Further Improvements Are Needed in Processes That Control and Report Misuse of Enforcement Statistics

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DEPARTMENT OF THE TREASURY
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INSPECTOR GENERAL
for TAX
ADMINISTRATION

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MEMORANDUM FOR COMMISSIONER ROSSOTTI

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Further Improvements Are Needed in Processes That Control and Report Misuse of Enforcement Statistics

This report presents the results of our review of restrictions on the use of enforcement statistics. Our audit objective was to determine if the Internal Revenue Service (IRS) was complying with restrictions on the use of enforcement statistics to evaluate IRS employees or to impose or suggest production quotas or goals.

In summary, we found that most employee evaluations and management documents did not contain tax enforcement results and did not impose production quotas and goals. However, there were some instances when records of tax enforcement results were used to evaluate employees or to impose or suggest production quotas or goals. The IRS could improve the processes it has implemented to report misuse of enforcement statistics. In addition, employees were not always provided with or evaluated on the performance standard requiring the fair and equitable treatment of taxpayers.

We recommended that the IRS revise its guidelines for the internal review sampling and reporting process to help increase the reliability of the information it provides regarding compliance with the IRS Restructuring and Reform Act of 1998 (RRA 98)[1] § 1204. The IRS should also work toward including the standard requiring the fair and equitable

[1] Pub. L. No. 105-206, 112 Stat. 685.

treatment of taxpayers within a single employee evaluation form for non-management employees.

IRS management agreed with these recommendations. Management's comments have been incorporated into the report where appropriate, and the full text of their comments is included as an appendix.

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

Table of Contents

Executive Summary

Section 1204 of the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)[1] prohibits the IRS from using records of tax enforcement results to evaluate employees or to impose or suggest production quotas or goals. Records of tax enforcement results include information such as dollars collected, number of liens filed or levies served, number of referrals for criminal investigation, dollar amount of assessments made, number of indictments, and number of property seizures made. The responsible supervisors must certify quarterly to the Commissioner as to whether or not they used enforcement statistics to evaluate employees or to impose or suggest production quotas or goals. RRA 98 § 1204 also requires the IRS to include the fair and equitable treatment of taxpayers as one of the standards used to evaluate employee performance.

The RRA 98 requires the Treasury Inspector General for Tax Administration to determine annually whether the IRS is in compliance with restrictions on the use of enforcement statistics.[2] The overall audit objective was to determine if the IRS is complying with restrictions on the use of enforcement statistics to evaluate IRS employees or to impose or suggest production quotas or goals. This report presents the results of our second annual review of the IRS' compliance with these restrictions. In our Fiscal Year (FY) 1999 review,[3] we reported that there were instances when records of tax enforcement results were being used to evaluate employees or to impose or suggest production quotas or goals. We also reported that the IRS had controls in place to identify and report violations, namely the self-certification and independent review processes; however, we did not evaluate those controls.

In carrying out the FY 2000 audit, we reviewed documents in 11 IRS offices, including 6 district offices, 2 service centers, a regional office, the Executive Officer for Service Center Operations, and the Chief Operations Officer.

Results

The IRS has initiated several measures to promote compliance with the restrictions of RRA 98 § 1204. The Office of Managing Statistics was created under the Deputy Commissioner Operations to provide oversight, guidance, and training on the appropriate

[1] Pub. L. No. 105-206, 112 Stat. 685.

[2] 26 U.S.C. § 7803(d)(1)(A)(i) (1999).

[3] *The Internal Revenue Service Should Continue Its Efforts to Achieve Full Compliance with Restrictions on the Use of Enforcement Statistics*, (Reference Number 199910073, dated September 1999).

use of data and statistics. In January 2000, the Office of Managing Statistics began training managers to better understand the restrictions on the use of tax enforcement results. In addition, the IRS has developed new performance measures and evaluation forms.

Nonetheless, the IRS could improve the processes it has implemented to report misuse of enforcement statistics. Most employee evaluations and management documents that we reviewed, and that the IRS also reviewed through its internal review processes, did not contain tax enforcement results and did not impose production quotas or goals. However, there were some instances when records of tax enforcement results were used to evaluate employees or to impose or suggest production quotas or goals. In addition, employees were not always provided with or evaluated on the performance standard requiring the fair and equitable treatment of taxpayers.

The Internal Revenue Service's Processes Could Be Improved to More Accurately Report Improper Use of Enforcement Statistics

RRA 98 § 1204 requires appropriate IRS managers to certify quarterly as to whether they used enforcement statistics to evaluate employees or to suggest production quotas or goals. In the IRS offices we reviewed, most supervisors (99 percent) who had employees covered by RRA 98 § 1204 completed the self-certifications required by law. To ensure that self-certifications are properly reporting compliance with the law, the IRS implemented an annual independent review process in which teams review samples of employee files and management documents to determine compliance with the law and to correct problems.

Nationwide, for the 6-month period ending June 30, 1999, the self-certifications by IRS managers reported 85 violations of RRA 98 § 1204. The IRS independent review teams reported 133 additional violations that were not identified by the self-certifications. These violations should have also been reported in the self-certifications. The 133 violations may be only a portion of the potential violations existing nationally because they represent only the sample results, which have not been projected nationally. Because of concerns that managers were not always aware of what constituted an improper use of enforcement statistics, the IRS has since implemented training to more specifically define the uses of enforcement results that are prohibited by law.

While the self-certifications did not always report violations, the reliability of the independent review results was also limited. For example, the guidelines used to identify violations were later revised to no longer consider some uses of enforcement statistics as violations and the method of drawing the sample for this process did not always identify the appropriate population of supervisors or documents. Because of these factors, the independent review results could not be used to reliably estimate the number of violations nationwide not identified by the self-certification process.

We independently reviewed a random sample of 5,558 documents from 11 IRS offices for the same 6-month period. In these offices, managers' self-certifications identified 21 violations and the IRS independent review teams identified 8 additional violations. In our sample, we identified another four violations. However, these four violations were based on the revised guidelines issued in September 1999, which are less restrictive because some records of tax enforcement results are no longer considered violations.

