



*Trends in Exempt Organizations Function  
Enforcement Activities for  
Fiscal Years 2001 - 2005*

**September 22, 2006**

**Reference Number: 2006-10-157**

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

**Redaction Legend:**

1 = Tax Return/Return Information

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TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

September 22, 2006

**MEMORANDUM FOR** COMMISSIONER, TAX EXEMPT AND GOVERNMENT ENTITIES  
DIVISION

*Michael R. Phillips*

**FROM:**

Michael R. Phillips  
Deputy Inspector General for Audit

**SUBJECT:**

Final Audit Report – Trends in Exempt Organizations Function  
Enforcement Activities for Fiscal Years 2001 – 2005  
(Audit # 200610026)

This report presents the results of our review of statistical data for the Exempt Organizations (EO) function's enforcement activities in Fiscal Years (FY) 2001 – 2005. The overall objective of this review was to analyze relevant statistical data for trends.

*Impact on the Taxpayer*

In recent years, public concerns about exempt organizations' operations and noncompliance have brought increased attention to the tax-exempt sector. In FY 2003, the EO function began initiating new processes to increase its presence in the tax-exempt community. While staffing applied to examinations remained stable during FYs 2001 – 2004, the number of completed examinations increased. In addition, assessment amounts for noncompliant organizations increased in all but 1 year since FY 2001. These actions served to increase the number of tax-exempt organizations that were brought back into compliance with the laws and regulations granting tax-exempt status.

*Synopsis*

Overall, EO function compliance activities have evolved, and they showed improvement during FYs 2001 – 2005. However, in FY 2005, the implementation of new programs and the need to train new staff resulted in a noticeable drop in the number of completed examinations. For example, while staffing applied to EO Examinations function (hereafter referred to as EO Examinations) activities remained stable in FYs 2001 – 2004, the number of completed



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examinations increased. There was a 15 percent decrease in closed examinations during FY 2005. This decrease is a consequence of attrition and limited hiring authority over a period of years, redirecting field examination personnel to train newly hired staff, and implementing new initiatives for increasing the EO function's presence.

The average amount of time needed to complete an examination increased nearly 15 percent for the 5-year period ending in FY 2005. The most noticeable change occurred during FYs 2004 - 2005 as EO Examinations began conducting audits of more complex returns. Assessment amounts for noncompliant organizations increased in all but 1 year since FY 2001. There was a noticeable upward trend during FY 2005 as the amount of tax assessed on large and more complex organizations increased significantly over that assessed in FY 2004.

***The EO function improved its ability to identify noncompliant organizations, but some compliance indicators decreased in FY 2005 due to a redirection of resources.***

However, fewer returns resulted in a tax change for these assessments. Overall, the percentage of cases resulting in some type of tax change decreased during the early period of our review and did so again in FY 2005, after increasing in FY 2004. During FY 2005, approximately 20 percent of FY 2005 closures were training returns, which historically have low change rates.

The quality of examinations completed by EO Examinations improved from the early periods of our review, and Customer Satisfaction ratings remained stable.

### *Response*

We made no recommendations in this report. However, key Internal Revenue Service management officials reviewed it prior to issuance and agreed with the facts and conclusions presented.

Copies of this report are also being sent to the Internal Revenue Service managers affected by this report. Please contact me at (202) 622-6510 if you have questions or Nancy A. Nakamura, Acting Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.



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## *Abbreviations*

AIMS	Audit Information Management System
EO	Exempt Organizations
EOCU	Exempt Organizations Compliance Unit
FTE	Full-Time Equivalent
FY	Fiscal Year
I.R.C.	Internal Revenue Code
IRS	Internal Revenue Service
TE/GE	Tax Exempt and Government Entities
TEQMS	Tax Exempt Quality Measurement System



## *Trends in Exempt Organizations Function Enforcement Activities for Fiscal Years 2001 – 2005*

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### *Background*

The Exempt Organizations (EO) function of the Tax Exempt and Government Entities (TE/GE) Division is responsible for ensuring charitable or other tax-exempt organizations are in compliance with the Internal Revenue Code sections (I.R.C. §) and regulations that govern organizations exempt from Federal income tax. The EO function has two primary programs for ensuring compliance: the Determinations Program (reviewing requests from organizations seeking tax-exempt status) and the Examinations Program (reviewing information about existing organizations). In general, an organization that wants to be recognized as tax-exempt under I.R.C. § 501(c)(3)<sup>1</sup> must apply to the Internal Revenue Service (IRS) for a determination of its status by completing an Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code (Form 1023). The EO Examinations function (hereafter referred to as EO Examinations) is responsible for identifying and reviewing potential noncompliance with the I.R.C. by tax-exempt organizations.

The Returns of Organization Exempt From Income Tax (Form 990) of selected exempt organizations are examined annually by the EO function to determine whether they meet various requirements. The EO function can accept Forms 990 as filed, impose excise taxes for certain types of violations, or revoke the exempt status if the violations are serious enough. In addition, employment tax returns can be examined concurrently with Form 990 returns if warranted. Employment tax examinations can result in additional assessments of tax to the exempt organizations.

In recent years, there has been a significant growth in the number of entities recognized as exempt from Federal income tax under the I.R.C. In Fiscal Year (FY) 2003, there were 1.6 million exempt organizations, compared to 1.1 million in FY 1993. However, there has been a significant reduction in resources dedicated by the TE/GE Division to examinations of these entities as a consequence of attrition and limited hiring authority over a period of years, resulting in a sharp decline in examination coverage. Examinations fell from approximately 12,300 in FY 1993 to 5,800 in FY 2004. However, during FY 2005, EO Examinations hired 76 additional revenue agents to increase examination coverage.

Public concerns about organizations' operations and compliance have brought increased attention from the press and oversight bodies regarding the accuracy of EO function customer account data and the declining level of enforcement activities across the IRS. In FY 2003, the EO function began initiating new processes to increase its presence in the tax-exempt community. Specifically, the entire Determinations Program was transferred from EO Examinations to the EO Rulings and Agreements function in early FY 2003, enabling

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<sup>1</sup> I.R.C. § 501(c)(3) (2006).



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EO Examinations to focus primarily on examination activities. In addition, EO Examinations began transitioning from a Coordinated Examination Program to a Team Examination Program.<sup>2</sup>

Further, the EO function established several new work groups within EO Examinations in FY 2005 to continue its focus on tax compliance. Specifically, the EO function established the:

- Exempt Organizations Compliance Unit (EOCU) to address noncompliance using correspondence and telephone contacts and to enable EO function field examination personnel to devote more time to face-to-face customer contacts.
- Review of Operations Unit to complete compliance reviews of exempt organizations and determine whether organizations are operating in accordance with their exempt purposes and are current with their filing requirements. Organizations found to be noncompliant are selected for examination.
- Data Analysis Unit to use various databases and information to investigate emerging compliance trends for improving the identification and selection of source work for the EO function.
- Exempt Organizations Financial Investigations Unit to assist in the Federal Government's effort to investigate and pursue instances of civil fraud and terrorism funding by charitable organizations.

