The Interim Revenue Accounting Control System Is Reliable

December 1999

Reference Number: 2000-10-012

INSPECTOR GENERAL
for TAX
ADMINISTRATION

December 17, 1999

MEMORANDUM FOR COMMISSIONER ROSSOTTI

Pamela J Gardiner

FROM: Pamela J. Gardiner
                       Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Interim Revenue Accounting Control
                       System Is Reliable

This report presents the results of our review of the Internal Revenue Service's (IRS) Interim Revenue Accounting Control System (IRACS). The objective of the review was to evaluate the internal controls over IRACS to ensure they provide accurate financial management information and data integrity.

In summary, we found that compliance with internal controls resulted in the IRACS providing IRS management with reasonable assurance that data processed, stored, and reported by the system are reliable.

Management responded that the successful implementation of IRACS was attributable to the partnership between the IRS' business and information systems organizations. The goal, which was met, was to develop an accounting system that addresses end-user requirements for accurate general ledger posting and provides the Information Systems function with a platform for delivering future enhancements. The full text of management's comments is included as an appendix to this report.

Copies of this report are also being sent to IRS managers who are affected by the report. Please contact me at (202) 622-6510 if you have questions, or your staff may contact Maurice S. Moody, Associate Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

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Executive Summary

The Internal Revenue Service (IRS) is dependent on its accounting system to effectively record and monitor accounting transactions and to document the $1.7 trillion in tax revenues collected each year. The General Accounting Office (GAO) started reporting in 1996 that the IRS revenue accounting system did not provide detailed financial data for assessments and did not comply with standard government accounting guidelines. The Interim Revenue Accounting Control System (IRACS) partially addresses these weaknesses.

The IRS has planned several initiatives to correct the weaknesses identified by the GAO. The first phase of the IRS' efforts was implementing the IRACS at all 10 IRS service centers in 1996. Additional enhancements to the IRS' revenue accounting system will be made as part of a new accounting system planned for implementation in April 2000 and the IRS' efforts to modernize its computer systems.

Our objective was to evaluate the internal controls for IRACS to ensure they provide accurate financial management information and data integrity.

Results

Although IRACS does not address all the weaknesses identified by the GAO, the System is operating as intended, and manual and system controls have provided IRS management with reasonable assurance that data processed, stored, and reported by the system are reliable.

System Requirements For the Interim Revenue Accounting Control System, Problem Identification Procedures, and System Security Are Satisfactory

We judgmentally sampled 24 system requirements in the IRACS Requirements Analysis Package that are critical to the maintenance of accurate IRS financial records. Our analysis of IRACS documentation indicated these requirements were met.

The Posting of Journal Entries To the General Ledger Is Accurate

We tested 550 transactions totaling $10 billion to determine that data are accurately posted to the general ledger. We also evaluated the reconciliation of the general ledger and the subsidiary ledgers of detailed accounts to the Masterfile, a file containing tax information for taxpayers filing tax returns and related documents. All 550 transactions were posted accurately to the general ledger.

Management Information Reports Used to Monitor Internal Revenue Service Transactions Are Accurate and Useful

Accounting employees were generally satisfied with the overall performance of the interim accounting system. All 17 manual assessments totaling $2.7 million that we reviewed were recorded correctly and were accurately reflected on IRS management's reports.

Management's Response: Management responded that the success of the IRACS implementation was attributable to the partnership between the business and information systems organizations. The project goal was to develop an accounting system with accurate general ledger posting, and provide Information Systems with a platform to assist them in timely delivering future enhancements or legislative changes.

Objective and Scope

Our objective was to evaluate the internal controls for the IRACS to ensure they provide accurate financial management information and data integrity.

The objective of this audit was to evaluate the internal controls for the Interim Revenue Accounting Control System (IRACS) to ensure they provide accurate financial management information and data integrity. We conducted testing in the Internal Revenue Service (IRS) National Office Accounting Branch in New Carrollton, Maryland; the Detroit Computing Center (DCC); and the Austin (AUSC), Memphis (MSC), and Ogden (OSC) Service Centers. The audit was performed from July to December 1998 in accordance with *Government Auditing Standards.*

To accomplish our objective, we focused on three aspects of the IRACS:

- Satisfaction of the system requirements.

- Accuracy of general ledger transactions.

- Accuracy and usefulness of management information reports.

We evaluated the processes and procedures designed to ensure data inputs are posted correctly and the data generated accurately reflect the financial activity of the IRS. We also evaluated the processes used to balance the subsidiary records (monthly trial balances and reconciliations) to general ledger accounts.

