

Treasury Inspector General for Tax Administration



Semiannual Report to the Congress

October 1, 2001 through March 31, 2002



Treasury Inspector General For Tax Administration

Mission Statement

Provide audit and investigative services that promote economy, efficiency and integrity in the administration of the internal revenue laws.

Vision Statement

We are a respected member of the government community:

- Independent, objective and professional in the conduct of our mission.
 - Dedicated and innovative professionals who take pride in promoting fair tax administration and good government.
 - Proud of our past and focused on the future.
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DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

April 30, 2002

The Honorable Paul H. O'Neill
Secretary of the Treasury
Washington, D.C. 20220

Dear Mr. Secretary:

I am pleased to submit to you the Treasury Inspector General for Tax Administration's (TIGTA) *Semiannual Report to Congress* for the reporting period October 1, 2001 through March 31, 2002. During this reporting period, TIGTA continued to focus on a variety of complex issues that relate to all aspects of tax administration.

TIGTA has actively supported the activities related to the aftermath events of September 11, 2001. For instance, TIGTA participated in the IRS' efforts to gain an understanding of the new security risks and to develop a comprehensive plan to deal with them. TIGTA also participated in many law enforcement activities that were directly associated with the events of September 11, 2001. Details of TIGTA's efforts are highlighted in the *Significant Activities* section of this report.

This has been a very productive period for TIGTA's Office of Audit and Investigations. Highlights of the Office of Audit's accomplishments include issuing 75 audit reports that identified over \$15.6 million in cost savings or funds put to better use, and an additional \$492 million in increased revenue and/or revenue protected. The Office of Audit also continues to identify significant issues related to information systems security, business systems modernization, returns processing, voluntary compliance and earned income credit.

The Office of Investigation received 3,389 complaints of alleged criminal wrongdoing and/or administrative misconduct, of which 1,582 warranted further investigation. In addition, 2,036 investigations were opened and 2,171 investigations were closed. The closed investigations included issues such as bribery, misuse of IRS computer systems, fraud, and embezzlement.

I look forward to continuing to work together with you, Congress and IRS officials to help the IRS address current and future challenges.

Sincerely,

David C. Williams
Inspector General

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September 11, 2001

Challenges

The events of September 11, 2001, changed the Internal Revenue Service's (IRS) security paradigm. The terrorist attacks and the subsequent anthrax scare made it a realistic possibility that multiple IRS locations simultaneously could be incapacitated. Since September 11th, IRS has worked aggressively to gain an understanding of these new risks and to deal with them.

The Treasury Inspector General for Tax Administration (TIGTA) has been participating in IRS' security efforts in two ways. First, the Office of Investigations (OI) meets daily with the Federal Bureau of Investigation (FBI) to stay abreast of new threats and is acting as the primary conduit of that information to IRS. Second, the Office of Audit (OA) is working in coordination with the General Accounting Office (GAO) to provide a comprehensive evaluation of IRS' security initiatives. Since

IRS is a highly visible potential target for domestic and international terrorism, appropriate congressional groups receive interim briefings. TIGTA will report formally on the results of its ongoing assessments in its next *Semiannual Report to Congress*.

Activities

Providing Emergency and Investigative Assistance

Immediately following the terrorist attacks of September 11, 2001, TIGTA provided extensive emergency and investigative assistance to federal, state and local law enforcement agencies. Initial recovery efforts required temporarily relocating the TIGTA staff and operations from the World Trade Center complex and maintaining the investigative continuity of the office. Congress approved supplemental funds to replace TIGTA's New York City office and the equipment destroyed at the World Trade Center.

TIGTA Headquarters temporarily ceased normal activities on September 11, 2001, and dedicated all available investigative resources towards the terrorist attack investigation. This included the implementation of a 24-hour TIGTA command post, participation at various command posts established in the area, and enhanced participation at the



FBI's Joint Terrorism Task Forces (JTTF) around the country. TIGTA personnel worked expanded schedules and assisted in various investigative efforts, to include conducting pertinent interviews and the collection of evidence at both the World Trade Center and the Pentagon.

TIGTA continues to maintain a presence at the FBI's JTTF and support efforts combating terrorism. Under *Section 7212 of Title 26 of the United States Code*¹ and the *Restructuring and Reform Act of 1998*² (RRA 98), TIGTA has statutory responsibility to investigate and pursue attempts to corrupt or forcibly interfere with the administration of internal revenue laws. A violation of this statute includes threats against IRS personnel and facilities.

TIGTA immediately redirected assets to support both the New York staff, as well as the national investigative efforts coordinated by the FBI. This included 24-hour staffing at the FBI command post for all agencies supporting the investigation. It served as the central location and repository for information and investigative results. TIGTA temporarily assigned 10 special agents and maintained coverage at the command post from September 2001 through January 2002.

Ol's Technical Services Section (TSS) provided extensive emergency and investigative assistance to federal, state and local law enforcement agencies during its response to the terrorist attacks on the World Trade Center in New York City. TSS deployed its mobile communications command post to coordinate two-way radio communications among United States (U.S.) Treasury bureaus and various elements of the state and local law enforcement first responders.

¹ The *Internal Revenue Code (I.R.C.)* is contained in *Title 26 of the United States Code (U.S.C.)*. Thus, *I.R.C. § 7212* and *26 U.S.C. § 7212* refer to the same code section.

² *Pub. L. No. 105-206, 112 Stat. 685.*

Diverting the Strategic Enforcement Division (SED) Staff

The entire SED staff assisted the FBI in the investigation of international and domestic terrorism. SED secured data and provided summaries of the information to the FBI. As a result of this effort, OI provided the FBI with vital information on data requests. In October 2001, SED expended approximately 2,700 staff hours in direct support of this investigation.



Pictured left to right: TIGTA Special Agent Al Rolek, Investigative Specialist Dave Verhun, Asst. Special Agent-in-Charge Mike Doak and Investigative Specialist Dave Weaver.

Participating in the Federal Aviation Administration (FAA) Air Marshal Program

Along with other participating agencies, TIGTA detailed special agents to participate in the FAA Air Marshal Program, which enabled the FAA to quickly strengthen the safety and security of air travel in the U.S. The newly created Transportation Security Administration is now deploying recently hired Air Marshals, which permits the return of TIGTA and other Treasury agents. TIGTA's participation in this effort concluded on April 1, 2002, and allowed the special agents who assisted in the Air Marshal Program to return to their posts of duty to resume their investigative responsibilities.

Detailing a TIGTA Computer Investigative Support Special Agent

A Computer Investigative Support special agent was detailed to the National Infrastructure Protection Center (NIPC) to assist in analyzing digital evidence developed during the national investigation. The TIGTA agent participated by using specialized forensic software to examine over 168 hard drives and 30 additional pieces of evidence to identify graphic image files that would otherwise not be detected. Leads from the examination were forwarded to a separate NIPC unit for further analysis and investigation.

Investigations

TIGTA, and its predecessor agency, IRS Inspection Service, have a 50-year history of investigating threats to IRS and its employees. Since the terrorist attacks of September 11th, TIGTA has investigated more than 40 incidents involving a suspicious biological or chemical material either mailed to or identified at an IRS lockbox or IRS facility, including anthrax hoax mailings and bomb threats.

Examples of these investigations follow.

Domestic Terrorism Disrupted IRS Service Center Operations

In an October 2001 incident that cost IRS almost \$16,000 in lost labor, an individual was arrested and indicted for mailing threatening communications to an IRS service center. The letter contained a newspaper article related to anthrax, a handwritten statement that read, "Call the FBI," and a diagram of a human body with marks where surgical incisions would be made. Inside the package was a brown paper bag folded several times. Due to the contents of the letter, a hazardous materials response team was notified, as well as state, local and

federal law enforcement agencies. That day approximately 50 employees were evacuated from the service center. Two employees underwent a thorough decontamination process. While the letter later tested negative for anthrax, criminal proceedings are pending against the individual who allegedly mailed the letter.

Bomb Threat Resulted In Arrest

In October 2001, TIGTA special agents arrested an individual who threatened to blow up IRS buildings during telephone contact with agency officials. When interviewed by TIGTA, the individual made reference to the "World Trade Center bombing." In November 2001, a federal grand jury returned an indictment charging this person with *18 U.S.C. § 844(e), Threat of Explosive*. Additionally, a charge of *18 U.S.C. § 111, Assaulting, Resisting, or Impeding Federal Officers* is pending since the individual assaulted TIGTA special agents at the time of arrest.

Taxpayer Perpetrated Anthrax Hoax

An envelope containing a white powdery substance was discovered at an IRS lockbox facility in December 2001. The envelope also contained a note that said, "This is anthrax." A female's name was listed as the sender of the envelope. Although the return address on the envelope was fictitious, TIGTA special agents identified the actual address and interviewed an individual who was subsequently cleared of involvement. A former suitor, however, confessed to sending the letter in an attempt to implicate his girlfriend. Although the powder in the envelope tested negative for anthrax, in January 2002 a federal grand jury indicted the individual on one count of violating *18 U.S.C. § 876* and one count of violating *26 U.S.C. § 7212, Attempting to Interfere with the Administration of Internal Revenue Laws*.

IRS Employee Pled Guilty to Anti-Muslim Hate Crime

In September 2001, subsequent to the terrorist acts at the World Trade Center and Pentagon, the FBI reported to TIGTA that an IRS employee was a suspect in a federal civil rights investigation concerning an anti-Muslim hate crime. It was alleged that the IRS employee vandalized an automobile. The FBI and a local police department substantiated the initial allegation, as well as additional violations of law. In November 2001, the IRS employee was charged with two counts of racial and religious harassment, one count of malicious destruction of property, one count of theft and one count of breaking and entering. In January 2002, the IRS employee pled guilty to one count of malicious destruction of property.

Other TIGTA Activities

Initiatives

Virtual Resource Solution (VRS)

TIGTA has fully embraced the concept of moving workers out of the traditional office environment and into a Telework environment. As a first step in this evolutionary process, eligible TIGTA employees have the flexibility to work remotely while still meeting the business needs of the organization. TIGTA believes this initiative will maximize its use of technology to improve productivity while still providing a safe, secure and family-friendly work environment for its employees. VRS is an integral part of TIGTA's *Engines of Change* (see below), which are designed to restructure and realign the organization to meet the challenges of the future workplace.

Engines of Change

The organization is currently undertaking four major management initiatives. The four initiatives are: Alignment, Leveraging Technology, Human Capital and Performance Driven Organization. These initiatives are designed to restructure and realign the organization to meet the challenges confronting it both today and in the future. By strategically addressing these initiatives, TIGTA plans to transform its work environment.

Inspector General (IG) Community Support

Dual IG Function

TIGTA's Inspector General, David C. Williams, served as the acting Inspector General for the Department of Housing and Urban Development (HUD) from July 2001 through March 2002. This dual responsibility was a temporary assignment until the permanent HUD Inspector General was confirmed on March 22, 2002.

President's Council on Integrity and Efficiency (PCIE)

TIGTA's IG serves as the editor-in-chief of *The Journal of Public Inquiry*, the twice yearly publication of the PCIE. *Journal* articles are written by members of the IG community, scholars, and professionals outside the federal government on topics important to the PCIE and the Executive Council on Integrity and Efficiency (ECIE). The Fall/Winter 2001 edition focused on the IG community's "War on Corruption." The edition was dedicated to the memory of those who died as a result of the September 11, 2001 terrorist attacks.

2002 Winter Olympics

TIGTA supported the security efforts at the 2002 Winter Olympics in Salt Lake City, Utah. For three weeks in February 2002, special agents were assigned at both the Coordination Center and the Soldier Hollow venue at the Olympics. The Soldier Hollow venue was the location of several Alpine competition events, including biathlon and cross-country skiing, while the coordination center served as the command post for federal agencies involved in the security efforts. Due largely to the overall preparation and implementation of a sound security plan, the 2002 Winter Olympic Games concluded without the occurrence of any significant security incidents.

Employee Recognition

Employees are TIGTA's most important assets. It is through their hard work and dedication that TIGTA is able to successfully accomplish its mission. While the organization is proud of all its employees, TIGTA would like to give special recognition to those individuals who have been honored by individuals and organizations outside of TIGTA.

IRS Commissioner Recognizes TIGTA Employees

On November 5, 2001, IRS Commissioner Charles O. Rossotti, presented the *Commissioner's Award* to the TIGTA employees in the New York Field Division. Special Agent-in-Charge Michael Delgado accepted the award on behalf of the New York Field Division. Commissioner Rossotti commended the New York Field Division for the manner in which they responded to the events of September 11, 2001, and their participation in the government business resumption effort. Additionally, Commissioner Rossotti praised the Division special agents for their significant contribution toward the

terrorism investigation. Specifically, Commissioner Rossotti acknowledged the New York Field Division efforts to assist the FBI's JTTF and the TIGTA presence at the multi-agency Leads Desk and the Command Center. Commissioner Rossotti also acknowledged TIGTA's Technical Services, TIGTA's Office of Audit, Office of Information Technology, Office of Management Services and the Management Assistants in the New York Field Division for their efforts in our nation's resumption efforts and our fight against terrorism.

Deputy Inspector General for Audit Awarded Presidential Rank Award

Each year the President recognizes a small percentage of the Senior Executive Service for their ability to lead a Government that delivers great service, achieves results and continually pushes to get the job done more effectively and efficiently. This year, TIGTA's Deputy Inspector General for Audit, Pamela J. Gardiner, was awarded the *Presidential Rank Award for Meritorious Service* for her achievements within the Audit community.

Special Agent Recognized by U.S. Attorney's Office

On December 7, 2001, the United States Attorney of Los Angeles, California, recognized TIGTA Special Agent William Schafer for his "distinguished service" and leadership in an identity theft investigation conducted by the U.S. Attorney's Organized Crime Strike Force. The task force was composed of members from various federal and local law enforcement agencies. Special Agent Schafer was the lead agent on the investigation that led to the successful prosecution of 18 individuals and court-ordered restitution and fines in excess of \$12 million dollars.

Performance and Results Information System (PARIS) Team Receives PCIE's Special Act Award

The PCIE recognized the tremendous effort put forth by the PARIS team in developing a new management information system for TIGTA's Office of Investigations. The PARIS system has quickly drawn the interest of other agencies in the Inspector General community. Those TIGTA employees recognized for this award included: Cammie Weaver, Steven McConville, Laura West, J. Robert Donnan, Christine Orcutt, Thomas Salter, Sunghee Heil, Jan Flowers, Samuel Wilcox, Lois Gray, Candace Farr, Wilma Figueroa, and Kathleen Johnson.

Joint PCIE-ECIE Award for Excellence

Several TIGTA employees detailed to the Inspector General Criminal Investigator Academy were among those recently recognized by the PCIE and the ECIE.

The TIGTA employees recognized included: Terry Freedy, Kay Arthur, Emily Ball, Rick Barrett, Ron Hudson, Suzanne Smith Courtney, and Sue Wainwright.

Special Agent Receives Accolades from United States Attorney

On December 20, 2001, the United States Attorney and Assistant United States Attorney of Grand Rapids, Michigan recognized TIGTA Special Agent Jon Street for his performance during an investigation and subsequent trial. Special Agent Street's recollection of the specific events throughout the enormous investigation was described by the United States Attorney as "fantastic," and ultimately led to the conviction by a unanimous jury on all 67 counts.

Agency Accountability: A Key Watchword of the Administration

The *President's 2001 Management Agenda* calls for performance and budget integration - the underlying information essential to government - and for an agency's thinking to shift from asking "how much money" it needs to an explanation of "how well" it is doing. This focus allows taxpayers to more easily assess the relative effectiveness of any program for which their money is spent.

Each agency's budget submission is now being scrutinized for such a link. As the Office of Management and Budget's Comptroller of Federal Financial Management points out, "... (we are) asking agencies and advocates to supply evidence of program effectiveness instead of assuming effectiveness in the absence of evidence to the contrary."³

To embrace this new direction, for this six-month reporting period, TIGTA highlights the results of its work related to its strategic goals.⁴ These are:

- Improving the economy, efficiency, and effectiveness of tax administration.

TIGTA's audit work supporting this goal revolves around information security; business systems modernization; returns processing; compliance; earned income credit; Government Performance and Results Act; and, the Federal Financial Management Improvement Act.

- Detecting and deterring fraud, waste, abuse or misconduct by employees, as well as persons outside the IRS.

Investigative and audit work supporting this area revolves around internal and external fraud.

³ Testimony of the Honorable Mark W. Everson, Comptroller of Federal Financial Management, Office of Management and Budget, before the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations, February 15, 2002.

⁴ TIGTA's *Strategic Plan for Fiscal Years 2000-2005*.

TIGTA Strategic Goal: Improving the Efficiency and Effectiveness of Tax Administration

During this reporting period, TIGTA's audit work supported its strategic goal to improve efficiency and effectiveness of tax administration. By conducting comprehensive, independent performance and financial audits of IRS programs and operations, TIGTA promoted the sound administration of the nation's tax laws through timely reports on program and operational deficiencies. TIGTA audits made recommendations to improve tax administration services and to strengthen controls over IRS programs and operations.

Information Systems Security

The networking of computers and increased use of the Internet, combined with the growing number of destructive computer viruses, has made the IRS more vulnerable to the risk of data loss or theft.

During this reporting period, OA conducted six reviews related to information systems security.

The following summarizes the results of those reviews.

OA continues to identify significant security weaknesses in IRS' computer systems and networks. Recent audits indicate that IRS remains vulnerable to attacks by outside hackers, and to internal abuses by unethical or disgruntled employees.

