide documentation about the issues being audited. In turn, IRS auditors are to examine the documentation to determine the correct tax liability.

IRS does two types of face-to-face audits in its district offices to examine individual taxpayers' documentation: (1) field audits in which an IRS revenue agent visits an individual who has business income or a very complex return and (2) office audits in which an individual who has a less complex return visits a tax auditor at an IRS office. At IRS' service centers, IRS uses correspondence audits in which tax examiners correspond with taxpayers about potential discrepancies on their returns. Unlike the district audits, these audits usually involve only one tax issue, such as dependent exemptions.

Regardless of the type of audit, IRS auditors must decide, when closing it, whether to recommend changes to the audited tax issues and to the reported tax. If an auditor recommends a tax change, the taxpayer has the right to agree with or appeal this tax change. Depending on the outcome of any taxpayer appeal, the recommended additional taxes may or may not be assessed and collected.

CID carries out IRS' criminal law enforcement responsibilities under three principal statutes. Under title 26 U.S. Code, IRS has the authority to investigate alleged criminal tax violations, such as tax evasion and filing a false tax return. Under title 18 U.S. Code, IRS has the authority to investigate a broad range of fraudulent activities, such as false claims against the government and money laundering. Under title 31 U.S. Code,

IRS is responsible for enforcing certain recordkeeping and reporting requirements of large currency transactions, such as cash bank deposits of more than \$10,000. In fulfilling these responsibilities, CID coordinates as necessary with IRS' District Counsel, the Criminal Tax Division in DOJ, and the U.S. Attorney to prosecute violators of the statutes.

CID special agents<sup>4</sup> are responsible for conducting investigations to determine if criminal tax fraud or nontax financial crimes might have occurred. Investigations usually start on the basis of information provided by (1) IRS' Examination or Collection Divisions, (2) CID projects, (3) the public and other government agencies, or (4) reports of currency transactions. Investigators are to gather the evidence to determine if a criminal violation has occurred. In fiscal year 1997, CID initiated 5,335 investigations and referred 3,817 investigations for prosecution.<sup>5</sup>

## Scope and Methodology

To identify factors that might explain differences in the audit, criminal investigation initiation, and prosecution referral rates for individuals across the country, we interviewed Examination Division and CID officials in IRS' National Office to obtain explanations of the differences. We were not able to adjust for all of the factors IRS identified when we analyzed the extent to which rates differed across locations.

To compare IRS' unadjusted audit, criminal investigation initiation, and prosecution referral rates across locations during fiscal years 1992 through 1997, we first defined the South as those states included in IRS' Southeast region, except for three states—Indiana, Maryland, and Delaware. We excluded these states on the basis of discussions with your offices and because these states generally are not considered to be part of the South. As a result, this report defines the South as 7 IRS districts that cover 11 states—Alabama, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, and West Virginia. We shifted IRS' Indiana district to the Midstates region and the Maryland-Delaware district to the Northeast region. We made no other changes to IRS' regional boundaries.<sup>6</sup>

<sup>4</sup>CID special agents are federal criminal investigators whose specialty is financial investigations. Their training includes accounting and federal law enforcement procedures.

<sup>5</sup>Due to their lengths, investigations usually start in one year and end with any referrals in another year.

<sup>6</sup>If we had not shifted the three states from the Southeast region, our analyses would have resulted in slightly lower audit, investigation, and referral rates—between 1 percent and 5 percent lower—than we report for the South.

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We collected and analyzed data on IRS audit rates—the percentage of individual tax returns that IRS audited compared to the number of filers of individual tax returns. We computed audit rates for districts, service centers, and regions for each of the 6 years as well as an average rate for all 6 years. We then ranked (from highest to lowest) the rates for all 6 years and for all locations. We also compared the annual audit rates in the Tennessee-Kentucky district and the districts for the South with the national average. Appendix I shows these annual audit rates by district, service center, and region.

We also collected and analyzed IRS data on criminal investigation initiation and prosecution referral rates. We computed these rates by dividing the number of initiations and referrals by the number of filers. For ease of comparison, we computed the rates for every 100,000 filers in a location. As with audit rates, we analyzed criminal investigation initiation and referral rates across locations through (1) rankings of the average rates for all 6 years and (2) comparisons of the rate at a specific location in each of the 6 years with the national average rate. Appendix II shows the investigation and referral rates by district and region.

We also analyzed the number of audits, criminal investigation initiations, and prosecution referrals by geographic location. Appendix III presents this analysis and its results, which were similar to those for our analysis of rates.

The audit data used in our analyses came from IRS' Audit Information Management System (AIMS) and our prior work on audit rates for some fiscal years.<sup>7</sup> We used data from the Criminal Investigation Management Information System (CIMIS) on criminal investigations and prosecution referrals for both tax and nontax issues. We did not test the reliability of the AIMS and CIMIS data, but we did talk to Examination and CID officials about their data and concluded that we could use the data for our analyses.

Because of TRAC's study on alleged data discrepancies between CID and other agencies,<sup>8</sup> we collected information and interviewed officials at these agencies about the reasons for any discrepancies. We interviewed TRAC officials about the same issue. Rather than reconciling the data, our goal

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<sup>7</sup>Tax Administration: Audit Trends and Results for Individual Taxpayers (GAO/GGD-96-91, April 26, 1996).

<sup>8</sup>These other agencies include DOJ's Criminal Tax Division, the Executive Office for U.S. Attorneys (EOUSA), and the Administrative Office of the U.S. Courts (AOUSC).

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was to determine whether we could use CID data on criminal investigations and prosecution referrals. We concluded that we could use the data because TRAC's reported discrepancies did not focus on the initiation of criminal investigations and referrals for prosecution.

To identify IRS' controls over audits, criminal investigations, and prosecution referrals, we interviewed Examination and CID officials in the National Office. We collected and reviewed relevant IRS documents on audit standards as well as criminal investigation and prosecution standards and policies. To determine whether IRS used the controls, we sought available documentation. We interviewed responsible IRS officials on the use of the controls, and we reported data from our work<sup>9</sup> on the use of certain audit controls.

We did our work at IRS' National Office, DOJ's Criminal Tax Division, EOUSA, and AOUSC in Washington, D.C., between May and September 1998 in accordance with generally accepted government auditing standards. We requested comments from the Commissioner of Internal Revenue on a draft of this report, and these comments are discussed at the end of the report.

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## IRS Expects Variations in Enforcement Rates Across the Country

IRS officials said that variation across the country in the audit, criminal investigation initiation, and prosecution referral rates for individual taxpayers should be expected due to several factors. The main factor is that the rates for civil and criminal tax noncompliance vary geographically. Because the types of taxpayers are not homogeneous from district to district, the noncompliant behaviors of some are not uniformly distributed in each district.

In linking this geographic variation in noncompliance with audit rates, Examination officials also pointed out that audit rates vary with how many auditors are allocated to specific locations. The officials stated that allocation of auditors is based primarily on statistically valid research data, which shows that some locations have more filed returns with a higher potential for noncompliance than other locations. IRS said it considers this fact when determining how many auditors to assign to a location.

Beyond the number of auditors, IRS Examination officials said that the audit rates can vary across locations on the basis of how the auditors are

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<sup>9</sup>Tax Administration: More Criteria Needed on IRS' Use of Financial Status Audit Techniques (GAO/GGD-98-38, Dec. 30, 1997); Tax Administration: IRS' Use of Information Gathering Projects (GAO/GGD-98-39, Feb. 5, 1998); and IRS Audits: Workpapers Lack Documentation of Supervisory Review (GAO/GGD-98-98, Apr. 15, 1998).



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used. For example, more auditors might be available to do audits when an IRS location uses fewer auditors for nonaudit efforts, such as taxpayer education and outreach to improve compliance. These officials explained that because the need for such services can vary across IRS locations, the assignment of some auditors to nonaudit efforts also will vary.

IRS Examination officials also identified several other factors that might affect geographic variations in audit rates. According to the officials, variability in the audit rates can be attributed to the use of projects that focus on known compliance issues in specific locations.<sup>10</sup> The officials said that audit rates might be higher if a location has more tax returns from certain types of taxpayers who have proven to be more noncompliant, such as certain self-employed taxpayers operating cash businesses. Further, some variation from year to year could be expected depending on the changing number of returns that are filed by taxpayers at specific locations.

CID officials also pointed to these factors. In addition, they attributed variability in the criminal investigation and prosecution referral rates to a recent shift towards investigating certain types of tax fraud and narcotic crimes and identifying major types of new tax fraud issues. Moreover, they said that investigations are resource intensive. If many investigations happen to take more time than usual, the start of new investigations would be delayed. If investigations take longer in certain locations compared to others, differences in the investigation rates would arise, which also could affect future referral rates.

Finally, CID officials said some variability in rates might be due to difficult-to-quantify factors, such as differences in the experience and skill of the investigators. More skilled investigators may be assigned more complex and time-intensive investigations. On the other hand, their skills might allow them to do investigations more quickly. Further, the officials stated that some variation could be expected depending on the number and location of assistant U.S. Attorneys and judges in the judicial system.

