

**The Wage and Investment Division's  
Automated Underreporter Program  
Effectively Monitored Performance Data  
to Meet Annual Program Goals**

**October 2004**

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**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.**



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

October 27, 2004

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

*Gordon C. Milbourn III*

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

SUBJECT: Final Audit Report - The Wage and Investment Division's  
Automated Underreporter Program Effectively Monitored  
Performance Data to Meet Annual Program Goals  
(Audit # 200440024)

This report presents the results of our review of the Wage and Investment (W&I) Division's Automated Underreporter (AUR) Program. The overall objective of this review was to determine whether the Program is effectively managed to help ensure it meets its intended goals, including the evaluation of Program performance through adequate data collection, evaluation of Program deficiencies, and Program management accountability.

To assess the AUR Program, we used the Program Assessment Rating Tool (PART) criteria created by the Office of Management and Budget to rate Federal Government programs. The PART is a systematic method of assessing the performance of program activities across the Federal Government and is a diagnostic tool with the main objective to improve agency program performance and link performance to budget decisions.

The AUR Program Manager reported that the AUR analysts monitored the monthly workload results of each campus<sup>1</sup> to ensure ample progress was being made toward achieving established performance goals. Our review of the various national- and campus-level management information reports confirmed that the AUR Program was on schedule to meet its Fiscal Year 2004 goals. W&I Division management held the AUR Program Manager and the associated AUR campus managers accountable for meeting the AUR Program's annual goals by including the goals in their annual performance

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<sup>1</sup> The data processing arm of the Internal Revenue Service. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

standards. To maintain a high level of performance, management in the Reporting Compliance function began to perform operational reviews at the W&I Division campuses to help manage and enhance the AUR Program.

We made no recommendations in this report. However, key Internal Revenue Service management officials reviewed it prior to issuance and provided their concurrence with its contents via email.

Copies of this report are also being sent to the IRS managers affected by the report results. Please contact me at (202) 622-6510 if you have questions or Michael R. Phillips, Assistant Inspector General for Audit (Wage and Investment Income Programs), at (202) 927-0597.

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### Background

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The Internal Revenue Service's (IRS) Information Reporting Program is the cornerstone of voluntary compliance and affects compliance and revenue across every taxpayer and market segment. The Information Reporting Program helps ensure a high level of compliance by requiring third parties such as employers, banks, brokerage firms, and others to file information returns reporting taxpayer income and certain deductions to the IRS.<sup>1</sup> In Fiscal Year (FY) 2003, the IRS received over 130 million individual income tax returns and over 1.3 billion information returns.<sup>2</sup>

The Automated Underreporter (AUR) Program is part of the Information Reporting Program. The mission of the AUR Program is to reduce taxpayer burden and increase voluntary taxpayer compliance. The AUR Program has evolved as a compliance initiative using the third-party information returns to identify income and deductions that were not reported on tax returns.

The AUR Program is administered by the Compliance functions in the Wage and Investment (W&I) and Small Business/Self-Employed (SB/SE) Divisions operating through six IRS campuses.<sup>3</sup> The Reporting Compliance function in the W&I Division administers the AUR Program through the three W&I Division campuses located in Atlanta, Georgia; Austin, Texas; and Fresno, California.

The annual AUR process begins when the Martinsburg Computing Center creates an inventory list of potential underreporter cases by matching taxpayer return data against the data in the third-party information return database, identifying taxpayers with discrepancies. The first

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<sup>1</sup> Information returns are submitted by third parties to report certain business transactions to the IRS (e.g., the amount of payments made to and from individuals such as wages, interest, dividends, and sales of certain assets). The information is reported to the IRS on various forms such as the Form 1099 series (for various incomes such as Miscellaneous, Interest, Dividend, etc.) and the Wage and Tax Statement (Form W-2).

<sup>2</sup> The IRS reported this information in its IRS 2003 Data Book.

<sup>3</sup> The campuses are the data processing arms of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

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match occurs between July and September of each year; a second match, picking up additional filers, occurs during January and February of each year. The 2 matches result in a total of approximately 15 million potential underreporter cases. Due to resource capacity constraints, the W&I and SB/SE Division AUR Programs can work only about 3 million of these cases annually, with 55 percent of the cases worked in the W&I Division and the balance in the SB/SE Division. During FY 2003, the W&I Division AUR Program closed 1.52 million cases and assessed \$1.42 billion in unpaid taxes.