For example, the agency's Internet gateways are vulnerable. Audits have shown that Internet gateway firewalls and routers were not patched when new security weaknesses were identified and their configurations were weak. Activity logs were not generated and reviewed.

Sufficient and capable staffing was not assigned to administer firewalls. In addition, many Internet gateways still did not have intrusion detection installed.

Internal networks were also vulnerable. Audits have shown that IRS cannot detect many unauthorized accesses because it still does not routinely review audit trails for its sensitive systems except for one major system and possibly a small number of others. This weakness has persisted over several years and sufficient actions have not been taken to address these issues. IRS has cited a lack of computer capacity, a lack of tools and guidelines, and insufficient staffing as contributing to these problems.

OA attributes many of these conditions to:

- A reluctance by program managers to take responsibility for the security of the systems they operate. The Chief Information Officer's Office of Security has primary accountability, contrary to Office of Management and Budget (OMB) policy, which states that program managers are responsible for the systems they own.
- Many IRS employees with key security responsibilities do not have the requisite knowledge and skills.
- IRS employees are not sufficiently aware of security risks and their own responsibilities. During a recent test of security awareness, 71 of 100 employees agreed to change their password to one requested by a TIGTA contractor posing as a "help desk" employee. The extremely high percentage of employees willing to compromise their passwords indicates that the IRS has not done enough to

train employees on their security obligations. Even the best security procedures and controls can easily be circumvented if employees are not aware of their responsibilities.

OA made recommendations to correct the weaknesses identified and, generally, IRS has taken or planned appropriate corrective actions. *A list of information systems security related reports issued during this period are included in Appendix V on page 71.*

Business Systems Modernization (BSM)

During this reporting period, BSM's program success is considered at significant risk due to several factors including: the cost of implementation; IRS' continued struggle to accomplish modernization efforts; and because IRS reforms, such as improved debt collection, are dependent on modernized systems.

OA conducted three reviews in this area during this reporting period. Findings show that the IRS has made progress in modernizing its information technology systems, but the overall pace of the modernization has been considerably slower than expected.

Examples of the progress made since October 1, 2001 include the recent deployment of an improved Computer User Helpdesk that will eventually consolidate 19 separate help desks, and an Asset Inventory System that should help address a chronic problem of tracking the IRS' computers and other technology assets. The IRS has also developed and updated an Integrated Master Schedule to help sequence new projects and identify dependencies among the various projects. IRS is working on several key projects that are scheduled for release later in 2002. The IRS has made incremental

improvements in some management capabilities, such as configuration and change management, and has also stabilized its funding process so it has funds available for the projects scheduled for 2002.

However, IRS continues to struggle with developing and integrating the discipline and repeatable processes needed to effectively and efficiently modernize its technology. OA continues to monitor and report on the areas that, at this stage, pose potential barriers to the success of BSM (*see page 10*).

OA recommended corrective actions to strengthen the controls over the conditions identified. For those reports where a response has been received, IRS management agreed with most of the recommendations and has taken or planned corrective actions to implement the recommendations.

All Information Systems and Business Systems reviews are considered statutory based on *RRA 98*. *A listing of all statutory reports, including the reports summarized above, are listed in Appendix V, page 68.*



Business Modernization Issues

To date, virtually all BSM projects controlled by the PRIME contractor have been delayed and have incurred cost increases. As of September 30, 2001, IRS had spent or obligated over \$575 million in modernization funds, and it plans to spend or obligate \$390 million in 2002. The IRS intends to deliver several projects with direct taxpayer benefits in 2002; however, some of these projects will be deployed later than planned, and others have been scaled back in order to meet delivery dates. The IRS and the PRIME contractor continue to be unreasonably optimistic about their timetable for delivering modernized systems given the immaturity of their management processes.

Performance-based contracting processes have not been fully implemented. Although quality review processes had been established to monitor contractor deliverables, most of the task orders OA evaluated did not contain incentives or disincentives to encourage contractor timeliness and quality. While IRS can withhold payment to the contractor until quality products are delivered, this option does not provide any compensation for delays in delivering promised improvements to taxpayers. Additionally, when quality problems were identified, IRS did not always require that the contractor stop and address the problems before progressing to the next project phase.

Project monitoring processes have not adequately captured project cost information. Currently, actual costs are measured against estimated costs for the current phase (milestone) of the project rather than the project's full budget. In addition, accurate measurements of internal IRS costs are not included in project monitoring data, and the measurement system has not been validated. Without an accurate accounting of all project costs, it is difficult for IRS and Congress to determine if a project is worth the investment.

The IRS and the PRIME contractor have not implemented adequate application testing processes. Neither IRS nor the PRIME contractor could provide evidence that all critical capabilities of the project intended to increase taxpayer telephone and communication service levels to those similar to the private sector were sufficiently tested to ensure they were working as intended. Further, there was a lack of documentation to show how problems or defects identified during these tests were resolved. Without this documentation, the IRS had no evidence to support how or if detected problems or defects were corrected.

Project teams have experienced problems in implementing key systems development processes. Project teams are having problems implementing and following key processes, such as requirements gathering, risk management, and investment decision management.

OA found similar problems on non-BSM projects. For example, the IRS' project to consolidate its many mid-range systems was not following any structured systems life cycle methodologies, nor has IRS implemented a process to properly fund or monitor the project. These contributed to significant consolidation risks, including inadequate staffing at the project office and computing centers, insufficient training for systems and database administrators, and a delay in implementing an automated disaster recovery process. Lastly, the consolidation of mid-range systems has already encountered significant delays in consolidating applications which, when combined with the unresolved risks and project management issues, increase the likelihood of cost overruns and possible failure of the project to achieve intended goals.

Returns Processing

Tax law complexity is the highest-ranking IRS problem area faced by individual and business taxpayers. It is further compounded as IRS proceeds with its multi-year computer modernization effort. Some affected areas include IRS' internal processing procedures and IRS' communication of tax law changes to taxpayers through publications and notices.

Audit highlights in these areas follow.

The Internal Revenue Service Has Made Some Progress, But Significant Improvements Are Still Needed to Reduce Errors in Manual Interest Calculations (Reference No. 2002-30-042)

IRS employees must manually calculate interest on some accounts because the computer system is not programmed to apply numerous changes in laws, regulations and policies. This is referred to as "restricted interest" because the computer system is "restricted" from making the interest computations. Over the years these changes, as well as the complexity of the calculations and supporting analyses, have increased the number of accounts requiring restricted interest calculations. Between Calendar Years (CY) 1995 and 1999, over 198,000 business tax accounts became restricted, totaling over \$7 billion in restricted interest assessments or abatements.

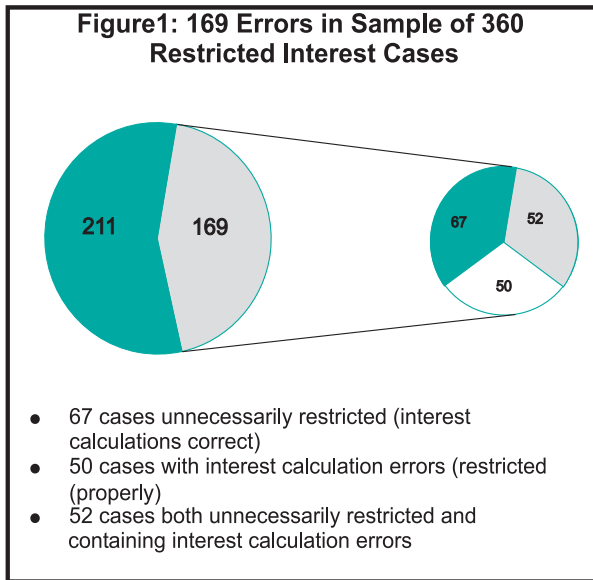
Restricted interest calculations are very complex, time-consuming, and highly subject to human error. Because it is well known that the IRS makes a significant number of errors in these calculations, accounting firms, law firms and others have actively marketed consulting services to assist taxpayers in recalculating interest and filing claims for refunds of amounts incorrectly assessed. In

1994, in accordance with the *Federal Managers' Financial Integrity Act*,⁵ the IRS reported this issue as a material weakness in its internal control system. As a result, the IRS established a goal to reduce its high number of erroneous restricted interest assessments.

While IRS has achieved some success in increasing the automation of interest calculations overall, IRS' actions taken to address the material weakness have not been effective. From CYs 1995 to 1999, the number of business accounts for which interest calculations were restricted increased by more than 4,500. OA identified 35,580 business accounts that became restricted in 1999 (12,792 with restricted interest transactions for zero dollars and 22,788 with restricted interest transactions containing dollar amounts). From a statistical sample of 380 accounts, 44 percent (169 accounts) contained errors in interest amounts computed by IRS employees. These accounts were unnecessarily restricted or contained errors in interest amounts computed by IRS employees, or both (see *Figure 1* on page 12). Based on the results of this sample, OA estimated that, over a five-year period, the IRS could overcharge some taxpayers over \$247 million in interest, and undercharge other taxpayers more than \$145 million.

OA recommended that IRS management limit the calculation of restricted interest to centralized staffs within IRS functions and locations of IRS; establish a national quality review process that includes all restricted interest cases; ensure employees receive appropriate training before working on restricted interest cases; authorize a standard interest computation tool; and explore all available options to provide the technology and programming necessary to allow more computerized interest calculations to be performed by computer.

⁵ 31 U.S.C. §§ 1105, 1113, and 3512 (1994 & Supp. IV 1998).



IRS management agreed with the report findings and proposed a number of creative actions to address the problems identified in the report.

The Internal Revenue Service Continues to Owe Millions of Dollars in Interest to Taxpayers with Frozen Refunds (Reference No. 2002-30-062)

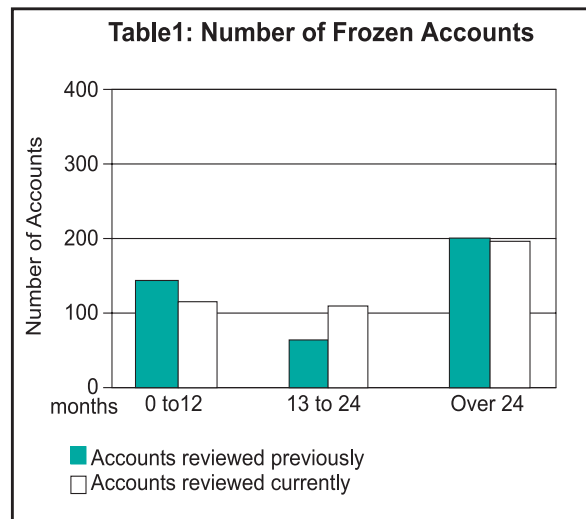
OA first reported in September 1999⁶ that IRS was experiencing problems in releasing large dollar refunds because of the automatic freeze placed on accounts containing a credit balance of \$1 million or more. Findings included: (1) controls did not ensure that frozen refunds were timely released, and (2) additional interest of approximately \$17.5 million was paid to taxpayers with frozen accounts.

OA recommended that IRS change its computer system to systemically release refunds that fall below the *Million Dollar Freeze* threshold and establish alerts for employees to take appropriate resolution

⁶ *Controls Should Be Strengthened Over Business Taxpayer Accounts with Frozen Million Dollar Refunds* (Reference No. 199940057).

actions on frozen accounts. Instead of implementing the recommendations as agreed, IRS increased the threshold for automatically freezing refunds from \$1 million to \$10 million. However, increasing the threshold did not correct the problem, and IRS continues to pay millions of dollars in additional interest to taxpayers with frozen accounts.

This follow-up review of 412 frozen accounts identified 209 (51 percent) improperly frozen accounts that resulted in IRS eventually issuing approximately \$185.8 million in refunds and paying taxpayers an additional \$15.4 million in interest. *Table 1* shows a comparison between the accounts identified as frozen in the previous review and the frozen accounts identified in this review.



Source: Extracts from IRS' Masterfile on April 4, 1998 and March 31, 2001

Two reasons why IRS' corrective actions were not effective were:

- Refunds can drop below the *Million Dollar Freeze* threshold, which is now set at \$10 million.
- IRS employees are not always aware of the need to take appropriate resolution actions on accounts frozen for extended periods.

As reported in 1999, the *Million Dollar Freeze* indicator was not displayed on key computer screens used by employees to resolve problem accounts. In addition, the system did not generate periodic alert notices to employees on frozen accounts.

OA recommended that IRS management should initiate action to modify IRS' computer system to systemically release refunds that fall below the *Million Dollar Freeze* threshold and establish alert mechanisms for employees to take appropriate resolution actions to correct the problem with frozen refunds. Taking these actions will provide the government an opportunity over a five-year period to put an estimated \$12.9 million (an average of \$2.5 million a year) that it paid in interest to better use.

IRS management agreed with the findings in the report and proposed a number of actions to correct the problems identified.

While Most Taxpayers Received Accurate and Timely Notification of Their Advance Refunds, Millions Did Not (Reference No. 2002-40-016)

This report presents the results of the initial phase of OA's reviews of the advance refund provisions of *H.R. 1836*, also known as the *Economic Growth and Tax Relief Reconciliation Act of 2001*.⁷ This initial phase was to determine whether IRS would timely and accurately notify taxpayers about their advance refunds. The IRS developed an extensive plan, implemented new computer programming, and hired a private vendor to print and mail more than 120 million advance refund notices. While this significant accomplishment was performed in a very limited amount of time, OA identified two problems that affected the calculation of the advance refunds and the timely issuance of the advance refund notices.

⁷ *Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, 115 Stat. 38.*

First, IRS did not accurately calculate the advance refund amount for some taxpayers. OA alerted IRS to this condition on July 3, 2001. The IRS timely addressed this problem, which included changing computer programming. For all returns processed as of July 5, the change prevented 535,000 taxpayers from receiving advance refunds totaling at least \$117.6 million more than the amount allowed by law. However, IRS' initial mail-out included advance refund notices that reflected amounts greater than the taxpayers would receive.

Second, 5.3 million taxpayers who timely filed their tax returns would have delays from one to nine weeks in receiving their advance refund notices. These delays were due to the way IRS processed timely filed returns received with payments that fully paid the amount owed and the way programming was developed to generate advance refund notices.

To address IRS' problem in calculating the advance refund, OA recommended that IRS management correct the computer programming problem, issue corrected advance refund notices to affected taxpayers, issue a press release informing the public that advance refund notices with incorrect amounts were sent out, and update its *Customer Service* procedures. To address the 5.3 million delayed advance refund notices, OA recommended that IRS management inform its employees and issue a press release to advise taxpayers about the advance refund notice delays. OA also recommended that IRS management change the programming used to generate the advance refund notices to prevent additional delays.

IRS management agreed and took immediate corrective action on all the recommendations, except to change the programming used to generate the advance refund notices. IRS management stated that to help minimize the risk of any errors occurring, the programming would not be changed. OA understood the

potential for error and accepted IRS' reasons for not changing the programming.

Improvements Need to Be Made to Publications and Instructions to Assist Taxpayers in Successfully Signing Their Tax Returns Electronically (Reference No. 2002-40-046)

In an effort to move towards paperless tax return filing, IRS successfully implemented the *Self-Select Personal Identification Number (PIN) Program* in Filing Season 2001. This program enabled nine million of the 35 million taxpayers who filed an electronic tax return to sign their tax returns electronically. However, for Filing Season 2001, one-quarter of the tax returns submitted with electronic signatures were rejected because the authentication information the IRS required taxpayers to provide (e.g., name and date of birth) did not match IRS' records for the taxpayer. The publications and instructions for taxpayers' to use when signing tax returns electronically contained inaccurate, inconsistent and unclear information.

OA recommended that IRS management: (1) create a quality review process for the *Self-Select PIN Program* to ensure guidance is appropriate to enable electronic signatures, (2) develop procedures to ensure tax guidance in electronic tax return preparation software packages is accurate and clear, and (3) follow the oversight review and approval process for preparing and revising electronic filing guidance.

IRS management agreed with the first and third recommendations and has already implemented corrective actions. A process for the development and approval of public information already existed, but was not previously published as an employee guide. The IRS will follow this established process in the future. While IRS management did not

specifically disagree with the second recommendation, it indicated that the development of software packages is not within the purview of the IRS. However, IRS management stated that they would work closely with the private sector as they develop tax preparation software by providing current and accurate information.

Compliance

The IRS' goal of providing world-class service to taxpayers hinges on the theory that, if the IRS provides taxpayers with the right mix of education, support, up-front problem solving, and targeted enforcement, the overall rate of voluntary taxpayer compliance with the tax laws will increase. The challenge to IRS management is to establish a tax compliance program that identifies those citizens who do not meet their tax obligations, either by not paying the correct amount of tax or by not filing proper tax returns.

Audit highlights in this area follow.

Interim Actions Can Be Taken to Determine Partnerships' Compliance in Withholding Taxes on Foreign Partners (Reference No. 2002-30-076)

I.R.C. § 1446 requires partnerships to withhold taxes on effectively connected income allocable⁸ to foreign partners. "Effectively connected income" is taxable income connected with the conduct of a trade or business in the U.S. The number of U.S. partnerships with foreign partners increased from about 22,000 in 1995 to over 30,000 in 1999, an increase of more than 36 percent.

⁸ The provision applies to allocable income, regardless of whether distributions were made during the partnership's tax year.

In FY 2001, OA issued a report that discussed the increasing population of partnerships with foreign partners and concluded that IRS should enhance programs to ensure partnerships' compliance with the withholding provisions.⁹ The report recommended taking interim measures to identify potentially non-compliant partnerships until permanent programming changes could automate the process.

