

[4830-01-u]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 801

REG 119192-98

RIN 1545-AW80

Establishment of a Balanced Measurement System

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations relating to the adoption by the IRS of a balanced system to measure organizational performance within the IRS.

These proposed regulations further implement a requirement that all employees be evaluated on whether they provided fair and equitable treatment to taxpayers and bar use of records of tax enforcement results to evaluate or to impose or suggest goals for any employee of the IRS. These regulations implement sections 1201 and 1204 of the Internal Revenue Restructuring and Reform Act of 1998. These regulations affect internal operations of the IRS and the systems that agency employs to evaluate the performance of organizations within IRS and individuals employed by IRS. This document also provides notice of public hearing on these proposed regulations.

DATES: Written comments and electronic comments must be received by **[INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]**. Outlines of oral comments to be presented at the public

hearing scheduled for Thursday, May 13, 1999 at 10 a.m. must be received by Thursday, April 22, 1999.

ADDRESSES: Send submissions to: CC:DOM:CORP:R (REG-119192-98), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R (REG-119192-98), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting comments directly to the IRS Internet site at http://www.irs.ustreas.gov/prod/tax_regs/comments.html. The public hearing will be held in room 2615, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Julie Barry (202) 401-4013; concerning submission of comments, the hearing, or to be placed on the building access list to attend the hearing, Michael Slaughter, (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed regulations to establish a Balanced System for Measuring Organizational and Individual Performance Within the Internal Revenue Service (26 CFR Part 801).

Section 1201 of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA), Public Law 105-206 (112 Stat. 685, 713 et seq (1998)), requires the Internal Revenue Service to establish a performance management system for those employees covered by 5 U.S.C 4302 that, inter alia establishes "goals or objectives for individual, group, or organizational performance (or any combination thereof), consistent with the Internal Revenue Service's performance planning procedures, including those established under the Government Performance and Results Act of 1993, division E of the Clinger-Cohen Act of 1996 ..., Revenue Procedure 64-22 ..., and taxpayer service surveys." It further requires the IRS to use "such goals and objectives to make performance distinctions among employees or groups of employees," and to use "performance assessments as a basis for granting employee awards, adjusting an employee's rate of basic pay, and other appropriate personnel actions" Finally, section 1201 expressly requires that any performance management system adopted by the IRS conform to the requirements of section 1204 of RRA.

Section 1204 of RRA provides that the IRS shall not use "records of tax enforcement results" in the evaluation of IRS employees or to suggest or impose production goals for such employees. It further provides that the IRS shall use the "fair and equitable treatment of taxpayers by employees as one of the standards for evaluating employee performance." Finally, section 1204 requires that "each appropriate supervisor" certify quarterly in a letter to the Commissioner "whether or not tax enforcement results are being used in a manner prohibited by" that section.

Antecedents to Sections 1201 and 1204

Until the recent change, the Mission Statement for the IRS had provided, in part: "The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost" Consistent with this Mission Statement, the IRS has long adhered to the principle that all IRS officials with discretion to make decisions regarding enforcement matters in individual cases should do so only on the basis of the correct application of the law to the facts of each individual case. It has also sought to give the taxpayers maximum efficiencies in its day-to-day operations and has applied many modern management techniques to measure and encourage such efficiencies.

In order to achieve these dual goals, the IRS has adopted a number of systems by which it sets goals for and measures the success of its various operating units, and directs the activities of its employees. The ultimate objective of these measurement systems is to help the IRS achieve its overall mission.

Measuring Organizational Performance

In General. The Government Performance and Results Act of 1993, Public Law 103-62 (107 Stat. 285 (Aug. 3, 1993)) (GPRA), requires the IRS and other federal agencies to establish a hierarchy of performance measures and goals applicable to various organizational units within their agencies. These performance measures and goals should be expressed in objective, quantifiable and measurable forms to define the level of performance to be achieved by a program activity.

As indicated by the General Accounting Office ("Executive Guide: Effectively Implementing the Government Performance and Results Act," (GAO/GGD-96-118 at 24)):

[L]eading organizations ... strive to align their activities and resources to achieve mission-related goals[;] they also seek to establish clear hierarchies of performance goals and measures. Under these hierarchies, the organizations try to link the goals and performance measures for each organizational level to successive levels and ultimately to the organization's strategic goals. They have recognized that without clear, hierarchically linked performance measures, managers and staff throughout the organization will lack straightforward roadmaps showing how their daily activities can contribute to attaining organizationwide strategic goals and mission.