This review was the second part of our strategy to determine whether the W&I Division was reducing the risk of taxpayer noncompliance as a result of work performed through the AUR Program. This strategy focused on using the Program Assessment Rating Tool (PART) created by the Office of Management and Budget (OMB) to rate Federal Government programs. The PART is a systematic method of assessing program performance across the Federal Government and is a diagnostic tool with the main objective to improve performance in agency programs and link performance to budget decisions.

Our review of the AUR Program focused on assessing Program management using Section III of the PART. Section III focuses on whether a program is effectively managed to meet annual program performance goals. Key areas include the evaluation of program improvements, performance data collection, and program management accountability.

This review was performed in the AUR Program Office at the W&I Division Headquarters in Atlanta, Georgia, during the period April through September 2004. 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.

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### **The Automated Underreporter Program Manager Effectively Used Data to Monitor Annual Performance Goals**

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The AUR Program Manager reported that, through the AUR Program analysts, the monthly progress of each W&I Division campus was monitored to ensure ample progress was being made throughout the year toward meeting the established Program goals. Our review of the various national- and campus-level management information reports confirmed that the AUR Program was on schedule to meet its FY 2004 goals.

The progress of the AUR Program was tracked through a number of internal information reports. For example:

- Maintaining a case quality level of 92 percent (AUR Paper Quality) was tracked through the AUR Paper Quality Report.
- Opening 1,608,000 AUR cases (AUR Starts) was monitored through the AUR Work Scheduling Tool.
- Closing 1,561,000 cases (AUR Case Closures) was tracked through the AUR Closures by Disposition Report.
- Assessing \$1.5 billion in additional tax revenue (AUR Assessments) was tracked using the Enforcement Revenue Information System Report.
- Maintaining an AUR telephone call accuracy level of 92 percent (AUR Telephone Quality) was monitored through the AUR Phone Quality Report.
- Keeping overage correspondence at a level below 22 percent (AUR Overage Correspondence) was tracked using the Compliance Inventory Report-Summary.

The AUR Program Manager stated that he used the available data to monthly monitor each campus' progress toward accomplishing the annual performance measures, including those goals listed above. In addition, the AUR Program Manager reported contacting the AUR campus managers to discuss performance progress. If the AUR Program Manager determined that a campus might be in danger of not meeting an annual performance goal, a plan would be developed in consort with the responsible AUR campus manager to get the campus back on track toward meeting the established goal.

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For example, the AUR Program Manager explained that, during his review of the January 2004 performance measures, he identified a potential problem with a campus meeting the annual goal of Full-Time Equivalent (FTE)<sup>4</sup> use. The AUR Program Manager believed this was caused by the selection of employees for open positions who could not report until after the filing season.<sup>5</sup> The scheduling conflict delayed the local campus' ability to timely process the planned volume of cases. The AUR Program Manager worked with the local AUR campus manager to develop a plan to address the underused FTE resources. As a result of this action, the campus was able to meet its planned goal for established FTE use and meet the case processing requirements. Without this adjustment, the goals for the number of AUR starts, closures, and assessments could have been adversely affected.

The OMB PART process stresses that agencies need to "regularly collect timely and credible performance information and use it to manage the program and improve performance." By effectively gathering performance data and continuing to monitor the Program's success in achieving its annual goals, AUR Program management can continue to ensure their existing resources are maximizing the AUR Program compliance efforts.

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### **The Automated Underreporter Program Manager and the Automated Underreporter Campus Managers Were Held Accountable for Program Performance Results**

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W&I Division management held the AUR Program Manager and the AUR campus managers accountable for meeting the AUR Program's annual goals. Specific AUR Program performance expectations were included in the annual performance standards for the AUR Program Manager and the AUR campus managers as an addendum to the general performance standards required for all IRS managers. While these expectations did not individually address each specific Program goal, they did set the expectation that the managers would be evaluated on their ability to meet all of the AUR Program's annual goals.