This review was performed at the TE/GE Division Headquarters in Washington, D.C., during the period July through August 2006. The audit was conducted in accordance with *Government Auditing Standards*. However, we relied on information accumulated by the IRS in established reports and the EO function's management information system and did not verify its accuracy. We also relied on data taken from prior Treasury Inspector General for Tax Administration reports. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

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<sup>2</sup> In FY 2004, the EO function completed its migration from the Coordinated Examination Program to the Team Examination Program. While both Programs involve examinations of large organizations, the Team Examination Program uses a more systemic (versus manual) approach to identify these large entities and make selections for audit. In addition, under the Team Examination Program, EO function revenue agents are assigned to groups dedicated exclusively to examinations of large organizations.



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***Results of Review***

***The Exempt Organizations Function Improved Its Ability to Identify  
Noncompliant Organizations, but Some Compliance Indicators  
Decreased in Fiscal Year 2005 Due to a Redirection of Resources***

Overall, EO function compliance activities have evolved, and they showed improvement during FYs 2001 – 2005. However, in FY 2005, the implementation of new programs and the need to train new staff resulted in a noticeable drop in the number of completed examinations.

For example, while staffing applied to EO Examinations activities remained stable in FYs 2001 – 2004, the number of completed examinations increased. There was a 15 percent decrease in closed examinations during FY 2005. This coincides with:

- Redirecting field examination personnel to train newly hired staff.
- Implementing new initiatives for increasing the EO function's presence.

The average amount of time needed to complete an examination increased nearly 15 percent for the 5-year period ending in FY 2005. The most noticeable change occurred during FYs 2004 and 2005 as EO Examinations began conducting audits of more complex returns.

Assessment amounts for noncompliant organizations increased in all but 1 year since FY 2001. In FY 2003, there was a significant increase in total assessments<sup>1</sup> [REDACTED]

[REDACTED] There was also a noticeable upward trend during FY 2005 as the amount of tax assessed on large and more complex organizations increased significantly over that assessed in FY 2004. However, fewer returns resulted in a tax change for these assessments. Overall, the percentage of cases resulting in some type of tax change decreased during the early period of our review and did so again in FY 2005, after increasing in FY 2004. While the change rate dropped in FY 2005, approximately 20 percent of FY 2005 closures were training returns, which historically have low change rates.

The quality of examinations completed by EO Examinations improved from the early periods of our review. Customer Satisfaction ratings remained stable and indicated three areas for increased emphasis:

- Explaining the time needed to complete an audit.
- Providing simple and accurate explanations regarding the reasons for the adjustment(s).
- Providing a detailed explanation of the audit process, for customers as a whole.





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The following sections of this report reflect the efforts of EO Examinations to enforce compliance with the I.R.C. provisions related to exempt organizations. This includes analyses of the EO function's enforcement and staffing data for FYs 2001 – 2005 to identify trends in the following areas:

- Resources applied to EO function enforcement. This is measured by the number of Full-Time Equivalents (FTE)<sup>3</sup> applied to EO Examinations activities.
- Number of completed examinations.
- Time expended on examinations.
- Change rates. This is measured by the percentage of returns in which noncompliance is found and for which the organization is required to make corrections to bring itself into compliance with the law. Conversely, a no-change rate is the percentage of returns that were determined to be in compliance with the law and no change is proposed to the return.
- Dollars assessed as a result of examination.
- Examination quality. This is measured by the results of quarterly quality reviews of completed examinations by EO Examinations Special Review staff.
- Customer Satisfaction. This is measured by feedback from customers after their examinations have been completed, as captured by EO function Customer Satisfaction surveys.

**Resources applied to EO Examinations activities increased in FY 2005, after remaining stable since FY 2001**

Data from the TE/GE Division Technical Time Reporting System<sup>4</sup> showed the number of FTEs applied to EO Examinations activities was relatively constant in FYs 2001 – 2004. As a result of FY 2005 budget decisions, EO Examinations had hired 76 revenue agents through September 30, 2005.

This follows several fiscal years during which EO Examinations staffing stayed at essentially the same level. For example, in FYs 2001 and 2002, EO Examinations hired and trained new revenue agents. However, due to budget constraints and a high rate of attrition, there was a limited net increase in overall staffing between FYs 2001 and 2003. With continued high attrition and an inability to hire, there was an overall decline in EO Examinations FTEs in

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<sup>3</sup> A measure of labor hours in which 1 FTE is equal to 8 hours multiplied by the number of compensable days in a particular fiscal year.

<sup>4</sup> The TE/GE Division Technical Time Report is used to gather information required by management at all levels for time application by TE/GE Division personnel.



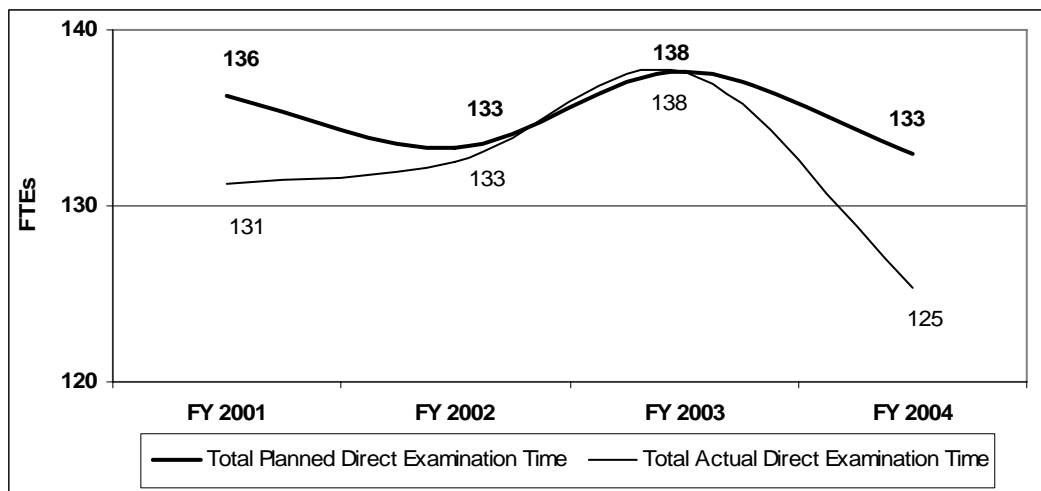
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FY 2004. Between FYs 2001 and 2004, the percentage of resources applied to the Examinations Program steadily increased, from 29.6 percent in FY 2001 to more than 50 percent in FY 2004.

Figures 1 and 2 show the following, respectively:

- FTEs planned and expended on the EO function's Direct Examination activities.<sup>5</sup>
- Total FTEs expended on all EO Examinations activities (Direct Examination time and overhead items such as management and training) and by the EO function overall.