Overall, our review indicates that the number of violations is low. However, because the violations are based on only a sample of documents in certain offices, it also indicates there are some instances in which inappropriate uses of enforcement statistics have not been identified or corrected by either of the two IRS internal review processes. This could allow the continued use of these statistics by these managers. IRS management recognized that additional actions were needed to better identify RRA 98 § 1204 violations. They are developing guidance to more consistently count the number of RRA 98 § 1204 violations and are discussing methods to make the independent review process more statistically valid.

Employees Were Not Always Evaluated on the Standard Requiring the Fair and Equitable Treatment of Taxpayers

In addition to the restrictions on the use of enforcement statistics, RRA 98 § 1204 also requires the fair and equitable treatment of taxpayers to be incorporated as a performance standard for employee evaluations. In order to meet this standard, an IRS employee must administer the tax laws fairly and equitably, protect taxpayers' rights, and treat each taxpayer ethically with honesty, integrity, and respect.

For a sample of 816 employee personnel files selected at 11 IRS offices, 51 employees (6 percent) had not signed for receipt of this standard. Personnel rules require that employees receive a performance standard at least 60 days before the end of a rating period in order to be evaluated on the standard. Without providing the standard, the IRS cannot evaluate these employees on the fair and equitable treatment of taxpayers, as required by the RRA 98. In addition, 22 of 202 employees (11 percent) who completed a rating period for which they had received this standard, did not have it included as part of their evaluations.

This standard was distributed as a separate document that some managers misplaced or forgot to include when providing employees their performance standards or evaluations. Subsequently, the IRS incorporated the fair and equitable treatment standard into managers' performance agreements and evaluations. The IRS has not done this for employee appraisals because it would require additional union negotiation. As a result, the employee appraisal will continue to be distributed as a separate document.

The New Balanced Measurement System Conforms to the Restrictions on the Use of Enforcement Statistics

The IRS developed procedures to implement a new Balanced Measurement System. The intent of this System is to shift the focus away from achieving specific targets or numbers to achieving the overall mission and strategic goals of the IRS. This System measures performance in three areas: business results (including quality, quantity, and outreach), customer satisfaction, and employee satisfaction. The IRS plans to begin collecting quality and quantity data in FY 2001. Quality and quantity measures will be used together to evaluate organizational performance. Quality measures include an evaluation of whether appropriate actions were taken to resolve cases. Quantity measures include the number of cases processed, as well as the time spent on outreach to taxpayers.

The business results measures will not be the only data that managers use to monitor their organizations. Tax enforcement results data will still be used to prioritize the use of resources and as a diagnostic tool to identify and correct problems. However, the balanced measurement plan requires supervisor evaluations based on actions taken to achieve desired organizational results and not on tax enforcement results data. Balanced measures were included within the manager evaluation process as of December 1999. In our opinion, the balanced measures developed to date, as well as the planned data collection and the planned distributions and use of the data, do not violate the restrictions on the use of enforcement statistics.

Summary of Recommendations

The Office of Managing Statistics (or equivalent in the new organization structure) should revise its guidelines for the independent review teams' sampling and reporting process to help increase the reliability of the information it provides on RRA 98 § 1204 compliance. The independent review teams should maintain adequate documentation of their statistical sampling process so that the overall numbers and types of violations can be estimated and projected nationwide. The Director, Personnel Division (or equivalent in the new organization structure) should also work toward incorporating the standard requiring the fair and equitable treatment of taxpayers into the evaluation forms for all employees.

Management's Response: IRS management agreed with our recommendations and is in the process of revising independent review guidelines to address our recommendations and plans to incorporate the standard requiring the fair and equitable treatment of taxpayers into the evaluation forms for all employees.

Management's complete response to the draft report is included as Appendix VI.

Objective and Scope

The Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)[1] requires the Treasury Inspector General for Tax Administration to determine annually whether the IRS is in compliance with restrictions on the use of enforcement statistics.[2] This report presents the results of our second annual review of the IRS' compliance with these restrictions. In our Fiscal Year (FY) 1999 review,[3] we reported that there were instances when records of tax enforcement results were being used to evaluate employees or to impose or suggest production quotas or goals. We also reported that the IRS had controls in place to identify and report violations, namely the self-certification and independent review processes; however, we did not evaluate those controls.

Our objective was to determine if the IRS is complying with restrictions on the use of enforcement statistics.

The overall audit objective of this review was to determine if the IRS is complying with restrictions on the use of enforcement statistics to evaluate IRS employees or to impose or suggest production quotas or goals. We performed this audit between November 1999 and April 2000 in accordance with *Government Auditing Standards*.

We conducted testing in two offices within the IRS' National Office (the Chief Operations Officer and the Executive Officer for Service Center Operations), one regional office (Northeast Region), two service centers (Cincinnati and Philadelphia), as well as six district offices located in the following four regions:

[1] Pub. L. No. 105-206, 112 Stat. 685.

[2] 26 U.S.C. § 7803(d)(1)(A)(i) (1999).

[3] *The Internal Revenue Service Should Continue Its Efforts to Achieve Full Compliance with Restrictions on the Use of Enforcement Statistics,* (Reference No 199910073, dated September 1999).

• Midstates Region	North Central District
• Northeast Region	Manhattan District Pennsylvania District
• Southeast Region	Gulf Coast District
• Western Region	Central California District Rocky Mountain District

We judgmentally selected the district offices and service centers based upon past audit coverage and results. We reviewed the IRS independent review teams' results covering the period January 1 to June 30, 1999. We also reviewed a separate sample, which included reviews of supervisory documents, as well as employee performance files (EPFs), for the same period. Appendix V shows the numbers and types of documents reviewed.

One significant difference between the FY 1999 audit report and this one is the audit period covered. Because manager annual appraisals are completed for the period ending September 30 each year, manager appraisals were not within the scope of our review. They were included in our review last year, and most of the violations we identified in that review were in evaluation documents. We did review mid-term appraisal information in this review. Due to restricted access to grand jury information, our review within the Criminal Investigation Division was limited to EPFs and performance appraisals.

Details of our audit objective, scope, and methodology are presented in Appendix I. Major contributors to this report are listed in Appendix II.