Appendix I contains the detailed objective, scope, and methodology for our review. Appendix II contains a listing of major contributors to this report.

Background

The IRACS is the computer system the IRS uses as the general ledger, comprised of various accounts such as tax receipts and accounts receivable, to account for the processing of transactions. The processing and reporting of revenue are performed by 10 service centers located throughout the United States, a centralized computing center in Martinsburg, West Virginia, and a computer (mainframe) database at the DCC.

The IRACS was implemented at all 10 IRS service centers in 1996 to resolve weaknesses in the original accounting system. The IRACS was designed to:

- Replace obsolete computer hardware and software while maintaining current processing.

- Improve balancing routines and computer validity checks to ensure the accuracy and consistency of account information.

- Provide additional information through the computer system.

- Increase the IRS' ability to retain historical revenue data.

- Interact electronically with other tax processing systems.

As taxpayer transactions are processed, they are categorized as either pre-journalized or post-journalized accounting transactions. Pre-journalized accounting transactions, usually summarized by type of tax, are posted to the general ledger before going to the Masterfile, a file containing tax information for taxpayers filing tax returns and related documents. Post-journalized accounting transactions are posted to the general ledger after being posted to the Masterfile accounts.

Results

The IRACS' manual and system controls have provided IRS management with reasonable assurance that data processed, stored, and reported by the System are reliable. The current processes and procedures for processing financial data provide reasonable assurance that the data are posted to the general ledger timely and accurately. In addition, the management information reports we reviewed are accurate. These reports provide a record of federal tax deposits and detailed tax assessment data.

The IRACS does not address all the weaknesses identified by the General Accounting Office (GAO), although the System is operating as intended. The GAO-identified weaknesses of the Revenue Accounting Control System (RACS) are contained in Appendix IV. The IRS has addressed two of the six RACS weaknesses with the IRACS and will address the remaining weaknesses with the planned implementation of the Financial Reporting Release System in April 2000.

System Requirements For the Interim Revenue Accounting Control System, Problem Identification Procedures, and System Security Are Satisfactory

The IRACS was designed to serve as the IRS' record of tax revenue due the federal government. System users established the system requirements (the processing and archiving abilities the system must contain).

The IRACS system requirements ensure the maintenance of an accurate record of the IRS' financial transactions.

We judgmentally sampled 24 system requirements in the IRACS Requirements Analysis Package that are critical to the maintenance of accurate IRS financial records. Our analysis of the IRACS documentation indicated these requirements were met. In addition, we judgmentally sampled 50 of 193 trouble tickets

processed by the National Office Command Center between June 1996 and September 1998. The 50 system problems identified by these tickets had been corrected.

The IRS has improved computer security and the satisfaction of internal users in its revenue accounting system, but has not addressed all the weaknesses. In response to the GAO findings, the IRS issued a report to the Department of the Treasury outlining weaknesses that will be addressed by either the IRACS, a new accounting system, or other initiatives. The report also identifies the weaknesses that cannot be addressed because the IRS' computer equipment needs to be modernized. The IRS is taking steps to modernize its computer equipment to address these unresolved weaknesses.

The Posting of Journal Entries to the General Ledger Is Accurate

One of the primary procedures the IRS uses to ensure the completeness and the accuracy of the IRACS is the reconciliation of the accounting records to the Masterfile. We validated the process used to perform this reconciliation, including a review of the reconciliations of the subsidiary records to the general ledger and of the general ledger to the Masterfile. Monthly Trial Balance accounts with a balance opposite the normal balance (i.e., a credit account with a debit balance) were being resolved. The procedures being used for the reconciliation and review of the IRS' revenue accounting records are sound, and all items carried over from one month were reconciled within the next month.

Accounting transactions are posting accurately and timely to the general ledger.

In addition, accounting transactions are posting accurately and timely to the general ledger. We evaluated the accuracy and timeliness of accounting entries through a judgmental sample of the following transactions: 100 assessments, 99 refunds, 100 cash receipts, 101 federal tax deposits and 100 debit

vouchers, which posted during June and November 1998 in the AUSC and the OSC. We also evaluated the accuracy of federal tax deposits through a judgmental sample of 50 Electronic Federal Tax Payment System transactions processed during September 1998 in the MSC. All 550 transactions, totaling approximately $10 billion, were posted accurately and timely to the general ledger.

IRS accounting review procedures also help to ensure transactions are posting correctly to the general ledger. Our analysis of the procedures used to review IRACS generated error reports and our evaluation of an additional 100 transactions that went through accounting review processes indicate the review processes and procedures are functioning as intended. Accounting personnel were conducting required reviews before certifying assessments and refunds. In addition, the certifying and assessment officers and database administrators have been properly appointed and are complying with applicable rules and regulations.