In this follow-up report, OA determined that sufficient information existed in the IRS' computer systems to take interim action and begin a process to determine partnerships' compliance with withholding requirements. Also, IRS could better use information on income and foreign partners from partnerships' tax returns and the withholding information documents that partnerships separately file to more effectively identify potential non-compliance.

OA recommended that IRS contact a sample of taxpayers to determine whether there are compliance issues with the withholding provisions, and use our methodology as an interim measure until an automated identification process is developed.

IRS management's response was not received prior to the issuance of the audit report.

The Internal Revenue Service's Levy Process Can Be Improved to Ensure Compliance With the Internal Revenue Code (Reference No. 2002-10-078)

Congress believed that taxpayers should not have collection activity taken against them once the IRS has determined that any tax owed is uncollectible because a taxpayer is

⁹ *Stronger Actions Are Needed to Ensure Partnerships Withhold and Pay Millions of Dollars in Taxes on Certain Income of Foreign Partners* (Reference No. 2001-30-084, dated June 2001).

facing an economic hardship situation. As a result, Congress included a provision in *RRA 98* that added *I.R.C. § 6343(e) (1999)* requiring the IRS to release a wage levy as soon as practicable upon agreement with the taxpayer that the tax is not collectible. In addition, *I.R.C. § 6343(a)* requires IRS to release all levies when it determines that the levy is creating an economic hardship due to the financial condition of the taxpayer.

OA determined that IRS is not always releasing levies as required. OA identified cases in which IRS received levy payments after the case was closed as a Currently Not Collectible (CNC) (hardship) case. In addition, OA identified cases that should not have been a closed CNC (hardship) because IRS either did not determine that an economic hardship existed or appeared to disregard the taxpayer's ability to make payments. Finally, OA identified numerous cases that had non-levy payments erroneously recorded as levy payments on IRS' management information system.

OA recommended that the IRS improve controls to ensure IRS personnel recognize levies at the time a case is closed CNC (hardship) and release levies as required. IRS should strengthen procedures to ensure cases are closed as CNC (hardship) only when appropriate. Also, the IRS should clarify guidelines to ensure payments received by IRS personnel are accurately recorded on IRS' computer system.

IRS management agreed with the recommendations and is taking corrective actions.

Earned Income Credit

Both the President and Congress have expressed concern with the large number of erroneous payments made annually by federal agencies. Although many IRS programs are susceptible to erroneous

payments and potential fraud, particularly vulnerable is the IRS' administration of the Earned Income Credit (EIC) Program.

Audit highlights in this area follow.

Earned Income Credit Was Paid to Taxpayers Who Did Not Provide Required Documentation During Audits (Reference No. 2002-40-004)

EIC is a refundable tax credit created in 1975 to offset the impact of Social Security taxes on low-income families and encourage them to seek employment rather than welfare. In CY 2000, a total of 19,226,015 taxpayers received the EIC. While the IRS does not question most EIC claims, in FY 2000 it completed 325,654 audits and recommended over \$411 million in additional taxes where EIC claims were in question. Audits of EIC claims represented 74 percent of the total audits completed by IRS' Remote Examination function during the fiscal year.

OA identified that taxpayers did not receive consistent treatment when IRS audited their EIC claims. Specifically, some taxpayers were allowed the EIC without having to provide required documentation during the audit to justify their EIC claim. This occurrence was the result of inadequate managerial case reviews designed to ensure consistency and accuracy of audits.

OA recommended that IRS management should develop expectations that case reviews will be completed and establish a process to ensure these reviews are done timely. IRS management agreed with the recommendation and took appropriate corrective action.

Better Controls Are Needed to Ensure Appropriated Funds Are Used to Improve the Application of the Earned Income Credit (Reference No. 2002-40-020)

Congress has been concerned with IRS' ability to administer the EIC. In 1997, Congress enacted legislation¹⁰ that authorized the IRS to spend \$716 million over a five-year period for the improved application of the EIC. The five-year period began in FY 1998. Each year, IRS spends over \$100 million appropriated by Congress. The IRS established the EIC Program Office to administer the EIC appropriation and oversee the EIC-related activities of IRS functions involved in efforts to ensure the efficient application of the law; to increase participation of eligible taxpayers; and to reduce fraud, waste, and abuse.

Each year, the Program Office develops a plan that outlines how the EIC funds will be used. However, IRS did not have an effective process in place to ensure that the expenditure of the EIC appropriation was used only for EIC issues, programs, and projects. OA's analysis of the total labor expenses for two IRS functions and a judgmental sample of the IRS' equipment purchases for FY 2000 and the first quarter of FY 2001 identified approximately \$28 million in questionable expenses.

The IRS is scheduled to receive \$146 million in EIC funds in FY 2002, the last year of the current five-year appropriation. Without effective controls in place to assure Congress that the funds are being spent appropriately, IRS is at risk that future appropriation funding beyond FY 2002 could be in jeopardy. OA recommended that IRS management establish procedures to ensure that funds appropriated by Congress for the improved application of the EIC are used for that purpose.

¹⁰ The *Balanced Budget Act of 1997*, Pub. L. No. 105-33, 111 Stat. 251.

While IRS management took some corrective action, OA believes the corrective action only strengthened controls for the functions' requests and authorizations to expend EIC appropriation funds. The corrective action does not include provisions for conducting periodic reviews of actual functional EIC expenditures to ensure they are EIC related and, therefore, should be paid from EIC appropriation funds. OA believes these reviews are critical to ensuring EIC funds are used for EIC purposes.

IRS management disagreed with OA's reported outcome that \$28 million of EIC appropriation funds were used for questionable labor and equipment purchases. However, they did agree with OA's statements that not all the expenses OA reviewed were directly related to the EIC. Therefore, until IRS has sufficient information to determine how much of these items are directly related to EIC, OA believes its outcome measure is still valid.

There Are Significant Weaknesses in the Internal Revenue Service's Efforts to Measure Earned Income Credit Compliance (Reference No. 2002-40-021)

IRS originally planned to measure EIC compliance levels annually. The audit results were to provide a baseline for comparing measurements from subsequent years. The basis for the compliance levels would come from annual audits of tax returns claiming the EIC.

While IRS made some improvements in its methodology to measure EIC compliance from Tax Year (TY) 1997 to TY 1999, significant weaknesses still exist. Specifically:

- Some audits in the TYs 1997 and 1999 EIC compliance studies lacked the necessary information to support the IRS' results.

- There was inconsistency in the IRS' methodology applications between studies.
- Emphasis on EIC taxpayers with business income during the TY 1999 EIC compliance study increased the time spent on the audits, but did not produce any apparent benefits.
- Poor planning caused taxpayers to be needlessly audited as part of the TY 1998 EIC compliance study.

IRS management disagreed with OA's recommendations that there were significant weaknesses in its methodology for measuring EIC compliance and questioned the relevance of the audit recommendations. IRS management stated that improvements have been made to the EIC program due to the results of its current measurement methodology and compliance efforts.

In OA's opinion, IRS' response did not adequately support the disagreement with OA's assessment of the EIC compliance measurement methodology. OA recognizes that several initiatives have been made over the past few years to improve the administration of the EIC program. However, the majority of the improvements listed in the IRS response were not the result of its current efforts at measuring EIC compliance.

At the time of OA's review, IRS had issued only one report as a result of its last three EIC compliance studies. That report, *Compliance Estimates for Earned Income Tax Credit Claimed on 1997 Returns*, was issued more than two years after most of the audits in the study were completed. Since OA's review was completed, a second report, *Compliance Estimates for Earned Income Tax Credit Claimed on 1999 Rates*, was issued in February 2002.

Government Performance and Results Act

Congress passed the Government Performance and Results Act of 1993 (GPRA)¹¹ to increase agency accountability and improve the quality and delivery of government services. GPRA holds federal agencies accountable for program results by emphasizing goal setting, customer satisfaction, and results measurement.

TIGTA performed the following reviews as part of its strategy to assess IRS' compliance with GPRA.

GPRA: Criminal Investigation Can Improve Its Performance Measures to Better Account for Its Results (Reference No: 2002-10-009)

The IRS' Criminal Investigation (CI) has a budget of \$395 million and a staff of approximately 3,700 special agents and support personnel. CI's mission is to serve the American public by investigating potential criminal violations of the *Internal Revenue Code* and related financial crimes in a manner intended to foster confidence in the tax system and compliance with the tax law. OA identified that CI's performance measures do not address its mission and that only the number of cases initiated was included in IRS' GPRA measures.

CI developed outcome-neutral measures¹² to report as its business results because of its concern about *26 CFR Part 801*. This regulation prohibits using quantity measures to impose or suggest production goals for any organizational unit whose employees exercise

¹¹ *Government Performance and Results Act of 1993 (GPRA)*, Pub. L. No. 103-62, 107 Stat. 285 (codified, as amended in scattered sections of 5 U.S.C., 31 U.S.C., and 39 U.S.C.)

¹² Measures that do not contain information regarding tax enforcement results.

judgment with respect to tax enforcement results. It also forbids establishing goals for individual employees based on records of tax enforcement results. As such, CI's business results measures are not outcome oriented and do not accurately show the results of CI's activities.

CI also did not have a measure for its refund fraud program, a major management challenge for IRS. CI measured its outreach efforts (activities to educate the public about CI and the consequences of violating the tax laws) by the staff years spent on those efforts. Its case quality review measure includes only discontinued and non-prosecution cases with no grand jury involvement (about 27 percent of the total CI workload), and excludes the cases with the most impact on taxpayers. The CI customer satisfaction survey was sent only to U.S. Attorneys and did not include the Department of Justice Tax Division Attorneys.

OA was not allowed access to the Criminal Investigation Management Information System (CIMIS),¹³ the source of most of CI's performance measures. While not able to validate the CIMIS data, OA determined that system audit trails were not complete and were not effectively used, creating a potential security risk.

OA recommended that measures be developed, such as the number of individuals indicted, convicted, and sentenced; CI's effect on voluntary compliance and the tax gap; the results of major programs like refund fraud; and the results of a quality review process that includes all cases. Also, CI should consider a survey to assess CI's outreach efforts; ensure that audit trail requirements are met and documented; and fully disclose CIMIS data limitations.

IRS management disagreed with five of the nine recommendations in the report. IRS

¹³ CIMIS is a computer database used to inventory, control, and track the progress of CI investigations.

management did not agree to expand CI business results measures; establish measures to assess CI's impact on non-compliance and the tax gap; better measure the effectiveness of CI's outreach efforts; and, disclose the limitations affecting the accuracy of CIMIS data or to expand the quality review process.

The Internal Revenue Service Could Improve Its Process to More Reliably Measure the Accuracy of Its Toll-Free Tax Law Assistance (Reference No. 2002-40-051)

Design and implementation weaknesses in the current sampling strategy used to measure the accuracy of IRS toll-free tax law assistance had the potential to bias the accuracy of the results. The 73.78 percent accuracy rate that IRS reported for the 2001 Filing Season may not be accurate. A different rate may influence management decisions concerning assignment and training of customer service personnel, which could affect IRS budget decisions.

OA noted that managerial reviews were not conducted as required at critical periods during the 2001 Filing Season, and they were not conducted in an independent setting.

OA recommended that IRS management:

- Design the sampling plan to include all tax law calls in the population and randomly select from all hours of all call site operations.
- Ensure the sampling plan is implemented as designed, the latitude of reviewers to select and disconnect calls (in terms of both application and call site) is limited, and the required number of calls is reviewed at critical times during the filing season.

- Conduct the required managerial reviews of the work performed by quality reviewers and perform the on-line, joint-monitoring aspect of these reviews remotely so that it can be done in an independent setting.
- Develop an automated call recording system to measure the accuracy of tax law assistance that ensures that all tax law calls are included in the population, the selection of calls is truly random, and the sampling plan is implemented as designed.

IRS management agreed with the audit recommendations and has initiated corrective actions where possible. IRS management could not develop corrective actions for managerial reviews of quality reviewers due to telephone system limitations. IRS management strengthened controls to ensure that each Centralized Quality Review Site (CQRS) manager meets minimum monitoring standards. In addition, while IRS management agreed that an automated call recording system is the best way to achieve random call selection, they pointed out that the IRS is not technologically able to do so at this time. The IRS is aggressively pursuing automated call recording. Lastly, the telephone equipment used by the CQRS staff cannot track disconnected calls.

Federal Financial Management Improvement Act¹⁴

The *Federal Financial Management Improvement Act of 1996 (FFMIA)* mandates, among other things, that agencies

“...implement and maintain financial management systems that comply substantially with Federal financial management systems requirements,

¹⁴ *Federal Financial Management Improvement Act of 1996, 31 U.S.C. § 3512.*

applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level.”

FFMIA also requires that remediation plans be developed for any entity that is unable to report substantial compliance with these requirements. OA's evaluation of IRS' remediation plans follows.

***Management Advisory Report:
The Internal Revenue
Service's Federal Financial
Management Improvement Act
Remediation Plan Complies With
Reporting Requirements
(Reference No. 2002-10-069)***

OA conducted a review of IRS' *FFMIA* remediation plan to identify any instances and reasons for missed intermediate target dates, and to evaluate whether the IRS is meeting its responsibilities in fulfilling the intent of the *FFMIA*. This review was performed to meet OA's requirement under the *FFMIA* that each IG shall report to Congress instances and reasons when an agency has not met the intermediate target dates established in the remediation plan.

No instances were found where the IRS did not meet established intermediate target dates contained in the remediation plan. OA did identify where intermediate target dates were extended with reasonable explanations. Also, the IRS received required Office of Management and Budget concurrence for remedial actions with intermediate target dates that extend longer than three years; incorporated all GAO financial statement audit recommendations pertinent to the *FFMIA* guidelines into its remediation plan; and, has taken actions to reconcile inconsistencies between GAO and IRS reported status of remedial actions. The IRS has also taken positive steps to implement corrective actions addressing prior OA recommendations.

TIGTA Strategic Goal: Detecting and Deterring Fraud in IRS Programs and Operations

TIGTA is responsible for conducting investigations and audits to help prevent, detect, and deter fraud and abuse in IRS programs and operations. This includes investigating allegations of misconduct by IRS employees; protecting IRS against external attempts to corrupt or threaten its employees; and performing reviews of activities related to fraud, waste, abuse, and mismanagement of IRS and related entities, such as the IRS Oversight Board and IRS Chief Counsel. TIGTA's work serves as a deterrent against those contemplating illegal actions that would undermine the integrity of federal tax administration.

Internal Fraud

OI conducts investigations that protect taxpayers from IRS employees who commit criminal violations and administrative misconduct. These inquiries may involve allegations of unauthorized access to and disclosure of confidential taxpayer information, bribery, financial fraud, false statements and abuse of taxpayer rights.

Investigative highlights in this area follow.

A Twenty-Two Year IRS Veteran Charged with Unauthorized Access (UNAX) to Taxpayer Accounts

As a result of a UNAX violation, an IRS employee pled guilty to one count of computer fraud and was sentenced to two years probation, fined \$5,000 and ordered to perform 100 hours of community service. After the employee's spouse was fired from a private company, it was determined that the employee made numerous accesses to the tax accounts of the spouse's co-workers and executives of the company. These findings, in

conjunction with field interviews, resulted in the indictment of the IRS employee on seven counts of computer fraud and unlawful inspection of tax return information. The employee subsequently resigned from IRS.

Former IRS Employee Indicted for Converting Property

A grand jury indicted a former IRS employee on seven counts of converting taxpayers' property. According to the indictment, the former employee embezzled \$32,583 by electronic transfer of funds from taxpayers' original tax returns to accounts belonging to the employee.

IRS Employee Arrested by TIGTA Special Agents for Solicitation of \$200,000 Bribe

In December 2001, an attorney representing a corporation reported that during a routine IRS examination, an IRS employee solicited a cash bribe of \$200,000 from the company's attorney to reduce the company's tax liability. The attorney subsequently agreed to cooperate with TIGTA in its investigation.

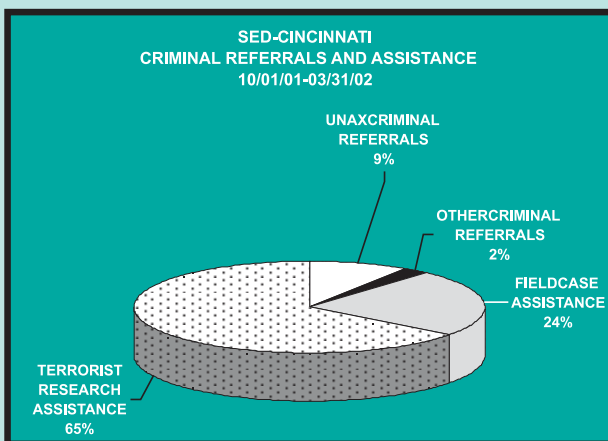
In January 2002, with assistance from TIGTA's TSS, an electronically recorded meeting took place between the attorney and the employee. After receiving the \$200,000 bribe, the IRS employee provided the attorney with a fraudulent Revenue Agent Report. TIGTA special agents arrested the IRS employee before the employee left the meeting.

The Strategic Enforcement Division

Strategic Enforcement Division (SED) is an entire division within TIGTA's OI that is devoted to computer criminology. It is comprised of three components with distinct and complementary missions. A collaborative effort of special agents, forensic data analysts, and computer programmers assigned to SED Cincinnati Operations execute proactive programs to detect internal fraud in IRS operations and unauthorized access to IRS computer systems. Computer matching is used nationwide in proactive initiatives. These initiatives are included in *Computer Matching Act*¹⁶ agreements approved by Treasury's Data Integrity Board and published in the *Federal Register*.