Because many factors affect geographic variations in the audit, criminal investigation initiation, and prosecution referral rates, comparisons of these rates must be interpreted with caution. Some factors fall outside IRS' direct control. For example, IRS does not control whether taxpayers

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<sup>10</sup>IRS staff can propose audit projects on the basis of past audits or studies that have shown noncompliance for selected taxpayer populations, such as those in a particular occupation, industry, geographic area, or economic activity.

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engage in civil and criminal tax noncompliance at higher rates in some locations than in others. Nor does IRS control the actions of outside parties that influence the initiation of many investigations, such as those involving grand juries.<sup>11</sup> Other factors are more subject to IRS' control, such as how many auditors or investigators it assigns to a location.

We were not able to adjust for all such factors in comparing audit, criminal investigation initiation, and prosecution referral rates across locations. Had we been able to make these adjustments, the results of our rate comparisons could have been different.

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## Unadjusted Audit Rates in the Tennessee-Kentucky District and the South Were Generally at or Below the National Averages

Without adjusting for external factors that can affect the geographic variation of IRS audit rates, we found that IRS did not appear to have audited individual taxpayers at a higher rate in the Tennessee-Kentucky district and the South compared to the national average during fiscal years 1992 through 1997.

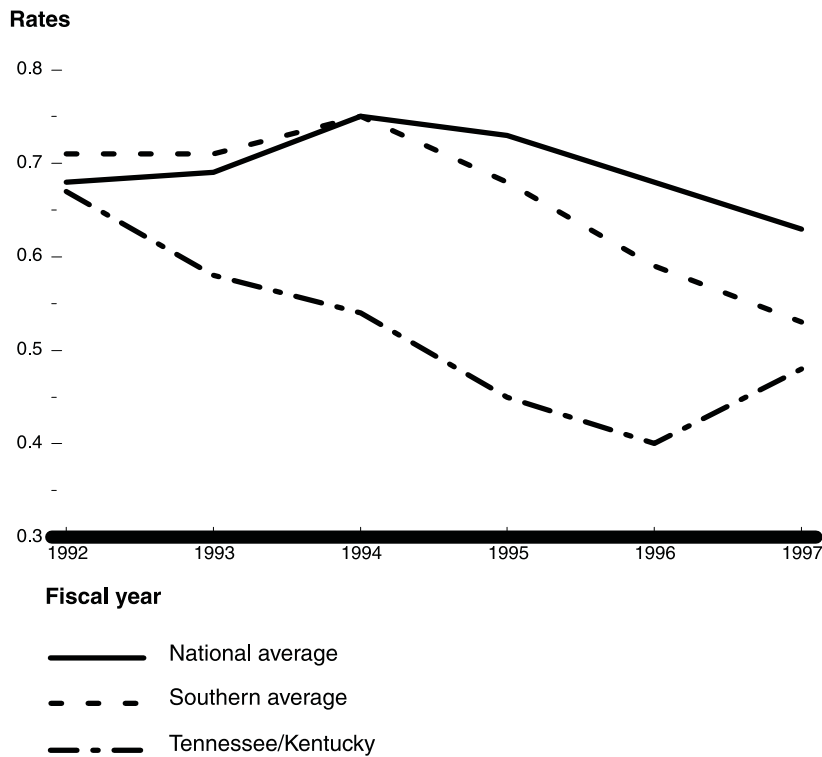
For all 6 years, the Tennessee-Kentucky district's audit rate averaged 0.52 percent, which was below the national average, and ranked 21st of 33 districts. The Memphis Service Center ranked 9th in the audit rate among 10 service centers. The South's audit rate averaged 0.65 percent, placing it close to the national average of 0.67 percent and second among the four regions. However, the average rate for the South was similar to the rates ranked third and fourth, which averaged 0.63 and 0.46 percent, respectively.

On an annual basis, audit rates in the Tennessee-Kentucky district and the South were generally at or below the national average. The Tennessee-Kentucky district rates almost always fell below the national averages each fiscal year, 1992 through 1997. Annual audit rates in the South were more likely to be below than above the national averages. Figure 1 shows the trends in these rates for the Tennessee-Kentucky district, the South, and the national average over the 1992 through 1997 period. Appendix I presents detailed information on audit rates by location for 1992 through 1997.

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<sup>11</sup>CID officials stated that grand jury investigations account for 66 percent of the criminal cases initiated by CID.

Figure 1: Individual Audit Rates



Source: GAO analysis of IRS data.

## Unadjusted Criminal Investigation Initiation and Referral Rates in the Tennessee-Kentucky District and the South Were Approximately at or Below the National Averages

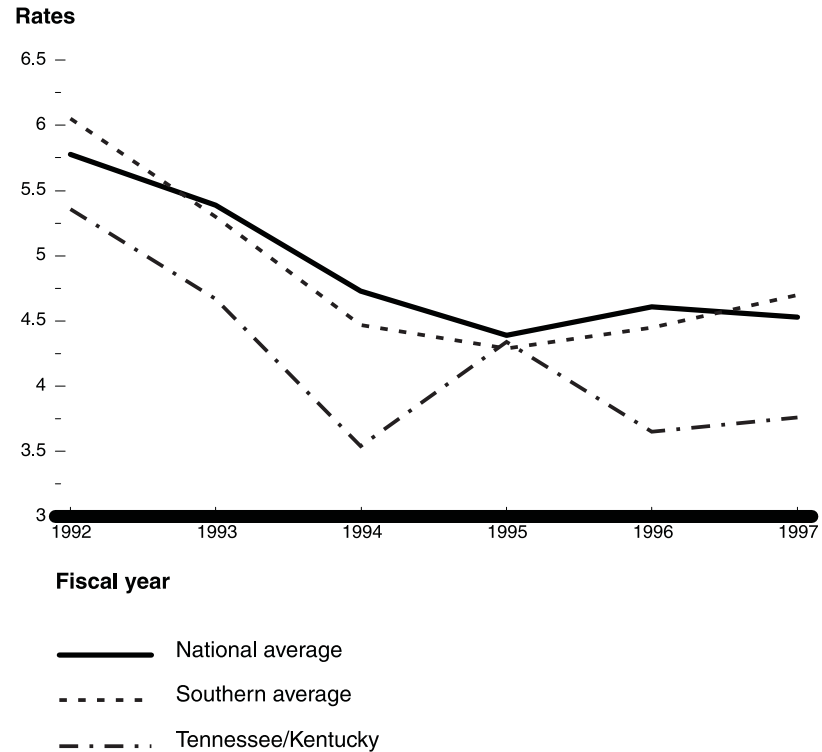
Without adjusting for the external factors that can affect the geographic variation of IRS' rates, we found that IRS did not appear to have investigated or referred for prosecution individual taxpayers in Tennessee-Kentucky and the South at a higher rate compared to the rest of the country during fiscal years 1992 through 1997.

Over all 6 years, the Tennessee-Kentucky district initiated an average of 4.22 investigations per 100,000 individual filers, ranking 20th of 33 districts and below the national average. The South ranked third with a 4.87 average rate over all 6 years for initiating investigations. However, the range among the 4 regions was small— from 4.86 to 4.96 investigations initiated per 100,000 filers.

As shown in figure 2, for each of the 6 years, the Tennessee-Kentucky district's rates for initiations generally were below the national averages. The South's initiation rates were slightly below the national average in 4 years and slightly above it in 2 other years. Appendix II presents detailed

information on the investigations initiated and prosecutions referred per 100,000 individual filers by location for 1992 through 1997.

**Figure 2: Criminal Investigation Initiation Rates per 100,000 Individual Filers**

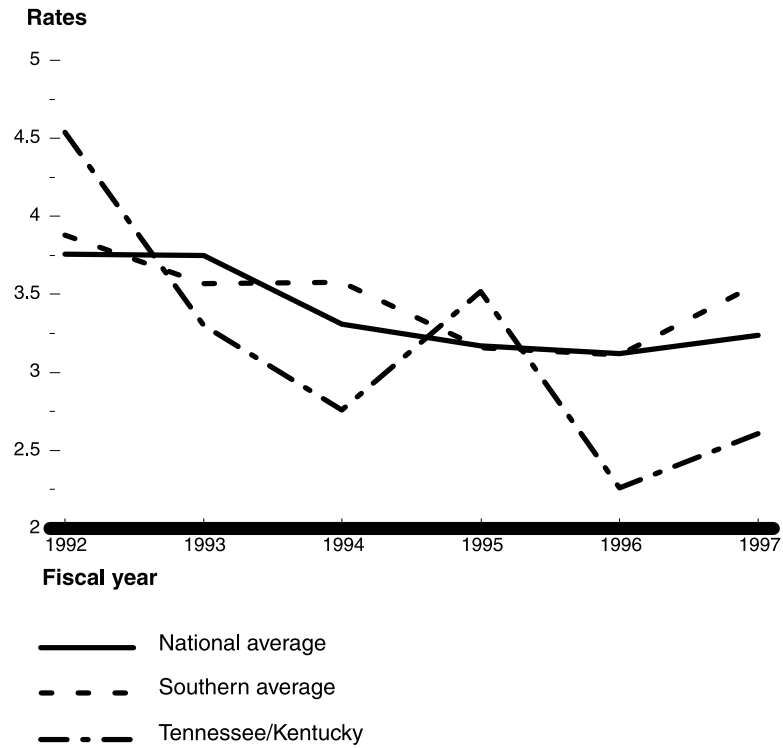


Source: GAO analysis of IRS data.