Background

The RRA 98 became law on July 22, l998.
Section 1204, Basis for Evaluation of Internal Revenue

RRA 98 § 1204 prohibits the IRS from using records of tax enforcement results to evaluate employees or to impose or suggest production quotas or goals.

Service (IRS) Employees,[4] of this law prohibits the IRS from using records of tax enforcement results to evaluate employees or to impose or suggest production quotas or goals for such individuals. The IRS also must use the fair and equitable treatment of taxpayers by IRS employees as one of the standards for evaluating employee performance. These provisions apply to evaluations originating on or after July 22, 1998.

The responsible supervisors must certify quarterly in writing as to whether or not they used enforcement statistics to evaluate employees or to impose or suggest production quotas or goals. To help ensure that self-certifications are properly reporting compliance with the law, the IRS implemented an annual independent review process in which teams of employees and managers from each district, service center, and the National Office area[5] review samples of EPFs and employee evaluations.

The Managing Statistics Handbook has been modified two times since July 1998:

- *June 1999, revised the self-certification and independent review procedures.*
- *September 1999, changed definitions and procedures to conform with, "Establishment of a Balanced Measurement System."*

To assist managers in complying with the law, the IRS issued the Managing Statistics Handbook in July 1998 in the Internal Revenue Manual (IRM).[6] The Managing Statistics Handbook established definitions of records of tax enforcement results and procedures for self-certifications and independent reviews. The Handbook has been modified two times since July 1998—once in June 1999 to provide revised guidance on the self-certification and independent review procedures, and again in September 1999 to change definitions and procedures to be consistent with the new regulation, "Establishment of a Balanced Measurement System."[7] The definitions provided by the Handbook and regulation to help determine compliance with the RRA 98 § 1204 are shown in Appendix IV.

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[4] IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, 112 Stat. 722.

[5] This is based on the IRS organizational structure in effect during our review.

[6] IRM 105.4.

[7] 26 C.F.R. § 801 (August 1999).

Statistics used to monitor inventory or workload (such as hours per case or number of cases closed) are no longer considered to be records of tax enforcement results.

The September 1999 Handbook revision also changed the IRS' position on statistics that measure quality or timeliness of actions and quantity measures. Statistics used to monitor inventory or workload (such as hours per case or number of cases closed) are no longer considered to be records of tax enforcement results. Examples of items still considered to be records of tax enforcement results include information such as dollars collected, number of liens filed or levies served, number of referrals for criminal investigation, dollar amount of assessments made, number of indictments, and number of property seizures made.

Results

The IRS has initiated several measures to promote compliance with the restrictions in RRA 98 § 1204. The Office of Managing Statistics was created under the Deputy Commissioner Operations to provide oversight, guidance, and training on the appropriate use of data and statistics. In January 2000, it began training managers to better understand the restrictions on the use of tax enforcement results. In addition, the IRS has developed new performance measures and evaluation forms.

Most employee evaluations and management documents that we reviewed, and that the IRS reported in its internal review processes, did not contain tax enforcement results and did not impose production quotas and goals.

Nonetheless, the IRS could improve the processes it has implemented to identify and report misuse of enforcement statistics. Most employee evaluations and management documents that we reviewed and that the IRS reported in its internal review processes did not contain tax enforcement results and did not impose production quotas and goals. However, there were some instances when records of tax enforcement results were used to evaluate employees or to impose or suggest production quotas or goals. In addition, employees were not always provided with or evaluated on the performance standard requiring the fair and equitable treatment of taxpayers.

The Internal Revenue Service's Processes Could Be Improved to More Accurately Report Improper Use of Enforcement Statistics

The two primary IRS controls to identify and report RRA 98 § 1204 violations are the self-certification and independent review processes. While the IRS has ensured that these processes are followed, improvements are needed in these processes to more accurately report the improper use of enforcement statistics. Details about these two processes and the areas for improvement follow.

Quarterly self-certification process

As required by law, responsible IRS managers must certify to the Commissioner as to whether or not they used enforcement statistics to evaluate employees or to impose or suggest production quotas or goals.

As required by law, responsible IRS managers must certify to the Commissioner as to whether or not they used enforcement statistics to evaluate employees or to impose or suggest production quotas or goals. To complete this self-certification, managers are required by the IRM to review employee evaluations, EPFs, and management documents and activities, such as operational review results, minutes of meetings, and other pertinent documents and files. If any violations of the law are identified, managers must propose corrective actions to the next management level. The heads of office consolidate the results of these certifications and report the number of violations to the Commissioner.

Most managers (99 percent) in our sample completed self-certifications.

At the 11 IRS offices we reviewed, most IRS supervisors (99 percent) who had employees covered by RRA 98 § 1204 completed a self-certification. Of the 1,367 supervisors identified from organizational charts or timekeeping reports, only 16 did not complete or maintain self-certifications for the quarter ending June 30, 1999. Managers in these cases stated they forgot to complete self-certifications or stated self-certifications were completed but could not be found.

Also, an additional 27 managers without tax enforcement employees (RRA 98 § 1204 employees) completed self-certifications. Managers without tax enforcement employees completed self-certifications because IRS site management thought it was better to have all managers certify. However, since independent review teams selected samples based on listings of managers who completed self-certifications, this conservative approach caused independent review teams to sample and review a number of non-enforcement employees.

Independent review process

To ensure that self-certifications are properly reporting compliance with the law, the IRS implemented an independent review process.

To ensure that self-certifications are properly reporting compliance with the law, the IRS implemented an independent review process. In this process, teams review samples of EPFs and employee evaluations. Teams may also review other management documents, such as operational review results.

Independent review teams randomly select a sample from listings of managers completing self-certifications. Review teams are required to list the immediate employees or subordinate managers in tax enforcement positions for each selected supervisor and randomly select at least two employees per supervisor. This is to ensure review teams sample files of managers and employees that are covered under RRA 98 § 1204.

Independent review teams are required to capture and maintain the number of managers submitting self-certifications, number of managers selected for review, number of EPFs reviewed, and number of other documents reviewed. This information, along with the number of violations identified and the proposed corrective actions, are included within independent review memoranda eventually combined at the national level and reported to the Commissioner.