During this period, there were six ongoing initiatives, and 19 criminal referrals to field special agents for further investigation.

Computer Investigative Specialist Program (CIS) is a unit of SED that provides support and advice concerning the search and seizure of computers and computer-related media; the processing of seized electronic evidence; and assistance with Internet-related crimes and investigations. Agents assigned to the *Computer Investigative Support Program* provide forensic processing of seized computers and other electronic media in support of TIGTA investigations.



Since October 2001, CIS special agents have conducted forensic examinations in 56 TIGTA investigations, reviewing 141 devices containing 872 gigabytes of storage space.

System Intrusion Network Response Attack Team (SINART) is another SED unit in which assigned agents and computer programmers investigate attempts to interfere with the security, integrity, and reliability of IRS computers by external sources.

Since October 2001, SINART special agents and computer specialists have conducted nine computer security reviews and 17 criminal investigations. Additionally, SINART special agents and computer specialists have:

- ✓ Participated with the IRS Computer Security Incident Response Team in a penetration test designed to evaluate the security controls in place within the *www.irs.gov* environment. The tests were conducted to ensure the confidentiality, integrity, and availability of data over the networks, and to gauge the new IRS website's ability to withstand Internet-based attacks. The penetration test team used common foot printing and attacks utilized by hackers, including remote procedure calls, telnet, and other exploitations. The penetration test results were reported to the IRS Office of Cyber Security.

- ✓ Established proactive initiatives to evaluate the IRS network for specific vulnerabilities, including an initiative designed to identify unauthorized wireless network access technology on IRS and TIGTA networks. Wireless scans of several IRS facilities have been completed. Another initiative was launched to identify unauthorized connections to IRS computers through unregistered modems. A total of 33 modems were identified. Each modem was investigated to determine the extent of vulnerability. The results of SINART proactive initiatives are provided to the IRS Office of Cyber Security.

¹⁶ Pub. L. No. 101-56, 103 Stat. 149 (1989)

IRS Employee Pled Guilty to Knowingly Possessing Visual Depictions of Minors Engaged in Sexually Explicit Conduct

An IRS internal review identified an employee who accessed sexually explicit websites using government time and equipment. Examination of the employee's computer hard drive revealed 30,664 graphics files. Most of the graphics were pornographic or sexually explicit in nature and numerous images were classified as child pornography. The employee pled guilty to knowingly possessing visual depictions of minors engaged in sexually explicit conduct. In October 2001, the employee signed a pre-trial diversion agreement and prosecution was deferred 18 months.

Former IRS Employee Pled Guilty to Misuse of IRS Computer System and Improper Relationships with Taxpayers

In November 2001, a former IRS revenue officer was charged with allegedly accepting gifts from different taxpayers, including approximately \$1,000 in cash, a television set, free health club privileges, free auto repairs, and free garage door repairs, for a payment plan of taxes and abatement of penalties owed by the taxpayers totalling \$158,741.

The former employee also was charged with allegedly accessing an IRS computer without authorization and thereby obtaining information from the IRS and with allegedly failing to deposit money of the United States under his control. The former IRS employee pled guilty to all three counts and in March 2002, was sentenced to four months imprisonment, supervised release for two years, home detention for 120 days and

participation in a mental health treatment program. The former employee was ordered to pay restitution of \$11,648.

IRS Employee Pled Guilty to Embezzling Tax Payments

In May 2001, an IRS employee was discovered to have received a \$2,800 cash tax payment from a taxpayer and then gambled and lost that money at a local casino. During a subsequent interview by TIGTA special agents, the employee admitted to collecting cash from taxpayers and using the money to gamble. IRS records revealed that during the six-month period prior to the \$2,800 embezzlement, the IRS employee delayed processing an additional \$9,040 in cash payments.

After pleading guilty to one count of embezzlement in January 2002, the employee was sentenced to three years probation, and ordered to pay \$2,800 in restitution to IRS. Administrative action is currently pending.

External Fraud

OI is responsible for protecting against external attempts to corrupt the IRS, its employees, facilities and data systems. OA is responsible for conducting audit and investigative activities designed to prevent, detect and deter external fraud and abuse impacting IRS programs and operations and to recommend remedial actions.

Audit and investigative highlights follow.

Management Advisory Report: Significantly More Individual Taxpayers Inappropriately Received Disabled Access Credits for Tax Year 2000 Than for 1999 (Reference No. 2002-30-048)

In September 2001, OA reported¹⁶ that individual taxpayers were inappropriately receiving tax credits on their TY 1999 *U.S. Individual Income Tax Returns (Form 1040)*. These taxpayers received the Disabled Access Credit (a business incentive credit intended to help eligible small businesses comply with the requirements of the *Americans with Disabilities Act*)¹⁷ even though their tax returns indicated no business reasons for taking the credits. Although the number of taxpayers involved was limited, the issue was significant for two reasons:

- Many of the taxpayers involved were elderly Americans who were possible victims of promoters recommending unwise investments in pay telephones and automated teller machines and promising bogus tax credits.
- Based on the media coverage the issue had received,¹⁸ OA believed the problem was most likely increasing.

One of the recommendations in a prior report was for IRS to analyze the results of a computer analysis completed by OA for TY 1999 returns, perform a similar analysis of TY 2000 returns, and develop a compliance approach to address this issue. To facilitate IRS' corrective action, OA agreed to perform a

¹⁶ *Some Individual Taxpayers Are Inappropriately Receiving Tax Credits Intended for Businesses That Provide Access for Disabled Americans* (Reference No. 2001-30-158).

¹⁷ *Americans with Disabilities Act (ADA)*, 42 U.S.C. §§ 12101-12213 (1994 & Supp. IV 1998).

¹⁸ Noelle Knox and Greg Farrell, "Seniors Lose Big in Risky Deals Through Insurance Agents," *USA Today* (February 28, 2001).

computer analysis of TY 2000 tax returns. From TY 1999 to TY 2000, the number of tax returns for which the Disabled Access Credit was inappropriately allowed increased 28 percent. The amount of credit allowed on these returns totaled over \$1.25 million. OA also determined that 64 taxpayers inappropriately received the credit for both TYs 1999 and 2000.

As of January 2002, IRS was on schedule to add information to its *Small Business/Self Employed Community Website* to alert taxpayers about investments in pay telephones and automated teller machines fraudulently promoted as qualifying for the Disabled Access Credit.

IRS management also agreed to work on another enhancement to the IRS' website that would provide links from other sections of IRS' website to the text in the *Small Business/Self-Employed* section.

As no formal recommendations were made in this report, an IRS management response was not required.

Computer Programming Can be Used to More Effectively Stop Refunds on Illegal Claims for Reparations Credits (Reference No. 2002-30-071)

Since the early 1990s, thousands of taxpayers have filed specious tax claims with the IRS for reparations credits payable to descendants of slaves. The *Internal Revenue Code* does not provide for, or allow, such a credit. As a result, the IRS tries to identify tax returns containing these claims, deny the claims, and stop any resulting refunds before they are issued to taxpayers. IRS employees manually identify the vast majority of these claims before any data is input to the IRS' computer systems. For example, during CY 2001, IRS employees manually identified close to 80,000 such claims. Because the

manual screening of tax returns by IRS employees is subject to human error, and because some employees may knowingly allow these illegal claims to be processed, some invalid claims for reparations credits are processed and refunds sent to taxpayers.

Early in CY 2001, IRS found that this was occurring more often. Many taxpayers claiming reparations credits had received refunds, some of which exceeded \$80,000 for married taxpayers claiming reparations credits for each spouse. As a result, management from IRS' *Frivolous Return Program* asked OA to help improve IRS' controls by developing a computer program to identify tax returns being processed that contained claims for reparations credits.

Overall, the controls designed by IRS to identify and stop claims for reparations credits from refunding, once the claims were entered into IRS computers, could be significantly improved by using an OA-developed computer program. OA estimated that by using this program, IRS employees could identify 91 percent more of the returns that made it through the initial manual screening than they could using the existing processes, and stop an additional \$90.7 million in refunds from claims for reparations credits over a five-year period. Further, OA identified current and former IRS employees who claimed reparations credits on their own tax returns. Pertinent information regarding these individuals was referred to OI.

OA recommended that IRS management permanently implement and maintain the computer program developed by OA and ensure that employees assigned to the *Frivolous Return Program* are given access to and training regarding a computer command code. This command code is under development for the CI function. It will

allow those employees to stop refunds from being issued during accelerated returns processing cycles.¹⁹

IRS management agreed with the recommendations and initiated appropriate corrective actions.

**Significant Efforts Have Been Made to Combat Abusive Trusts, But Additional Improvements Are Needed to Ensure Fairness and Compliance Objectives Are Achieved
(Reference No: 2002-30-050)**

The IRS anticipates that almost 3.7 million *U.S. Income Tax Returns for Estates and Trusts (Form 1041)* will be filed for CY 2001. Trust returns are now the third most frequently filed income tax return, behind individual and corporate returns. An abusive trust arrangement generally involves a promoter who claims that owners are allowed to both retain full benefit of business or personal assets, and reduce or eliminate taxes.

Since 1997, IRS has made significant efforts to combat abusive trusts. Abusive trust issues are being addressed through a nationally coordinated strategy that includes the IRS CI function, the Small Business/Self-Employed Division's Compliance function, the Office of Chief Counsel, and the Department of Justice. The IRS has emphasized the identification of abusive trust promotions and the use of civil and criminal enforcement actions. Further, IRS has increased its examinations of *Forms 1041* from 567 in FY 1997 to over 4,400 returns in FY 2000. These additional

¹⁹ The IRS must process individual refund returns within 45 days of the return due date to avoid paying interest. To minimize interest payments, the IRS accelerates its processing routines during the weeks before the 45-day deadline to ensure returns are timely processed. The IRS saved almost \$9 million in interest by accelerating processing in certain weeks of its 2001 Filing Season.

examinations yielded a substantial increase in proposed tax assessments, averaging \$104,000 per return. *Table 2* shows that IRS tax assessments involving abusive business trusts and related returns increased from \$8 million in FY 1997 to over \$467 million in FY 2000.

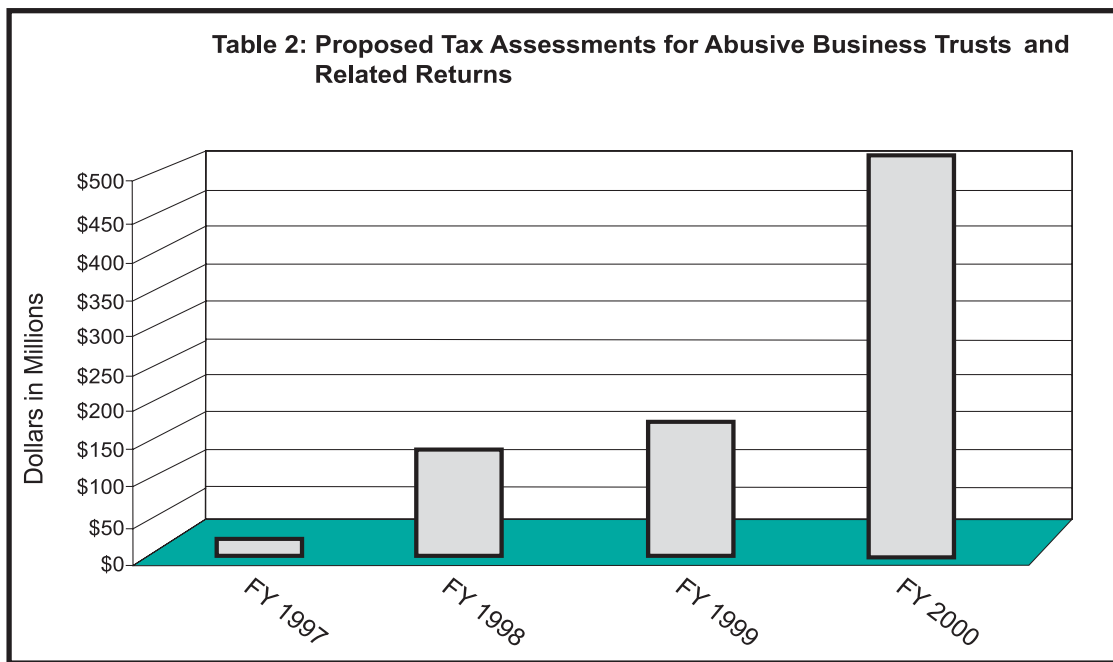
However, additional improvements are needed in the program to ensure that IRS achieves its goal of combating abusive trusts. OA's review of abusive trust-related returns examined and closed during the first quarter of FY 2001 showed that IRS may not be consistently asserting the accuracy-related penalty. The IRS assessed the accuracy-related or fraud penalty in only 26 percent of a sample of these cases. If the IRS assessed the accuracy-related penalty based on the additional tax assessments of \$467 million, penalty assessments could range from an estimated \$69.1 to \$138.2 million over a two-year period. There is a risk that not penalizing taxpayers involved with abusive trusts could result in further

noncompliance, because these taxpayers may simply move to other abusive arrangements.

One of the methods that the IRS' National Trust Initiative uses to accomplish its primary goal of combating abusive trusts is pre-filing and outreach activities. However, IRS does not have performance measures to determine if its pre-filing and outreach activities are increasing taxpayer compliance. Finally, IRS does not have a system to capture results of *Form 1041* examinations that would identify emerging abusive trust issues.

OA recommended that IRS management develop new penalty tables to monitor the application of the accuracy-related penalty and develop a system to capture *Form 1041* examination data.

IRS management agreed to the recommendations and is proposing a number of actions to address the problems identified in the report.



Source: Project Code 233 Analysis as of September 2000 provided by the National Trust

Federal Requirements Need Strengthening at Lockbox Banks to Better Protect Taxpayer Payments and Safeguard Taxpayer Information (Reference No. 2002-30-055)

The IRS lockbox program consists of commercial banks that have contracted with the Financial Management Service, another government agency, to process tax payments. This program was designed to accelerate the deposit of tax payments by having taxpayers send their payments to commercial banks rather than to the IRS.

With this acceleration came significant risks, as evidenced in FY 2001 when control weaknesses contributed to the loss of taxpayer payments and taxpayer information at a lockbox bank in Pittsburgh, Pennsylvania. Approximately 71,000 taxpayer remittances valued in excess of \$1.2 billion were lost or destroyed.

The Los Angeles lockbox bank processes tax payments for the Fresno Submission Processing Center. The bank received payments for *U.S. Individual Income Tax Returns (Form 1040 series)*, employment tax returns (Form 940 series), and other miscellaneous tax payments. The Los Angeles lockbox bank handled approximately 10 percent of the more than 84 million payments, totaling \$311 billion, processed for the entire lockbox network in FY 2000.

OA reported that the Los Angeles lockbox bank was in compliance with established *Lockbox Processing Guidelines* concerning physical and data security for CY 2001. However, additional controls are needed in the *Guidelines* to reduce the risks associated with processing large volumes of taxpayer remittances that could lead to financial losses and loss of taxpayer confidence.

OA recommended that the Lockbox Processing Guidelines be strengthened or clarified in the following areas: adding controls for mail delivered by courier from the post office to the lockbox bank; establishing inventory controls earlier over tax payments received; enhancing video surveillance systems; testing disaster recovery plans; providing for biological safeguards; requiring couriers, bank associates, and temporary employees to undergo background clearance checks prior to handling IRS material; and further specifying guard service and courier service requirements.

IRS management agreed with most of the findings and recommendations in the report, and plans numerous corrective actions.

Pricing Discrepancies on the Long Term Maintenance Computing Center Contract (TIR-NO-96-D-0021) (Reference No. 2002-10-008)

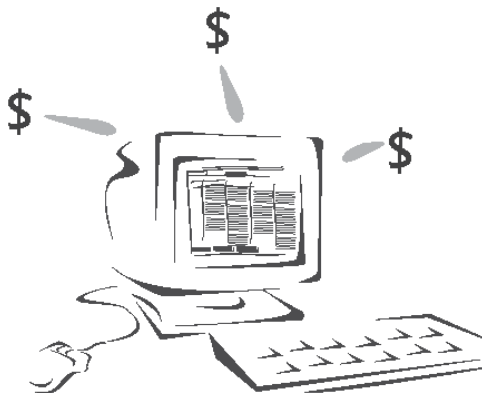
OI received an allegation that a contractor had mischarged IRS for monthly software maintenance fees. From this allegation, OA reviewed the subcontractor's records and determined that IRS was mischarged on nine *Contract Line Items (CLIN)* on the *Long Term Maintenance Computing Center* contract. The subcontractor records indicated that these services were provided to the contractor at a significantly lower cost than the IRS was billed. The contractor was charging IRS yearly costs on a monthly basis. This resulted in IRS unnecessarily paying the contractor \$433,000 over the life of the contract.

Additionally, IRS paid for a higher-priced software upgrade than that provided by the contractor. The IRS ordered a specific *CLIN* upgrade, costing approximately \$199,500. However, the contractor

replaced the item with another, lower-priced product. The cost to the contractor for this upgrade was \$46,908. Therefore, the estimated cost to the government should have been approximately \$52,500, allowing the contractor a modest increase for general and administrative expenses and profit. OA found no indication that the contractor notified IRS of the product differences. As a result, IRS unnecessarily spent approximately \$147,000 for this software upgrade.