**Figure 1: Total FTEs Planned and Expended on EO Examinations Direct Examination Activities (FYs 2001 – 2004)**



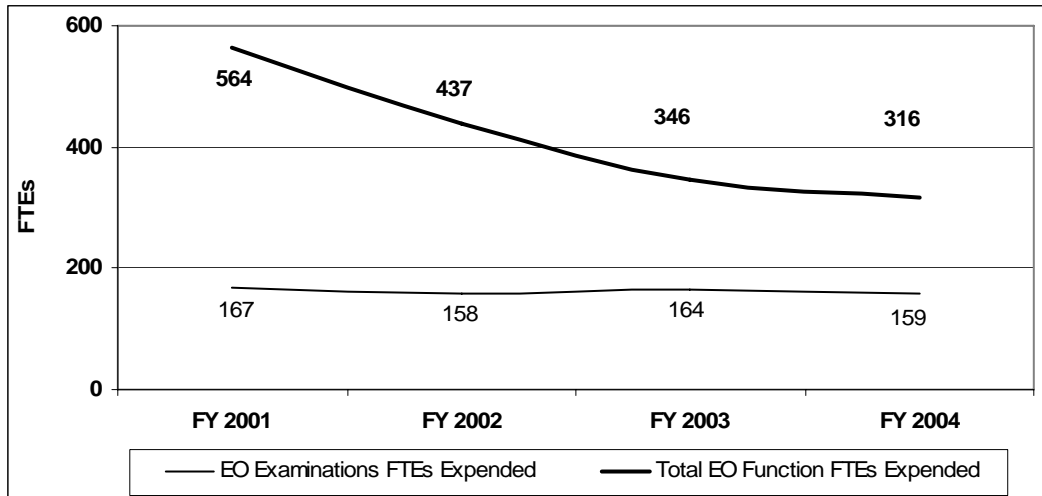
Source: *EO TECHNICAL TIME REPORT 14* for FYs 2001 – 2004. Due to issues related to implementation of a new management information system, FTE data were not available for FY 2005.

<sup>5</sup> Direct Examination activity – Time expended to conduct an audit (examination) of a return.



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**Figure 2: Total FTEs Expended on EO Examinations Activities and by the EO Function Overall (FYs 2001 – 2004)**



*Source: EO TECHNICAL TIME REPORT 14 for FYs 2001 – 2004. Due to issues related to implementation of a new management information system, FTE data were not available for FY 2005.*

**The number of completed examinations increased overall in FYs 2001 – 2004 but dropped nearly 15 percent in FY 2005**

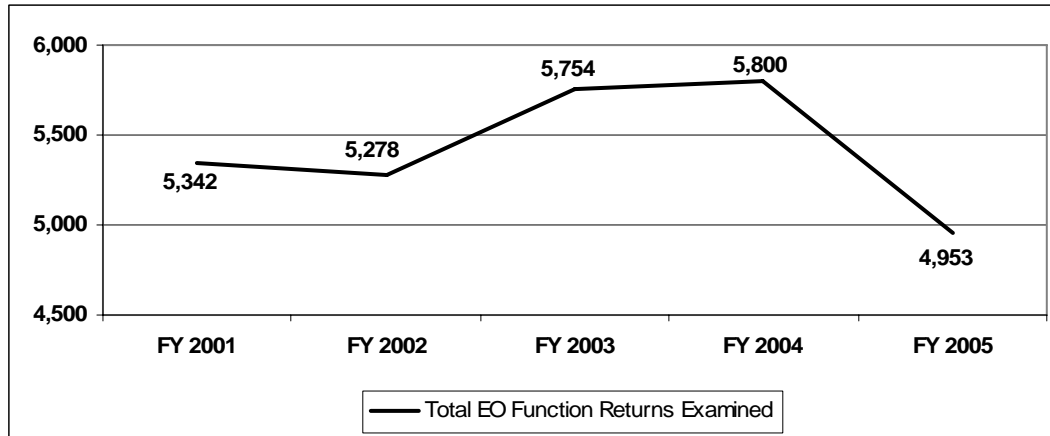
There are a variety of measures for gauging the impact of EO Examinations activities on compliance. One primary measure is the number of examinations completed during a fiscal year. As shown in Figure 3, the total number of closed examinations increased overall in FYs 2001 – 2004 but dropped in FY 2005. Factors contributing to this decline include:

- The diversion of experienced revenue agents during the first quarter of FY 2005 to serve as job instructors for nearly 100 new employees.
- Field revenue agents expending their time on a variety of other nonexamination duties, including the need to redirect staff to higher priority work (classification of approximately 1,200 Disaster Relief returns and assisting the Joint Terrorism Task Force).



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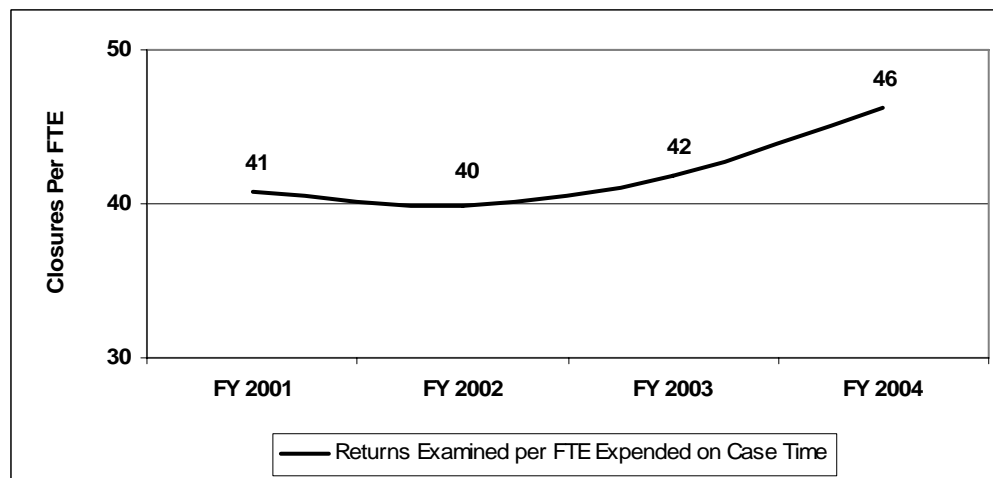
**Figure 3: Total Number of Closed Examinations (FYs 2001 – 2005)**



Source: Audit Information Management System (AIMS)<sup>6</sup> Report 20 (FYs 2001 – 2005).

As shown in Figure 4, during FYs 2001 – 2004, there was an increase in the number of examinations completed per FTE expended on Direct Examination case time.

**Figure 4: Number of Examinations Closed per Direct Examination FTE (FYs 2001 – 2004)**



Sources: AIMS Report 20 (FYs 2001 – 2004), EO TECHNICAL TIME REPORT 14 for FYs 2001 – 2004. Due to issues related to implementation of a new management information system, FTE data were not available for FY 2005.