The legislative history underlying passage of GPRA indicates that not only must performance goals be established on an hierarchal basis throughout an organization, but those goals must reflect the full range of the organization's objectives. As the Senate Report accompanying the Act indicates (S. Rep. No. 103-58, 103d Cong., 1st Sess. at 29 (1993)):

The Committee believes agencies should develop a range of related performance indicators, such as quantity, quality, timeliness, cost, and outcome. A range is important because most program activities require managers to balance their priorities among several subgoals. Reliance on any single one of these measures could create a perverse incentive for managers to achieve one subgoal at the expense of the others.

As a government agency responsible for collecting 95 percent of the nation's revenues, the IRS adopted, pursuant to GPRA and other statutes¹, a number of performance measures that focus on the amount of adjustments proposed by examination units or the dollars collected by collection offices. For example, the budgets submitted by the IRS since the mid-1990's have contained performance measures that were heavily focused upon enforcement revenue collected or protected.

¹ Both the Chief Financial Officers Act of 1990, Pub. L. 101-576, 104 Stat. 2838 (1990), and Division E, National Defense Authorization Act for Fiscal Year 1996 (the Clinger-Cohen Act of 1996), Pub. L. 104-106, 110 Stat. 186, 679 (1996), also contain requirements that federal agencies establish performance measurement systems.

The two performance measures for field examination units contained in the FY 1997 budget request were examination dollars recommended and examination dollars recommended per employee (FTE). A similarly enforcement-focused set of measures applied to field collection functions: dollars collected, dollars collected per FTE, and average cycles per TDA/TDI (tax delinquency account/tax delinquency investigation) disposition.

Measures of Special Compliance Programs.

The IRS, apart from requirements imposed upon it by statutes and regulations of general applicability, has periodically been required by Congress to establish and to report on other performance measures. For example, in connection with expected additional funding promised for FY 1995 through FY 1999 pursuant to a Compliance Initiative, the IRS made a commitment to generate \$9.179 billion in additional enforcement revenues. It was expected both to track how those additional funds were employed and to provide "quarterly reports ... identifying the progress being made through these enhanced activities to collect taxes due." S. Rep. No. 103-286, 103d Cong., 2d Sess. at 40 (1994); see H. R. Rep. No. 103-534, 103d Cong., 2d Sess. at 33 (1994); "IRS FY 1995 Compliance Initiatives Final Report," Document 9383 (Rev. 1-96), Catalog Number 21508R.

More recently, the appropriation for the IRS for FY 1998 provided additional monies for "funding essential earned income tax credit compliance and error reduction initiatives." The Conference Report accompanying that appropriation bill stated (H. R. Conf. Rep. No. 105-284, 105th Cong., 1st Sess. at 64 (1997)) that "the IRS should

establish a method to track the expenditure of funds and measure the impact [of the additional funding] on compliance. The IRS shall submit quarterly reports to the Committee on Appropriations which identify the expenditures and the change in the rates of compliance." In the absence of accurate information regarding compliance rates, the IRS has attempted to comply with this congressional requirement by reporting, inter alia, on amounts of revenue protected or collected by various EITC compliance programs. See, e.g., "IRS Tracking Earned Income Tax Credit Appropriation," Document 9383 (Rev. 6-98), Catalog Number 21508R.

Measuring the Performance of Employees

The IRS also must comply with a variety of government-wide mandates to measure the performance of individual employees. The civil service rules require that the IRS evaluate the performance of employees on an annual basis. Performance evaluations also figure in recommendations for awards, incentives, allowances or bonuses, an assessment of an employee's qualifications for promotion, reassignment or other change in duties, and the ranking of other than full-time permanent personnel for purposes of release/recall schedules. While these individual performance ratings are based upon the elements set forth in various workplans and job elements, a manager's success in achieving organizational goals will inevitably play an important role in any evaluation of his or her performance. Other employees' performance with respect to items set forth in their job elements will be viewed in light of these goals.

Past Criticisms

Over the years, the IRS has been repeatedly criticized for placing too much reliance upon tax enforcement measures it has adopted. The critics have charged that front-line personnel have felt pressured by performance measures that were focused on tax enforcement outcomes, such as dollars assessed per FTE or dollars collected per FTE, to take inappropriate enforcement actions in order to achieve perceived enforcement goals. The bulk of this criticism has focused on the impact such tax enforcement measures have had upon field personnel in the examination and collection functions.

For example, in 1955, a report by an advisory group appointed by the Chairman of the Joint Committee on Internal Revenue Taxation (The Internal Revenue Service: Its Reorganization and Administration, July 25, 1955, at 6) describes a 1954 initiative by the IRS to "establish specific office standards of production [for examination personnel in regional and district offices], so that both supervisors and employees know what is considered normal." This advisory group reported that imposition of these standards "appears to have caused a worsening of the enforcement picture."