The mischarges on the software maintenance and the upgrade have been discussed with an Assistant United States Attorney (AUSA), who considered the prosecutable merits of the case. After consulting with the contractor's legal counsel, the AUSA declined civil and criminal prosecution.

OA recommended IRS take the necessary administrative actions to recover the \$580,000 associated with the pricing discrepancies. IRS management responded that avenues to recoup the costs are limited. The contract is completed and the contractor holds no other contract with the IRS. Moreover, the contractor has filed for Chapter 11 in the United States Bankruptcy Court. As an alternative, IRS issued a letter to the contractor requesting an equitable adjustment in the amount of \$580,000. However, given the contractor's bankruptcy status, recouping any costs from the contractor is unlikely.



Individual Jailed for Sabotaging IRS Computers

In October 2001, a person was sentenced to 15-months incarceration and three years probation for intentionally causing damage to a protected computer. The individual, an employee of an IRS contractor, was also ordered to pay restitution to IRS in the amount of \$108,804. By inserting active destructive computer codes on three separate IRS computer servers, this person manipulated the code so that, once executed, it would destroy all data on the three servers. After these activities were discovered, the contracting firm and IRS shut down the servers in order to remove the destructive code and reestablish the security and integrity of the system.

Health Insurance Employee Defrauds Government through Bogus Refund Scam

A former health insurance company employee was charged with one count of making false claims against the U.S. In October 2001, this individual, using the names, addresses, and Social Security numbers of unsuspecting policyholders from various states across the country, created false tax returns in a scheme to defraud IRS of \$278,000 in refunds, of which the individual succeeded in obtaining almost \$40,000.

Bank security contacted TIGTA to report a suspicious transaction when numerous tax refunds were electronically deposited into the same account but the names on the refunds did not match the bank account holder's name. TIGTA identified numerous bank accounts associated with this scheme and advised bank security to freeze the accounts to prevent the individual from receiving the money. No evidence was found linking this individual or the friend to any IRS employee.

Attorney Sentenced for Submitting Bogus Release of Levy Form

In January 2002, an attorney pled guilty to corrupt interference with tax administration. According to the indictment, IRS had issued a *Notice of Levy* to an employer, instructing the employer to pay a certain portion of an individual's salary each week to IRS in order to collect funds owed to IRS. The indictment alleged that the attorney submitted a bogus release of levy form to the employer, causing the employer to erroneously release IRS' levy on the wages.

In connection with this guilty plea, a federal judge sentenced the attorney to five years probation. The attorney must serve the first six months in home confinement and was ordered to meet with the IRS to determine the prior tax liability.

Business Owner Convicted of Bribery

A business owner pled guilty to federal charges of making bribe overtures totaling \$20,000 to an IRS employee. Following a routine meeting to discuss a federal tax liability with business partners, this individual contacted and offered an IRS employee \$10,000 to reduce the company's liability by half its original debt. The IRS employee reported the bribe overture to TIGTA. In a subsequent meeting with the business owner, the cooperating IRS employee agreed to the offer and later accepted the \$10,000 cash.

With assistance from special agents from OI's TSS, electronic evidence was gathered through the use of audio and video recording devices. Following the first payoff, the attorney offered the cooperating IRS employee a second bribe of an additional \$10,000 if the employee would reduce the liability of another partner in the same fashion. A second, covertly monitored meeting was arranged where the attorney provided another \$10,000

cash payment. The attorney was arrested at the conclusion of this meeting and subsequently pled guilty to federal bribery charges. Results of this investigation confirmed that the attorney acted alone without the knowledge of his business partners.

Individual Pled Guilty in Scheme to Defraud Elderly Woman

TIGTA received information from an IRS employee who reported suspicions that a senior citizen was the victim of a fraudulent scheme. An acquaintance reportedly made the senior citizen believe that IRS was holding over one million dollars in refunds, which would be lost unless IRS tax payments were made. From September 1997 to May 2000, the senior citizen gave the acquaintance over \$40,000 via wire transfers to make payments to IRS for this purpose. The indictment alleged that the individual did not represent the IRS and instead converted all of these payments to the acquaintance's own use. The senior citizen, who sold her home and several rental properties to make these fictitious tax payments, was living penniless in a homeless shelter when interviewed by TIGTA.

As a result of interviews with witnesses, analyses of financial documents, and electronic monitoring, the acquaintance was indicted, arrested, and subsequently pled guilty in November 2001 to money laundering and was to be sentenced in April 2002. The victim is currently receiving Social Security benefits and is now living in a convalescence care facility.

Individual Indicted on Six Counts of Fraud

In March 2002 an individual was indicted on one count of making false, fictitious or fraudulent claims; one count of influencing or inuring an officer or juror; one count of

attempting to interfere with the administration of Internal Revenue laws; and three counts of bankruptcy fraud.

The indictment alleges that the individual presented a check in the amount of \$12,990 to the IRS on a closed bank account; that he filed Chapter 7 involuntary petitions in U.S. Bankruptcy Court identifying an IRS employee and a judge as debtors (the petitions contained false claims against them relating to their role in a trial); and that the individual devised a scheme to defraud two individuals of certain alleged equity in their property by filing false and fraudulent petitions. The indictment also alleges that the individual filed the four involuntary bankruptcy petitions without lawful payment of the filing fees.

Man Arrested for Sending Threatening Letters

In February 2002, special agents arrested a man who allegedly sent a series of threatening communications to an IRS employee in January and February 2002. The man was arrested pursuant to a criminal complaint that alleged one count of forcible interference with tax administration.

Two Charged with Bank Fraud, Mail Fraud and Conspiracy

In March 2002, the United States Attorney's office charged two individuals with mail fraud, bank fraud, and conspiracy. The information alleges the individuals paid bribes to an IRS taxpayer service representative to access confidential IRS records relating to delinquent taxpayers. The individuals then offered to represent the delinquent taxpayers before the IRS and solicited monies from them on the false representation that the monies would be paid over to the IRS as payments on an Offer in Compromise. The individuals allegedly converted over \$600,000 for their own use from funds given to them by the delinquent taxpayers.

TIGTA Organization

Organization of the Treasury Inspector General for Tax Administration

TIGTA provides independent oversight of IRS activities, the IRS Oversight Board, and the IRS Office of Chief Counsel. TIGTA is organizationally placed within Treasury, but is independent of the Department and all other Treasury offices. TIGTA's focus is devoted to all aspects of work related to tax administration.

TIGTA's primary organizational components are the Office of Audit and the Office of Investigations. TIGTA's Offices of Chief Counsel, Information Technology, and Management Services support both components' efforts.

TIGTA's audit and investigative activities are designed to:

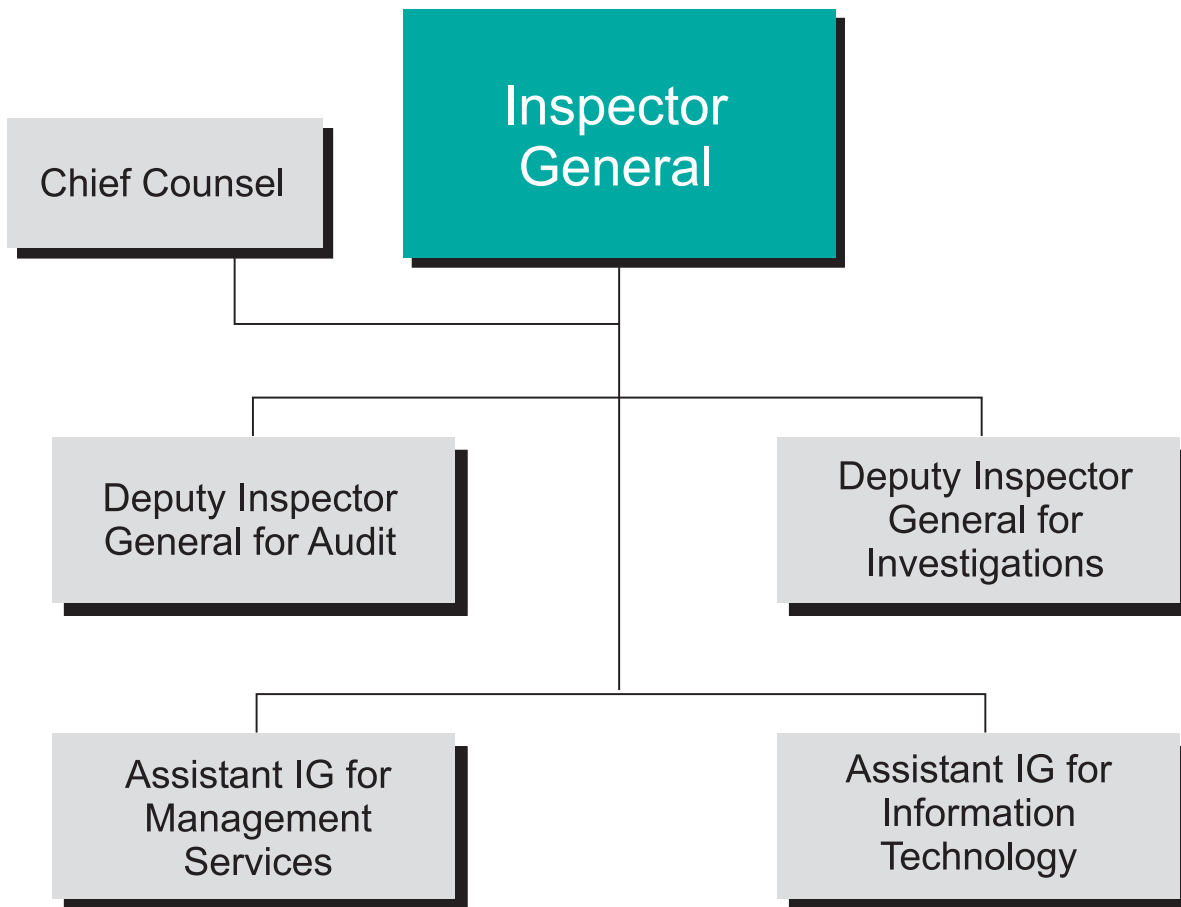
- ▶ *Promote economy, efficiency, and effectiveness in administering the nation's tax system.*
- ▶ *Detect and deter fraud and abuse in IRS programs and operations.*
- ▶ *Protect IRS against external attempts to corrupt or threaten its employees.*

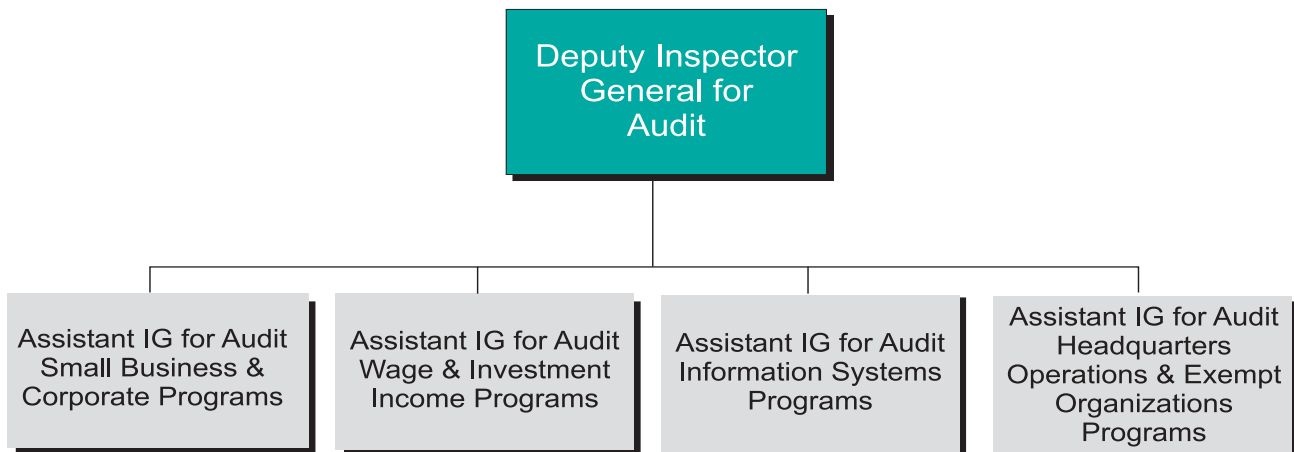
Authorities

TIGTA has all the authorities granted under the *Inspector General Act of 1978*.²¹ TIGTA also has access to tax information in the performance of its responsibilities and has the obligation to report potential criminal violations directly to the Department of Justice. The Inspector General and the Commissioner of the Internal Revenue Service have established policies and procedures delineating responsibilities to investigate potential criminal offenses under the internal revenue laws.

In addition, *RRA 98* amended the *Inspector General Act of 1978* to give TIGTA special agents statutory authority to carry firearms and execute the provisions of the *I.R.C. § 7608(b)(2)*. These provisions include law enforcement authority to execute and serve search warrants, serve subpoenas, and make arrests.

²¹ *Pub. L. No. 95-452 Stat. 1101*, as amended, at *5 U.S.C., App 3*.





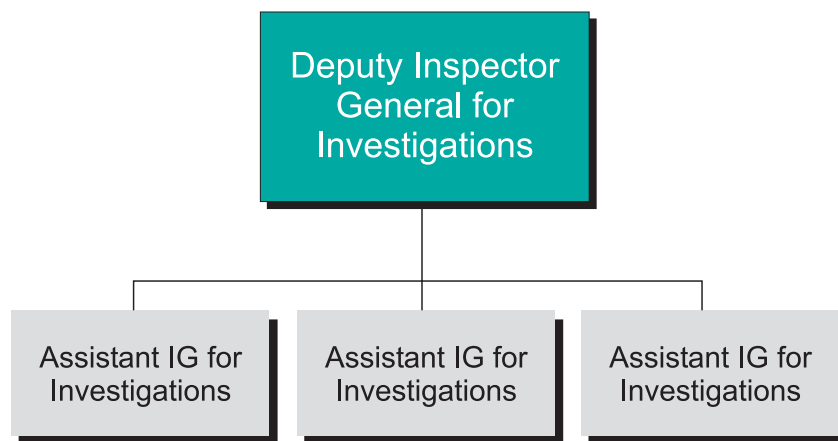
Office of Audit

OA identifies opportunities to improve administration of the nation's tax laws by conducting comprehensive, independent performance and financial audits of IRS programs and operations to:

- Assess efficiency, economy, effectiveness, and program accomplishments.
- Ensure compliance with applicable laws and regulations.
- Prevent, detect, and deter fraud, waste, and abuse.

The Audit program is comprised of reviews mandated by statute or regulation, as well as reviews identified through the annual planning process. The *Annual Audit Plan* describes audit responsibilities, audit focus and audit direction for the fiscal year. The planning process begins with independent risk assessments, which are designed to prioritize areas based on the greatest risks to the IRS. Major management issues, as well as specific areas of concern to Congress, the IRS Commissioner and the IRS Oversight Board, are considered as part of this planning process.

OA is organized around IRS' core business activities (Small Business and Corporate Programs; Wage and Investment Income; Information Systems; and Headquarters Operations and Exempt Organization Programs). Emphasis is also placed on the statutory audit coverage mandated by *RRA 98*, as well as on other statutory authorities and standards involving computer systems and financial management.



Office of Investigations

OI investigates activities related to fraud, waste, abuse and mismanagement concerning activities of the IRS and related entities. OI is organized around 12 field divisions, which are geographically dispersed around the country, with direct reporting responsibilities to TIGTA headquarters. Additionally, OI includes five headquarters divisions that perform special support functions and provide technical and investigative assistance to the field. These divisions include:

- **Operations** – provides OI with TIGTA’s guidance concerning all investigative matters. Some examples of Operations’ responsibilities include: responding to Congressional inquiries; liaison with other federal law enforcement agencies and preparation of recurring statistical reports for internal use and external use.
- **Complaints Management** – reviews and refers all complaints made to the TIGTA hotline and maintains OI’s records.
- **Strategic Enforcement** – executes a proactive program to detect fraud in IRS operations, unauthorized accesses (UNAX) to IRS computer systems by internal users, and attempts to interfere with the security of IRS computers by external sources. SED’s staff includes the combined expertise of auditors, special agents, and computer programmers.
- **Technical and Forensic Support** – provides technical support to the field through the Technical Services Section (TSS) and the Forensic Science Laboratory (FSL). TSS provides technical and investigative assistance, equipment, training and other specialized services to enhance TIGTA’s investigative activities. The FSL processes documentary, physical and chemical evidence, fingerprint and handwriting examination, and photography and chemical analysis.
- **Special Inquiries and Inspection** – conducts TIGTA’s most complex, high profile investigations involving IRS senior management officials, the IRS oversight board, and IRS international employees. This Division includes three other specialized programs: procurement fraud, domestic terrorism and inspection.

Appendices

Appendix I - Statistical Reports for the Office of Audit

Audit Reports With Questioned Costs

Two audit reports with questioned costs were issued during this semiannual reporting period.

The term “questioned cost” is defined as a cost that is questioned because of: (1) an alleged violation of a provision of a law, regulation, contract, or other requirement governing the expenditure of funds; (2) a finding that, at the time of the audit, such cost is not supported by adequate documentation, i.e., “unsupported cost” or (3) a finding that expenditure of funds for the intended purpose is unnecessary or unreasonable. The term “disallowed cost” is defined as a questioned cost that management, in a management decision, has sustained or agreed should not be charged to the Government.