In terms of prosecution referral rates, the Tennessee-Kentucky district ranked 16th and below the national average—with an average of 3.15 referrals per 100,000 individual filers for all 6 years. The South ranked first in these rates. However, the differences among the four regions were small over the period. The South’s 6-year average rate was 3.48 per 100,000 individual filers compared to 3.46, 3.40, and 3.19 in the other 3 regions.

Figure 3 shows that except for 1992 and 1995, the Tennessee-Kentucky district fell below the annual national averages in referrals per 100,000 individual filers. The South’s referral rates were below the national average in 3 years and above it in 3 other years.

**Figure 3: Referral Rates per 100,000 Individual Filers**



Source: GAO analysis of IRS data.

## IRS Has Established Controls Over Audits, Criminal Investigations, and Prosecution Referrals

IRS has established various controls over its audits, criminal investigations, and prosecution referrals. These controls generally consist of a series of standards to guide audit and investigation behavior and a series of reviews to check adherence to the standards. Appendixes IV and V provide detailed information on these controls and standards.

## IRS Audit Standards and Controls

IRS has standards for the selection of returns to audit and for audit quality. To check auditors' adherence to these standards, IRS has developed various types of reviews. These reviews are to occur at the start of all audits as well as during and after selected audits.

The basic audit selection standard is to select tax returns that appear to have a high likelihood of tax noncompliance. To help meet this standard, IRS has selected most returns for audits through computerized criteria

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designed to identify potential noncompliance. IRS also has selected returns for audit through many other sources, such as through projects that focus on known compliance issues within a specific location or a select group of taxpayers. Regardless of how the returns are selected, IRS generally requires various levels of IRS managers and staff to check, among other things, for adherence to the audit selection standard. For the audit projects, IRS districts also require authorization by a district director or higher level management official before audits can begin.

To guide auditors' behaviors during audits, IRS has established quality standards in such areas as developing evidence, considering the potential for fraud, and documenting audit results. IRS audit supervisors are to periodically review audits to determine conformity with the standards. IRS supervisors also are to separately review whether auditors are handling taxpayer inquiries and issues responsively.

After an audit, IRS district office employees and service center employees are to review a sample of audits closed in their offices. IRS Examination officials said that they believe the sample is statistically valid. IRS employees conduct these post-audit reviews to measure the quality of the audits against the standards.<sup>12</sup>

IRS did not have statistics available in a database on how often it uses audit controls through managerial and supervisory reviews at the start of audits and during audits. In prior reports,<sup>13</sup> we found evidence that supervisors reviewed about 6 percent of the workpapers during certain types of audits that closed during fiscal years 1995 and 1996. In noting that IRS did not require supervisors to document these reviews during audits, we recommended that IRS establish such a requirement, which IRS agreed to do.

IRS did have automated statistics on its use of post-audit reviews. These statistics showed that Examination staff in the districts reviewed adherence to quality standards in 12,170 of about 800,000 audits closed by district auditors during fiscal year 1996.<sup>14</sup> Our analysis did not evaluate

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<sup>12</sup>The audit quality measure is also to become part of the quality measurement across IRS. According to IRS officials, implementation of IRS' new measures on customer satisfaction, employee satisfaction, quantity, and quality for various IRS activities is scheduled for January 1999.

<sup>13</sup>GAO/GGD-98-38 and GAO/GGD-98-98.

<sup>14</sup>In December 1998, IRS Examination officials said that the fiscal year 1998 sample size for post-audit reviews in the district offices was approximately 11,900. These officials said that in fiscal year 1999, this sample size will be increased to about 46,900 in order to provide greater statistical validity and accountability at the managerial level in the district offices.

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IRS' sample selection or quality review processes, or whether IRS used the results of the reviews to improve quality.

Apart from these post-audit reviews, IRS Examination officials said that they do periodic operational and peer reviews. According to the officials, the reviews are intended to oversee the use of the controls as well as the entire audit process.

We are currently studying some of these audit selection controls at district offices and audit quality controls at service centers, and we expect to report results in 1999.

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## CID Standards and Controls for the Criminal Investigation and Referral Processes

IRS has established standards governing the criminal investigation and prosecution referral processes. CID also relies on multiple levels of review and approval to check adherence to the standards. If IRS refers a case for prosecution, outside offices are to review, in succession, whether prosecution was justified.

A major standard for initiating a criminal tax investigation involves prosecution potential. As a control for this standard, IRS requires the CID chief to approve investigations. During an investigation, the CID special agent is to gather evidence on whether a criminal violation of tax or nontax issues occurred and, if so, whether prosecution is justified. To check adherence to this and other evidence standards, CID managers are to periodically review the agent's work and evidence. The investigation is to continue until (1) during the course of gathering information the investigator determines a criminal case is not warranted; (2) sufficient evidence has been collected to justify a referral for successful prosecution; or (3) limited resources, cases with higher potential, or other circumstances warrant discontinuation.

If a special agent determines that the evidence pointed to criminal violations, the agent is to write a detailed report on violations that merit prosecution. The report is to be reviewed by the group manager, branch chief, and division chief to check the adequacy of the investigation, sufficiency of evidence, and conformance to legal requirements for prosecution.

If the division chief approves, the prosecution referral is to move to the next levels of review—IRS District Counsel, DOJ's Criminal Tax Division, and the U.S. Attorney. The ultimate responsibility for criminal prosecutions lies with the U.S. Attorney. The U.S. Attorney is to consider two standards in deciding whether to prosecute:

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- (1) sufficient evidence to establish guilt beyond a reasonable doubt, and  
(2) reasonable probability of conviction.

CID did not have automated statistics on how often it used its controls over the investigation and referral processes. However, CID officials said that they believe that the controls to initiate and refer criminal investigations are always used. For example, CID officials stated that during fiscal years 1992 through 1997, 66 percent of the investigations initiated were grand jury investigations, which are opened only with the approval and control of DOJ. Further, the officials said that DOJ and the U.S. Attorney accept most of the referrals for prosecution, which cannot be done without the Chief of CID and the District Counsel's approval of the referral.

In addition, CID officials said that they do quarterly and biannual reviews as well as peer reviews of their operations. The officials said that these reviews are intended to address such things as workload, documentation, and the selection and management of investigations.

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## Agency Comments and Our Evaluation

We requested comments on a draft of this report from the Commissioner of Internal Revenue. Officials representing the Assistant Commissioners for the Examination Division and Criminal Investigation Division, as well as a representative from the Commissioner's Office of Legislative Affairs, provided IRS' comments in a December 3, 1998, meeting. IRS also provided written comments, which are reprinted in appendix VI.

IRS' comments were technical in nature to clarify specific sections of the draft report that described (1) frequency of the use of controls over audits, criminal investigations, and referrals; (2) peer review and other periodic operational reviews; and (3) differences between the Examination and Criminal Investigation Divisions, including those factors that are somewhat outside their control but can affect audit, investigation initiation, and referral rates. We have incorporated these comments into the report where appropriate.

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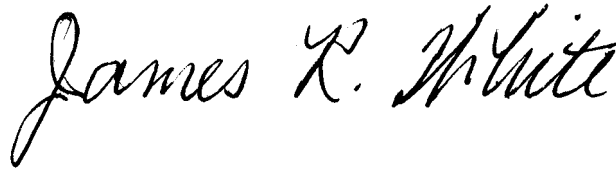
Copies of this report are being sent to the Chairman and the Ranking Minority Member, Senate Committee on Finance; the Chairman and the Ranking Minority Member, Senate Committee on Governmental Affairs; and the Chairman and the Ranking Minority member, House Committee on Ways and Means. We will also send copies to the Director of the Office of Management and Budget; the Secretary of the Treasury; the Commissioner of the Internal Revenue Service; and officials at the Department of Justice,



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Executive Office for U.S. Attorneys, and Administrative Office of the U.S. Courts. We will also make copies available to others upon request.

Major contributors to this report are listed in appendix VII. Please contact me on (202) 512-9110 if you or your staff have any questions about this report.

A handwritten signature in black ink that reads "James R. White". The signature is written in a cursive style with a large, prominent initial "J".