[U]nder the established production quota system proper standards of individual performance and proper standards of examination are ignored in favor of number of returns examined. The established production quota procedure has too frequently reduced the agent's investigation to a cursory examination of readily available records and a quick look for a few obvious items on which a change can be made so as to close the case and meet the quota set.

In 1957 and again in 1959, questions were raised during hearings before the House Ways and Means Committee regarding IRS production quotas. "Reorganization and Administration of the Internal Revenue Service," Hearings before the

Subcommittee on Internal Revenue Taxation of the Committee of Ways and Means, 85th Cong., 1st Sess., at 118-119 (1957); "Income Tax Revision, Panel Discussions before the Committee on Ways and Means, House of Representatives," 86th Cong., 1st Sess. at 805, 808 (1959); "Compendium of Papers on Broadening the Tax Base Submitted to the Committee of Ways and Means," 86th Cong., 1st Sess. at 1527, 1533 (1959).

In November of 1959, the IRS issued a revised policy statement that provided, in part:

If the duties of the position require the exercise of judgment based on detailed knowledge of laws and regulations or involve material factors of technical or professional judgment, performance must be evaluated in the light of the actual cases or other assignments handled, and no quantitative measurement may be utilized which does not take such differences into account. Dollar production shall not be used as the measurement of any individual's performance.

Policy Statement P-1200-9, approved Nov. 24, 1959

Questions regarding "the rating of revenue agents on the basis of numbers of examinations made and amounts of additional tax recommended" were again raised during the 1961 confirmation hearings held for Commissioner-designate Caplin. Hearings Before the Committee on Finance, United States Senate, 87th Cong., 1st Sess., at 14-15 (1961). Following his confirmation, Commissioner Caplin announced in July of 1961 that the IRS was embarking on a "New Direction," which was designed to counter what he described as the "undue emphasis" placed upon production statistics and the "adverse effect" the perception that production statistics formed the "main basis" for evaluation of offices and individuals had upon examination quality. Under

this "New Direction," production goals and statistics would be de-emphasized, statistical data would be given more limited circulation and qualitative measures of performance would be adopted. "New Audit Program Concepts: Views of Commissioner Caplin on Evaluation of Individuals, Programs and Offices in the Audit Activity."

The following year, Commissioner Caplin issued a Special Message to All Audit Personnel, discussing some misunderstandings that had arisen regarding the new audit program. The Commissioner indicated that while supervisors were not allowed to evaluate performance on the basis of statistics or to pressure agents to produce deficiencies at the cost of inadequate audits or inequities to the taxpayer, nothing in the new audit program prohibited supervisors from keeping track of the quality and amount of work produced by agents. Indeed, "this is exactly what the supervisor of a group of agents is expected to do." The Message went on to state "Special Message from the Commissioner," dated September 7, 1962, at 2:

More serious than these misunderstandings, is the fact that enforcement results have fallen off very substantially. Despite having 1,022 more agents and office auditors in FY 62 than in FY 61, the number of returns examined decreased by 13,000, while additional taxes and penalties recommended decreased by \$66 million.

You can readily see how this drop-off endangers our Long Range Plan for gradually increasing our manpower and doing our work more effectively. Under this plan, we have been allowed almost 10,000 additional people over the last three years, and it calls for the addition of about 24,000 more by 1968. Yet, when a substantial increase in staff is followed by this kind of a drop in our enforcement results, the appropriating authorities naturally begin to wonder about the wisdom of financing the rest of our proposed expansion.

Issues regarding the IRS' use of production statistics also came up during Commissioner Alexander's 1973 confirmation hearings before the Senate Finance Committee. When questioned about his opinion toward production quotas, Commissioner Alexander responded that he was completely opposed to their use. Hearings Before the Committee on Finance, United States Senate, 93d Cong., 1st Sess., at 4-5 (1973).

In November of 1973, the IRS adopted the current version of Policy Statement P-1-20, revising its policies regarding the use of records of tax enforcement results and prohibiting absolutely the use of enforcement statistics to evaluate the performance of enforcement personnel; this statement permitted the accumulation and use of enforcement statistics only for "long-range planning, financial planning, allocation of resources, work planning and control, effective functional management, or other related staffing utilization systems and plans." In an accompanying Special Message to all Enforcement Personnel, Commissioner Alexander stated that this prohibition was applicable to all personnel who exercised judgment in determining tax liability or the ability to pay. Commissioner Alexander further declared, "[i]ndividual case or dollar goals—formal, informal, or implied—are not permitted and will not be tolerated."