Reports With Questioned Costs (10/01/01 - 3/31/02) Report Category	Number of Reports ¹	Questioned Costs ² (In Thousands)	Unsupported Costs (In Thousands)
1. For which no management decision had been made by the beginning of the reporting period	2	\$136	\$0
2. Which were issued during the reporting period.. . . .	2	\$1,679	\$0
3. Subtotals (Item 1 plus Item 2).	4	\$1,815	\$0
4. For which a management decision was made during the reporting period.			
- Dollar value of disallowed costs.	1	\$135	\$0
- Dollar value of costs not disallowed.	2	\$581	\$0
5. For which no management decision had been made by the end of the reporting period. (Item 3 minus Item 4).	1	\$1,099	\$0
6. For which no management decision was made within six months of report issuance.	0	\$0	\$0

¹ See Appendix IV for identification of audit reports involved.
² “Questioned Costs” include “Unsupported Costs.”

Report Recommendations that Funds be Put to Better Use

Three reports with recommendations that funds be put to better use were issued during this semiannual reporting period.

The term “recommendation that funds be put to better use” is defined as a recommendation that funds could be used more efficiently if management took actions to implement and complete the recommendation, including: (1) reductions in outlays; (2) deobligations of funds from programs or operations; (3) costs not incurred by implementing recommended improvements related to operations; (4) avoidance of unnecessary expenditures noted in pre-award reviews of contract agreements; or (5) any other savings which are specifically identified. The term “management decision” is defined as the evaluation by management of the findings and recommendations included in an audit report and the issuance of a final decision concerning its response to such findings and recommendations, including actions concluded to be necessary.

Reports With Recommendations That Funds Be Put to Better Use (10/01/01 - 3/31/02)	Number of Reports ¹	Amount (In Thousands)
Report Category		
1. For which no management decision has been made by the beginning of the reporting period.	1	\$98
2. Which were issued during the reporting period.	3	\$14,005
3. Subtotals (Item 1 plus Item 2).	4	\$14,103
4. For which a management decision was made during the reporting period.		
• Dollar value of recommendations that were agreed to by management		
- Based on proposed management action.	2	\$1,198
- Based on proposed legislative action.	0	\$0
• Dollar value of recommendations that were not agreed to by management.	0	\$0
5. For which no management decision has been made by the end of the reporting period. (Item 3 minus Item 4)	2	\$12,905
6. For which no management decision was made within six months of issuance.	0	\$0

¹ See Appendix IV for identification of audit reports involved.

Reports with Additional Quantifiable Impact on Tax Administration

In addition to questioned costs and funds put to better use, OA has identified additional measures that demonstrate the value of audit recommendations on tax administration and business operations. These issues are of interest to IRS and Treasury executives, Congress, and the taxpaying public, and are expressed in quantifiable terms to provide further insights to the value and potential impact of OA's products and services. Including this information also advances adherence to the intent and spirit of GPRA.

Definitions of Additional Measures

- ❑ **Taxpayer Rights and Entitlements at Risk:** The protection of due process (rights) that is granted to taxpayers by law, regulation, or IRS policies and procedures. These rights most commonly arise in the performance of filing tax returns, paying delinquent taxes, and examining the accuracy of tax liabilities. The acceptance of claims for and issuance of refunds (entitlements) are also included in this category, relating to instances when taxpayers have a legitimate assertion of overpayments of tax.
- ❑ **Reduction of Burden on Taxpayers:** Decreases by individuals or businesses in the need for, frequency of, or time spent on contacts, record keeping, preparation, or costs to comply with tax laws, regulations, and IRS policies and procedures.
- ❑ **Increased Revenue or Revenue Protection:** Assessment or collection of additional taxes (increased revenue), or proper denial of claims for refund, including recommendations that prevent erroneous refunds or efforts to defraud the tax system (revenue protection).
- ❑ **Taxpayer Privacy and Security:** Protection of taxpayer financial and account information (privacy). Processes and programs that provide protection of tax administration, account information, and organizational assets (security).
- ❑ **Protection of Resources:** Safeguarding human and capital assets, used by or in the custody of the organization, from inadvertent or malicious injury, theft, destruction, loss, misuse, overpayment, or degradation. This measure will often be expressed as a value of the entity or program affected by the issue(s) described in the audit report.
- ❑ **Reliability of Management Information:** Ensuring the accuracy, validity, relevance, and integrity of data, including the sources of data and the applications and processing thereof, used by the organization to plan, monitor, and report on its financial and operational activities. This measure will often be expressed as an absolute value (i.e., without regard to whether a number is positive or negative) of overstatements or understatements of amounts recorded on the organization's documents or systems.

Reports With Additional Quantifiable Impact on Tax Administration

The number of taxpayer accounts, hours, and dollar values shown in this chart were derived from analyses of historical data, and are thus considered potential barometers of the impact of audit recommendations. Actual results will vary depending on the timing and extent of management's implementation of the corresponding corrective actions, and the number of accounts or subsequent business activities applicable from the dates of implementation. Also, a report may have issues that impact more than one outcome measure category.

Reports With Additional Quantifiable Impact on Tax Administration (10/01/01 - 3/31/02)					
Outcome Measure Category	Number of Reports in Category ¹	Number of Taxpayer Accounts	Number of Hours	Dollar Value (In Thousands)	Other ⁷
1. Taxpayer Rights and Entitlements at Risk	3	9,736 ²	--	\$247,706	
2. Reduction of Burden on Taxpayers	6	6,564,429	--	--	⁸
3. Increased Revenue	2	20,990	--	\$283,360 ³	
4. Revenue Protection	4	3,737	--	\$208,961 ⁴	
5. Taxpayer Privacy and Security	1	--	--	--	⁹
6. Protection of Resources	3	--	--	\$30,341 ⁵	
7. Reliability of Management Information	4	542	--	\$174,861 ⁶	

¹ See Appendix IV for identification of audit reports involved.

² In one report (Reference No. 2002-10-068), consisted of two recommendations that impacted 137 taxpayers. However, accounts may be duplicated between two recommendations.

³ In one report (Reference No. 2002-30-050), IRS management did not concur with TIGTA's calculation of the Increased Revenue of \$138.2 million.

⁴ In one report (Reference No. 2002-40-021), IRS management did not concur with TIGTA's calculation of the Revenue Protection of \$557,058 for 831 taxpayers.

⁵ In one report (Reference No. 2002-40-020), IRS management did not concur with TIGTA's calculation of the \$28 million of resources protected.

⁶ In one report (Reference No. 2002-10-006), consisted of \$13.9 million in offset fees shortfall that pertained to the Financial Management Service (FMS) and does not affect IRS. This review was coordinated with the Treasury's Office of Inspector General that has responsibility for FMS.

⁷ Some reports contained "Other" quantifiable impacts besides the number of taxpayer accounts, number of hours, and dollar value. These outcome measures are described in footnotes 8 and 9 below.

⁸ Other measures of "Taxpayer Burden" consist of 68 Chief Counsel Advice documents released for public inspection based on TIGTA's recommendations.

⁹ Other measures of "Taxpayer Privacy and Security" consist of 281,153 *Form 990 Returns* requiring improved protection.

Appendix II - Statistical Reports for the Office of Investigations

Investigative Results October 1, 2001 - March 31, 2002

Investigations Opened and Closed

Total Investigations Opened	2,036
Total Investigations Closed	2,171

Financial Accomplishments

Embezzlement/Theft Funds Recovered	\$506,480
Court Order Fines, Penalties and Restitution	\$9,267,148
Out-of-Court Settlements	\$0

Investigative Results

October 1, 2001 - March 31, 2002

Status of Closed Criminal Investigations

	Employee	Non-Employee	TOTAL
Criminal Referrals¹			
Referred - Accepted for Prosecution	18	86	104
Referred - Declined for Prosecution	313	352	665
Referred - Pending Prosecution Decision	25	106	131
TOTAL CRIMINAL REFERRALS	356	544	900
No Referrals	601	572	1,173

¹ Criminal referrals include both federal and state dispositions.

Criminal Dispositions²

	Employee	Non-Employee	TOTAL
Guilty	14 (14)	79 (97)	93 (111)
Nolo-Contendere	0 (0)	1 (0)	1 (0)
Pre-trial Diversion	5 (9)	9 (29)	14 (38)
Deferred Prosecution ³	1 (4)	2 (1)	3 (5)
Not Guilty	0 (0)	3 (1)	3 (1)
Dismissed ⁴	2 (2)	7 (13)	9 (15)
TOTAL CRIMINAL DISPOSITIONS	22 (29)	101 (141)	123 (170)⁵

² Final criminal dispositions during the reporting period. This data may pertain to criminal investigations referred in prior reporting periods and does not necessarily relate to the criminal investigations referred in the *Status of Closed Criminal Investigations* table.

³ Generally, in a deferred prosecution, the defendant accepts responsibility for his/her actions, and complies with certain conditions imposed by the court. Upon defendant's completion of the conditions, the court dismisses the case. If the defendant fails to fully comply, the court reinstates prosecution of the charge.

⁴ Court dismissed charges.

⁵ Numbers in parentheses reflect updated data that were previously reported in TIGTA's April 1 - September 30, 2001 Semiannual Report to the Congress. The data were updated due to a programming error in a new management information system. Numbers not in parentheses reflect the data for this reporting period.

Investigative Results

October 1, 2001 - March 31, 2002

Administrative Status and Disposition on Closed TIGTA Investigations¹	
	TOTAL
Removed, Terminated or Other	115
Suspended/Reduction in Grade	43
Oral or Written Reprimand/Admonishment	108
Closed - No Action Taken	261
Clearance Letter Issued	81
Employee Resigned Prior to Adjudication	47
TOTAL ADMINISTRATION DISPOSITIONS	655

¹ Final administrative dispositions during the reporting period. This data may pertain to investigations referred administratively in prior reporting periods and does not necessarily relate to the investigations closed in the *Investigations Open and Closed* table.

Investigative Results

October 1, 2001 - March 31, 2002

Complaints/Allegations Received by TIGTA	
	TOTAL
Complaints Against IRS Employees	1,415
Complaints Against Non-Employees	1,974
NUMBER OF COMPLAINTS/ALLEGATIONS	3,389

Status of Complaints/Allegations Received by TIGTA	
	TOTAL
Investigations Initiated	1,582
In Process Within TIGTA ¹	175
Referred to IRS for Action	207
Referred to IRS for Information Only	528
Referred to a Non-IRS Entity ²	17
Closed with No Referral	820
Closed with All Actions Completed	60
TOTAL COMPLAINTS	3,389

¹ Complaints for which final determination had not been made at the end of the reporting period.

² A non-IRS entity includes other law enforcement entities or Federal agencies.

Note: IRS made 66 referrals to TIGTA that would more appropriately be handled by IRS and, therefore, were returned to IRS. These are not included in the total complaints shown above.

Allegations of Misconduct Against IRS Employees

The following three tables consist of allegations of misconduct against individual IRS employees recorded in the IRS Automated Labor and Employee Relations Tracking System (ALERTS). Employee misconduct cases investigated by TIGTA have been extracted from the next two tables and have been reported on the previous two pages. IRS management conducted the inquiries into the cases reflected in these tables.

	Case Type		
	Administrative ²	Employee Tax Matter ³	Total
Inventory on April 1, 2002	929	732	1,661
Add: Cases Received	2,477	736	3,213
Less: Cases Closed	(2,513)	(727)	(3,240)
Duplicates	(25)	(75)	(100)
Not Misconduct	(11)	(0)	(11)
Total Closures	(2,549)	(802)	(3351)
Inventory on Sept. 30, 2001	857	666	1,523

¹ Because of potential duplication of taxpayer complaints tracked in IRS' various management information systems, IRS is unable to report on the total number of taxpayer complaints received.

² Administrative - Any matter involving an employee in which management conducted an inquiry into alleged misconduct.

³ Employee Tax Matter - Any matter that becomes of official interest involving an employee's tax compliance.

Allegations of Misconduct Against IRS Employees

Disposition of Employee Misconduct Cases Investigated by IRS Management

Disposition	Administrative	Employee Tax Matter	Total
Removal	57	5	62
Separation of Probationary Employees	280	13	293
Separation of Temporary Employees	11	7	18
Resignation/Retirement	144	37	181
Suspensions	128	57	185
Reprimands	231	114	345
Counseling	820	286	1,106
Alternative Discipline	36	17	53
Clearance	98	27	125
Closed Without Action	629	157	786
Forwarded to TIGTA	16	0	16
Not Otherwise Coded	63	7	70
	TOTAL		
	2,513	727	3,240

Allegations of Misconduct Against IRS Employees

IRS Summary of Substantiated <i>Section 1203</i> Allegations¹		
1203 Violation ²	Removals	Penalty Mitigated
Seizure Without Approval	0	0
False Statement Under Oath.	0	0
Constitutional & Civil Rights Issues	0	0
Falsifying or Destroying Records	0	0
Assault or Battery	0	0
Retaliate or Harass	1	0
Misuse of 6103	0	0
Failure to File Federal Tax Return	3	36
Understatement of Federal Tax Liability	0	1
Threat to Audit for Personal Gain	1	0
TOTAL	5	37

¹ The cases reported as "Removals" and "Penalty Mitigated" do not reflect the results of any third party appeal.

² The cases reported as "Removals" and "Penalty Mitigated" do not reflect the results of any third party appeal.

Source: IRS Automated Labor and Employee Relations Tracking System (ALERTS) and 1203 Review Board records.