Management Information Reports Used to Monitor Internal Revenue Service Transactions Are Accurate and Useful

The IRACS users are generally satisfied with the System's performance.

Our analysis included a review of the accuracy of two system-generated reports, the Federal Tax Deposit Daily Wire Report and the Summary Record of Assessments Report. The first report provides a record of all federal tax deposits received by type of tax. The second report provides detailed assessment data by type of tax and identifies whether an assessment is based on the tax return filed or an assessment related to an additional tax deficiency. Both reports provide accurate, useful information to system users.

In addition to our analysis of the reports, we reviewed all eight manual assessments, totaling approximately $2.6 million, that were processed on August 19, 1998, in the AUSC and all nine manual assessments, totaling over $147,000, that were processed on

October 22, 1998, in the OSC. All the manual
transactions reviewed were recorded correctly and were
accurately reflected in the respective reports.

Conclusion

*The IRACS has performed
well within its current
environment, and controls
have provided IRS
management with reasonable
assurance of data integrity.*

The IRS is taking steps to address GAO-identified
weaknesses in the revenue accounting system through
various system replacements and its modernization
efforts. Current processes and procedures have provided
reasonable assurance that data processed, stored, and
generated by the IRACS are reliable. System and
manual controls ensure the IRS' revenue accounting
transactions are posting properly to the general ledger.
In addition, IRACS management information documents
are accurate and provide useful information.

The IRS Commissioner responded that the success of
the IRACS implementation was attributable to the
partnership between the business and information
systems organizations. The project goal was to develop
an accounting system with accurate general ledger
posting, and provide Information Systems with a
platform to assist them in timely delivering future
enhancements or legislative changes.

Detailed Objective, Scope, and Methodology

The overall objective of our audit was to evaluate the internal controls for the Interim Revenue Accounting Control System (IRACS) to ensure they provide accurate financial management information and data integrity.

I. Determined whether the IRACS meets the objectives in the requirement analysis dated April 12, 1993, and other best practices for new systems implementation.

    A. Conducted meetings with Customer Service and Information Systems (IS) personnel in the National Office and Accounting personnel in the Ogden (OSC) and Austin Service Centers (AUSC) to determine whether the IRACS meets the system requirements.

        1. Determined the benefits derived from the system implementation.
        2. Identified any planned system enhancements, including those that could be implemented in the new accounting system.
        3. Traced a judgmental sample of 24 critical requirements to the IRACS Business Case, the Investment Evaluation Review, and other IRACS documentation and determined whether the system requirements were satisfied by the IRACS implementation.

    B. Interviewed IS personnel in the Detroit Computing Center (DCC) and Accounting personnel in the OSC and the AUSC to determine if the IRACS replaced obsolete computer hardware and software and if this resulted in improved response time and operation.

        1. Reviewed the IRACS project documentation and actual response time reports as of September 24, 1998.
        2. Reviewed the last volume test report dated April 17, 1996, and reviewed current system documentation to determine if the IRACS is able to handle the volume of transactions processed through the system and whether the system will be able to maintain three years of data.
        3. Evaluated whether the system has sufficient capacity for any expected increase in volume until a new system is implemented.

    C. Reviewed problems identified with the IRACS to determine whether they were corrected and identified the effect any existing problems may have on the System.

1. Interviewed Accounting personnel in the AUSC and the OSC to determine if problems they identified with the System were reported to the National Office.
2. Interviewed Customer Service and IS personnel at the National Office, and reviewed requests to change the System and 50 trouble tickets (indicating system problems) submitted to the National Office Command Center between June 1996 and September 1998, to evaluate the process used to review problems identified by either the service centers or the National Office.
3. Reviewed the Investment Evaluation Review prepared by the Chief Financial Officer's (CFO) Office of Economic Analysis and evaluated the review results. We also determined the methodology used to conduct the review and whether the System was functioning as planned.

D. Reviewed the General Accounting Office's (GAO) examination of the Internal Revenue Service's (IRS) Fiscal Year 1997 financial statements and the IRS' response to the GAO's identification of the general ledger system as a material weakness.

1. Determined what actions the IRS has taken to correct the identified material weaknesses in the general ledger system.
2. Contacted National Office personnel in Customer Service, the CFO Office, and the new system Project Office to determine what actions were planned to correct weaknesses in the general ledger system and the expected completion/implementation dates.
3. Determined what actions the IRS is taking to compensate for the inadequacies of the general ledger system between now and the implementation of its overall modernization effort.