During 1974, Senate Appropriations Committee hearings again focused on allegations that taxpayers were being mistreated as a result of production quotas (both case closings and dollar amounts). A number of witnesses and the Committee chairman expressed concerns that individual production statistics were being used to evaluate field employees, notwithstanding the existing policy. Testimony during those

hearings also indicated that pressure to increase the number of cases closed in Collection directly led to inappropriate seizures. Hearings Before the Subcommittee on the Department of the Treasury, U.S. Postal Service, and General Government Appropriations of the Committee on Appropriations, United States Senate, 93d Cong., 2d Sess., at 2-25, 520, 543-546, 574-584, 586-601, 653-670 (1974); see also, "Taxpayer Assistance and Compliance Programs," Hearings before the Senate Committee on Appropriations, 93d Cong., 1st Sess. at 41-46, 568-569, 642-643, 680-681 (1974).

In 1988, the Senate Appropriations Committee held hearings focusing again on allegations that the IRS' use of enforcement statistics to evaluate programs and personnel had led to inappropriate enforcement actions. Treasury, Postal Service and General Government Appropriations, Fiscal Year 1989, Before the Committee on Appropriations, 100th Cong., 2d Sess. at 588-590 (1988). On November 10, 1988, the Technical and Miscellaneous Revenue Act of 1988, Public Law 100-647 (102 Stat. 3734 (1988)) (TBOR 1) was enacted. Section 6231 of that measure prohibits the use of records of tax enforcement results:

- 1) to evaluate employees directly involved in collection activities and their immediate supervisors, or
- 2) to impose or suggest production quotas or goals [for such employees and supervisors].

During the appropriation hearings for FY 1989, Commissioner Gibbs testified about the TBOR 1 prohibition (Treasury, Postal Service and General Government Appropriations, Fiscal Year 1989, Before the Senate Committee on Appropriations, 100th Cong., 2d Sess. at 589 (1988)):

The problem that I have with our policy statement--that policy statement, by the way, being in the taxpayer bill of rights--is that it tells our people what not to do. It says, "Don't use enforcement statistics." ... I don't think that this helps someone on the front line very much to tell them what not to do.

What we have started, within the last 18 months that I have been the Commissioner, is to begin to develop at the working level criteria as to what constitutes a quality collection action, what constitutes a quality examination action. It is an entirely different approach to collection and examination, trying to train the people as to how to approach what they are doing so that if they do it the right way, the numbers will flow. The idea is to get away from simply dollar amounts, comparing one another in terms of how they are doing with respect to collections, or seizures, or anything like that.

The General Accounting Office has expressed a somewhat different view of the appropriate use of enforcement results to measure IRS performance. Its December 10, 1991, report on "IRS' Implementation of the 1988 Taxpayer Bill of Rights" stated (GAO/GGD- 92-23 at 14-15):

In an October 1987 letter to the Chairmen of the House Committee on Ways and Means and the Senate Committee on Finance, we commented on various proposals to prohibit the use of collection statistics in performance evaluations. Our position then and now is that collection statistics should not be the only indicator of performance but, along with other factors, could very well be a useful tool in evaluating employees. We pointed out that relying on a single factor can place more emphasis on that factor than on overall performance. We said that it is not totally inappropriate to generally consider the amount of revenues collected as part of an employee's evaluation if that consideration is only one of several factors under review. We added that setting arbitrary quotas for amounts collected, property seized, or cases closed cannot be justified in evaluating performance, particularly because of the negative impact that trying to achieve those quotas can have on taxpayers.

In its May 11, 1993, report on "Tax Administration: New Delinquent Tax Collection Methods for IRS" (GAO/GGD093-67 at 9), GAO reiterated this view:

As we have stated in the past, IRS should be able to use collection performance as a criterion in determining compensation and rewards for individual collectors. We believe that information such as taxes collected is a reasonable basis on

which to judge the performance of employees whose job it is to collect taxes as long as other criteria, such as fair and courteous treatment of taxpayers, are also evaluated.