Appendix III - Statistical Reports - Others

Audit Reports With Significant Unimplemented Corrective Actions

The *Inspector General Act of 1978* requires identification of significant recommendations described in previous semiannual reports on which corrective actions have not been completed. The following list is based on information from the IRS Office of Management Control's automated tracking system maintained by Treasury management officials.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
093602	April 1999		<i>The Internal Revenue Service Needs To Improve Treatment of Taxpayers During Office Audits</i>
		10/01/02	<u>F-1, R-3, P-2.</u> Require a separation of duties among auditors who identify Midwest Automated Compliance System (MACS) returns with potential tax changes, auditors who select MACS returns to be audited, and auditors who conduct the examinations.
		10/01/05	<u>F-1, R-4, P-2.</u> Ensure that all MACS data discs forwarded from the MACS Development Center to district offices are properly accounted for and secured.
		08/01/02	<u>F-2, R-4, P-1.</u> Clarify the Internal Revenue Manual to provide specific guidance for conducting correspondence audits in district office settings.
094206	May 1999		<i>The Examination Returns Control and Integrated Data Retrieval Systems Can Be Improved to Protect Taxpayer Rights During the Audit Process</i>
		04/01/02	<u>F-3, R-1, P-2.</u> Ensure the issues are addressed to enable the Examination Returns Control System audit trail to be used to its fullest extent.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary
			(F = Finding Number, R = Recommendation Number, P = Plan Number)
093009	June 1999		<i>Review of the Electronic Fraud Detection System</i>
		04/01/02	<u>F-1, R-2, P-2.</u> Initial and periodic password changes should be systemically enforced for the Electronic Fraud Detection System (EFDS) application program.
		04/01/02	<u>F-1, R-3, P-2.</u> Workstation terminals should be disabled after a selected number of failed login attempts to the EFDS application program.
		04/01/02	<u>F-1, R-4, P-2.</u> Password change information should be part of the EFDS application audit trail.
		01/01/03	<u>F-2, R-1, P-2.</u> Program the EFDS application trail to record all accesses to taxpayer data.
		01/01/03	<u>F-2, R-2, P-2.</u> Design an audit trail application to record accesses to taxpayer data through secondary sources such as the database administrator, system query tools, or contract vendors.
		01/01/03	<u>F-3, R-1, P-2.</u> Ensure that the programming changes are made. The EFDS application audit reports should be changed to include a date range field and service center site field where applicable.
		07/01/03	<u>F-3, R-4, P-2.</u> The assessment should take into consideration the audit trail issues referred to in the Memorandum of Understanding to improve the usefulness of the EFDS application audit trail.
		04/01/02	<u>F-3, R-5, P-2.</u> Because of the sensitivity of the data maintained on the EFDS, and the number of people who have access to the system (with more planned in the future), the audit trail problems referred to in the report should be included by IRS as a <i>Federal Managers' Financial Integrity Act</i> material weakness.
		06/01/02	<u>F-5, R-2, P-1.</u> In the upcoming certification process, Information Systems should ensure that the issues discussed in this report are corrected, and that all other controls necessary for a proper certification are in place and functioning.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
199920063	August 1999		<i>The General Controls Environment Over the Internal Service's Unisys 2200 Systems Can Be Improved Revenue</i>
		07/01/02	<u>F-2, R-1, P-1.</u> Standardize control settings for files common to the Unisys 2200 production mainframes.
		07/01/02	<u>F-3, R-1, P-1.</u> Ensure all improperly owned files are identified and assigned an owner present on the Unisys 2200 system at each service center, with the exception of files required to be unowned, prior to movement of that service center's mainframe to the consolidated Unisys 4800 environment.
		P-2: 07/01/02 P-3: 01/01/03	<u>F-3, R-2, P-2, P-3.</u> Institute a policy requiring that all files owned by users being removed from the Unisys 2200 and Unisys 4800 systems either be deleted or assigned to a user present on the system.
		07/01/02	<u>F-4, R-1, P-1.</u> Examine the possibility of tracking individual user actions while using the MASTER user-id on the Unisys 4800 system and, if possible, implement this feature as soon as feasible.
		05/01/02 07/01/02	<u>F-6, R-1, P-1.</u> Ensure that all required C-2 documentation is prepared for the Unisys 4800. <u>F-6, R-2, P-1.</u> Develop and maintain a security policy for the Unisys 4800.
199910072	September 1999		<i>The Internal Revenue Service Needs to Improve Compliance With Legal and Internal Guidelines When Taking Taxpayers' Property for Unpaid Taxes</i>
		P-1: 06/01/02 P-2: 06/01/02 P-3: 06/01/02	<u>F-2, R-3, P-1, P-2, P-3.</u> Verify that all applicable items on the the pre-seizure checklist are completed prior to approving the seizure and that all applicable items on the seizure and post-seizure checklists under development are completed.
2000-30-015	December 1999		<i>Consolidated Report on Opportunities for the Internal Revenue Service to Improve Service to Business Taxpayers</i>
		10/01/02	<u>F-2, R-1, P-1.</u> Expand the current Federal Tax Deposits alert reengineering effort to re-evaluate the cost effectiveness of the Program.
2000-10-033	February 2000		<i>The Internal Revenue Service Can Further Reduce the Burden on Taxpayers Who Disagree With Proposed Assessments</i>
		10/01/02	<u>F-1, R-1, P-1.</u> Send letters of proposed changes (30-Day Report) via certified mail, with return receipt requested, when taxpayers do not respond to the initial contact letter.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
2000-10-058	March 2000		<i>The Internal Revenue Service Needs to Improve Its Compliance With Procedures When Processing Requests for Information Under the Freedom of Information Act</i>
		11/01/02	<u>F-3, R-2, P-1.</u> Obtain controlled access to the IRS' tax account information in the National Office of Governmental Liaison and Disclosure to research the availability of the requested records.
2000-30-057			<i>Opportunities Exist for Further Reducing Erroneous Fuel Tax Credits</i>
		06/01/02	<u>F-1, R-1, P-1.</u> IRS needs to emphasize the importance of checking prior year returns for fuel tax credits, when closing current year fuel tax cases with an adjustment, and to establish management controls to ensure that the requirement is followed.
2000-30-059			<i>The Internal Revenue Service Can Improve the Estate Tax Collection Process</i>
		07/01/02	<u>F-1, R-1, P-1.</u> Assign the responsibility for determining whether a bond or tax lien should be secured to the service center employees who process the installment agreements, instead of to the district offices.
		04/01/02	<u>F-1, R-2, P-2.</u> Review and approve all requests for payment extensions. The review should ensure the estate has demonstrated reasonable cause before granting the payment extension.
		11/01/02	<u>F-2, R-1, P-1.</u> Instruct managers and employees to conduct a 100 percent review of all current estate cases to ensure active tax liens are input to the Automated Lien System (ALS), tax liens and lien fees are properly reflected on the taxpayer accounts, and all tax liens are released on accounts that have no tax obligation.
		07/01/03	<u>F-2, R-2, P-1.</u> Develop procedures to periodically reconcile tax liens on the ALS with information shown on the taxpayer accounts.
		11/01/02	<u>F-2, R-3, P-1.</u> Clarify procedures to employees that all estate tax liens should be recorded on the ALS.
		07/01/02	<u>F-3, R-3, P-1.</u> Ensure all estate tax accounts with collection statute abatements are manually reviewed to verify or correct CSED calculations.
		01/01/03	<u>F-3, R-4, P-1.</u> Coordinate to develop a procedure to identify accounts with multiple assessments and collection statute dates to ensure partial abatements occur when the earliest CSED is reached.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
2000-40-055		10/01/02	<i>The Internal Revenue Service Needs to Improve Its Coordinated Oversight of the Substitute for Return Process</i> F-2, R-1, P-1. Coordinate the development of a Substitute For Return (SFR) process to monitor the future filing compliance of taxpayers with SFR tax assessments regardless of which function processed the account.
2000-40-063	May 2000	04/01/02	<i>Increased Attention Is Needed to Ensure Timely, Accurate Determinations on Innocent Spouse Claims for Relief</i> F-2, R-1, P-2. Design and implement a system of internal controls that addresses the quantity, cost, and timeliness of the Innocent Spouse Program to complement the existing internal controls over the quality of the Program.
2000-30-088	June 2000	07/01/02	<i>Millions of Dollars in Internal Revenue Service Excess Collections Accounts Could be Credited to Taxpayers</i> F-2, R-1, P-4. Coordinate education efforts for employees handling these accounts and develop strategies for increasing taxpayer and practitioner awareness of the law on the statute of limitations for refunding and crediting payments related to overdue tax returns.
2000-20-092		10/01/02	<i>Certifying the Security of Internal Revenue Service Computer Systems is Still a Material Weakness</i> F-1, R-4, P-1. Ensure that IRS' certification process includes follow-ups with the accrediting executives' prior to the expiration of their systems security certification to ensure that they are aware that a new certification and accreditation is required.
		10/01/02	F-1, R-5, P-1. Ensure that all functional executives for individual systems are fully aware of the overall certification and accreditation process.
		10/01/02	F-1, R-6, P-1. Centralize the process for identifying and tracking all information systems requiring certification and accreditation.
		10/01/02	F-2, R-1, P-1. Ensure that IRS' certification process includes follow-ups with the accrediting executives to ensure that necessary information relevant to the official accreditation is provided and to educate them on the importance of providing this information.
2000-20-094		04/01/02	<i>A Comprehensive Program for Preventing and Detecting Computer Viruses Is Needed</i> F-2, R-1, P-1. Develop and implement IRS-wide procedures detailing the frequency and steps to be followed for reliably updating anti-virus software on both networked and portable notebook computers.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
2000-20-094		05/01/02	<u>F-2, R-2, P-1</u> . Establish controls for ensuring all updates have been successfully accomplished.
		05/01/02	<u>F-3, R-1, P-1</u> . Develop a system for gathering information to help analyze and monitor the effectiveness of the program's virus detection and prevention activities.
		05/01/02	<u>F-4, R-1, P-1</u> . Strengthen procedures for ensuring that employees comply with the Internal Revenue Manual requirements for preparing Virus Incident Reports.
2000-20-099	June 2000		<i>Significant Risks Need to Be Addressed to Ensure Adequate Oversight of the Systems Modernization Effort</i>
		09/30/01	<u>F-1, R-3, P-1</u> . Finalize and fully implement Quality Assurance policies and procedures throughout the organization.
		09/01/01	<u>F-2, R-1, P-1</u> . Develop a staffing plan for the Program Management Office (PMO) to ensure that the PMO is adequately staffed and the personnel have proper training.
		12/31/01	<u>F-2, R-4, P-1</u> . Develop a back-up plan for key personnel to ensure that the PMO is adequately staffed and the personnel have proper training.
		12/31/01	<u>F-2, R-5, P-1</u> . Develop policies and procedures to regularly update the staffing plan, skills analysis, training plan, and back-up plan for key personnel.
		10/01/01	<u>F-3, R-3, P-1</u> . Assess the PRIME contractor's processes to ensure that performance monitoring data being provided to IRS are complete and accurate.
2000-30-111	August 2000		<i>Improvements Are Needed in Resolving In-Business Trust Fund Delinquencies to Prevent Tax Liabilities From Pyramiding</i>
		01/01/03	<u>F-2, R-1, P-1</u> . Use all collection tools, including enforcement tools and require the filing of monthly, rather than quarterly, returns.
2000-30-120			<i>Expanding the Electronic Tax Law Assistance Program</i>
		05/01/02	<u>F-1, R-1, P-1</u> . To meet its Electronic Tax Administration goals, IRS needs to redesign the Electronic Tax Law Assistance (ETLA) program to leverage technology that will provide enhanced access to tax information, maximize efficiency, and improve electronic customer service.
		09/01/02	<u>F-2, R-1, P-1</u> . To effectively administer the rapid growth of taxpayer demand, economically use resources, and design future enhancements of the program, IRS needs to fully commit to the ETLA program by converting it from a long-term research project to a fully supported independent function.

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2000-30-120		12/31/02	<u>F-3, R-1, P-1.</u> Until there are technological changes and an organizational commitment, IRS needs to delay the marketing of the ETLA program. In the interim, IRS should expand the ETLA program to additional call sites to process the ever-increasing taxpayer demand for this electronic service while reducing the need to use more expensive Compliance function personnel.
2000-30-130	September 2000		<i>Opportunities Exist to Enhance the International Field Assistance Specialization Program</i>
		04/30/02	<u>F-2, R-1, P-1.</u> Improve the management information system by linking the International Field Assistance Specialization Program (IFASP) indicator to specific issues listed in the International Case Management System.
		06/01/03	<u>F-2, R-2, P-2.</u> Ensure international examiners gain greater access to IRS' Intranet so that the IFASP can accumulate and disseminate more information electronically, including an electronic referral form for IFASP assistance.
2000-10-145			<i>Improvements Are Needed to Ensure Control and Accountability Over Automated Data Processing Assets</i>
		06/01/02	<u>F-1, R-1, P-1.</u> Conduct quality reviews prior to forwarding the Automated Data Processing Property Certifications to the Chief Information Officer for final approval and certification to the Commissioner.
		07/01/02	<u>F-2, R-1, P-1.</u> Re-evaluate resource commitments needed to successfully implement the Single Point Inventory Function and elevate to the Deputy Commissioner Operations for resolution any staffing shortages that imperil successful implementation.
2000-30-146			<i>Opportunities Exist to Identify Unreported Taxes from Employer's Quarterly Federal Tax Returns</i>
		P-3: 07/01/02 P-4: 07/01/02	<u>F-1, R-1, P-3, P-4.</u> Increase <i>Employer's Quarterly Tax Return (Form 941)</i> compliance efforts.
2000-30-154			<i>Significant Improvements Are Needed in Processing Gift Tax Payments and Associated Extensions to File</i>
		01/01/03	<u>F-1, R-1, P-1.</u> Require that all balance due notices generated for gift tax accounts be reviewed. Tax examiners should be instructed to review the taxpayers' corresponding individual income tax and gift tax accounts to determine if the taxpayers' gift tax payments and extensions were correctly processed.
2000-20-158			<i>Additional Actions Are Needed to Strengthen the Development and Enforcement of the Enterprise Architecture</i>
		10/01/01	<u>F-5, R-2, P-1.</u> Establish a waiver process to approve minor deviations from the established architecture standards.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
2000-30-162	September 2000		<i>The Internal Revenue Service Needs to Better Address Bankruptcy Automatic Stay Violations</i>
		10/01/02	<u>F-1, R-2, P-1.</u> Provide additional computer programming enhancements to improve the value of litigation transcripts.
		04/01/02	<u>F-1, R-5, P-1.</u> Provide consistent guidelines to the SPf units on how to notify the Examination function that the taxpayer is in bankruptcy.
		P-1: 10/01/02 P-2: 08/01/02	<u>F-2, R-1, P-1, P-2.</u> Request that the Automated Insolvency System be reprogrammed so that the actual receipt date of the case can be input into the system to provide management with more accurate data on timeliness of input of new case information.
		P-1: 10/01/02 P-2: 08/01/02	<u>F-2, R-2, P-1, P-2.</u> Ensure that all employees review the Potentially Invalid Taxpayer report and resolve all cases promptly to ensure timely posting of the bankruptcy to the taxpayer's account.
2001-30-014	November 2000		<i>The Internal Revenue Service Does Not Effectively Use the Trust Fund Recovery Penalty as a Collection Enforcement Tool</i>
		02/01/03	<u>F-1, R-5, P-1.</u> Make programming changes to the Automated Trust Fund Recovery System to ensure that delinquent tax returns are addressed when making trust fund recovery penalty calculations.
2001-40-008		07/01/02	<i>Electronic Returns Were Processed Effectively</i> <u>F-2, R-1, P-4.</u> Develop national standards, goals, and procedural guidance to ensure consistent and effective customer service is provided by all processing site Help Desks.
2001-20-016		05/01/02	<u>F-1, R-2, P-1.</u> Mandate that all Internet-related activity logs from IRS firewall and proxy servers are retained and periodically reviewed to identify inappropriate accesses.
		05/01/02	<u>F-1, R-3, P-1.</u> Augment the vendor's blocking criteria list with other known inappropriate sites identified during monitoring efforts or from referrals.
		P-2: 05/01/02 P-4: 05/01/02	<u>F-1, R-4, P-2, P-4.</u> Consider the impact on IRS resources prior to deciding to implement a "limited personal use" Internet policy.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
2001-10-026	December 2000		<i>Additional Management Actions Are Needed to Ensure the Timely and Successful Modernization of the Tax Exempt and Government Entities Division</i>
		P-1: 09/30/01 P-2: 10/01/02	<u>F-3, R-1, P-1, P-2.</u> Ensure that the risks associated with Tax Exempt and Government Entities (TE/GE) Division core processes that could result in disruptions to customer service are identified and monitored. Also, all other TE/GE Division workaround processes to ensure that permanent solutions are in place and working as intended.
		12/31/01	<u>F-5, R-2, P-1.</u> Enhance the Service Level Agreement with the Information Systems organization to ensure the TE/GE Division receives sufficient support from the IS organization and establish a practice to resolve issues related to non-performance.
2001-40-024			<i>The Program for Ensuring Compliance With Anti-Money Laundering Reporting Requirements Should Be Improved</i>
		04/01/02	<u>F-2, R-2, P-1.</u> Improve tracking of productivity and achievement of performance indicators by ensuring reliable <i>Title 31</i> information is timely provided by field units.
		08/01/02	<u>F-1, R-7, P-1.</u> Ensure sufficient training is provided nationwide on a timely basis.
2001-20-022			<i>Controls Over the Development of the Practitioner Secure Messaging System Prototype Should Be Improved</i>
		06/01/02	<u>F-3, R-1, P-1.</u> Require the contractor to break down the total hours worked by task on each status report, break down by individual project the labor hours and other costs billed on each payment voucher, report as "current" (not "cumulative") all costs that are included on the payment voucher with an appropriate comment when the costs apply to another accounting period, and report the amount billed for each person's current hours.
2001-40-021	January 2001		<i>Additional Efforts Are Needed for Improving Revenue Protection</i>
		P-1: 10/01/02 P-2: 10/01/02	<u>F-1, R-1, P-1, P-2.</u> Ensure that the Revenue Protection Strategy (RPS) is a long-term strategic plan that is coordinated among functional areas. The RPS should recognize and take steps to defeat known fraud and abuse, as well as outline proactive measures for attempting to eliminate potential areas of fraud and abuse.
		P-1: 10/01/02 P-2: 10/01/02	<u>F-1, R-2, P-1, P-2.</u> Establish measurable goals and objectives to evaluate the effectiveness of the RPS. The goals and objectives should ensure that revenue is protected and taxpayer burden is reduced.
		P-1: 10/01/02 P-2: 10/01/02	<u>F-2, R-1, P-1, P-2.</u> Develop a process to measure the effectiveness of individual initiatives on reducing noncompliance, until the RPS is developed and implemented. Once developed, the RPS should also contain provisions for measuring the effect of its components on reducing noncompliance.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary
			(F = Finding Number, R = Recommendation Number, P = Plan Number)
2001-10-027	January 2001		<i>Improved Case Monitoring and Taxpayer Awareness Activities Can Enhance the Effectiveness of the Tax Practitioner Disciplinary Proceedings Program</i>
		03/01/03	<u>F-1, R-1, P-1.</u> Upgrade the automated case management system to provide more timely and accurate data on case activities and the use of program resources.
		07/01/02	<u>F-1, R-2, P-1.</u> Conduct an annual workload and staffing analysis to identify the staffing necessary to take prompt action on allegations of tax practitioner violations.
2001-20-043	February 2001		<i>Electronic Signature Initiatives Could Be Better Defined and Evaluated</i>
		05/01/02	<u>F-1, R-1, P-1.</u> Finalize IRS requirements for the use of Personal Identification Numbers as alternative signatures for electronically filed returns based on evolving guidance and the draft IRS authentication security policy and implementation
		guide. 07/01/02	<u>F-1, R-2, P-1.</u> Ensure that all operational alternative signature initiatives comply with the requirements.
2001-30-052	March 2001		<i>Program Improvements Are Needed to Encourage Taxpayer Compliance in Reporting Foreign Sourced Income</i>
		01/01/03	<u>F-1, R-1, P-1.</u> Ensure the prior recommendations are implemented. Establishing a formal program with goals, objectives, processes and measures could help ensure that sufficient management attention is devoted to improving the use of the Routine Exchange of Information Program for compliance.
		01/01/03	<u>F-2, R-1, P-1.</u> Identify the highest risk foreign sourced income documents and use them to coordinate with tax treaty partners to positively identify the U.S. taxpayers involved.
2001-30-063		P-1: 01/01/07 P-2: 01/01/07	<u>F-3, R-1, P-1, P-2.</u> Improve systems that process data IRS receives on foreign sourced income.
		04/01/02	<i>More Consideration Is Needed During Examinations to Identify Potential Fraud Issues and Refer Cases to Criminal Investigation</i> <u>F-1, R-2, P-1.</u> Continue demonstrating to front-line employees their commitment to the Fraud Referral Program and regularly emphasize the priority it has.
2001-30-099	June 2001	P-2: 07/10/03 P-3: 07/10/03	<i>Management Advisory Report: The Internal Revenue Service Could Reduce the Number of Business Tax Returns Destroyed Because of Missing Information</i> <u>F-1, R-1, P-2, P-3.</u> Make necessary modifications to tax forms and instructions to ensure taxpayers understand that their names, addresses, and taxpayer identification numbers are required on both their tax forms and payment vouchers.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
2001-30-099		05/01/02	<u>F-1, R-2, P-1.</u> Ensure that lockbox banks are provided clear instructions to review taxpayer identifying information on tax returns before separating the returns and payment vouchers.
2001-10-103	August 2001		<i>Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements</i>
		05/01/02	<u>F-1, R-1, P-1.</u> Clarify procedures to require that approving officials approve both the installment agreement or levy release and the <i>Tax Collection Waiver (Form 900)</i> simultaneously and ensure the revised collection statute expiration date is extended beyond the full payment date of the installment agreement.
		05/01/02	<u>F-1, R-2, P-1.</u> Correct the collection statute expiration dates on the 16 taxpayer accounts in which an installment agreement was not secured with the <i>Form 900</i> as required by <i>RRA 98 §3461(a)</i> .
		07/01/02	<u>F-2, R-1, P-1.</u> Develop a comprehensive plan for implementing the provisions of <i>RRA 98 §3461(c)</i> .
		05/01/02	<u>F-3, R-1, P-1.</u> Update the <i>Internal Revenue Manual</i> based on the IRS reorganization to reflect the new locations for storing signed collection statute extension forms in each of the new IRS business units.
		05/01/02	<u>F-1, R-3, P-1.</u> Correct the 27 taxpayer accounts in which the extended date on the <i>Form 900</i> does not match the date on the taxpayer's account as shown on the IRS' computer system.
		09/01/02	<u>F-4, R-1, P-1.</u> Provide training to applicable IRS employees and managers on the requirements and the method to compute installment agreements and collection statute extensions, consistent with the law and IRS policy and procedures.
2001-20-146			<i>The Internal Revenue Service Is Making Progress, But Is Not Yet in Full Compliance With the Requirements of the Clinger-Cohen Act</i>
		09/01/02	<u>F-1, R-1, P-1.</u> Prepare an overall strategy, plan and schedule to bring the IRS in full compliance with the <i>Clinger-Cohen Act</i> .
2001-30-117			<i>Letter Report: Additional Controls Are Necessary to Ensure that All Businesses Are Classified by Their Principal Business Activity</i>
		05/01/02	<u>F-1, R-1, P-1.</u> Identify business taxpayers by their principal business activity (PBA) from information provided on the <i>Application for Employer Identification Number (Form SS-4)</i> for entry to the IRS' masterfile.
		05/01/02	<u>F-2, R-1, P-1.</u> Implement processing controls to identify Individual Masterfile tax returns with invalid or missing PBA codes, and Business Master File Tax returns with invalid PBA codes for research and correction during processing.

