Preparations Were Successful for Implementation of New Business Provisions in the Jobs and Growth Tax Relief Reconciliation Act of 2003

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INSPECTOR GENERAL
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MEMORANDUM FOR DEPUTY COMMISSIONER FOR SERVICES AND ENFORCEMENT

Gordon C. Milbourn III

FROM: Gordon C. Milbourn III
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Preparations Were Successful for Implementation of New Business Provisions in the Jobs and Growth Tax Relief Reconciliation Act of 2003 (Audit # 200330038)

This report presents the results of our review to evaluate the Internal Revenue Service's (IRS) actions to implement the business provisions of the Jobs and Growth Tax Relief Reconciliation Act of 2003.[1] This included evaluating the actions planned or taken to update and/or create necessary computer programs, processing procedures, tax forms, instructions, and publications related to the business provisions.

This review focused on three new provisions. One provision increased first-year bonus depreciation, another provision increased the amount of cost for tangible depreciable property that can immediately be expensed (rather than depreciated over several years), and a third provision postponed 25 percent of corporate estimated tax payments due on September 15, 2003, until October 1, 2003. The Congressional Joint Committee on Taxation estimated that these three provisions would reduce business taxes by $32 billion over a 5-year period and shift revenue totaling over $6 billion from the Fiscal Year (FY) 2003 budget to the FY 2004 budget.

In summary, the IRS successfully identified all major actions necessary to properly implement the legislative provisions affecting business taxpayers and successfully completed all of the required action items due at the time of our review. Some of the

[1] Pub. L. No. 108-27, 117 Stat. 752.

action items were pending completion but appeared to be on schedule and had reasonable completion dates.

Management's Response: IRS management reviewed the draft report and concurred with its contents. Since there were no recommendations requiring a formal response, the IRS agreed the report should be issued with no formal written response.

Please contact me at (202) 622-6510 if you have questions or Richard J. Dagliolo, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs), at (631) 654-6028.

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Background

The Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA)[1] introduced a host of new rules, accelerated some benefits, and created tax provisions with various effective dates. The new law contained significant tax cuts for both individual and business taxpayers.

For business taxpayers, the JGTRRA included two temporary tax breaks designed to encourage immediate capital investments. One provision in the Act increased first-year bonus depreciation, another provision increased the amount of cost for tangible depreciable property that can immediately be expensed (rather than depreciated over several years), and a third provision postponed 25 percent of corporate estimated tax payments due on September 15, 2003, until October 1, 2003. (For a more detailed description of each provision, please see Appendix IV.) The Congressional Joint Committee on Taxation estimated that these 3 provisions would reduce business taxes by $32 billion over a 5-year period and shift revenue totaling over $6 billion from the Fiscal Year (FY) 2003 budget to the FY 2004 budget.

The Internal Revenue Service (IRS) is responsible for ensuring that new legislative provisions are incorporated and reflected in their tax forms, computer programs, and internal processing manuals. In addition, the IRS is required to inform taxpayers of the new provisions through publications, instructions, and multi-media.

Within the IRS, the Office of Tax Administration Coordination (OTAC) is responsible for monitoring and tracking the implementation of enacted legislation. The OTAC assigns ownership and target dates for each action item necessary to implement the provision, works with the provision owners to ensure appropriate implementation plans are developed, and monitors the progress of the plan. This process utilizes the Legislative Implementation Tracking System (LITS), an intranet-based system that reflects real-time status updates for provisions and actions and provides management information capabilities. The LITS is IRS management's primary control to monitor the implementation of new tax laws.

[1] Pub. L. No. 108-27, 117 Stat. 752.

This review was performed at the Ogden, Utah, office of the Treasury Inspector General for Tax Administration through analysis and review of IRS data from October through December 2003. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Appropriate Actions Were Taken to Ensure Implementation of New Provisions Affecting Businesses

The IRS successfully identified all major actions necessary to properly implement legislative provisions of the JGTRRA affecting business taxpayers. The IRS was also successful in completing all of the required action items that were due at the time of our review. At that time, some of the action items were still pending completion, but appeared to be on schedule and all had reasonable completion dates.

The IRS took actions ensuring that appropriate tax forms were modified, business taxpayers and practitioners were effectively informed of the tax law changes, IRS employees were properly informed, and IRS computer programs affected by the new provisions were properly modified.

Tax forms and associated instructions were modified to reflect new tax provisions

To implement the depreciation and expense provisions of the JGTRRA, the IRS successfully modified four different forms and their related instructions. The forms and instructions affected and changed to reflect the new provisions included the following:

- Depreciation and Amortization (Form 4562).
- Employee Business Expenses (Form 2106).
- Sales of Business Property (Form 4797).
- Underpayment of Estimated Tax by Corporations (Form 2220).

All changes made to the tax forms and related instructions accurately reflected the new provisions, were completed timely, and were presented clearly to facilitate taxpayer compliance.

Business taxpayers and practitioners were effectively informed

The IRS took proper actions to ensure business taxpayers and practitioners affected by the new provisions were properly informed of the changes. At the time of our review, the IRS had updated 5 of the 10 publications that needed modification. The updated information included in the five publications was accurate and clearly written. The five publications updated included the following:

- *Your Federal Income Tax* (Publication 17).
- *Farmer's Tax Guide* (Publication 225).
- *Residential Rental Property* (Publication 527).
- *Sales and Other Dispositions of Assets* (Publication 544).
- *Direct Sellers* (Publication 911).

The other five publications had pending changes at the close of our review. All of these pending changes had reasonable due dates. The publications included the following:

- *Travel, Entertainment, Gift, and Car Expenses* (Publication 463).
- *Business Use of Your Home* (Publication 587).
- *How to Depreciate Property* (Publication 946).
- *Starting a Business and Keeping Records* (Publication 583).
- *Tax Highlights for Commercial Fisherman* (Publication 595).