In a similar vein, a December 23, 1993, report by the GAO on the offer in compromise program ("Tax Administration: Changes Needed to Cope with Growth in Offer in Compromise Program" (GAO/GGD-94-47 at 24) indicated:

The Commissioner of Internal Revenue should develop the indicators necessary to evaluate the Offer in Compromise Program as a collection and compliance tool. The indicators should be based on accurate data and include (1) the yield of the program in terms of costs expended and amounts collected, (2) the amount of revenues collected that would not have been collected through other collection means

In September 1997, the Senate Finance Committee held three days of widely-publicized oversight hearings on the Internal Revenue Service. During these hearings, several IRS employees testified that IRS' performance measurement system was creating an environment in which they felt pressured to achieve certain quantitative goals for tax enforcement results (such as dollars recommended or collected). In his testimony at the conclusion of these hearings, the Acting Commissioner responded to the concerns that had been raised about the negative impact of the IRS performance measurement system by announcing a number of immediate changes in the system. In particular, he announced that IRS would suspend the comparative ranking of its 33 district offices and suspend distribution of any goals related to revenue production to field offices. "Practices and Procedures of the Internal Revenue Service," Hearings before the Committee on Finance, United States Senate, 105th Cong., 1st Sess., at 3,

105-106, 123-128, 153, 155-156, 162-163, 206-209, 212-213, 303-304, 310, 317-318, 320-322, 325-326, 330, 333, 351-356.

Following these hearings, the IRS Office of Chief Inspector undertook three management audits to determine how enforcement statistics were then being used as part of the IRS performance measurement system. See, "Review of the Use of Statistics and the Protection of Taxpayer Rights in the Arkansas-Oklahoma District Collection Field Function," Internal Audit Reference Number 380402 (December 5, 1997); "Use of Enforcement Statistics in the Collection Field Function," Internal Audit Reference Number 081904 (January 12, 1998); "Examination Division's Use of Performance Measures and Statistics," Internal Audit Reference Number 084303 (July 7, 1998). These three inquiries generally confirmed that IRS performance measures were focused largely on enforcement goals and productivity as defined by statistics relating to dollars recommended, assessed or collected, or other enforcement actions taken. They found a lack of corresponding emphasis on quality casework, adherence to law, and protection of taxpayer rights.

In order to deal with specific allegations of misconduct made during the September hearings, or discovered in the course of the management audits described above, the IRS Office of Chief Inspector also undertook a number of individual investigations. The Commissioner then established a Special Review Panel of career executives from outside the IRS to review the evidence and to recommend appropriate personnel actions. The Special Review Panel issued a Report to the Commissioner in August 1998. In its Report, the Special Review Panel agreed with earlier conclusions that IRS

had responded to external pressures to close the revenue gap through improved productivity by shifting management emphasis to goals and measures that placed a heavy emphasis on use of enforcement statistics. See also "IRS Personnel Administration: Use of Enforcement Statistics in Employee Evaluations" (GAO/GGD-99-11, November 30, 1998).

Internal Revenue Service Restructuring and Reform Act of 1998

Sections 1201 and 1204 of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA) represent the most recent legislative action regarding performance measures used by the IRS. Section 1201 directs the IRS, consistent with its current performance planning procedures, including those established under the GPRA, to establish a performance management system that will establish "goals or objectives for individual, group, or organizational performance." The IRS is directed to use this performance system in the evaluation of employees or groups of employees, in determining salary adjustments and awards, and in other personnel matters. The Conference Report accompanying RRA (H. R. Conf. Rep. No. 105-599, 105th Cong., 2d Sess., at 228 (June 24, 1998) indicates that "in no event would performance measures be used which rank employees or groups of employees based solely on enforcement results, establish dollar goals for assessments or collections, or otherwise undermine fair treatment of taxpayers."

Section 1204 of RRA repealed section 6231 of TBOR 1 and replaced TBOR 1's prohibition on the use of "records of tax enforcement results" to evaluate or to impose or suggest goals for personnel directly involved in collection activity with a prohibition

against using such records of tax enforcement results to evaluate, or to impose or suggest production quotas or goals for, any IRS "employee."

Explanation of Provisions

Proposed Effective Date

These regulations are proposed to be effective thirty days after the date of publication in the **Federal Register** of the final regulations.

Balanced Measurement System

These proposed regulations provide guidance and direction for the establishment of a balanced performance measurement system for the Internal Revenue Service. They also provide guidance for implementing the restrictions on the use of "records of tax enforcement results" in evaluating, or imposing or suggesting goals for employees and for establishing "fair and equitable treatment of taxpayers" as one of the standards for evaluating employees.

These proposed regulations establish a new balanced system for measuring the performance of and establishing performance goals for various operational units within the Internal Revenue Service. The three elements of this balanced measurement system are (1) Customer Satisfaction Measures, (2) Employee Satisfaction Measures and (3) Business Results Measures. These measures will, consistent with GPRA, be based on "quantifiable and measurable" data, and will be numerically scored.