II. Determined if transactions are properly journalized to the general ledger.

A. Performed a walk-through in the Accounting Units in the AUSC and the OSC for each of the following types of transactions – federal tax deposits, cash receipts, assessments, and refunds – and in the Memphis Service Center (MSC) for Electronic Federal Tax Payment System (EFTPS) transactions. Traced the documentation through the IRACS and flowcharted the process.

B. Identified which transactions are processed at the DCC.

1. Documented these transactions and associated programs to identify journal entries that are system generated.
2. Identified any major impact on the DCC processing when receiving the IRACS data from the service centers.

C. Selected a judgmental sample using a random start and interval selection technique of:

- 50 cash receipts, 50 assessments, and 50 refunds processed in the AUSC between July 31, 1998, and September 16, 1998.
- 50 cash receipts, 50 assessments, and 49 refunds processed in the OSC during October and November 1998.

1. Traced the transactions back to the Daily Posting Summary (DPS) in the Accounting Unit to determine whether the transactions were journalized correctly.
2. Evaluated the timeliness of the journalized transactions.

D. Selected a judgmental sample using a random start and interval selection technique of:

- 50 federal tax deposits from the AUSC with deposit dates between August 20, 1998, and September 8, 1998.
- 51 federal tax deposits in the OSC with deposit dates between August 6, 1998, and October 6, 1998.

In addition, we judgmentally selected 50 debit vouchers processed by the Accounting Unit in the AUSC between June 1, 1998, and June 25, 1998, and 50 debit vouchers processed in the OSC between September 11, 1998, and October 5, 1998.

1. Selected 60 (30 in the AUSC and 30 in the OSC) of the 101 federal tax deposits sampled and traced them from the Federal Reserve Bank (FRB) Day Classified Report to the Control Record List (CRL) to verify the accuracy of the report.
2. Selected two transactions (one in the AUSC and one in the OSC) identified from the FRB Day Classified Report and CRL and traced them to the original advice of credit and deposit tickets to verify the accuracy of the transactions.
3. Traced 101 deposit tickets and 100 debit vouchers to the DPS and reconciled the deposit tickets to the FRB Day Classified Reports to ensure all transactions had been correctly journalized.

E. Selected a judgmental sample using a random start and interval selection technique for 50 EFTPS payments processed at the MSC during September 1998.

1. Traced these transactions from the EFTPS information back to the DPS in the Accounting Unit.

2. Reviewed the transactions to determine if the transactions were timely journalized and if the correct general ledger accounts were used.

F. Reviewed Accounting Branch reconciliations to determine whether the reconciliations help ensure that transactions are posting accurately to the IRACS.

1. Reviewed Reciprocal Account Control Record reconciliations for July 1997 through December 1997 in the AUSC, and for January 1998 through June 1998 in the OSC.
2. Reviewed the Reconciliation of General Ledger Accounts (Form 3997) for July 1997 through December 1997 in AUSC, and for January 1998 through June 1998 in the OSC.
3. Reviewed the Monthly General Ledger Trial Balance for July 1997 through December 1997 in the AUSC, and for July 1997 through June 1998 in the OSC.
4. Evaluated any unresolved issues identified through these reconciliations, determined how long these conditions were unresolved, and determined what corrective actions were planned.

G. Identified the reviews performed to ensure transactions are processed accurately.

1. Reviewed the Internal Revenue Manual to determine the requirements for quality and managerial reviews.
2. Interviewed Accounting managers at the AUSC and the OSC to determine what types of reviews, both quality and managerial, are performed before and after work is input to the System, what actions are taken based on the reviews, and how the reviews are documented.
3. Reviewed for accuracy a judgmental sample of 50 transactions that had been through the daily Quality Review process in the AUSC during February, April, and August 1998. We also judgmentally selected and reviewed 50 transactions that had been through the reversal journal entry (17 cases), the journal corrections (16 cases), and the credit transfer document (17 cases) review processes in the OSC between March and October 1998.
4. Identified error reports produced by the IRACS. We evaluated the review process for these reports and the documentation maintained, and reviewed a judgmental sample of these reports to determine how errors are corrected.

H. Reviewed the delegation orders to determine if the Accounting Officer, Certifying Officers, Assessment Officers, and Database Administrators are being properly appointed and complying with applicable rules and regulations.

1. Interviewed the Chief, Accounting Branch, and the Chief, Accounting Control Section, in the AUSC and the OSC to determine if the Service Center

Directors have delegated the authority to carry out the Accounting function. Obtained copies of orders delegating this authority.