During the early part of FY 2005, EO function management recognized they would not meet their goal for examination closures. To address this, EO function management made a workload

<sup>6</sup> The AIMS tracks the source, location, and status of each examination from start to finish.



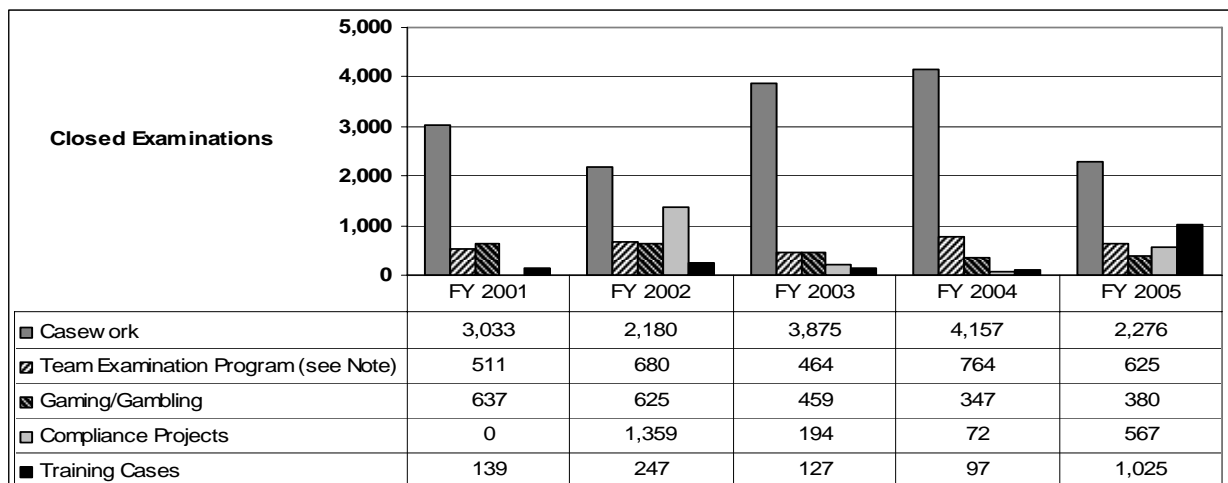
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shift within the EOCU to increase the number of contacts with exempt organizations. The EOCU began operation in January 2004 to address noncompliance by using correspondence and telephone contacts. Its primary goals are to reach and affect a greater number of exempt organizations than would be possible through traditional audits.

During the first half of FY 2005, the EOCU contacted more than 18,000 organizations through a combination of educational and compliance check<sup>7</sup> mailings. These contacts were related to issues such as unreported business income, filing of an incorrect form, bingo activities, and excessive compensation. Due to the EOCU's success in increasing coverage of exempt organizations, the EO function made plans to enlarge the Unit from one group to three.

As shown in Figure 5 and the accompanying Table, more than one-half of all closures were attributable to Casework.<sup>8</sup> Overall, the types of cases shown in Figure 5 accounted for over 90 percent of all closed examinations during FYs 2001 – 2005.

**Figure 5: Total Number of Closed Examinations,  
Key Program Areas (FYs 2001 – 2005)**



*Source: AIMS Report 20 (FYs 2001 – 2005). Note: In FY 2004, the EO function completed its migration from the Coordinated Examination Program to the Team Examination Program.*

<sup>7</sup> A compliance check is a contact with the customer that involves a review of filed information and tax returns of the entity to determine whether the entity is adhering to record keeping and information reporting requirements. A compliance check is not an examination, and the customer may legally choose not to participate in the compliance check.

<sup>8</sup> Casework arises from known or potential noncompliance issues related to specific taxpayers (generally the result of referrals from sources such as other IRS operating divisions, informants, or the media); returns selected as a result of certain conditions, or a combination of conditions, being present on returns; or when IRS action is otherwise necessary (e.g., when an organization submits a claim for refund, EO Examinations staff review the claim to determine whether the refund is appropriate or additional information is needed).



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**Figure 5 Table**

<b>Program Area</b>	<b>Percentage of Total Closures FYs 2001 – 2005</b>
Casework	57.2%
Team Examination Program	11.2%
Gaming/Gambling	9.0%
Compliance Projects	8.1%
Training Cases	6.0%

*Source: AIMS Report 20 (FYs 2001 – 2005). The percentages do not sum to 100 percent because these areas of emphasis account for most but not all examinations closed in FYs 2001 – 2005. The percentage for each program area was calculated using the total number of examinations closed in FYs 2001 - 2005 (27,127, as shown in Figure 3).*

**The amount of time needed to complete an examination has been increasing**

There are two measures for gauging time on examinations:

- Average time per case, which represents the average amount of time revenue agents devoted to completing examination cases.
- Cycle time, which is measured from the date a taxpayer is initially contacted to the date the examination case is closed on the AIMS.

As shown in Figure 6, the average time per case increased nearly 15 percent (from 46.2 hours to 53.0 hours per case) for the 5-year period ending in FY 2005. The most noticeable change occurred during FYs 2004 and 2005. Reviews by EO function staff showed the increased time per case was attributable to the following factors:

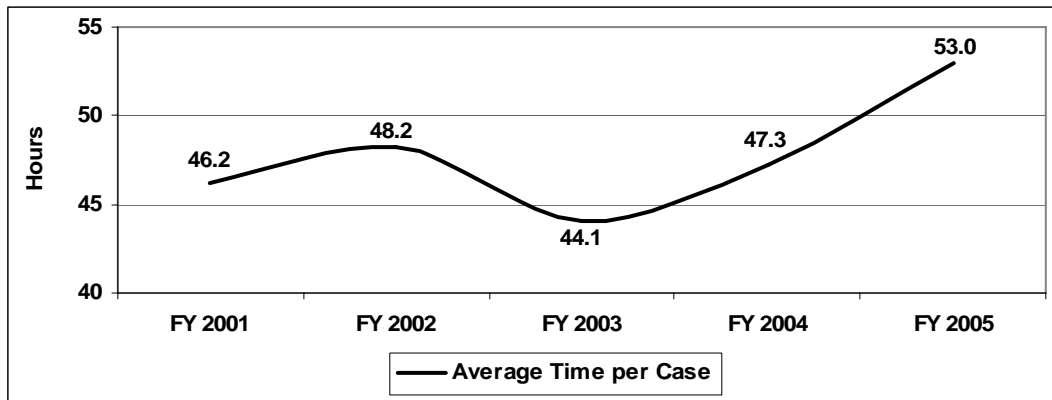
- FY 2004: As documented by the Hours Per Case study team, there were several potential reasons for these results including rising complexity of case work, changing priorities, and deficiencies in inventory management techniques.
- FY 2005: There was a transition to critical initiative returns which were generally more complex and time consuming than the mix of returns worked in prior years. There was also an expectation that average hours per return would further increase in FY 2006 due to a number of unagreed revocations of tax-exempt status in the Abusive Tax Avoidance Transaction Projects.<sup>9</sup>

<sup>9</sup> These Projects evaluate returns containing a potential Abusive Tax Avoidance Transaction, which is defined as a specific tax transaction/scheme that reduces tax liability by taking a tax position that is not supported by tax law or manipulates the law in a way that is not consistent with the intent of the law (tax evasion).