The proposed regulations do not provide procedures for certifying whether or not records of tax enforcement results have been used in a manner prohibited by section 1204. Subsequent guidance will provide that information.

a. Customer Satisfaction

To measure customer satisfaction, the IRS will develop data from customer satisfaction surveys it receives from a statistically valid sample of taxpayers with whom it has dealt. Among other things, taxpayers will be asked to provide information regarding whether they were treated courteously and professionally, whether they were informed of their rights and whether they were given an opportunity to voice their concerns and adequate time to respond to IRS requests. Using data derived from these surveys, the IRS will derive quantitative indices of customer satisfaction which will be used to measure progress in achieving customer satisfaction goals.

b. Employee Satisfaction

To measure employee satisfaction, the IRS will utilize an employee survey that permits employees to provide, on an anonymous basis, their assessment of the wide variety of factors that determine whether employees believe that the work environment permits them to perform their duties in a professional manner. Among other items included in the employee survey, the questionnaires should elicit information regarding employees' assessment of the quality of supervision and the adequacy of training and support services. As in the case of the Customer Satisfaction measures, the goals and the accomplishments of units subject to the balanced measurement system will be expressed in quantified form.

c. Business Results

The IRS will employ two parallel avenues to measure business results.

1. Quality Measures

The first of these approaches will focus on the quality of the work done in a sample of cases that were worked on by employees. Such reviews will be conducted of a statistically valid sample of cases worked on by units designated by the Commissioner, such as a collection or examination unit. A staff of personnel specially dedicated to the task will review and numerically score the quality of work done by IRS personnel. These reviews will focus on such factors as whether IRS personnel provided proper and timely service to the taxpayer, properly analyzed the facts, correctly applied the law, protected taxpayer rights by following applicable IRS policies and procedures, devoted an appropriate amount of time to the case, made appropriate judgments regarding liability for tax and ability to pay and provided accurate answers to tax law or account questions posed by callers.

2. Quantity Measures

The quantity measures element of the business results measure will focus exclusively on outcome-neutral production data. Accordingly, as described in the regulation, data concerning the enforcement outcome in cases, such as the dollar amount of audit adjustments, the numbers of liens filed or levies served, and the number of referrals for criminal investigation, would be excluded from the production data used in the quantity measures. On the other hand, outcome-neutral production data, such as cases closed, time per closing or cycle time, which do not reflect the outcome produced by any IRS official's exercise of judgment in determining liability for tax or the collection mechanism to be employed may be used in determining the production element of the business results measures. The IRS has determined,

however, that as a matter of policy such outcome-neutral production data may not be used to set goals for or for evaluating any non-supervisory employee with tax enforcement responsibilities.

Further, an organization with enforcement responsibilities may not be given a goal or an evaluation based on enforcement-neutral production data regarding matters calling for the exercise of judgment with respect to tax enforcement results unless that goal or evaluation constitutes only one element in a set of goals or one element in an evaluation based also upon the balanced measurement system.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations and, because these regulations do not impose on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any electronic and written comments (a signed original

and eight (8) copies) that are submitted timely to the IRS. The IRS and Treasury specifically request comments on the clarity of the proposed regulation and how it may be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for Thursday, May 13, 1999, beginning at 10 a.m. in room 2615 of the Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC. Due to building security procedures, visitors must enter at the 10th Street entrance, located between Constitution and Pennsylvania Avenues, NW. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 15 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601 (a) (3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit comments and an outline of the topics to be discussed and the time to be devoted to each topic by Thursday, April 22, 1999. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Julie A. Barry, Office of Assistant Chief Counsel (General Legal Services). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects in 26 CFR Part 801

Government employees, organization and functions (Government agency).

Proposed Amendments to the Regulations

Accordingly, 26 CFR Chapter I is proposed to be amended by adding part 801 to Subchapter H to read as follows:

PART 801--BALANCED SYSTEM FOR MEASURING ORGANIZATIONAL AND INDIVIDUAL PERFORMANCE WITHIN THE INTERNAL REVENUE SERVICE

Sec.

801.1 Balanced performance measurement system; in general.

801.2 Balanced performance measurement system.

801.3 Customer satisfaction measures.

801.4 Employee satisfaction measures.

801.5 Business results measures.

Authority: 5 U.S.C 9501 et seq. ; secs. 1201, 1204, Pub. L. 105-206, 112 Stat. 685, 715-716, 722 (26 U.S. C. 7804 note).

§801.0-1 Balanced performance measurement system; in general

(a) In general. The regulations in this part 801 implement the provisions of sections 1201 and 1204 of the Internal Revenue Service Restructuring and Reform Act of 1998 (Pub. L. 105-106, 112 stat. 685, 715-716, 722) and provide rules relating to the establishment by the Internal Revenue Service of a balanced performance measurement system.