At the 11 IRS offices we reviewed for the period January 1 to June 30, 1999:

- Review team members were appropriately selected and had the necessary training or experience needed to review management documents.

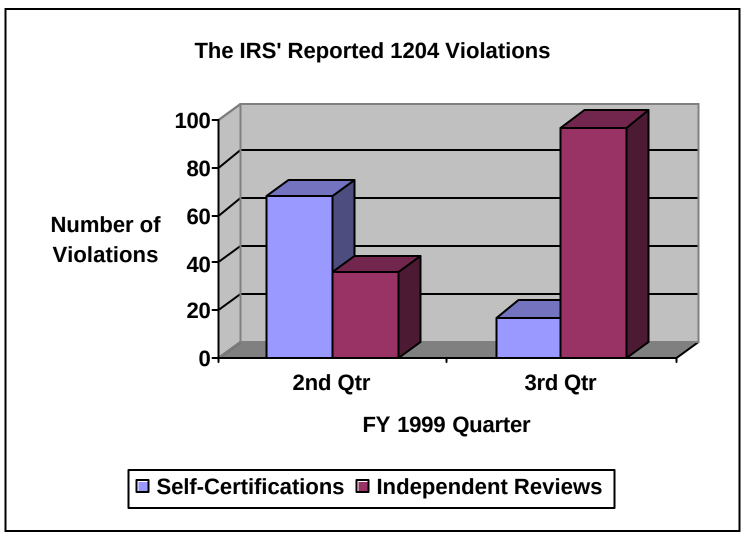
- Managers completed corrective action plans for violations identified by independent review teams.
- Review teams documented and reported the numbers of managers submitting self-certifications, managers selected for review, and employees reviewed.

<u>Results reported in self-certifications and independent reviews and areas for improvement</u>

Self-certifications by IRS managers reported 85 violations. Independent review teams reported 133 additional violations that were not identified by the self-certifications. The 133 violations may be only a portion of the potential violations existing nationally.

Nationwide, for the 6-month period ending June 30, 1999, the self-certifications by IRS managers reported 85 violations of RRA 98 § 1204. The IRS independent review teams reported 133 additional violations that were not identified by the self-certifications. These violations should have also been reported in the self-certifications. The 133 violations may be only a portion of the potential violations existing nationally because they represent only the sample results, which have not been projected nationally. The chart below shows the number of violations reported by quarter by each process.

The IRS' Reported Section 1204 Violations by Self-Certification and Independent Review Samples



Source: Section 1204 Certification Third Quarter FY 1999 Summary of Violations

The IRS determined that the additional violations found in the independent review sample were due to differences in knowledge and understanding between managers completing self-certifications and individuals completing independent reviews.

The IRS determined that the additional violations found in the independent review sample were due to differences in knowledge and understanding between managers completing self-certifications and individuals completing independent reviews. Because of concerns that managers were not always aware of what constituted an improper use of enforcement statistics, the IRS has taken several actions to more specifically define the uses of enforcement results that are prohibited by law. The IRS has implemented training and is revising current guidelines and an Internet question and answer site for employees.

While self-certifications did not always report violations, the reliability of independent review results is also limited for a number of reasons. Because of the following factors, the independent review results cannot be used to reliably estimate the number of violations nationwide not identified by the self-certification process.

Inconsistent sampling and review of management documents

Some independent review teams did not review many important management documents, such as operational review results, that must be covered by the manager self-certifications.

Some independent review teams did not review many important management documents, such as operational review results, that must be covered by the manager self-certifications. Of the 11 independent review team results memoranda reviewed for the period January 1 to June 30, 1999:

- One team reported reviewing no management documents.
- Three teams reported reviewing management documents but did not report the number reviewed.
- Six teams reported reviewing from 3 to 72 management documents.
- One team reported reviewing 288 management documents.

IRS guidelines do not require independent review teams to review management documents.

Changing the IRS' interpretation of RRA 98 § 1204 violations

The IRS changed its interpretation of inappropriate use of enforcement statistics to provide managers with types of quantity measures.

The IRS changed its interpretation of the inappropriate use of enforcement statistics, and as a result, certain records of tax enforcement results were no longer considered violations. For example, under guidelines in effect for the independent reviews conducted during January 1 through June 30, 1999, front-line Customer Service managers could not have access to reports measuring the duration of telephone calls. Of the 133 violations identified by the independent reviews, 28 violations were from managers using worksheet-monitoring reports containing this measure. Under revised guidelines (September 1999), this measure, as well as other quantity measures, such as hours per case or number of cases closed, are not records of tax enforcement results and would not be considered violations.

Non-enforcement managers included in samples

Independent review teams reviewed 86 of 943 (9 percent) employees who were not in tax enforcement positions.

Some independent review teams' samples included employees who were not in tax enforcement positions and did not make decisions related to the assessment or collection of tax. At the 11 locations we visited, independent review teams reviewed 86 of 943 (9 percent) employees who were not in tax enforcement positions. Review teams were not required to screen self-certification listings (some managers without tax enforcement employees were completing self-certifications) to ensure samples were chosen from only managers of tax enforcement employees. Review teams were also not following IRS guidance to identify tax enforcement employees for each supervisor selected. For example, at 1 of the 11 locations we visited, 24 of 109 (22 percent) employees chosen for review were from non-tax enforcement support functions within Quality Assurance and Management Support.

Lack of documentation of the independent review sampling process

In addition, 5 of 11 independent review teams did not maintain documentation that showed how supervisors and employees were selected for review.

In addition, 5 of the 11 independent review teams did not maintain documentation that showed how supervisors and employees were selected for review (2 of the 5 also did not maintain a complete listing of employees actually reviewed). IRS guidelines do not require independent review teams to maintain complete sampling and reviewer documentation.

Comparison of review results in selected locations

We independently reviewed a random sample of 5,558 documents from 11 IRS offices for the same period (January 1 to June 30, 1999). We reviewed 3,026 employee documents within 816 EPFs and 2,532 supervisor documents. The numbers and types of documents reviewed are shown in Appendix V.