James R. White  
Director, Tax Policy and  
Administration Issues

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## Abbreviations

AIMS	Audit Information Management System
AOUSC	Administrative Office of the United States Courts
CIMIS	Criminal Investigation Management Information System
DOJ	Department of Justice
EOUSA	Executive Office for United States Attorneys
IRS	Internal Revenue Service
TRAC	Transactional Records Access Clearinghouse

# IRS' Individual Audit Rates for Districts, Regions, and Service Centers, Fiscal Years 1992 Through 1997

Table I.1: Individual Audit Rates by District and Ranked, FYs 1992 Through 1997

District	Audit rates						FYs 92-97 Average	Rank
	1992	1993	1994	1995	1996	1997		
Los Angeles	1.37	1.39	1.32	1.34	1.59	1.54	1.43	1
Southern California	1.10	1.28	1.15	1.57	1.62	1.34	1.34	2
Northern California	1.04	1.16	1.15	1.17	1.24	1.34	1.18	3
Southwest	1.00	1.01	1.23	0.98	0.80	0.81	0.97	4
Georgia	0.92	1.07	1.11	1.13	0.78	0.64	0.94	5
Central California	0.93	0.86	0.74	0.92	1.17	0.91	0.92	6
North Texas	0.80	0.82	0.90	1.03	0.96	0.82	0.89	7
Arkansas-Oklahoma	0.95	0.96	1.01	0.85	0.72	0.63	0.85	8
Gulf Coast	0.88	0.80	0.90	0.89	0.83	0.74	0.84	9
Manhattan	0.78	0.62	0.77	1.07	0.75	0.77	0.79	10
Rocky Mountain	0.79	0.80	0.87	0.86	0.73	0.67	0.78	11
South Florida	0.84	0.83	0.87	0.68	0.71	0.68	0.77	12
Houston	0.75	0.81	0.86	0.79	0.76	0.64	0.76	13
Connecticut-Rhode Island	0.69	0.69	0.82	0.83	0.60	0.45	0.68	14
North Central	0.58	0.58	0.83	0.61	0.68	0.76	0.67	15
<b>National average</b>	<b>0.66</b>	<b>0.66</b>	<b>0.72</b>	<b>0.70</b>	<b>0.66</b>	<b>0.61</b>	<b>0.67</b>	
Pacific-Northwest	0.71	0.69	0.73	0.68	0.63	0.51	0.66	16
South Texas	0.67	0.71	0.72	0.73	0.55	0.50	0.64	17
North Florida	0.69	0.67	0.70	0.57	0.52	0.45	0.60	18
Kansas-Missouri	0.46	0.71	0.77	0.55	0.51	0.45	0.57	19
Indiana	0.53	0.51	0.63	0.61	0.51	0.43	0.54	20
<b>Tennessee-Kentucky</b>	<b>0.67</b>	<b>0.58</b>	<b>0.54</b>	<b>0.45</b>	<b>0.40</b>	<b>0.48</b>	<b>0.52</b>	<b>21</b>
Brooklyn	0.48	0.42	0.47	0.59	0.58	0.56	0.52	22
Illinois	0.39	0.39	0.69	0.51	0.47	0.53	0.50	23
North-South Carolina	0.50	0.53	0.55	0.56	0.48	0.34	0.49	24
Delaware-Maryland	0.47	0.42	0.50	0.47	0.53	0.53	0.49	25
New England	0.48	0.46	0.57	0.53	0.46	0.37	0.48	26
Virginia-West Virginia	0.49	0.47	0.60	0.46	0.39	0.39	0.46	27
Midwest	0.34	0.35	0.48	0.49	0.53	0.52	0.45	28
Michigan	0.45	0.40	0.54	0.47	0.44	0.36	0.44	29
Upstate New York	0.44	0.46	0.48	0.43	0.36	0.37	0.42	30
New Jersey	0.39	0.42	0.39	0.39	0.42	0.39	0.40	31
Pennsylvania	0.36	0.37	0.44	0.40	0.36	0.41	0.39	32
Ohio	0.49	0.38	0.34	0.33	0.34	0.32	0.37	33

Source: GAO analysis of IRS data.

**Appendix I**  
**IRS' Individual Audit Rates for Districts, Regions, and Service Centers, Fiscal Years 1992 Through 1997**

**Table I.2: Individual Audit Rates by Region and Ranked, FYs 1992 Through 1997**

Region	Audit rates						FYs 92-97	Rank
	1992	1993	1994	1995	1996	1997	Average	
Western	0.99	1.02	1.02	1.07	1.09	0.99	1.03	1
<b>National average</b>	<b>0.66</b>	<b>0.66</b>	<b>0.72</b>	<b>0.70</b>	<b>0.66</b>	<b>0.61</b>	<b>0.67</b>	
<b>South</b>	<b>0.70</b>	<b>0.69</b>	<b>0.74</b>	<b>0.67</b>	<b>0.58</b>	<b>0.52</b>	<b>0.65</b>	<b>2</b>
Midstates	0.56	0.60	0.74	0.66	0.61	0.58	0.63	3
Northeast	0.48	0.44	0.50	0.50	0.45	0.42	0.46	4

Source: GAO analysis of IRS data.

**Table I.3: Individual Audit Rates by Service Center and Ranked, FYs 1992 Through 1997**

Service center	Audit rates						FY 92-97	Rank
	1992	1993	1994	1995	1996	1997	Average	
Fresno	0.92	0.36	1.08	3.48	3.15	2.01	1.81	1
Brookhaven	0.47	0.39	0.40	1.34	1.18	1.04	0.80	2
Austin	0.31	0.44	0.46	0.88	1.25	0.45	0.64	3
<b>National average</b>	<b>0.40</b>	<b>0.26</b>	<b>0.37</b>	<b>0.98</b>	<b>1.02</b>	<b>0.68</b>	<b>0.62</b>	
Ogden	0.33	0.20	0.25	0.78	0.86	0.74	0.53	4
Philadelphia	0.26	0.15	0.28	1.01	0.83	0.45	0.49	5
Atlanta	0.48	0.24	0.33	0.61	0.80	0.41	0.48	6
Andover	0.33	0.26	0.29	0.55	0.58	0.63	0.44	7
Kansas City	0.32	0.21	0.20	0.61	0.68	0.41	0.40	8
<b>Memphis</b>	<b>0.32</b>	<b>0.22</b>	<b>0.17</b>	<b>0.41</b>	<b>0.60</b>	<b>0.47</b>	<b>0.37</b>	<b>9</b>
Cincinnati	0.31	0.23	0.24	0.42	0.42	0.43	0.34	10

Source: GAO analysis of IRS data.

# IRS' Criminal Investigation Initiation and Prosecution Referral Rates for Districts and Regions, Fiscal Years 1992 Through 1997

**Table II.1: Criminal Investigation Initiation Rates per 100,000 Individual Filers by District and Ranked, FYs 1992 Through 1997**  
Initiation rates per 100,000 Individual filers

District	1992	1993	1994	1995	1996	FYs 92-97		Rank
						1997	Average	
Manhattan	12.22	17.44	17.12	11.23	12.75	9.89	13.44	1
South Texas	10.47	8.43	10.26	5.40	8.04	9.02	8.57	2
South Florida	7.32	7.75	8.39	7.34	8.54	7.76	7.86	3
North Texas	11.10	6.98	6.68	5.65	5.64	5.97	6.98	4
Arkansas-Oklahoma	7.44	8.23	6.73	5.12	7.51	6.45	6.91	5
Brooklyn	7.45	7.72	5.92	5.67	6.42	6.66	6.64	6
Houston	7.60	7.29	5.38	6.39	6.50	6.11	6.53	7
Southwest	6.73	6.72	5.31	4.98	6.05	6.97	6.13	8
Rocky Mountain	8.00	5.98	5.82	5.61	6.18	5.13	6.09	9
Virginia-West Virginia	7.35	5.75	5.93	4.07	4.26	7.15	5.75	10
Delaware-Maryland	6.09	6.10	4.35	5.36	4.61	6.61	5.52	11
Georgia	6.80	5.54	5.54	4.86	3.87	3.96	5.06	12
Northern California	5.64	4.66	4.66	3.72	6.49	4.44	4.94	13
New Jersey	4.81	5.15	5.66	5.37	3.81	4.66	4.91	14
<b>National average</b>	<b>5.78</b>	<b>5.39</b>	<b>4.73</b>	<b>4.39</b>	<b>4.61</b>	<b>4.53</b>	<b>4.90</b>	
North Florida	6.48	6.16	3.52	3.79	4.17	4.78	4.81	15
Pacific-Northwest	5.19	5.46	4.60	5.47	4.59	3.46	4.78	16
Connecticut-Rhode Island	5.48	5.00	5.17	2.90	5.15	4.56	4.72	17
Los Angeles	6.84	4.44	4.70	4.43	3.63	3.22	4.58	18
Pennsylvania	4.86	5.10	4.48	5.19	3.51	3.63	4.46	19
<b>Tennessee-Kentucky</b>	<b>5.36</b>	<b>4.67</b>	<b>3.54</b>	<b>4.34</b>	<b>3.65</b>	<b>3.76</b>	<b>4.22</b>	<b>20</b>
Illinois	5.43	4.29	2.97	3.73	4.35	4.49	4.21	21
Michigan	5.71	5.10	4.59	2.41	4.08	2.57	4.08	22
Indiana	4.13	6.67	3.85	3.37	3.19	3.24	4.06	23
Kansas-Missouri	3.81	4.55	4.43	4.07	3.20	4.04	4.02	24
Southern California	3.64	4.74	3.21	4.73	3.63	4.13	4.01	25
Ohio	5.80	4.62	3.61	3.35	3.12	2.97	3.91	26
Gulf Coast	5.47	4.03	2.65	3.56	4.27	3.35	3.89	27
North-South Carolina	4.61	4.41	3.49	3.29	3.54	3.48	3.79	28
Upstate New York	3.54	3.27	3.77	3.23	3.60	3.12	3.42	29
Central California	4.01	3.62	3.25	2.26	3.07	4.19	3.40	30
North Central	3.16	3.08	3.49	3.19	3.72	3.42	3.34	31
New England	3.25	4.21	2.94	2.66	3.83	3.06	3.33	32
Midwest	3.43	2.44	2.53	3.36	2.64	2.34	2.79	33

Source: GAO analysis of IRS data.