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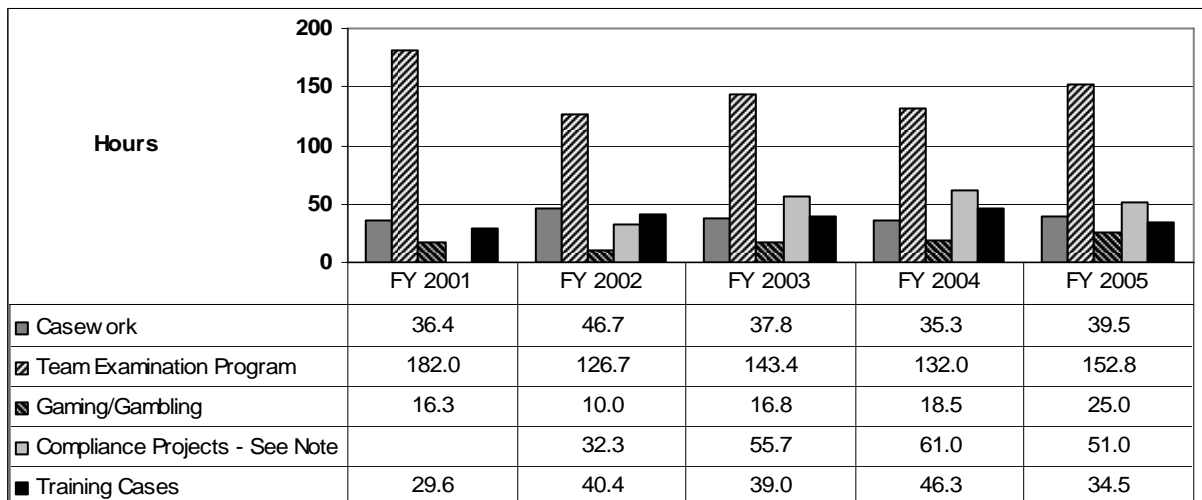
**Figure 6: Average Time per Case (FYs 2001 – 2005)**



Source: AIMS Report 20 (FYs 2001 – 2005).

Figure 7 shows average time per case for key programs, which represent the majority of total closures during FYs 2001 – 2005 (see Table included with Figure 5). In general, during the later part of the review period, overall time per case increased as more complex issues were being addressed and there was a need for more contact with taxpayers. For example, average hours per return for the Casework category increased from 35.0 to 39.0 between June 2004 and June 2005. At the same time, the percentage of returns resulting in a change to tax increased. Another factor contributing to the increase in average time per case was the time required to close employment tax returns in the Team Examination Program. Employment tax return closures from the Team Examination Program were closed at an average of 54.9 hours per return in FY 2005, compared to 16.8 hours in FY 2003.

**Figure 7: Average Time per Case, Key Program Areas (FYs 2001 – 2005)**



Source: AIMS Report 20 (FYs 2001 – 2005). Note: There were no cases for “Compliance Projects” in FY 2001.

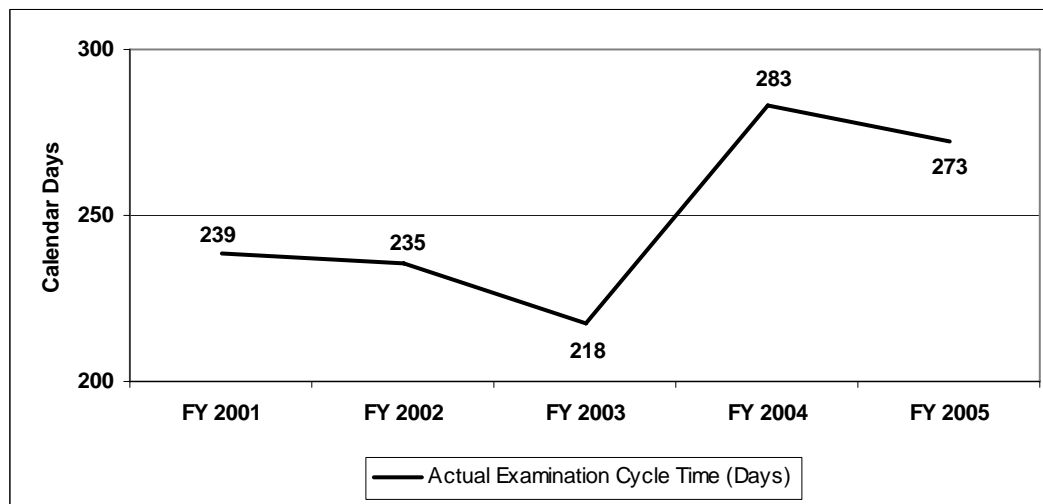


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Figure 8 shows cycle time increased 34 calendar days (14 percent) during FYs 2001 – 2005. As with average time per case data shown in Figures 6 and 7, the most noticeable increases occurred during FYs 2004 and 2005. Reviews by EO function staff attributed these increases to the following:

- FY 2004: Average cycle time is actually higher than expected. One potential cause is the improvement in the change rate, which affects the amount of time needed to complete an examination. Also, EO function management took actions to identify and reduce processing bottlenecks in the Examinations Program and Review groups that added days to the examination cycle.
- FY 2005: EO function staff expected cycle time to increase further in FY 2005 due to the emphasis on closing out the in-process inventory in preparation for concentrating resources on critical examination initiatives.

**Figure 8: Cycle Time (FYs 2001 – 2005)**



Sources: AIMS Report 60 for FYs 2001 – 2005.