We identified another four violations in our sample that were based on the revised guidelines issued in September 1999, which are less restrictive because some records of tax enforcement results are no longer considered violations.

In these offices, managers' certifications identified 21 violations and the IRS independent review teams identified 8 additional violations for the same 6-month period. In our sample, we identified another four violations that were based on the revised guidelines issued in September 1999, which are less restrictive because some records of tax enforcement results are no longer considered violations. Managers' self-certifications and independent review teams did not report the violations that we later identified. Three of the violations we identified were instances in which managers were provided reports comparing the number of fraud referrals among Examination groups. The fourth violation was due to the use of dollar results information in an evaluation that had also been included in a prior evaluation. Managers were not aware that these instances were violations. Independent review teams did not review fraud referral reports or the one EPF with violations.

Overall, our review indicates the number of the RRA 98 § 1204 violations is low. However, because our results are based on only a sample of documents in certain offices, it also indicates there are some instances in which inappropriate uses of enforcement statistics have not been identified or corrected by either the self-certification or independent review processes. This could allow the continued use of these statistics by these managers.

IRS management recognized that additional actions were needed to better identify RRA 98 § 1204 violations. They are developing guidance to more consistently count the number of RRA 98 § 1204 violations and are discussing methods to make the independent review process more statistically valid.

Recommendations

1. The Office of Managing Statistics (OMS) (or equivalent in the new organization structure) should revise independent review guidelines to:
   - Require independent review teams to also review a representative sample of management documents.
   - Require team leaders to screen listings of managers completing self-certifications to ensure only managers with tax enforcement employees are within the population to be sampled.
   - Establish procedures to estimate the projected number of violations for all IRS managers based on sample results.
   - Maintain documentation of each review teams' complete sampling methodology.

<u>Management's Response</u>: The OMS is in the process of revising independent review guidelines to require that operational review documents be included in the independent review sample and to strongly suggest that the management documents most commonly referenced in the self-certifications also be included in the independent review process. The OMS also developed a RRA 98 § 1204 self-certification waiver process for managers who believe their groups' activities are

non-RRA 98 § 1204 activities and worked with the IRS' Research Division to determine the most reliable sampling and reporting process for the independent reviews. The OMS has developed a basic methodology and format for submission for the independent review process, which will be maintained by the appropriate supervisor.

2. The OMS (or equivalent in the new organization structure) should ensure that these procedures are carried over into the new IRS business units, as the units become operational.

Management's Response: The OMS is taking action to integrate the RRA 98 § 1204 process within the new IRS Operating Divisions. Independent review guidelines are being clarified based upon feedback from the new Operating Divisions.

Employees Were Not Always Evaluated on the Standard Requiring the Fair and Equitable Treatment of Taxpayers

The IRS implemented procedures to incorporate the fair and equitable treatment of taxpayers as a performance standard for employee evaluations.

In addition to the restrictions on the use of enforcement statistics, RRA 98 § 1204 also requires the fair and equitable treatment of taxpayers to be incorporated as a performance standard for employee evaluations. In order to meet this standard, an IRS employee must administer the tax laws fairly and equitably; protect all taxpayers' rights; and treat each taxpayer ethically with honesty, integrity, and respect. The IRS implemented the following procedures to comply with this provision:

- As of July 1999, all employees must sign for receipt of the fair and equitable treatment standard.
- If evaluations are due after 60 days of an employee's receipt of the standard, the supervisor must rate the employee as to whether the employee met the standard.

- Employees not meeting this standard are not eligible for performance awards, within grade increases, and promotions. Probationary (new) employees would not be made permanent. Intentional failure to follow proper procedure is also a conduct violation and could result in termination of employment.[8]

From a sample of 816 EPFs, 51 employees (6 percent) had not received this standard. In addition, 22 of 202 employees (11 percent) that received the standard did not have it included as part of their evaluations.

To determine whether the IRS is properly providing and rating employees on this standard, we reviewed a random sample of employee personnel files in 11 offices. From a sample of 816 EPFs, 51 employees (6 percent) had not received this standard. Personnel rules require that employees receive a performance standard at least 60 days before the end of a rating period in order to be evaluated on the standard. Without providing the standard, the IRS cannot evaluate these employees on the fair and equitable treatment of taxpayers, as required by the RRA 98. In addition, 22 of 202 employees (11 percent) who completed a rating period for which they had received this standard at least 60 days before the end of the period did not have it included as part of their evaluations.

Since the IRS distributed the standard as a separate form from the evaluation, managers misplaced the forms or forgot to complete them when providing employees their performance standards or evaluations. Subsequently, the IRS incorporated the fair and equitable treatment standard into managers' performance agreements and evaluations. The IRS has not done this for employee appraisals because it would require additional union negotiation. As a result, the employee appraisal will continue to be distributed as a separate document.

Recommendation

3. The Director, Personnel Division (or equivalent in the new organization structure) should work toward incorporating the standard requiring the fair and

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[8] Pub. L. No. 105-206, 112 Stat. 685 § 1203.

equitable treatment of taxpayers into the evaluation forms of all employees.

Management's Response: The IRS plans to incorporate the fair and equitable treatment standard into both the job elements and performance rating forms of all employees. The IRS has also issued memoranda to managers advising them of the RRA 98 § 1204(b) requirements regarding this standard and has instructed independent review teams to determine whether employees are being evaluated on the fair and equitable treatment standard.

The New Balanced Measurement System Conforms to the Restrictions on the Use of Enforcement Statistics

The intent of the Balanced Measurement System is to shift the focus away from achieving specific targets or numbers to achieving the overall mission and strategic goals of the IRS.

In September 1999, the IRS established a regulation[9] that creates the Balanced Measurement System and sets forth rules governing the use of "records of tax enforcement results" as required by the RRA 98.[10] The intent of the Balanced Measurement System is to shift the focus away from achieving specific targets or numbers to achieving the overall mission and strategic goals of the IRS. The Balanced Measurement System measures performance in three areas: customer satisfaction, business results, and employee satisfaction. The table below shows the goals and objectives for each measure.

[9] 26 C.F.R. Part 801 (August 1999).