**Appendix II**  
**IRS' Criminal Investigation Initiation and Prosecution Referral Rates for Districts and Regions, Fiscal Years 1992 Through 1997**

**Table II.2: Criminal Investigation Initiation Rates per 100,000 Individual Filers by Region and Ranked, FYs 1992 Through 1997**

Region	Initiation rates						FYs 92-97	Rank
	1992	1993	1994	1995	1996	1997	Average	
Midstates	5.97	5.33	4.75	4.30	4.67	4.75	4.96	1
Northeast	5.53	5.72	5.06	4.39	4.50	4.28	4.91	2
<b>National average</b>	<b>5.78</b>	<b>5.39</b>	<b>4.73</b>	<b>4.39</b>	<b>4.61</b>	<b>4.53</b>	<b>4.90</b>	
<b>South</b>	<b>6.05</b>	<b>5.30</b>	<b>4.47</b>	<b>4.29</b>	<b>4.45</b>	<b>4.70</b>	<b>4.87</b>	<b>3</b>
Western	5.66	5.10	4.51	4.59	4.86	4.46	4.86	4

Source: GAO analysis of IRS data.

**Table II.3: Criminal Investigation Prosecution Referral Rates per 100,000 Individual Filers by District and Ranked, FYs 1992 Through 1997**

District	Referral rates per 100,000 individual filers						FYs 92-97	Rank
	1992	1993	1994	1995	1996	1997	Average	
Manhattan	7.72	10.01	9.63	11.94	10.36	8.92	9.75	1
South Texas	7.95	5.57	6.62	3.85	4.29	5.82	5.65	2
North Texas	9.38	5.41	5.01	3.89	3.44	4.73	5.28	3
South Florida	5.65	3.71	6.20	5.69	5.38	5.01	5.27	4
Brooklyn	4.29	6.45	4.58	4.09	5.35	4.67	4.91	5
Houston	5.05	5.69	3.36	3.73	3.66	3.99	4.24	6
Southwest	4.57	3.60	5.18	3.01	3.93	4.33	4.10	7
Virginia-West Virginia	3.37	5.14	5.10	3.36	2.33	5.17	4.08	8
Arkansas-Oklahoma	4.53	4.11	2.56	3.49	4.96	4.59	4.05	9
Rocky Mountain	5.12	3.97	3.63	3.32	3.52	3.10	3.75	10
Georgia	4.54	3.18	4.01	3.24	3.77	2.84	3.58	11
Delaware-Maryland	3.21	4.00	3.63	2.60	2.78	5.23	3.58	12
New Jersey	2.82	3.81	4.22	3.70	3.05	3.58	3.53	13
<b>National average</b>	<b>3.76</b>	<b>3.75</b>	<b>3.31</b>	<b>3.17</b>	<b>3.12</b>	<b>3.24</b>	<b>3.39</b>	
Pennsylvania	3.19	4.06	3.26	3.32	3.52	3.10	3.38	14
North Florida	2.81	3.78	2.84	2.47	2.97	4.14	3.18	15
<b>Tennessee-Kentucky</b>	<b>4.54</b>	<b>3.30</b>	<b>2.76</b>	<b>3.52</b>	<b>2.26</b>	<b>2.61</b>	<b>3.15</b>	<b>16</b>
Pacific-Northwest	3.34	3.63	2.78	3.34	3.33	2.34	3.12	17
Connecticut-Rhode Island	3.64	3.54	2.68	2.15	3.20	3.22	3.08	18
Kansas-Missouri	3.70	3.20	2.53	2.95	3.14	3.08	3.07	19
Southern California	2.45	3.88	2.68	3.85	2.62	2.78	3.05	20
Northern California	3.04	2.94	3.19	2.53	3.56	2.44	2.95	21
North-South Carolina	3.54	3.26	3.28	1.98	2.57	3.00	2.93	22
Illinois	3.49	3.86	2.25	2.79	2.52	2.39	2.89	23
Indiana	3.14	4.14	3.34	2.50	1.81	2.33	2.87	24
Gulf Coast	3.37	2.82	1.97	2.81	3.23	2.90	2.85	25
Los Angeles	3.13	3.55	2.68	2.42	3.44	1.74	2.84	26
Ohio	3.49	3.72	2.50	2.92	1.97	2.32	2.82	27
Michigan	3.74	3.32	3.32	2.41	1.90	2.09	2.79	28
Central California	3.19	3.00	2.09	2.30	2.32	2.04	2.49	29

**Appendix II  
IRS' Criminal Investigation Initiation and Prosecution Referral Rates for Districts and  
Regions, Fiscal Years 1992 Through 1997**

Referral rates per 100,000 Individual filers								
District	1992	1993	1994	1995	1996	1997	FYs 92-97 Average	Rank
Upstate New York	2.30	1.86	2.26	2.17	3.14	2.30	2.34	30
New England	1.91	2.01	1.63	2.23	2.27	2.59	2.11	31
Midwest	2.21	2.19	1.69	2.77	1.63	1.64	2.02	32
North Central	1.92	2.20	2.01	1.65	1.62	2.60	2.00	33

Source: GAO analysis of IRS data.

**Table II.4: Criminal Investigation Prosecution Referral Rates per 100,000 Individual Filers by Region and Ranked, FYs 1992 Through 1997**

Referral Rates per 100,000 Individual filers								
Region	1992	1993	1994	1995	1996	1997	FYs 92-97 Average	Rank
<b>South</b>	<b>3.88</b>	<b>3.57</b>	<b>3.58</b>	<b>3.16</b>	<b>3.11</b>	<b>3.57</b>	<b>3.48</b>	<b>1</b>
Northeast	3.39	3.95	3.42	3.40	3.26	3.37	3.46	2
Midstates	4.38	3.84	3.07	3.02	2.85	3.25	3.40	3
<b>National average</b>	<b>3.76</b>	<b>3.75</b>	<b>3.31</b>	<b>3.17</b>	<b>3.12</b>	<b>3.24</b>	<b>3.39</b>	
Western	3.48	3.53	3.15	3.03	3.26	2.69	3.19	4

Source: GAO analysis of IRS data.

# Total Number of IRS Audits, Criminal Investigation Initiations, and Prosecution Referrals for Fiscal Years 1992-1997

Tables III.1 to III.3 show how the Tennessee-Kentucky district, Memphis Service Center, and the South ranked in total number of audits closed during fiscal years 1992 through 1997. During this period, IRS' Tennessee-Kentucky District audited 118,545 individual returns. The district ranked 18th of 33 districts and averaged about 20,000 audits annually. The Memphis Service Center ranked 10th among the 10 service centers, averaging about 40,000 audits annually over the 6 years. The South ranked 3rd among 4 regions, averaging about 168,000 audits annually over the 6 years.