In addition, the IRS issued a number of news releases to further ensure that the taxpayers affected by these new provisions were aware and fully informed. The information was also available in several locations on *The Digital Daily*, the IRS' official internet website.

IRS processing instructions were effectively updated

The IRS also identified and made changes to the instructions for processing business tax returns that were affected by the new provisions. Specifically, the Internal Revenue Manuals were accurately updated to reflect the legislative changes. In addition, Servicewide Electronic Research Program Alerts were issued IRS-wide to provide general notification of impending changes.

A change to IRS computer programming was appropriately implemented

The provision of the Act that postponed 25 percent of corporate estimated tax payments due on September 15, 2003, was the only provision of the three reviewed that required a change to IRS computer programming.

A Request for Information Services (RIS)[2] was developed for the change and received and signed by the Information Technology Services (ITS) function on June 12, 2003. The RIS provided an accurate description of the necessary changes.

An ITS programmer made the change to existing computer programs that essentially created an additional payment due date. Instead of 4 equal payments due on the standard due dates, the third payment due was calculated at 75 percent of the average quarterly payment. A new due date was made for October 1, 2003, requiring the remaining 25 percent of the normal quarterly tax payment.

The ITS followed a series of steps to ensure the proper changes were made to the programming and then conducted tests to ensure the changes worked properly. In addition, the Product Assurance function performed systems acceptability tests. All tests and programming changes were completed on time.

[2] IRS' formal method of requesting a computer programming change from the Information Technology Services function.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to evaluate the Internal Revenue Service's (IRS) actions to implement the business provisions of the Jobs and Growth Tax Relief Reconciliation Act of 2003.[1] This included evaluating the actions planned or taken to update and/or create necessary computer programs, processing procedures, tax forms, instructions, and publications related to these new provisions. To accomplish our objective, we:

I. Reviewed the Act and identified significant tax law changes that affected the filing of business tax returns and determined the steps needed to be taken to effectively implement them. We specifically focused on Section 201, "Increased bonus depreciation," Section 202, "Increased expensing for small business," and Section 501, "Time for payment of corporate estimated taxes."

II. Reviewed the Legislative Information Tracking System[2] and determined if the plan identified major changes needed for computer programs, tax forms and instructions, publications, and Internal Revenue Manual procedures.

III. Reviewed all Requests for Information Services[3] that related to the key business provisions and determined if they contained adequate and accurate information to properly prepare required programs. Also, we determined whether programming changes were properly made and whether the changes were tested.

IV. For the three business legislative tax provisions, determined whether changes to tax forms, instructions, and publications were timely and accurately prepared; written in plain, clear, and courteous language that would help facilitate taxpayer compliance; and in compliance with the legislative provisions of the new law.

V. Evaluated the level and effectiveness of the IRS' taxpayer education efforts for the business legislative tax provisions.

[1] Pub. L. No. 108-27, 117 Stat. 752.
[2] An intranet-based system that reflects real-time status updates for provisions and actions and provides management information capabilities.
[3] IRS' formal method of requesting a computer programming change from the Information Technology Services function.

Appendix II

Major Contributors to This Report

Richard J. Dagliolo, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs)
Kyle R. Andersen, Acting Director
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Appendix III

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Appendix IV

Details of Business Provisions in the Jobs and Growth Tax Relief Reconciliation Act of 2003[1]

Section 201 - Increased Bonus Depreciation

The Act provides an additional first-year depreciation deduction equal to 50 percent of the adjusted basis of qualified property, effective for taxable years ending after May 5, 2003.

Qualified property is defined in the same manner as for purposes of the 30 percent additional first-year depreciation deduction provided by the Job Creation and Worker Assistance Act of 2002,[2] except that the applicable time period for acquisition (or self construction) of the property is modified. In general, in order to qualify for the 50 percent additional depreciation deduction, the property must be acquired after May 5, 2003, and before January 1, 2005.

Property does not qualify if it was acquired pursuant to a binding written contract in effect before May 6, 2003. Property for which the 50 percent additional first-year depreciation deduction is claimed is not eligible for the 30 percent additional first-year depreciation deduction.

Section 202 – Increased Expensing for Small Business

The Act increases the Code Section 179 (tangible depreciable personal property) expensing limit to $100,000 for property placed in service in taxable years beginning in 2003, 2004, and 2005. In addition, the phase-out of the limit (currently, a dollar-for-dollar reduction in the limit for the amount of qualifying property placed in service during the year in excess of $200,000) is modified so that the phase-out starting point is increased to $400,000 for property placed in service in taxable years beginning in 2003, 2004, and 2005. Both the $100,000 limit and $400,000 starting point are indexed annually for inflation in 2004 and 2005. The Act included off-the-shelf computer software placed in service in a taxable year beginning in 2003, 2004, and 2005 as qualifying property. The Act allows taxpayers to make or revoke expensing elections on amended tax returns with respect to taxable years beginning in 2003, 2004, or 2005 without the consent of the Internal Revenue Service Commissioner.

Section 501 – Time for Payment of Corporate Estimated Taxes

The Act provided that 25 percent of the corporate estimated tax payment otherwise due on September 15, 2003, was postponed to October 1, 2003. The due date for the remaining 75 percent of the September 2003 estimated payment was not changed. Only corporations on a calendar year tax basis qualified for the deferral.

[1] Pub. L. No. 108-27, 117 Stat. 752.
[2] Pub. L. No. 107-147, 116 Stat 21 (codified in scattered sections of 26 U.S.C., 29 U.S.C., and 42 U.S.C.).