[10] Pub. L. No. 105-206, 112 Stat. 685 § § 1201 & 1204.

Balanced Measures and IRS Goals

Goals and Objectives	Balanced Measure
Service to Each Taxpayer • Make filing easier • Provide first quality service to each taxpayer needing assistance • Provide prompt, professional, helpful treatment to taxpayers in cases where additional taxes may be due	Customer Satisfaction
Service to All Taxpayers • Increase fairness of compliance • Increase overall compliance	Business Results (Quality, Quantity, and Outreach)
Productivity through a Quality Work Environment • Increase employee job satisfaction • Hold agency employment stable while economy grows and service improves	Employee Satisfaction

Source: IRS Publication 3561 (01-2000)

According to the IRS, each element represents an important aspect of the organization's goals and each is of equal importance in carrying out the IRS' programs. Consequently, any activity involving balanced measures, such as setting goals, assessing progress, and evaluating results, must consider and address all elements of the Balanced Measurement System.

The IRS has developed balanced measures for most of its functions and new operating divisions, as well as appropriate methods for collecting and disseminating data. Different levels of data will be used by different levels of management to assess the effectiveness of their operations.

Quality and quantity measures will be used together to evaluate organizational performance.

The IRS plans to begin collecting quality and quantity data in the format needed for business results measures in FY 2001. Quality and quantity measures will be used together to evaluate organizational performance.

- Quality measures include an evaluation of whether appropriate actions were taken to resolve cases.

This will be determined through a statistical sample reviewed by the IRS quality review functions.

- Quantity measures will focus on workload and resource management, including factors such as the number of cases processed and the time spent on outreach to taxpayers. The IRS will use its inventory management systems to provide this type of information.

The table below shows some examples of business results used by the IRS in monitoring workload and performance.

Examples of Business Results

Function	Business Result	Frequency Measured
IRS-wide	Total Net Revenue Collected	Semiannually
IRS-wide	Total Enforcement Revenue Collected	Monthly
Submission (Returns) Processing	Timeliness of Refunds	Weekly and Monthly
Examination Division	Number of Returns Closed	Monthly
Collection Division	Percentage of Cases Overage	Monthly

Source: FY 2001 IRS Budget Submission (February 2000)

Tax enforcement results data will still be used to prioritize the use of resources and as a diagnostic tool to identify and correct problems.

The business results measures will not be the only data that managers use to monitor their organizations. Tax enforcement results data will still be used to prioritize the use of resources and as a diagnostic tool to identify and correct problems. However, the balanced measurement plan requires supervisor evaluations for balanced measures to be based on actions taken to achieve desired organizational results and not on tax enforcement results data. Balanced measurement criteria were included within the manager evaluation process as of December 1999. Under the new criteria, management responsibilities include:

- Leadership.
- Employee Satisfaction.

- Customer Satisfaction.
- Business Results.
- Equal Employment Opportunity.

In our opinion, the balanced measures developed to date, as well as the planned data collection and the planned distributions and use of the data, do not violate the restrictions on the use of enforcement statistics.

Conclusion

The IRS has initiated several measures to promote compliance with tax enforcement statistics restrictions, including better training and guidance, as well as new performance measures and evaluation forms. Most employee evaluations and management documents did not contain tax enforcement results and did not impose production quotas and goals.

However, there were some instances when records of tax enforcement results were used to evaluate employees or to impose or suggest production quotas or goals. The IRS could improve the processes it has implemented to report misuse of enforcement statistics. In addition, the IRS needs to ensure that employees are properly evaluated on the performance standard requiring the fair and equitable treatment of taxpayers.

The IRS created a Balanced Measurement System to shift the focus away from achieving specific targets or numbers to achieving the overall mission and strategic goals of the IRS. The procedures developed to date for this system comply with the restrictions on the use of enforcement statistics.

Appendix I

Detailed Objective, Scope, and Methodology

The overall audit objective was to determine if the Internal Revenue Service (IRS) is complying with restrictions on the use of enforcement statistics to evaluate IRS employees or to impose or suggest production quotas or goals. To accomplish our objective, we performed the following tests:

I. Reviewed IRS managers' IRS Restructuring and Reform Act of 1998 (RRA 98)[1] § 1204 self-certifications and determined whether they were comprehensive and if the independent review process adequately assessed the accuracy of enforcement statistics reported in managers' self-certifications.

A. Reviewed the IRS' guidance and directives (specifically the Internal Revenue Manual (IRM) 105.4 Chapter 10 *Certification and Independent Review Process* dated June 4, 1999, and September 15, 1999) to determine if they were comprehensive and consistent with the requirements of RRA 98 § 1204.

B. Reviewed the responses to the Deputy Commissioner Operations Section 1204 Certification memorandum dated April 5, 1999, for any reported suggestions on improving the certification and independent review processes.

C. Obtained, evaluated, and compared the results of the IRS' independent review and self-certification reports for the certification period covering January 1 to June 30, 1999, and identified offices and operations where there were differences between the numbers of violations.

At 11 IRS offices (the Office of the Chief Operations Officer, Executive Officer for Service Center Operations, Northeast Regional Office, Cincinnati and Philadelphia Service Centers, and the Central California, Gulf Coast, Manhattan, North Central, Pennsylvania, and Rocky Mountain District Offices), we:

D. Determined if the IRS appropriately identified all management employees required to prepare certifications for the quarter ending June 30, 1999.

E. Determined whether independent reviews were adequately conducted and appropriately identified all RRA 98 § 1204 violations for the period January 1 to June 30, 1999.

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[1] Pub. L. No. 105-206, 112 Stat. 685.

1. Determined whether review team members were appropriately selected (independent of the managers they were reviewing) and possessed the knowledge (training) necessary to identify a RRA 98 § 1204 violation.

2. Evaluated the process for conducting independent reviews of RRA 98 § 1204 certifications, including reviewing national guidelines governing the independent review process, as well as local procedures at the locations we visited.

3. Determined whether sampling methods were consistent with the IRM guidelines.

   - Determined whether any certifying managers were excluded from the independent review process (such as managers in remote posts-of-duty) and whether teams examined sufficient documentation to ensure the accuracy of the certifications.
   - Reviewed how violations were counted to determine if the IRS sites were consistent in reporting violations.
   - Determined whether teams identified all violations that occurred in the review period.