**Table III.1: Total Number of Audits by District and Ranked, FYs 1992 Through 1997**

District	Returns audited						Total	Rank
	1992	1993	1994	1995	1996	1997		
Southern California	44,432	52,306	45,755	62,034	63,962	53,991	322,480	1
Los Angeles	46,970	47,069	43,439	42,551	49,590	48,877	278,496	2
Northern California	37,241	41,670	40,586	41,152	43,880	48,363	252,892	3
Gulf Coast	38,511	35,557	39,943	40,386	37,961	34,547	226,905	4
Pacific-Northwest	31,543	31,806	33,738	31,899	29,693	24,500	183,179	5
Southwest	28,773	29,728	36,549	30,261	25,773	26,888	177,972	6
North Texas	25,072	26,113	28,510	33,437	31,397	27,625	172,154	7
Georgia	26,253	31,156	32,773	34,230	24,328	20,575	169,315	8
Rocky Mountain	25,537	26,523	29,529	29,915	26,386	24,717	162,907	9
Illinois	20,952	20,807	36,385	27,314	25,345	28,719	159,522	10
Central California	23,961	22,224	19,130	23,659	29,706	23,649	142,329	11
North-South Carolina	22,737	24,621	25,423	26,346	23,097	17,039	139,263	12
<b>National average</b>	<b>22,463</b>	<b>22,825</b>	<b>24,795</b>	<b>24,106</b>	<b>23,036</b>	<b>21,638</b>	<b>138,863</b>	
South Florida	23,208	23,197	24,364	19,382	20,327	20,047	130,525	13
Pennsylvania	20,100	20,134	23,718	21,378	19,685	22,298	127,313	14
North Florida	23,069	22,984	23,559	19,533	18,304	16,052	123,501	15
New England	20,483	19,013	23,638	22,109	19,252	15,631	120,126	16
Arkansas-Oklahoma	21,640	22,246	23,271	19,839	16,943	15,237	119,176	17
<b>Tennessee-Kentucky</b>	<b>24,731</b>	<b>21,721</b>	<b>20,211</b>	<b>17,148</b>	<b>15,637</b>	<b>19,097</b>	<b>118,545</b>	<b>18</b>
Midwest	14,657	15,053	20,686	21,025	23,171	22,903	117,495	19
Kansas-Missouri	15,544	23,774	26,022	18,627	17,693	15,813	117,473	20
Ohio	24,678	19,631	17,171	16,723	17,774	16,866	112,843	21
Michigan	18,769	16,740	21,943	19,319	18,605	15,607	110,983	22
North Central	14,984	15,179	21,741	16,352	18,585	21,147	107,988	23
Virginia - West Virginia	17,397	17,061	21,418	16,585	15,452	14,433	102,346	24
South Texas	15,564	17,118	17,565	18,343	14,176	13,346	96,112	25
Brooklyn	14,957	12,884	14,136	17,515	17,322	16,885	93,699	26
New Jersey	15,029	16,017	14,587	14,677	15,813	14,639	90,762	27
Houston	14,109	15,587	16,584	15,414	14,875	12,910	89,479	28
Manhattan	14,684	11,605	14,139	19,481	13,734	14,287	87,930	29
Delaware-Maryland	13,863	12,379	14,643	13,735	15,735	15,726	86,081	30
Connecticut-Rhode Island	14,687	14,137	16,512	16,629	11,930	8,994	82,889	31
Indiana	13,285	12,873	15,931	15,402	13,284	11,449	82,224	32
Upstate New York	13,849	14,299	14,625	13,108	10,782	11,198	77,861	33

Source: GAO analysis of IRS data.

**Appendix III**  
**Total Number of IRS Audits, Criminal Investigation Initiations, and Prosecution Referrals**  
**for Fiscal Years 1992-1997**

**Table III.2: Total Number of Audits by Region and Ranked, FYs 1992 Through 1997**

Region	Returns audited						Total	Rank
	1992	1993	1994	1995	1996	1997		
Western	238,457	251,326	248,726	261,471	268,990	250,985	1,519,955	1
<b>National average</b>	<b>185,317</b>	<b>188,303</b>	<b>204,556</b>	<b>198,877</b>	<b>190,049</b>	<b>178,514</b>	<b>1,145,616</b>	
Midstates	155,807	168,750	206,695	185,753	175,469	169,149	1,061,623	2
<b>South</b>	<b>175,906</b>	<b>176,297</b>	<b>187,691</b>	<b>173,610</b>	<b>155,106</b>	<b>141,790</b>	<b>1,010,400</b>	<b>3</b>
Northeast	171,099	156,839	175,112	174,674	160,632	152,131	990,487	4

Source: GAO analysis of IRS data.

**Table III.3: Total Number of Audits by Service Center and Ranked, FYs 1992 Through 1997**

Service Center	Returns audited						Total	Rank
	1992	1993	1994	1995	1996	1997		
Fresno	109,296	43,658	127,146	385,278	361,378	234,514	1,261,270	1
Ogden	42,451	25,976	32,602	105,074	119,695	105,097	430,895	2
<b>National average</b>	<b>45,921</b>	<b>30,272</b>	<b>41,548</b>	<b>112,195</b>	<b>117,970</b>	<b>80,363</b>	<b>428,268</b>	
Austin	32,689	46,808	48,496	95,977	137,371	50,804	412,145	3
Brookhaven	41,371	34,037	34,170	115,044	101,246	79,837	405,705	4
Philadelphia	31,048	17,835	33,073	121,002	99,000	54,980	356,938	5
Kansas City	41,569	27,858	25,967	80,048	91,168	55,507	322,117	6
Atlanta	50,280	25,997	35,011	66,379	88,949	47,022	313,638	7
Cincinnati	42,570	32,556	33,358	58,674	60,724	63,404	291,286	8
Andover	33,871	24,504	27,007	50,020	53,407	58,652	247,461	9
<b>Memphis</b>	<b>34,068</b>	<b>23,486</b>	<b>18,645</b>	<b>44,456</b>	<b>66,758</b>	<b>53,811</b>	<b>241,224</b>	<b>10</b>

Source: GAO analysis of IRS data.

Tables III.4 to III.7 show how the Tennessee-Kentucky district and the South ranked in total number of criminal investigations and prosecution referrals during fiscal years 1992 through 1997, compared to the rest of the country.

During this period, the Tennessee-Kentucky district initiated 960 investigations, ranking 22nd among 33 districts. Also, the South initiated 7,588 investigations, ranking 3rd of 4 regions. As for prosecution referrals during this period, the Tennessee-Kentucky district made 719 referrals, ranking 17th of 33 districts and averaging 120 referrals for all 6 years. The district ranked higher in 2 years—sixth in 1992 and ninth in 1995. The average number of prosecution referrals in the South for all 6 years ranked third of four regions.

**Appendix III**  
**Total Number of IRS Audits, Criminal Investigation Initiations, and Prosecution Referrals**  
**for Fiscal Years 1992-1997**

**Table III.4: Total Number of Criminal Investigations Initiated by District and Ranked, FYs 1992 Through 1997**

District	Investigations initiated						Total	Rank
	1992	1993	1994	1995	1996	1997		
Manhattan	231	326	313	205	234	184	1,493	1
Pennsylvania	268	280	242	279	190	198	1,457	2
North Texas	349	222	212	183	185	201	1,352	3
Illinois	289	230	157	198	233	244	1,351	4
South Florida	202	217	234	209	246	229	1,337	5
Pacific-Northwest	231	250	212	255	218	167	1,333	6
South Texas	245	203	251	136	208	240	1,283	7
Rocky Mountain	258	199	197	196	223	190	1,263	8
Virginia-West Virginia	262	207	213	148	157	267	1,254	9
Brooklyn	231	237	177	169	192	201	1,207	10
Ohio	294	236	183	171	162	157	1,203	11
Southwest	193	198	158	154	194	232	1,129	12
New Jersey	184	196	212	202	144	177	1,115	13
North-South Carolina	211	204	162	156	171	173	1,077	14
Northern California	202	168	165	131	230	160	1,056	15
Gulf Coast	240	180	118	161	196	157	1,052	16
<b>National average</b>	<b>198</b>	<b>186</b>	<b>162</b>	<b>152</b>	<b>161</b>	<b>162</b>	<b>1,021</b>	
Michigan	237	212	188	100	172	111	1,020	17
North Florida	217	210	119	130	146	172	994	18
Delaware-Maryland	180	180	127	157	136	197	977	19
Arkansas-Oklahoma	169	190	155	119	177	156	966	20
Southern California	147	194	128	187	143	166	965	21
<b>Tennessee-Kentucky</b>	<b>197</b>	<b>174</b>	<b>132</b>	<b>165</b>	<b>142</b>	<b>150</b>	<b>960</b>	<b>22</b>
Georgia	195	162	163	147	120	127	914	23
Los Angeles	234	150	154	141	113	102	894	24
New England	138	176	121	110	160	130	835	25
Kansas-Missouri	129	152	149	138	110	142	820	26
Houston	143	141	104	125	128	124	765	27
Midwest	146	105	108	144	115	104	722	28
Upstate New York	111	102	115	98	109	95	630	29
Indiana	104	169	97	85	83	86	624	30
Connecticut-Rhode Island	116	103	104	58	103	92	576	31
North Central	82	81	92	85	101	95	536	32
Central California	103	94	84	58	78	109	526	33

Source: GAO analysis of IRS data.

**Appendix III**  
**Total Number of IRS Audits, Criminal Investigation Initiations, and Prosecution Referrals**  
**for Fiscal Years 1992-1997**

**Table III.5: Total Number of Criminal Investigations Initiated by Region and Ranked, FYs 1992 Through 1997**

Region	Investigations initiated						Total	Rank
	1992	1993	1994	1995	1996	1997		
Northeast	1,990	2,048	1,782	1,549	1,602	1,542	10,513	1
<b>National average</b>	<b>1,635</b>	<b>1,537</b>	<b>1,337</b>	<b>1,250</b>	<b>1,330</b>	<b>1,334</b>	<b>8,422</b>	
Midstates	1,656	1,493	1,325	1,213	1,340	1,392	8,419	2
<b>South</b>	<b>1,524</b>	<b>1,354</b>	<b>1,141</b>	<b>1,116</b>	<b>1,178</b>	<b>1,275</b>	<b>7,588</b>	<b>3</b>
Western	1,368	1,253	1,098	1,122	1,199	1,126	7,166	4

Source: GAO analysis of IRS data.