### **The change rate declined in FY 2005 due to a significant increase in the no-change rate for training cases**

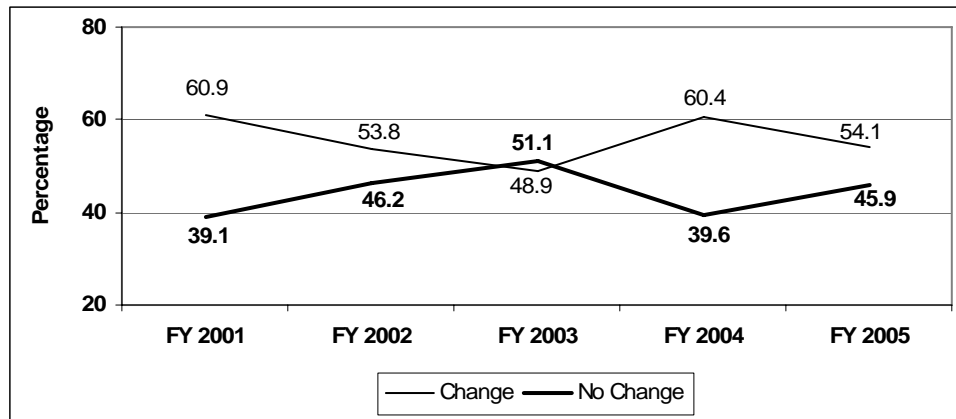
Another indicator of the Examinations Program's impact is the percentage of cases resulting in some type of tax change due to noncompliance with the I.R.C. Overall, the rate of change fell during the early period of our review and did so again in FY 2005, after increasing in FY 2004. Figure 9 shows the percentage of examinations resulting in either a change or no change in tax over the past 5 fiscal years.





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**Figure 9: Change Rate (FYs 2001 – 2005)**



Source: AIMS Report 20 (FYs 2001 – 2005).

The percentage of closed examinations resulting in a change to tax increased from 48.9 percent in FY 2003 to 60.4 percent in FY 2004. While the change rate dropped in FY 2005, approximately 20 percent of FY 2005 closures were training returns, which historically have low change rates. Disregarding those returns, the change rate for FY 2005 would be 61.3 percent, slightly higher than the FY 2004 change rate. The EO function's FY 2006 Implementing Guidelines<sup>10</sup> show that use of more sophisticated methods contributed to selecting more noncompliant cases for examination. One example cited was the new Data Analysis Unit's use of available databases combined with analyses of Form 990 line items to identify potential noncompliant returns. EO function management also took steps to ensure closing codes were revised to more accurately reflect how examinations were being closed.

In FYs 2002 and 2003, EO Examinations devoted resources to a market segmentation initiative. In October 2004, the Director, EO, decided to redirect resources from this area into other areas. For example, in FY 2005, the EO function began focusing on critical initiatives such as antiterrorism, abusive tax avoidance transactions, credit counseling, and excess compensation.

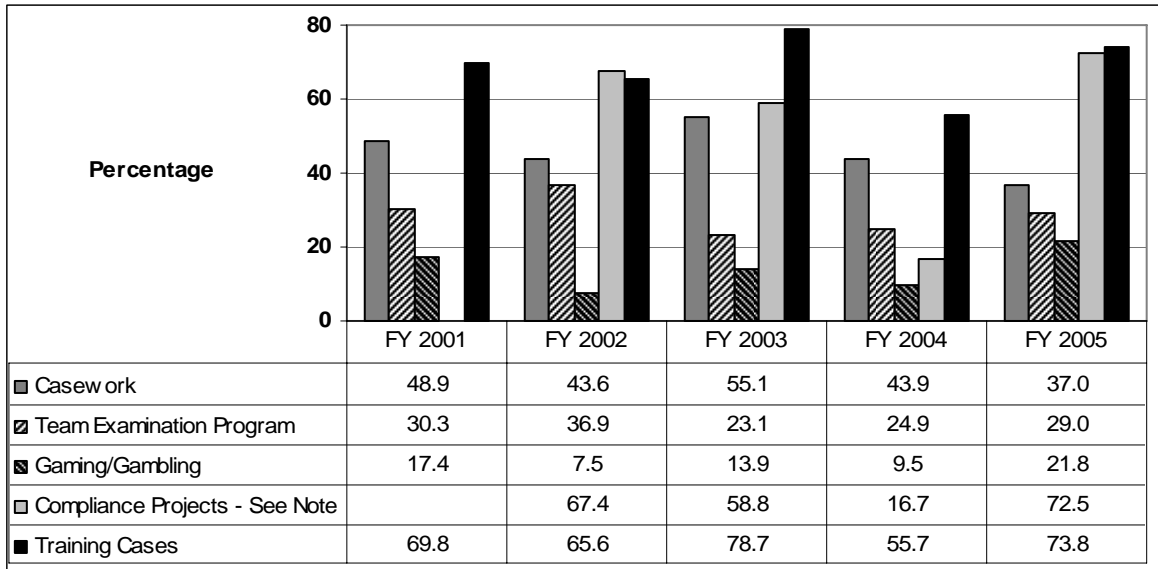
In addition, there was a marked reduction in the number of examinations closed without change for the "Casework" category, which accounted for nearly one-half of all closures in FY 2005. Figure 10 provides the no-change rate for key Examinations Program areas during FYs 2001 – 2005.

<sup>10</sup> The Implementing Guidelines show how the EO function plans to apply resources to programs that support its major strategies and priorities for the upcoming fiscal year.



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**Figure 10: No-Change Rate, Key Program Areas (FYs 2001 – 2005)**

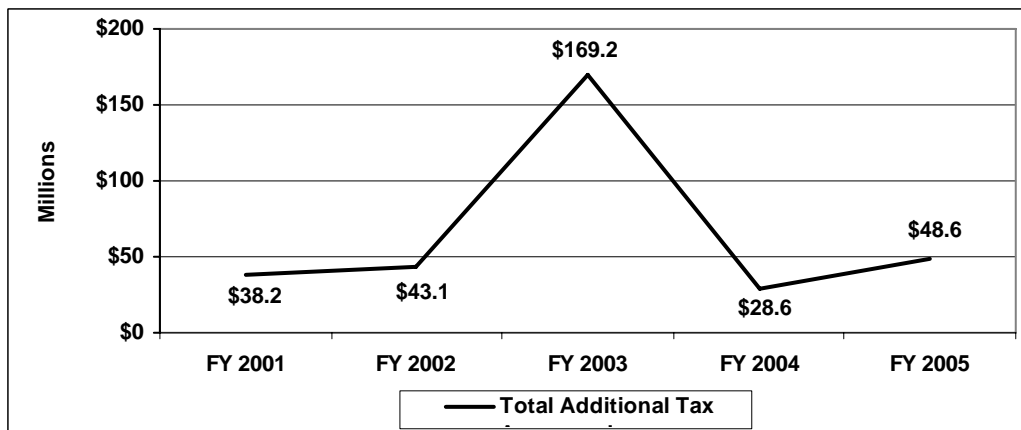


Source: AIMS Report 20 (FYs 2001 – 2005). Note: There were no cases for “Compliance Projects” in FY 2001.

**Assessment amounts for noncompliant organizations increased in all but 1 year since FY 2001**

Another indicator of the success of the Examinations Program is the amount assessed for the noncompliance issues identified during examinations. Figures 11 and 12 show total additional tax assessed during FYs 2001 – 2005, both in total and for key program areas.