4. Determined whether all identified violations had corrective action plans.

   - Evaluated plans to determine if corrective actions would reasonably be expected to eliminate additional violations.
   - Verified whether the appropriate IRS official reviewed and agreed to the corrective actions or specified alternatives for their respective operations.
   - For areas or groups with a significant number of violations, determined whether they took adequate corrective actions if they had violations reported in prior periods and whether the corrective actions should have prevented the recent violations from occurring.

F. Independently selected and reviewed a random sample of documents created during the period of January 1 to June 30, 1999, at the above listed 11 IRS offices.

1. Obtained listings of the 1,003 managers who completed self-certifications for the quarter ending June 30, 1999, and used statistical methods within the IRM to randomly select 408 managers for review. Randomly selected 816 employees (two employees for each of the 408 managers) and reviewed their employee performance files (EPFs), including case reviews, evaluations, self-assessments, feedback to evaluations, award narratives, performance plans, and improvement plans.

2. For the above managers, also reviewed managerial documents, such as meeting minutes, drop files (for employees selected), e-mails, read files, operational and workload reviews, grievances, group discussions, local guidance, and briefing documents (due to restricted access to grand jury information, our review within the Criminal Investigation Division was limited to EPFs and performance appraisals).
3. For each violation identified, determined whether the violation was reported in the manager's self-certification or in the independent review process and whether corrective actions were taken.
4. Determined whether non-enforcement statistics, such as cycle time and inventory, were being used to evaluate employees or establish quotas that may lead to inappropriate taxpayer treatment.

II. Determined whether the IRS incorporated the fair and equitable treatment of taxpayers into employee performance standards.

A. Obtained and reviewed the final regulations for incorporating the fair and equitable treatment of taxpayers into employee performance standards.

B. Determined whether the IRS' implementation guidance and directives were comprehensive and consistent with the requirements of RRA 98 § 1204.

C. Using the same random sample in I.F., reviewed 816 EPFs and determined if the standard requiring fair and equitable treatment of taxpayers was provided to employees and properly included in employee performance appraisals.

III. Determined whether the IRS' plans for the new Balanced Measurement System were in compliance with RRA 98 § 1204 provisions.

A. Obtained and reviewed the final regulations[2] establishing the Balanced Measurement System.

B. Reviewed sources and types of information that will be used for the IRS Balanced Measurement System, as well as the planned distribution of this information.

C. Determined whether the IRS has an implementation plan and is progressing toward integrating the Balanced Measurement System performance standards.

D. Determined whether any of the balanced measures for enforcement officers are not in compliance with RRA 98 § 1204.

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[2] 26 C.F.R. Part 801 (August 1999).

Appendix II

Major Contributors to This Report

Maurice S. Moody, Associate Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)
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Appendix III

Report Distribution List

Deputy Commissioner Operations C:DO
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Chief, Criminal Investigation CI
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Organizational Performance Management Executive C:DO:OPME
Director, Office of Managing Statistics C:DO:OMS
Assistant Commissioner (Collection) OP:CO
Assistant Commissioner (Customer Service) OP:C
Assistant Commissioner (Examination) OP:EX
Executive Officer for Service Center Operations OP:SC
Director, Office of Program Evaluation and Risk Analysis M:O
Office of Management Controls CFO:A:M
Director, Legislative Affairs CL:LA
Director, Personnel Division M:S:P
Director, Strategic Human Resources M:CE
Regional Commissioner (Northeast Region)
Regional Director of Appeals (Northeast Region)
Director, Cincinnati Customer Service Center
Director, Philadelphia Customer Service Center
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- Chief, Management and Finance M
- Chief Operations Officer OP
- Chief, Appeals C:AP
- Chief, Criminal Investigation CI
- National Taxpayer Advocate C:TA
- Assistant Commissioner (Collection) OP:CO

Assistant Commissioner (Customer Service) OP:C
Assistant Commissioner (Examination) OP:EX
Executive Officer for Service Center Operations OP:SC
Director, Office of Program Evaluation and Risk Analysis M:O
Director, Strategic Human Resources M:CE

Appendix IV

Definitions Used for Self-Certifications and Independent Reviews

Section 1204 Employee: The Internal Revenue Service (IRS) defines a "Section 1204 employee" as, "an employee who exercises judgment in recommending or determining whether or how the IRS should pursue enforcement of the tax laws." The IRS has many types of Section 1204 employees in its various functions, including:

- Revenue Officers (Collection).
- Revenue Agents (Examination).
- Special Agents (Criminal Investigation).
- Field Advocacy Analysts (Taxpayer Advocate).
- Appeals Officers.
- District and Service Center Directors.

Tax Enforcement Result: The September 1999 Managing Statistics Handbook defined a tax enforcement result as, "the outcome produced by an IRS employee's exercise of judgment recommending or determining whether or how the IRS should pursue enforcement of the tax laws."

Each IRS function has its own set of tax enforcement results. These results include a dollar amount of audit adjustment or a dollar amount collected on taxes owed. Results also include obtaining a delinquent return, filing a lien, serving a levy, or seizing an asset.

Record of Tax Enforcement Results: The July 1998 Managing Statistics Handbook defined a record of tax enforcement results as, "a figure resulting from the recordation, accumulation, tabulation, or mathematical analysis that is directly related to producing a tax enforcement result." The September 1999 revision changed this definition to allow managers to discuss tax enforcement results on individual cases. The new definition is, "data, statistics, compilations of information or other numerical or quantitative recordations of the tax enforcement results reached in one or more cases, but do not include the tax enforcement results of individual cases when used to determine whether an employee exercised appropriate judgment in pursuing enforcement of the tax laws based upon a review of the employee's work on that individual case."