**Table III.6: Total Number of Criminal Investigations Referred for Prosecution by District and Ranked, FYs 1992 Through 1997**

District	Prosecution referrals						Total	Rank
	1992	1993	1994	1995	1996	1997		
Pennsylvania	176	223	176	195	175	159	1,104	1
Manhattan	146	187	176	218	190	166	1,083	2
North Texas	295	172	159	126	113	159	1,024	3
Illinois	186	207	119	148	135	130	925	4
South Florida	156	104	173	162	155	148	898	5
Brooklyn	133	198	137	122	160	141	891	6
Virginia-West Virginia	120	185	183	122	86	193	889	7
Pacific-Northwest	149	166	128	156	158	113	870	8
Ohio	177	190	127	149	102	123	868	9
South Texas	186	134	162	97	111	155	845	10
North-South Carolina	162	151	152	94	124	149	832	11
New Jersey	108	145	158	139	115	136	801	12
Rocky Mountain	165	132	123	116	127	115	778	13
Gulf Coast	148	126	88	127	148	136	773	14
Southwest	131	106	154	93	126	144	754	15
Southern California	99	159	107	152	103	112	732	16
<b>Tennessee-Kentucky</b>	<b>167</b>	<b>123</b>	<b>103</b>	<b>134</b>	<b>88</b>	<b>104</b>	<b>719</b>	<b>17</b>
<b>National average</b>	<b>129</b>	<b>129</b>	<b>113</b>	<b>110</b>	<b>109</b>	<b>116</b>	<b>706</b>	
Michigan	155	138	136	100	80	90	699	18
North Florida	94	129	96	85	104	149	657	19
Georgia	130	93	118	98	117	91	647	20
Delaware-Maryland	95	118	106	76	82	156	633	21
Northern California	109	106	113	89	126	88	631	22
Kansas-Missouri	125	101	85	100	108	108	627	23
Arkansas-Oklahoma	103	95	59	81	117	111	566	24
Los Angeles	107	120	88	77	107	55	554	25
New England	81	84	67	92	95	110	529	26
Midwest	94	94	72	119	71	73	523	27
Houston	95	110	65	73	72	81	496	28
Indiana	79	105	84	63	47	62	440	29
Upstate New York	72	58	69	66	95	70	430	30
Central California	82	78	54	59	59	53	385	31
Connecticut-Rhode Island	77	73	54	43	64	65	376	32
North Central	50	58	53	44	44	72	321	33

Source: GAO analysis of IRS data.

**Appendix III**  
**Total Number of IRS Audits, Criminal Investigation Initiations, and Prosecution Referrals**  
**for Fiscal Years 1992-1997**

**Table III.7: Total Number of Criminal Investigations Referred for Prosecution by Region and Ranked, FYs 1992 Through 1997**

Region	Prosecution referrals						Total	Rank
	1992	1993	1994	1995	1996	1997		
Northeast	1,220	1,414	1,206	1,200	1,158	1,216	7,414	1
<b>National average</b>	<b>1,063</b>	<b>1,067</b>	<b>936</b>	<b>904</b>	<b>901</b>	<b>954</b>	<b>5,825</b>	
Midstates	1,213	1,076	858	851	818	951	5,767	2
<b>South</b>	<b>977</b>	<b>911</b>	<b>913</b>	<b>822</b>	<b>822</b>	<b>970</b>	<b>5,415</b>	<b>3</b>
Western	842	867	767	742	806	680	4,704	4

Source: GAO analysis of IRS data.

# Audit, Criminal Investigation, and Prosecution Standards

## Audit Standards

As table IV.1 shows, IRS has developed audit quality standards that IRS auditors are to follow. IRS also uses the standards to measure the accuracy and effectiveness of the audit process.

**Table IV.1: Description of IRS' Audit Standards**

<b>Audit standard</b>	<b>Purpose</b>
Adequate consideration of significant items	Requires consideration be given to the large, unusual, or questionable items (i.e., absolute/relative dollar value, multiyear comparisons, intent to mislead, industry/business practices, compliance impact) in both the initial contact stage and during the course of the audit.
Probes for unreported income	Requires that steps be taken to verify that the proper amount of income was reported.
Required filing checks	Requires that consideration be given to the filing and audit potential of all returns required by the taxpayer, including those entities in taxpayer's sphere of influence/responsibility.
Examination depth and conclusions reached	Requires that audited issues be complete to the extent necessary to provide sufficient information to determine substantially correct tax.
Findings supported by law	Requires that the conclusions reached be based on a correct application of tax law.
Penalties properly considered	Requires that the applicable penalties be considered and applied correctly.
Workpapers support conclusions	Requires that the audit techniques and audit trail be fully disclosed and documented.
Report writing procedures followed	Requires that audit findings be presented in the proper content and format and that they are accurate.
Time span or time charged	Requires that the complete audit process is timely.

Note: These standards apply to IRS revenue agents and tax auditors who do audits in district offices. Similar standards apply to correspondence audits done by tax examiners in the service centers, except for the probes for unreported income and the required filing checks.

Source: GAO summary of IRS data.

## Criminal Investigation and Prosecution Standards

A criminal case has two stages: (1) the investigation and review stage and (2) prosecution in court. The investigator assigned to the criminal case must follow specific CID standards in conducting the investigation.

Table IV.2 describes some of the standards that must be followed in the criminal investigation.



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**Appendix IV**  
**Audit, Criminal Investigation, and Prosecution Standards**

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**Table IV.2: Criminal Investigation Standards for Fraud Cases**

<b>Standard</b>	<b>Purpose</b>
Documentation of taxpayer's statements	Requires agents to document the statements made by a taxpayer for use in the criminal case.
Determination of the types of available records	Requires agents to determine whether taxpayer records and supporting documents are available and whether they can be reconciled with tax returns.
Discovery of third-party witness records	Requires agents to use any third-party records that are available to prove the taxpayer's net worth and expenditures.
Use of internal records	Requires agents to gather all records maintained by IRS that may be relevant or may provide investigative leads.
Determination of documentary sources of information	Requires agents to show that all sources of information were considered in gathering evidence of the tax violation, such as confidential sources; other government agencies; business records (i.e., private business records and bank, stock, credit bureau, and insurance records).

Source: GAO summary of IRS data.

Further, CID must apply criminal prosecution standards when investigating potential criminal violations and referring violations for prosecution. These standards include: (1) sufficient evidence must be gathered to establish guilt beyond a reasonable doubt, and (2) only cases having a reasonable probability of conviction should be considered for prosecution.

Other standards that must be considered when determining if a case warrants prosecution are:

- the potential for national or local press coverage that will generate awareness of criminal enforcement and thus foster voluntary compliance;
- localized areas of substantial noncompliance, including actions that appear to represent a trend or common attitude within the community, trade, industry;
- evidence of willful, flagrant, or repetitious violations;
- a pattern of noncompliance, usually over multiple years;
- nonvoluntary disclosure of the tax violation and deficiency;
- the health, age, and mental condition of a taxpayer; and
- whether the same acts or transactions have already been prosecuted.

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# IRS' Controls for Audit, Criminal Investigation, and Prosecution Referral Processes

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For years IRS has had various controls and procedures for conducting audits, criminal investigations, and prosecution referrals. These controls and procedures are designed to guard against any improprieties and misuse of audits and criminal investigations, as well as to better ensure productive use of resources. The following describes what these controls have included.

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## Controls Over the Audit Process

The controls over the audit process occur at three major stages of the audit: (1) selection of the return to audit, (2) supervisory review during the audit, and (3) quality review and measurement upon completion of the audit.

The selection of most audited returns relies on IRS' audit sources. IRS has about 40 audit sources (i.e., programs and techniques used to select potentially noncompliant returns for audit) for identifying returns that need to be audited on the basis of known or suspected noncompliance. The major source for identifying returns for audit is DIF--a computer-generated score designed to predict returns that, if audited, would be most likely to result in changes to the reported tax.<sup>1</sup>

Regardless of the selection method, IRS generally requires various levels of IRS managers and staff to check, among other things, for adherence to the audit selection standard. For the audit projects, IRS district offices also require authorization by a district director or higher level management official before audits can begin. Prior to that authorization, returns should also undergo review at multiple managerial and staff office levels in the district to help ensure an appropriate basis for selecting the return for audit. After selecting returns for audit, IRS requires manual review or classification of the returns. The purpose of classification is to decide whether to accept the return as filed by the taxpayer or to identify all tax issues on the return that should be audited.

During an audit, IRS auditors have a responsibility to do quality audits on a timely basis. IRS has established audit standards to guide auditors' behavior in such areas as probing for unreported income, checking taxpayer claims, developing evidence, considering the potential for fraud, and documenting the audit results. IRS audit supervisors are required to periodically review the audit workload to determine conformity with audit standards as well as the technical accuracy of the audits. In addition, IRS

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<sup>1</sup>Besides DIF, the other sources prompt audits for a variety of reasons. These reasons include taxpayer actions (such as a claim for refund), referrals from either outside or inside IRS, information provided by a third party, indications of fraud or noncompliance through another audits, and special compliance problems identified through projects.