**Figure 11: Total Additional Tax Assessments (FYs 2001 – 2005)**

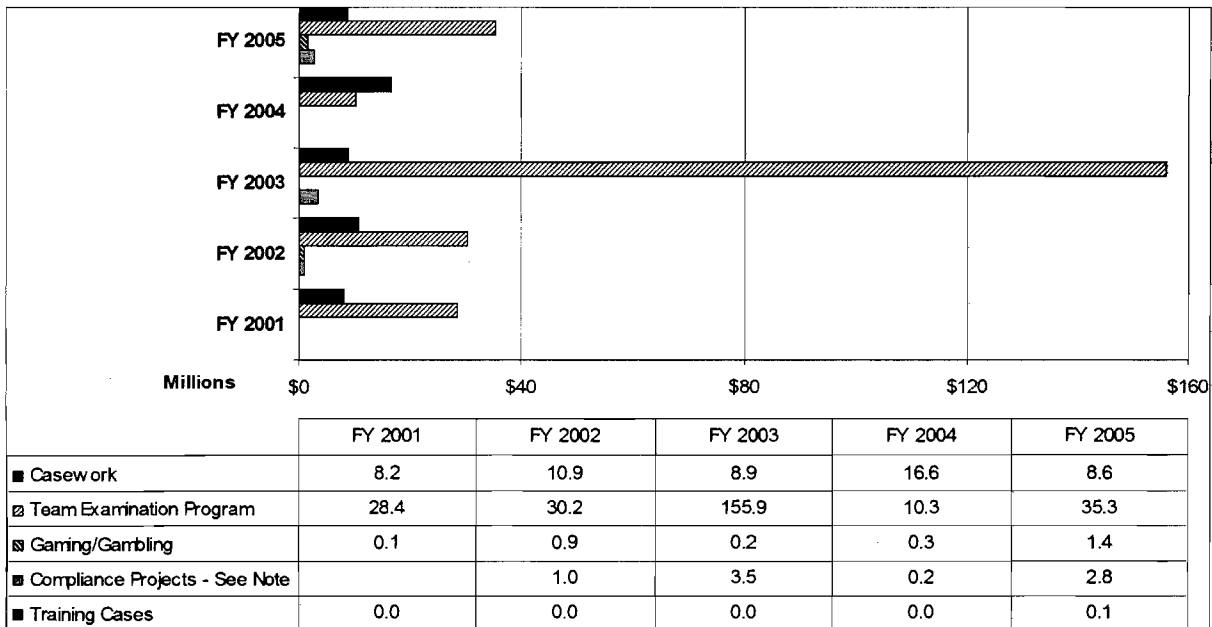


Source: AIMS Report 20 (FYs 2001 – 2005).



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**Figure 12: Total Additional Tax Assessments,  
Key Program Areas (FYs 2001 – 2005)**



Source: AIMS Report 20 (FYs 2001 – 2005). Note: There were no cases for “Compliance Projects” in FY 2001.

As shown in Figures 11 and 12, for FY 2003, the significant increase in total assessments was attributable to the Team Examination Program cases. For example, there was a substantial increase in the total assessments for this category from FY 2002 to FY 2003.

There was also an increase in FY 2005 for this same category, when the amount of tax assessed increased as compared to FYs 2001 – 2002 and FY 2004 despite a lesser number of examinations. The increase was a result of selecting better cases for examination.

**The EO function reported improvement in the quality of examinations from the early periods of our review**

The Tax Exempt Quality Measurement System (TEQMS) is designed to measure the quality of the EO function’s Examinations Program. The TEQMS measures the quality of examinations and provides a tool for management to identify achievements of the Examinations Program as well as opportunities for improvement.

Overall, the quality of examinations conducted by EO Examinations improved and ranged from a low of 73 percent to a high of 89 percent over the past 4 fiscal years. The notable improvement in quality during FY 2003 was the beginning of an upward trend that continued through

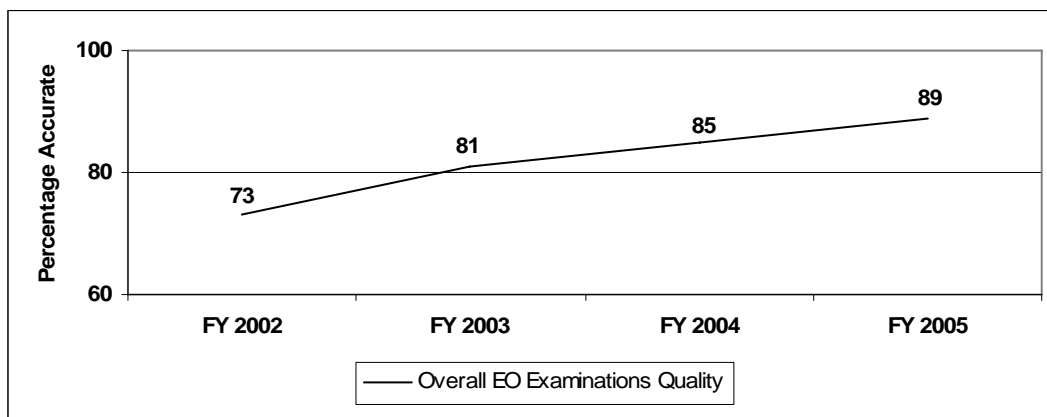


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FY 2005. The EO Examinations Special Review staff issued quarterly reports with comprehensive narratives detailing where revenue agents did well and where there was a need for improvement.

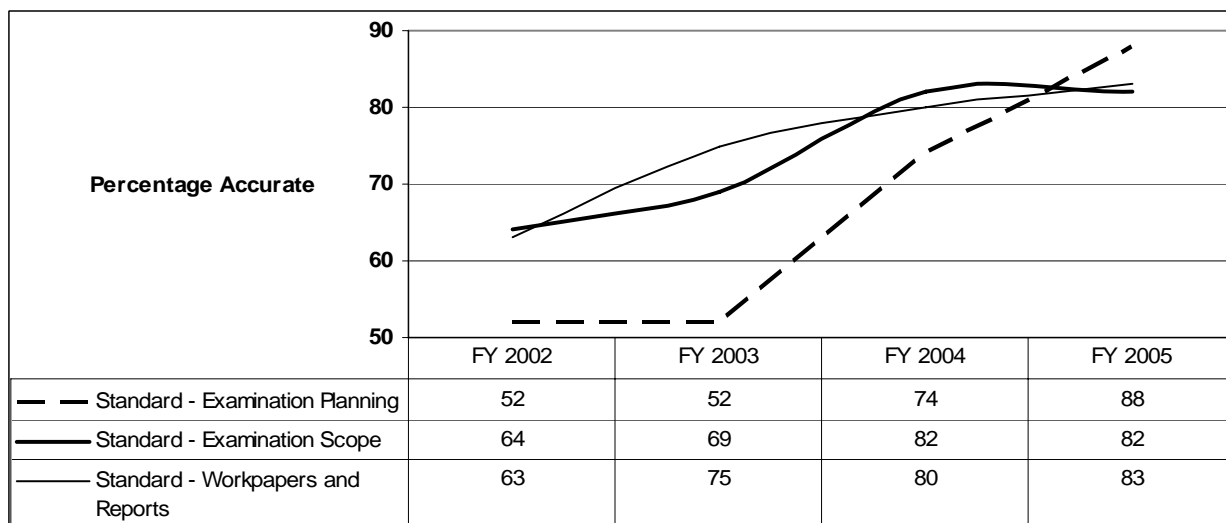
Figures 13 and 14 show overall TEQMS results for FYs 2002 – 2005 as well as the three standards having the lowest overall ratings.