Appendix V

Documents Reviewed by the Office of Audit

Types of Documents Reviewed	Number of Documents Reviewed	Number of RRA 98 § 1204 Violations
Case Reviews	1,730	0
Evaluations	464	1
Self-Assessments	99	0
Feedback to Evaluations	94	0
Awards Narratives	76	0
Performance Plans	16	0
Improvement Plans	9	0
Other Documents	538	0
Total Employee Documents	**3,026**	**1**
Meeting Minutes	1,002	0
Drop Files	277	0
Electronic Mail	202	0
Read Files	177	0
Operational Reports	152	0
Grievances	62	0
Group Discussions	43	0
Local Guidance	28	0
Other Documents	589	3
Total Supervisor Documents	**2,532**	**3**
Total Documents	**5,558**	
Total Violations		**4**

Source: Office of Audit Review

Appendix VI

Management's Response to the Draft Report

COMMISSIONER

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

RECEIVED
SEP 08 2000
10:45 AM

September 8, 2000

MEMORANDUM FOR TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

FROM: Charles O. Rossotti
for Commissioner of Internal Revenue

SUBJECT: Treasury Inspector General of Tax Administration (TIGTA) Draft Audit Report - Further Improvements Are Needed in Processes That Control and Report Misuse of Enforcement Statistics (Audit No. 199910110)

Thank you for the opportunity to respond to your draft report entitled "Further Improvements Are Needed in Processes That Control and Report Misuse of Enforcement Statistics." The report reflects the results of a review of 5,558 documents created between January 1, 1999, and June 30, 1999. We see this annual review as an opportunity to improve management control for identifying and reporting Restructuring and Reform Act of 1998 (RRA 98) Section 1204 violations, as well as assisting us in providing clearer guidance on managing statistics in a balanced measurement system.

Your report said the Internal Revenue Service could improve the processes it has implemented to identify and report misuse of enforcement statistics. We agree with these observations and recommendations and are pleased the report recognized that the IRS has taken significant steps to promote compliance with the restrictions in RRA 98 Section 1204.

The Deputy Commissioner Operations created the Office of Managing Statistics (OMS) to centralize the responsibilities for complying with section 1204 under one office and provide oversight, guidance, and training on the appropriate use of data and statistics. In January 2000, the IRS began training managers to better understand the restrictions on the use of tax enforcement results. Shortly after establishing OMS in October 1999, we implemented a consistent method of counting violations. We clarified through Course 9008 Managing Statistics in a Balanced Measurement System, and the Internal Revenue Manual which employees and managers are considered Section 1204 covered. In addition, we developed new performance measures and performance evaluation forms. The recent self-certification process for the quarter ending June 30, 2000, showed a 97 percent decrease in reported violations.

2

The report also recommends the IRS revise its guidelines for the independent review sampling and reporting process to help increase the reliability of the information it provides regarding compliance with the RRA 98 Section 1204. The report recommends the Office of Managing Statistics:

➢ **Require independent review teams to also review a representative sample of management documents.**

OMS is in the process of revising the IRM 105.4, Managing Statistics in a Balanced Measurement System Handbook, to strongly suggest that several optional review items be included in the independent review process and to include those items most commonly referenced in the manager's quarterly self-certifications. Operational reviews have been included as a mandatory review item. We will conduct an alternative review, called a special assurance review, after the independent review for 6-30-01 is completed to determine if the changes made have improved the process.

➢ **Require team leaders to screen listings of managers completing self-certifications to ensure only managers with tax enforcement employees are within the population to be sampled.**

OMS has developed a Section 1204 self-certification waiver process for managers who believe the activities in his/her group should be deemed non-Section 1204 activities. The appropriate supervisor will review the waiver request to determine if it should be approved based upon the definition of Section 1204 activities. The Section 1204 coordinator will be required to maintain a list of all Section 1204 covered managers reporting to the appropriate supervisor. The IRM 105.4 is being revised to include these procedures, which will establish accountability of every manager within the IRS. We will review the Section 1204 manager list and the waivers during the annual independent review and select samples based upon the Section 1204 list and approved waivers.

➢ **Establish procedures to estimate the projected number of violations for all IRS managers based on sample results.**

OMS worked with our Research Division to determine the most reliable sampling and reporting process, which will be included in the revised IRM. The special assurance review will also be used to determine if the revised independent review structure accurately reflects the effectiveness of Section 1204 implementation.

➢ **Maintain documentation of each review team's complete sampling methodology.**

OMS has revised the independent review procedures to include a basic methodology and a format for submission. The procedures require the submission of the methodology to the appropriate supervisor. The supervisor will maintain the methodology and the independent review results.

➢ **Ensure procedures are carried over into the new IRS business units, as the units become operational.**

OMS has consistently met with each Operating Division to ensure all requirements of the Section 1204 process are integrated effectively.
OMS is currently revising the IRM 105.4 to reflect the feedback from the new IRS Operating Divisions and clarifying the independent review process.

The report also states employees were not always evaluated on the standard requiring the fair and equitable treatment of taxpayers. The report recommends:

The IRS should also include the evaluation of fair and equitable treatment standard within a single employee evaluation form for non-management employees. The Office of Performance Management and Recognition, Personnel Planning and Policy Division, should work towards incorporating the fair and equitable treatment into the evaluation forms of all employees.

We agree with your recommendations and will take the following actions:

1. The Organizational Performance Management Executive and the Recognition, Personnel Planning and Policy Division, have issued an "All Manager" memorandum advising each manager of the Section 1204 (b) requirement to issue the retention standard at the beginning of each employee's rating period, and to evaluate employees on the retention standard at the end of each employee's rating period.

2. The special assurance review will also include adherence to Section 1204(b) as part of the review.

3. The Organizational Performance Division has incorporated Section 1204(b) review requirements into the Section 1204(a) & (c), annual independent review process, and will include them as part of the independent review.

4. By October 1, 2001, the IRS will revise Critical Job Element (CJEs) for employees who are not managers or management officials to align with our Balanced Measurement System. During this revision, we will include the retention standard on the same document as the CJEs for each employee, and revise the performance rating form to include a rating on the retention standard.

4

Please note in the new IRS structure, the Organizational Performance Division (OPD) will be responsible for the work currently performed by the OMS. If you have any questions or need additional information, please call me, or a member of your staff may contact Kelly Cables, Director, Organizational Performance Division at (202) 622-4909.