2. Reviewed appointing orders and periodic inspections performed by Certifying Officers at the AUSC and the OSC.
3. Reviewed appointing orders and responsibilities performed by the Assessment Officers at the AUSC and the OSC.
4. Interviewed the Database Administrators on their duties and responsibilities.

III. Determined the accuracy and usefulness of the Management Information Systems (MIS) reports provided by the IRACS that assist management in monitoring all IRS transactions.

   A. Interviewed National Office, AUSC and OSC Accounting personnel to determine if they were provided with MIS capabilities through access to IRACS current and historical data.

   1. Identified National Office and service center personnel MIS capabilities.
   2. Identified any new reports that are available to the service center or National Office personnel and determined how these reports are used.

   B. Reviewed the Summary Record of Assessments Report and Federal Tax Deposit Daily Wire Report to determine whether they are accurate and represent all transactions posting during a day.

   1. Reviewed all federal tax deposit transactions input on August 14, 1998, in the AUSC and on October 19, 1998, in the OSC. We also reviewed all manual assessment transactions input on August 19, 1998, in the AUSC and on October 22, 1998, in the OSC.
   2. Obtained a copy of the Summary Record of Assessments Report, the Federal Tax Deposit Daily Wire Report and the DPS for these processing days.
   3. Identified all transactions on the DPS pertaining to the Summary Record of Assessments Report and the Federal Tax Deposit Daily Wire Report for each day.
   4. Reviewed source documentation for all transactions identified in III.B.1. to determine if the transactions were posted properly and the information on the reports is accurate.

Major Contributors to This Report

Maurice S. Moody, Associate Inspector General for Audit (Headquarters Operations and
Exempt Organizations Programs)
Mary Baker, Director
Gary E. Lewis, Director
Nancy Nakamura, Director
Kyle Andersen, Audit Manager
Jim Westcott, Audit Manager
Gary Young, Audit Manager
Deann Baiza, Senior Auditor
Sharon Buford, Senior Auditor
Carl Parmer, Senior Auditor
Nancy Prather, Senior Auditor
Jeff Anderson, Auditor
Doug Barneck, Auditor
John Ojeda, Auditor
Bonnie Shanks, Auditor

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Material Weaknesses Identified by the General Accounting Office

The table below presents the material weaknesses the General Accounting Office identified in various reviews of the Internal Revenue Service's (IRS) revenue accounting system. The IRS has addressed two of the six weaknesses with Interim Revenue Accounting Control System (IRACS) and will address the remaining four weaknesses with the implementation of a planned new accounting system and the modernization of its tax processing systems.

Material Weakness	Addressed by IRACS
IRS' general ledger does not support the preparation of financial statements.	No
IRS lacks a subsidiary ledger for unpaid assessments.	No
Documentary support for unpaid assessments is inadequate.	No
Weaknesses exist in controls over refunds.	No
Revenue accounting and reporting does not meet user needs.	Yes – IRACS improved the satisfaction of internal users.
Controls over computer security are inadequate.	Yes – IRACS is certified C2 security compliant.

Management's Response to the Draft Report

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

OFFICE OF TREASURY
INSPECTOR GENERAL
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1999 NOV -2 A 10 19

FOR TAX ADMINISTRATION

COMMISSIONER

October 28, 1999

MEMORANDUM FOR TREASURY INSPECTOR GENERAL FOR TAX
ADMINISTRATION

FROM: Charles O. Rossotti
          Commissioner of Internal Revenue

SUBJECT: Office of Treasury Inspector General for Tax Administration
          (OTIGTA) Draft Audit Report – The Interim Revenue
          Accounting Control System is Reliable (Reference No.
          19980079)

Thank you for the opportunity to respond to the above-referenced draft report related to
the Interim Revenue Accounting Control System (IRACS). We are pleased that
OTIGTA has validated the integrity and effectiveness of IRACS. It is important to note
that the success of this implementation was attributable to the partnership between our
business and information systems organizations. The project goal was to develop an
accounting system which addresses end-user requirements for accurate general ledger
posting, and provides Information Systems with a platform to assist them in delivering
future enhancements or legislative changes in a timely fashion. This report confirms
that our goal was met.

Even though this report contained no recommendations, we are constantly striving to
enhance IRACS to improve the accuracy and usefulness of revenue accounting posting
and reporting activities; therefore, any additional recommendations are always
welcome.

If you have any questions regarding this response, please feel free to contact
Brien T. Downing, Assistant Commissioner (Forms and Submission Processing), at
(202) 622-2875.