(b) Effective date. This part 801 is effective thirty days after the date these regulations are published as final regulations in the Federal Register.

§801.2 Balanced performance measurement system.

(a) In general. Modern management practice and various statutory and regulatory provisions require the IRS to set performance goals for organizational units and to measure the results achieved by those organizations with respect to those goals. To fulfill these requirements, the IRS has established a balanced performance measurement system, composed of three elements: Customer Satisfaction Measures; Employee Satisfaction Measures; and Business Results Measures. The IRS is likewise required to establish a performance evaluation system for individual employees.

(b) Measuring organizational performance--(1) In general. The performance measures that comprise the balanced measurement system will, to the maximum extent possible, be stated in objective, quantifiable and measurable terms and, subject to the limitation set forth in paragraph (b)(2) of this section, will be used to measure the overall performance of various operational units within the IRS. In addition to implementing the requirements of the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. 105-206, 112 Stat. 685 , the measures described here will, where appropriate, be used in performance goals and performance evaluations established, inter alia, under Division E, National Defense Authorization Act for Fiscal Year 1996 (the Clinger-Cohen Act of 1996), Pub. L. 104-106, 110 Stat. 186, 679; the Government Performance and Results Act of 1993, Pub. L. 103-62, 107 Stat. 285; and the Chief Financial Officers Act of 1990, Pub. L. 101-576, 108 Stat. 2838.

(2) Limitation--quantity measures (as described in § 801.5) will not be used to evaluate the performance of or to impose or suggest production goals for any organizational unit with employees who are responsible for exercising judgment with respect to tax enforcement results (as defined in § 801.5) except in conjunction with an evaluation or goals based also upon Customer Satisfaction Measures, Employee Satisfaction Measures, and Quality Measures.

(c) Measuring individual performance. All employees of the IRS will be evaluated according to the critical elements and standards or other performance criteria established for their positions. In accordance with the requirements of 5 U.S.C. 4312 and 9508 and section 1201 of the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. 105-206 (112 Stat. 685), (as is appropriate to the employee's position), the performance criteria for each position will be composed of elements that support the organizational measures of Customer Satisfaction, Employee Satisfaction and Business Results; however, such organizational measures will not directly determine the evaluation of individual employees.

(1) Fair and equitable treatment of taxpayers. In addition to all other criteria required to be used in the evaluation of employee performance, all employees of the IRS will be evaluated on whether they provided fair and equitable treatment to taxpayers.

(2) Senior Executive Service and special positions. Employees in the Senior Executive Service will be rated in accordance with the requirements of 5 U.S.C.

4312 and employees selected to fill positions under 5 U.S.C. 9503 will be evaluated pursuant to workplans, employment agreements, performance agreements or similar documents entered into between the Internal Revenue Service and the employee.

(3) General workforce. The performance evaluation system for all other employees will:

(i) Establish one or more retention standards for each employee related to the work of the employee and expressed in terms of individual performance; and--

(A) Require periodic determinations of whether each employee meets or does not meet the employee's established retention standards; and

(B) Require that action be taken, in accordance with applicable laws and regulations, with respect to employees whose performance does not meet the established retention standards.

(ii) Establish goals or objectives for individual performance consistent with the IRS's performance planning procedures; and --

(A) Use such goals and objectives to make performance distinctions among employees or groups of employees; and

(B) Use performance assessments as a basis for granting employee awards, adjusting an employee's rate of basic pay, and other appropriate personnel actions, in accordance with applicable laws and regulations.

(4) Limitations. (i) No employee of the IRS may use records of tax enforcement results (as defined in § 801.5) to evaluate any other employee or to impose or suggest production quotas or goals for any employee.

(A) For purposes of the limitation contained in this paragraph (c)(4), employee has the meaning as defined in 5 U.S.C. 2105(a).

(B) For purposes of the limitation contained in this paragraph (c)(4), evaluate includes any process used to appraise or measure an employee's performance for purposes of providing the following:

(1) Any required or requested performance rating.

(2) A recommendation for an award covered by Chapter 45 of Title 5; 5 U.S.C. 5384; or section 1201(a) of the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. 105-206 (112 Stat. 685, 713-716).

(3) An assessment of an employee's qualifications for promotion, reassignment or other change in duties.

(4) An assessment of an employee's eligibility for incentives, allowances or bonuses.

(5) Ranking of employees for release/recall and reductions in force.

(ii) Employees who are responsible for exercising judgment with respect to tax enforcement results (as defined in § 801.5) in cases concerning one or more taxpayers may be evaluated with respect to work done on such cases only on the basis of information derived from a review of the work done on the taxpayer cases handled by such employee.