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<sup>4</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. For FY 2004, 1 FTE was equal to 2,096 staff hours.

<sup>5</sup> The filing season is the period from January through mid-April when most individual income tax returns are filed.



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The OMB PART process stresses that “the program agency identify the managers who are responsible for achieving key program results and establish performance standards for those managers.” Including specific AUR Program performance expectations in the individual managers’ performance standards established a link for the AUR Program between management performance and Program results. It also emphasized the importance of Program accomplishments by forcing management to focus their personal performance toward achieving their Program’s annual goals.

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### **Reporting Compliance Function Management Has Initiated Operational Reviews to Evaluate Management Effectiveness**

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To maintain a high level of performance, management in the Reporting Compliance function began to perform operational reviews at the W&I Division campuses to help manage and enhance the AUR Program. During FY 2004, the Reporting Compliance Director, using review teams consisting of program managers and senior staff analysts, conducted operational reviews of various compliance programs at the W&I Division campuses. The operational reviews addressed the entire Reporting Compliance function, which included the AUR Program and its progress toward meeting some of its annual performance goals. As part of the operational review, the review teams conducted focus group interviews with AUR Program employees and group managers.

As of July 2004, the Reporting Compliance function had completed and reported the results of operational reviews at the Austin, Texas, and Fresno, California, campuses. These reviews determined that both AUR Program campuses had made significant improvement in several performance measures, as compared to the same period in FY 2003. In particular, the campuses had met or exceeded the FY 2003 performance levels in areas involving case processing and telephone operation. The operational review teams did note some delays in timely processing of certain types of cases and recommended specific actions intended to improve case processing. While these issues apparently did not affect the campuses’ ability to meet established goals, adhering to the established AUR Program operating procedures would help the Program be more effective in processing the entire AUR Program workload.

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The OMB PART process stresses that management needs to “develop a system of evaluating program management and correcting deficiencies when they are identified.” By using the information obtained through periodic operational reviews, Reporting Compliance function management can effectively monitor management effectiveness in meeting performance goals and addressing program deficiencies.

**Detailed Objective, Scope, and Methodology**

The overall objective of this review was to determine whether the Wage and Investment (W&I) Division's Automated Underreporter (AUR) Program is effectively managed to help ensure it meets its intended goals, including the evaluation of Program performance through adequate data collection, evaluation of Program deficiencies, and Program management accountability. To accomplish this objective, we:

- I. Determined whether the AUR Program was effectively managed to meet its annual performance goals.
  - A. Interviewed AUR Program management and reviewed various national- and campus-level<sup>1</sup> management information reports to determine whether management used regularly collected timely and credible performance information to manage the AUR Program and improve performance. We did not audit the reliability of the data contained in the management information reports.
  - B. Interviewed AUR Program management and reviewed various national- and campus-level management information reports to determine whether the quality assurance process for the AUR Program ensured performance measures accurately reflected the Program's performance.
- II. Determined whether the AUR Program Manager and the AUR campus managers were held accountable for performance results.
  - A. Obtained and reviewed the Fiscal Year (FY) 2004 Internal Revenue Service manager performance standards and additional AUR Program expectations for the AUR Program Manager and the AUR campus managers involved in processing the AUR workload.
  - B. Compared the manager performance standards and additional expectations to the AUR Program's FY 2004 performance goals to determine whether the manager performance standards and additional expectations were linked to the Program's annual performance goals.
- III. Determined whether Reporting Compliance function management had taken meaningful steps to evaluate AUR Program management effectiveness and address management deficiencies.
  - A. Interviewed Reporting Compliance function management to determine how they monitored the AUR Program.

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<sup>1</sup> The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

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- B. Reviewed the W&I Division Business Performance Review Reports for FY 2003 and the first two quarters of FY 2004 to determine whether the AUR Program was effectively managed and whether any management deficiencies were identified during the reviews.
- C. Reviewed operational reviews conducted by Reporting Compliance function management at the Austin, Texas, and Fresno, California, campuses to evaluate Program management effectiveness and identify any management deficiencies in the AUR Program.

**Major Contributors to This Report**

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**Appendix III**

**Report Distribution List**

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