**Figure 13: Examination Quality (FYs 2002 – 2005)**



Source: TEQMS Reports (FYs 2002 – 2005). Note: There are no data shown for FY 2001 because data for that period were no longer available.

**Figure 14: Examination Quality (FYs 2002 – 2005)**



Source: TEQMS Reports (FYs 2002 – 2005). Note: There are no data shown for FY 2001 because data for that period were no longer available.



## *Trends in Exempt Organizations Function Enforcement Activities for Fiscal Years 2001 – 2005*

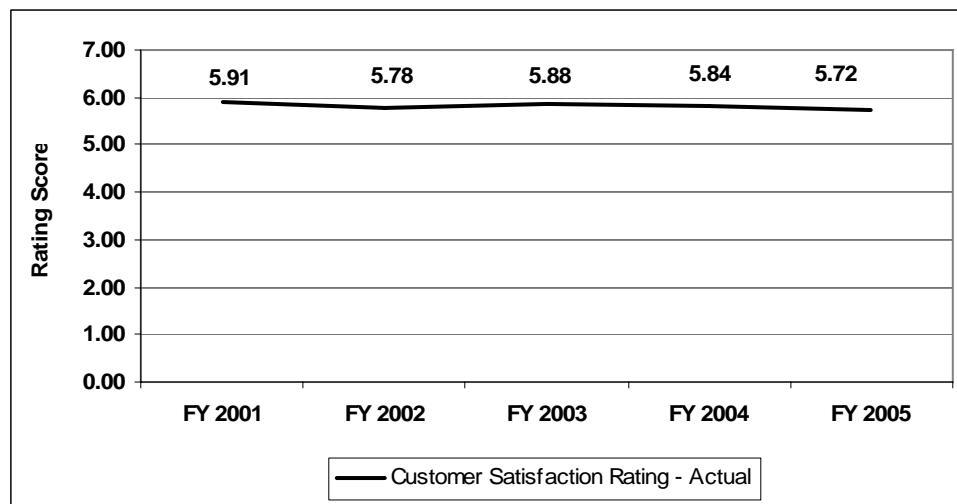
### **Customer Satisfaction ratings were consistent during the period of our review**

Customer Satisfaction research is part of the IRS' agency-wide initiative to monitor and improve taxpayer satisfaction with services provided. For EO Examinations, this research is designed to track Customer Satisfaction with the EO Examinations' process over time, identify which customer characteristics influence satisfaction ratings, and identify areas where improvements will have the greatest impact on Customer Satisfaction.

Customer Satisfaction ratings for examinations were generally consistent from FY 2001 to FY 2004, ranging from 5.78 to 5.91 on a 7-point scale (where ratings of 6 or 7 were designated as satisfied customers and ratings of 1, 2, or 3 were designated as dissatisfied customers). The overall satisfaction rating of 5.72 for FY 2005 was not significantly different from the ratings in previous periods.

The survey categories having the highest scores were "Courtesy of Staff" and "Professionalism of Staff," while the "Time Spent on Audit" and "Explanation of Adjustments" categories were rated lowest. Figure 15 shows overall Customer Satisfaction ratings for the past 5 fiscal years.

**Figure 15: Overall EO Examinations Customer Satisfaction (FYs 2001 – 2005)**



*Source: Customer Satisfaction Surveys (FYs 2001 – 2005). These ratings are based on data gathered over a 3-month period in FY 2001 and over 6-month periods in FYs 2002 – 2005.*

To increase customers' overall satisfaction with EO Examinations, the vendor conducting the survey suggested that improvement efforts focus on the following:

- Explaining thoroughly the amount of time entities will need to spend on their audits. This will let customers know what to expect and how to manage their time expectations accordingly. In addition, the IRS should ensure any necessary information requested from a customer is relevant to the case and requested all at once, if possible.



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- Providing simple and accurate explanations of the reasons for the adjustment(s) when working with customers who have adjustments made to their cases. “Explanation of Adjustments” is the top improvement priority for customers as a whole and the second-highest priority for satisfied customers.
- Working towards providing detailed explanations regarding what the audit process will entail for customers as a whole.

The above areas are consistent with data cited earlier in this report, which showed increases in both the percentage of examinations resulting in a change and the amount of time needed to complete an examination.



## **Appendix I**

### *Detailed Objective, Scope, and Methodology*

The overall objective of this review was to review relevant statistical data for the EO function's enforcement activities in FYs 2001 – 2005 and analyze the data for trends. To accomplish this objective, we reviewed IRS data publications and EO Examinations function information as shown below. We relied on information accumulated by the IRS in established reports and the EO function's management information system and did not verify its accuracy. We also relied on data taken from prior Treasury Inspector General for Tax Administration reports.

Specifically, we:

- I. Identified areas of emphasis for the EO function's enforcement activities during FYs 2001 – 2005 and how resources were allocated.
  - A. Obtained EO function Work Plans and Program Guidance to identify the major strategies, operating priorities, goals, and objectives.
  - B. Interviewed EO function management to identify what factors they used in determining these key program areas (e.g., expected high rate of noncompliance).
- II. Determined what factors EO function management used to gauge the overall success of key enforcement areas.
  - A. Interviewed management to determine what criteria are used in determining the success of individual examinations and the overall Examinations Program.
  - B. Determined what data management used to track these measures.
- III. Analyzed data relating to the EO function's enforcement activities in FYs 2001 – 2005.
  - A. Obtained the Employee Plans/Exempt Organizations Work Plans (Form 5440) to identify the total planned staff days for both the EO function overall and the EO Examinations Program.
  - B. Obtained TE/GE Division Technical Time Reporting System<sup>1</sup> data to determine the total time applied to EO function examination activities.
  - C. Obtained Statistics of Income function data showing the total number of returns examined and associated results.

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<sup>1</sup> The TE/GE Division Technical Time Report is used to gather information required by management at all levels for time application by TE/GE Division personnel.



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- D. Obtained AIMS<sup>2</sup> data to identify the total number of, source of, type of closure for, and time expended on examinations of EO function returns.
- E. Determined the extent of the productive and nonproductive trends for EO function-related returns.

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<sup>2</sup> The AIMS tracks the source, location, and status of each examination from start to finish.





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**Appendix II**

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**Appendix III**

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