(iii) Performance measures based in whole or in part on Quantity Measures (as described in § 801.5) will not be used to evaluate the performance of or to impose or

suggest goals for any non-supervisory employee who is responsible for exercising judgment with respect to tax enforcement results (as defined in § 801.5).

§ 801.3 Customer satisfaction measures.

The customer satisfaction goals and accomplishments of operating units will be determined on the basis of data derived from questionnaires, surveys and other types of information gathering mechanisms. Surveys designed to measure customer satisfaction for a particular work unit will be distributed to a statistically valid sample of the taxpayers served by that operating unit and will be used to measure whether those taxpayers believe that they received courteous, timely and professional treatment by the IRS personnel with whom they dealt. Taxpayers will be permitted to provide information requested for these purposes under conditions that guarantee them anonymity.

§ 801.4 Employee satisfaction measures.

The numerical ratings to be given operating units within the IRS for employee satisfaction will be determined on the basis of information derived from a questionnaire which will be distributed to all employees of the operating unit; the employees will be permitted to provide information on an anonymous basis. Data from these surveys will measure, among other factors bearing upon employee satisfaction, the quality of supervision and the adequacy of training and support services.

§ 801.5 Business results measures.

(a) In general. The business results measures will consist of numerical scores determined under the Quality Measures and the Quantity Measures described elsewhere in this section.

(b) Quality measures. The quality measure will be determined on the basis of a review by a specially dedicated staff within the IRS of a statistically valid sample of work items handled by certain functions or organizational units determined by the Commissioner or his delegate such as the following:

(1) Examination and collection units and Automated Collection System units (ACS). The quality review of the handling of cases involving particular taxpayers will focus on such factors as whether IRS personnel devoted an appropriate amount of time to a matter, properly analyzed the issues presented, developed the facts regarding those issues, correctly applied the law to the facts, and complied with statutory, regulatory and IRS procedures, including timeliness, adequacy of notifications and required contacts with taxpayers.

(2) Toll-free telephone sites. The quality review of telephone services will focus on such factors as whether IRS personnel provided accurate tax law and account information.

(3) Other workunits. The quality review of other workunits will be determined according to criteria prescribed by the Commissioner or his delegate.

(c) Quantity measures. The quantity measures will consist of outcome-neutral production and resource data, such as the number of cases closed, work items completed, hours expended and similar inventory, workload and staffing information,

that does not contain information regarding the tax enforcement result reached in any case involving particular taxpayers.

(d) Definitions--(1) Tax enforcement result. A tax enforcement result is 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 law with respect to any assessed or unassessed tax.

(i) Examples of data containing information regarding tax enforcement results.

The following are examples of data containing information regarding tax enforcement results: number of liens filed; number of levies served; number of seizures executed; dollars assessed; dollars collected; full pay rate; no change rate; and number of fraud referrals.

(ii) Examples of data that do not contain information regarding tax enforcement results. The following are examples of data that do not contain information regarding tax enforcement results: number of cases closed; time per case; direct examination time/out of office time; cycle time; number or percentage of overage cases; inventory information; toll-free level of access; talk time; and data derived from a quality review or from a review of an employee's or a workunit's work on a case, such as the number or percentage of cases in which correct examination adjustments were proposed or appropriate lien determinations were made.

(iii) Records of tax enforcement results. Records of tax enforcement results are data, statistics, compilations of information or other numerical or quantitative recordations of the tax enforcement results reached in one or more cases, but does not

include information, including the tax enforcement result, regarding an individual case to the extent the information is derived from a review of an employee's or a workunit's work on individual cases.

(e) Permitted uses of records of tax enforcement results. Records of tax enforcement results may be used for purposes such as forecasting, financial planning, resource management, and the formulation of case selection criteria.

(f) Examples. The following examples illustrate the rules of this section:

Example 1. In conducting a performance evaluation, a supervisor may take into consideration information showing that the employee had failed to propose an appropriate adjustment to tax liability in one of the cases the employee examined, provided that information is derived from a review of the work done on the case. All information derived from such a review of individual cases handled by an employee, including time expended, issues raised, and enforcement outcomes reached may be considered in setting goals or evaluating the employee.

Example 2. A supervisor may not establish a goal for proposed adjustments in a future examination, even though the goal was derived from analyses of previously-handled cases, because such enforcement goals are not based upon an analysis of the newly-assigned case.

Example 3. A headquarters unit may use records of tax enforcement results to develop methodologies and algorithms for use in selecting tax returns to audit.

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