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supervisors also are to do reviews to determine whether auditors are responsive to taxpayers in dealing with taxpayer inquiries and issues. These reviews cover such aspects as professionalism, timeliness, language used, and adequacy of IRS' responses.

During the audit, auditors may ask to expand the audit to include other tax years and related returns of the same taxpayer if, in their professional judgement, either the same or a related compliance problem exists. An auditor is not authorized to audit any tax return that does not meet this criterion. These requests to audit the other returns should be approved by the auditor's supervisor.

After an audit, IRS attempts to measure the quality of the audits against the audit standards.<sup>2</sup> IRS staff across the country review a sample of audits closed through the district offices. This sample usually totals less than 15,000 returns. Similar to the practice at district offices, service center staff are to review a small sample of all closed audits.

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## **Controls Over the Criminal Investigation and Referral Processes**

Controls over the criminal investigation and referral processes consist mainly of multiple levels of review within the Criminal Investigation Division, as well as successive levels of review and approval by the IRS District Counsel, DOJ, and U.S. Attorney. The controls have been put in place to ensure that investigators adhere to the criminal prosecution standards and policies.

In addition, CID officials conduct quarterly reviews, biannual reviews, and peer reviews of their operations. These reviews are intended to address such things as workload, documentation, and the selection and management of criminal investigations.

A criminal tax investigation begins after an investigator determines that a case has prosecution potential. If a case lacks potential, an investigation should not be started. However, if started, the investigation is done to gather evidence that would prove a criminal tax violation. Once the investigation has started, investigators are to continue until (1) during the course of gathering information the investigator determines a criminal case is not warranted; (2) sufficient evidence has been collected to justify a referral for a successful prosecution; or (3) limited resources, cases with higher potential, or other circumstances warrant discontinuation.

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<sup>2</sup> The audit quality measure will also become part of the quality measurement across IRS.

The CID chief is to approve the opening of an investigation. Once an investigation is opened, investigators (CID special agents) are to begin efforts to gather and analyze financial data, conduct interviews, and search public records. The primary function is to gather evidence that documents the movement of money for use in the criminal prosecution. CID managers review all ongoing investigations quarterly to insure that the evidence gathered meets established standards. Referrals for prosecution require review and approval by the CID manager, branch chief, and chief prior to review by District counsel and DOJ.

If the evidence cannot be obtained in any other way, IRS criminal investigators can request search warrants to authorize the search of property and possible seizure of evidence related to the alleged criminal activity. The request for use of a search warrant is to be approved by the CID chief and District counsel, if tax related, before going through the DOJ approval process prior to presentation before a magistrate.

Throughout the process of gathering evidence, the investigator continually analyzes and assesses the information to determine if the evidence substantiates criminal activity. If not, the investigator discontinues the case. Upon completion of data gathering, the criminal investigator prepares a written report detailing findings of violations of the tax law and refers the case for prosecution. The report is to be reviewed by the CID manager, branch chief, and chief for the adequacy of the factual investigation, sufficiency of the evidence, and conformance of the report to the legal requirements for prosecution. The CID manager, branch chief, or chief may determine that the evidence does not substantiate criminal activity and the case should not be prosecuted. In such instances, the case may be sent to the IRS Collection or Examination divisions for civil action.

If the referral is approved in CID, it moves to the IRS District counsel. If the District counsel approves the case, a criminal reference letter is prepared, and the case file is sent to DOJ's Criminal Tax Division. When prosecution is recommended by a Criminal Tax Division attorney and authorized by the Chief and Assistant Attorney General of the Tax Division, the case file is forwarded to the office of the U.S. Attorney in the judicial district where criminal proceedings will be carried out. The case file is sent with instructions to either obtain an indictment--formal accusation or charge for a tax-related crime or other offense--or use a grand jury to obtain further information bearing on the decision to prosecute.

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By the time a case file reaches the U.S. Attorney's Office, the case should have been reviewed and approved at all levels, including CID, the IRS District counsel, and DOJ's Criminal Tax Division, to ensure that established policies and standards have been met. However, upon a final review of the case file by the U.S. Attorney, a decision can also be made not to prosecute the case.

The U.S. Attorney leads the prosecution of individuals charged with violations of federal criminal law. The U.S. Attorney usually relies on the recommendation of the criminal tax specialists in DOJ's Criminal Tax Division on whether to proceed with the prosecution. However, the ultimate responsibility for carrying out the prosecution of a criminal tax case lies with the U.S. Attorney.<sup>3</sup> Generally speaking, the U.S. Attorney exercises a large degree of independence and discretion in handling cases as well as in determining which cases to prosecute.

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<sup>3</sup>The path described is that of a general criminal tax case. However, exceptions include cases that can be directly referred from CID to (1) DOJ and then to the U.S. Attorney, (2) IRS' District Counsel and then to the U.S. Attorney, and (3) the U.S. Attorney.

# Comments From the Internal Revenue Service



CHIEF OPERATIONS OFFICER

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

December 11, 1998

Mr. James R. White  
Director, Tax Policy and Administration  
United States General Accounting Office  
Washington, D.C. 20548

Dear Mr. White:

Thank you for the opportunity to review and comment on your recent draft report entitled "Tax Administration: IRS' Audit and Criminal Enforcement Rates for Individual Taxpayers Across the Country." The opportunity to provide comments to help further clarify certain areas of the report is appreciated.

You stated in your report that a variety of factors can affect the geographic variations in Internal Revenue Service (IRS) audit rates, criminal investigation initiation, and prosecution rates. We would emphasize that the most important factor is the location of taxpayers' noncompliant behavior. Your report states, and the data supports, that the audit rates in the Kentucky-Tennessee District and also in the South were generally at or below the national averages. We would like to emphasize that this relative ranking is based on where, and to the degree, we have identified noncompliance.

We do not have staffing sufficient to audit every return with an error. Therefore, we must allocate more staffing to those locations where our indicators show greater noncompliance. For audits, our primary indicator of noncompliance is, as you have stated, our statistically valid research data. This data enables us to select the returns with the greatest probability of error on a nationwide basis. With respect to returns selected by this system, IRS statistics indicate some states have more returns as a percentage of returns filed, with a higher potential for error than other states. This return "fallout" is a major factor in allocating audit resources and therefore determining audit rates. Thus, geographic locations are relevant only to the degree that noncompliance has been identified.

We also want to emphasize that a Criminal Investigation analysis conducted on the number of per capita convictions by judicial district showed results similar to your analysis of criminal investigation initiation and prosecution referral rates. There is variability across locations, but this variation is not enough over time to conclude that taxpayers in one judicial district are treated differently from those in another geographic location. While IRS conducts criminal investigations and recommends prosecution, the Department of Justice is ultimately responsible for the prosecution of individuals charged with tax and other financial crimes. Factors outside the control of IRS such as the level of illegal activity as well as the numbers of Assistant United States Attorneys and judges in a given geographic area, also contribute to differences in criminal enforcement results across geographic locations.

**Appendix VI**  
**Comments From the Internal Revenue Service**

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The report also makes a number of statements regarding the audit controls we have in place. These controls, as you indicate, are the auditing standards that our auditors are to adhere to as they conduct audits of tax returns. We again strongly emphasize that we actively monitor the entire audit process from start to finish. Return starts are tightly controlled. As you indicate in the report, at the local level, district managers conduct reviews of in-process audits on an ongoing basis. Operational reviews to assure adherence are also conducted by higher level district and region staff. Our extensive Peer Review Process which is ongoing assesses and evaluates the performance of our district operations to ensure adherence to IRS policies and procedures.

Our quality review is a statistically valid sample of closed cases that provides a quantitative measure of the adherence of our auditors to the auditing standards. As we indicated to you, the sample size, 11,900 in Fiscal Year (FY) 1998, was large enough to assure statistical validity to the district level. This means that we can track, on a district-by-district basis, how well our audit controls are adhered to. This information permits management to institute actions that improve adherence to auditing standards in ongoing examinations. As you have noted in the report in FY 1999, we will substantially increase this sample size to 46,900 in order to achieve statistical validity to an even lower managerial level in the districts. This is referred to as the branch level. We would also like to highlight your footnote regarding the fact that the quality of the work done will be one of our business results measures. This shows a strong commitment by the IRS to ensure auditing standard expectations are met.

One final point should be made. Our first priority is service to taxpayers. We are concerned not simply with enforcement rates but with how well we have assisted the taxpayer with meeting their responsibilities and assuring that the tax law has been applied with integrity and fairness to all taxpayers. In some locations, this may require providing a greater degree of taxpayer education and other outreach efforts, in other locations more enforcement may be required.

Again, we thank you for allowing us to provide comment on your report. Be assured that our commitment to quality in our work products and fairness to all taxpayers will always be our priorities.

Sincerely,

  
John M. Dalrymple

# Major Contributors to This Report

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**General Government  
Division, Washington,  
D.C.**

Thomas D. Short, Assistant Director

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**Atlanta Field Office**

Michelle E. Bowsky, Evaluator-in-Charge  
Mark Abraham, Evaluator



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