Reference Number	Issued	Projected Completion Date	Report Title and Recommendation Summary (F = Finding Number, R = Recommendation Number, P = Plan Number)
2001-30-132		07/01/02	<i>Significant Tax Revenue May Be Lost Due to Inaccurate Reporting of Taxpayer Identification Numbers for Independent Contractors</i> F-2, R-1, P-1. Explore opportunities to supplement the IRS' future Internet-based Taxpayer Identification Number (TIN) confirmation program with an automated telephone-based TIN confirmation process for those payers who do not have Internet access.
		07/01/02	F-2, R-4, P-1. Initiate a proposal recommending changes to the criteria for asserting the Incorrect Information penalty.
2001-10-147	September 2001	07/01/03	<i>Compliance with Certain Taxpayer Rights Provisions Contained in the Internal Revenue Service Restructuring and Reform Act of 1998 Could Be Improved</i> F-1, R-2, P-1. Complete the request for programming changes for the Integrated Data Retrieval System, Automated Collection System, and Integrated Collection System to print detailed interest and penalty notices.
2001-30-148		06/01/02	<i>Tax Law Changes Are Needed to Improve Fairness in Paying Interest on Tax Refunds</i> F-1, R-2, P-1. Propose legislation that will require the same rate of interest be paid to all taxpayers.
2001-30-158		10/01/02	<i>Some Individual Taxpayers are Inappropriately Receiving Tax Credits Intended for Businesses that Provide Access for Disabled Americans</i> F-1, R-2, P-1. Analyze the results of TIGTA's computer program; perform similar analyses of Tax Year 2000 returns; and develop a compliance approach to address the issue of taxpayers fraudulently claiming this credit.
2001-30-164		07/01/02	<i>The Internal Revenue Service Has an Opportunity to Relieve Considerable Taxpayer Burden Involving the Estimated Tax Penalty</i> F-1, R-1, P-1. Evaluate the design and clarity of <i>Underpayment of Estimated Tax by Individuals, Estates and Trusts (Form 2210)</i> and its instructions in order to alleviate the excess taxpayer burden.
		10/01/02	F-1, R-2, P-1. Coordinate any redesign of <i>Form 2210</i> with both the practitioner and tax software communities.

Statistical Reports - Others

❑ **Access to Information**

The *Inspector General Act of 1978* requires IGs to report on unreasonable refusals of information available to the agency which relate to programs and operations for which the IG has responsibilities. As of March 31, 2002, TIGTA issued one report where information or assistance requested by OA was refused.

Reference No. 2002-10-009, *GPRA: Criminal Investigation Can Improve Its Performance Measures to Better Account for Its Results*

OA was unable to issue an opinion about the quality of the data used to report the CI business results due to a scope impairment. CI denied OA access to the CIMIS database by stating that it contained information related to cases under grand jury investigation, access to which is restricted by the *Federal Rules of Criminal Procedure (18 U.S.C. Appendix)*. The *Federal Rules of Criminal Procedure, Rule 6(e)*, require that only those individuals approved by a government attorney may have access to grand jury material, and then only in furtherance of the criminal aspects of the case.

❑ **Disputed Audit Recommendations**

The *Inspector General Act of 1978* requires IGs to provide information on significant management decisions in response to audit recommendations with which the IG disagrees.

As of March 31, 2002, TIGTA did not issue a report where a significant recommendation was disputed.

❑ **Revised Management Decisions**

The *Inspector General Act of 1978* requires IGs to provide a description and explanation of the reasons for any significant revised management decisions made during the reporting period.

As of March 31, 2002, no significant management decisions were revised.

❑ **Audit Reports Issued in the Prior Reporting Period With No Management Response**

The *Inspector General Act of 1978* requires IGs to provide a summary of each audit report issued before the beginning of the current reporting period for which no management response has been received by the end of the current reporting period.

As of March 31, 2002, they were no prior reports where management's response was not received.

❑ **Review of Legislation and Regulations**

The *Inspector General Act of 1978* requires IGs to review existing and proposed legislation and regulations and to make recommendations concerning the impact of such legislation or regulations.

TIGTA's Office of Chief Counsel reviewed 135 proposed legislation and regulations during the six-month reporting period.

Appendix IV - Audit Products Listing

Audit Products

October 1, 2001 - March 31, 2002

Inspector General Congressional Responses:

Reference Number	Issued	Report Title
2002-OR-029	11/13/01	<i>Senate Finance Committee – IRS Identification of Illegal Aliens</i>

Audit Reports:

Reference Number	Issued	Report Title
2002-40-003	10/09/01	<i>Letter Report: The Internal Revenue Service Is Contributing to the Decline in TeleFile Volumes</i> (Taxpayer Burden: 690,000 taxpayers that will be prevented from using TeleFile.)
2002-40-004	10/10/01	<i>Earned Income Credit Was Paid to Taxpayers Who Did Not Provide Required Documentation During Audits</i> (Revenue Protection: \$72,126 for 26 accounts.)
2002-10-001	10/12/01	<i>The Office of the Chief Counsel Has Made Significant Progress in Making Its Advice Documents Available to the Public</i> (Taxpayer Burden: 68 Chief Counsel Advice documents released for public inspection.)
2002-10-008	10/17/01	<i>Pricing Discrepancies on the Long Term Maintenance Computing Center Contract (TIRNO-96-D-0021)</i> (Questioned Costs: \$580,000)
2002-10-002	10/17/01	<i>The National Taxpayer Advocate Needs to Ensure Operations Employees Receive Training to Identify Cases</i>
2002-40-016	10/24/01	<i>While Most Taxpayers Received Accurate and Timely Notification of Their Advance Refunds, Millions Did Not</i> (Revenue Protection: \$117,600,000; Taxpayer Burden: 5,823,000 taxpayers who received an incorrect or delayed advanced refund notice.)
2002-20-007	10/11/01	<i>The Internal Revenue Service Encrypts Data Transmitted Between Its Facilities, But Controls Over Cryptography Can Be Improved</i> (Taxpayer Privacy and Security and Protection of Resources: In Fiscal Year 2000 over 210 million returns that the IRS processed, for which \$2 trillion was collected and \$194 billion refunded, were at risk of unauthorized disclosure and loss.)
2002-1C-013	10/23/01	<i>TIR-89-0056 and TIRNO-95-D-00062 Incurred Costs Audit For Fiscal Year Ended December 31, 1999</i>

Reference Number	Issued	Report Title
2002-1C-010	10/29/01	<i>Incurred Costs and Indirect Expense Rates Audit for Fiscal Year 1998: TIRNO-93-C-0026, TIRNO-93-D-0026 and TIRNO-93-D-0036</i>
2002-1C-011	10/29/01	<i>TIRNO-93-C-0026 Incurred Costs and Indirect Expense Rates Audit Fiscal Year 1999</i>
2002-1C-012	10/29/01	<i>Report on Audit of Civil Group's Proposed Indirect Expense and Cost of Money Rates for Forward Pricing and Provisional Billing Rates</i>
2002-1C-014	11/05/01	<i>TIRNO-95-D-00057 Incurred Costs Audit For Fiscal Year Ending August 31, 1999 (Questioned Costs: \$1,098,764)</i>
2002-1C-018	11/05/01	<i>Report on Audit of Telecommunications Services</i>
2002-10-017	11/06/01	<i>Management Advisory Report: Restricting the Release of Information Through the Exempt Organization Return Imaging Project (Taxpayer Privacy and Security: 281,153 Form 990 Returns require improved protection of personal information; Revenue Protection: \$104,400,000 in credit election payments on Form 990 Returns required improved protection.)</i>
2002-1C-015	11/10/01	<i>Report on Audit of Billing System Internal Controls</i>
2002-1C-019	11/13/01	<i>TIRNO-95-D-00066 Incurred Cost Audit for Fiscal Years Ended June 30, 1998 and 1999</i>
2002-10-006	11/15/01	<i>Improvements Are Needed in Establishing Yearly Offset Fees for the Treasury Offset Program (Funds Put to Better Use: \$1,100,000; Reliability of Information: \$13,877,087 in offset fees did not allow for full recovery of all program costs.)</i>
2002-20-025	11/16/01	<i>Modernization Project Teams Need to Follow Key Systems Development Processes</i>
2002-1C-023	11/19/01	<i>Audit of Final Vouchers TIRNO-95-D-00060 Task Order Numbers 1, 2, 3, 5, 6, 7, 8 and 9</i>
2002-10-005	11/26/01	<i>The Internal Revenue Service Has Taken Significant Actions, But Increased Oversight Is Needed to Fully Implement the Uniform Asset Disposal Mechanism</i>
2002-1C-022	11/27/01	<i>Report on Audit of Timekeeping Practices For Fiscal Year 2001</i>
2002-10-024	11/29/01	<i>The Internal Revenue Service Should Continue to Make Improvements to the Low-Income Taxpayer Clinic Grant Program (Protection of Resources: \$441,000 paid to 6 organizations that had internal control findings in their most recent Single Audit Act report.)</i>
2002-10-030	11/29/01	<i>Management Advisory Report: Review of Lost or Stolen Sensitive Items of Inventory at the Internal Revenue Service</i>

Reference Number	Issued	Report Title
2002-10-027	11/30/01	<i>The Internal Revenue Service Should Ensure That Its Data on the Treasury's Performance Reporting System Have Been Verified and Validated</i>
2002-20-026	11/30/01	<i>Improvements Are Needed in the Telecommunications Data Network Management Program</i> (Protection of Resources: \$1,900,000 was spent to upgrade WAN circuits that were disconnected after being used for 1 to 11 months.)
2002-40-020	11/30/01	<i>Better Controls Are Needed to Ensure Appropriated Funds Are Used to Improve the Application of the Earned Income Credit</i> (Protection of Resources: \$28 million in Earned Income Credit funds were used for questionable labor and equipment purchases.)
2002-1C-032	12/06/01	<i>Audit of Final Voucher TIRNO-95-D-00058 Task Order Number 5</i>
2002-40-034	12/07/01	<i>Implementation of the Remote Examination Toll-Free Telephone Program Is Ongoing</i> (Taxpayer Burden: 45,000 taxpayers not assigned to a single IRS auditor and 3,067 taxpayers accessed an erroneously recorded tax message.)
2002-40-028	12/11/01	<i>Management Advisory Report: New Job Description Gives Employees Broad Authority Without Additional Compensating Controls</i> (Protection of Resources: \$1.8 trillion in outstanding liabilities and \$2 trillion collected in the year 2000 were at risk.)
2002-1C-031	12/11/01	<i>Audit of Final Voucher TIRNO-95-D-00058 Task Order Number 2</i>
2002-1C-033	12/11/01	<i>Audit of Final Voucher TIRNO-95-D-00058 Task Order Number 7</i>
2002-1C-036	12/11/01	<i>Report on Estimating System and Internal Controls Follow-up Audit</i>
2002-1C-037	12/11/01	<i>Audit of Final Voucher TIRNO-95-D-00057 Task Order Number 6</i>
2002-1C-038	12/11/01	<i>Audit of Final Voucher TIRNO-95-D-00057 Task Order Number 7</i>
2002-1C-039	12/11/01	<i>Audit of Final Voucher TIRNO-95-D-00057 Task Order Number 13</i>
2002-30-040	12/14/01	<i>Increased Management Attention Is Needed to Ensure the Success of Future Notice Redesign Efforts</i>
2002-30-035	12/19/01	<i>Management Advisory Report: The Small Business/Self-Employed Division Needs to Further Consider the Impact of Potential Examination Reengineering Recommendations</i>
2002-30-042	12/19/01	<i>The Internal Revenue Service Has Made Some Progress, but Significant Improvements Are Still Needed to Reduce Errors in Manual Interest Calculations</i> (Increased Revenue: \$145,159,560 for 20,990 accounts; Taxpayer Rights and Entitlements: \$247,705,560 for 9,595 accounts.) Note: Monetary benefit projected over a five-year period.

Reference Number	Issued	Report Title
2002-40-021	12/20/01	<i>There Are Significant Weaknesses in the Internal Revenue Service's Efforts to Measure Earned Income Credit Compliance (Revenue Protection: \$557,058 for 831 accounts; Taxpayer Burden: 3,349 taxpayers needlessly audited; Reliability of Information: 308 audit cases with incomplete information.)</i>
2002-30-041	12/26/01	<i>Management Advisory Report: The Small Business/Self-Employed Division Has Made Significant Progress in Addressing Its Human Capital Needs but Still Must Plan for Long-Term Challenges</i>
2002-20-043	01/09/02	<i>Improvements Are Needed in the Management of Mid-Level Computer Consolidation to Ensure the Accomplishment of Project Goals (Reliability of Information: \$7,840,771 in improperly captured project costs and a revised business case needed to more accurately project \$153,143,521 in investments benefits.)</i>
2002-20-045	01/17/02	<i>Controls Over the Procurement Web Site Should Be Improved to Better Deter and Detect External Attacks</i>
2002-1C-047	01/22/02	<i>Audit of Estimating System Internal Controls</i>
2002-10-009	01/28/02	<i>GPRA: Criminal Investigation Can Improve Its Performance Measures to Better Account for Its Results</i>
2002-30-048	1/29/02	<i>Management Advisory Report: Significantly More Individual Taxpayers Inappropriately Received Disabled Access Credits for Tax Year 2000 Than for 1999</i>
2002-1C-049	1/31/02	<i>Report on Adequacy and Compliance of Revised Disclosure Statement, Dated August 3, 2001</i>
2002-20-044	1/31/02	<i>The System-Level Controls Over the Security and Communications System Are Adequate; However, Improvements Can Be Made (Taxpayer Rights and Entitlements and Taxpayer Burden: Computer system contains over 26.4 million individual and business accounts that are available for inquiry each week.)</i>
2002-10-053	02/01/02	<i>Attestation Review of the Internal Revenue Service's Fiscal Year 2001 Annual Accounting of Drug Control Funds</i>
2002-40-051	02/15/02	<i>The Internal Revenue Service Could Improve Its Process to More Reliably Measure the Accuracy of Its Toll-Free Tax Law Assistance (Reliability of Information: IRS-developed Customer Service error rate of 73.78 percent may not be accurate.)</i>
2002-10-052	2/15/02	<i>Management Advisory Report: The Criminal Investigation Function Needs to Monitor the Lead Development Centers to Minimize the Risks Associated with the Accelerated Rollout</i>

Reference Number	Issued	Report Title
2002-30-055	2/27/02	<i>Federal Requirements Need Strengthening at Lockbox Banks to Better Protect Taxpayer Payments and Safeguard Taxpayer Information</i>
2002-30-050	2/27/02	<i>Significant Efforts Have Been Made to Combat Abusive Trusts, but Additional Improvements Are Needed to Ensure Fairness and Compliance Objectives Are Achieved (Increased Revenue: \$138,200,000) Note: Monetary benefit projected over a two-year period.</i>
2002-30-054	2/25/02	<i>The Centralization of Business Tax Return Processing to Two Submission Processing Centers Is on Schedule, but Disaster Contingency Plans Must Be Updated and Tested</i>
2002-20-056	03/01/02	<i>The Customer Communications Project 2001 Release Was Deployed, but Testing Processes Did Not Ensure All Applications Were Working As Intended</i>
2002-20-057	03/01/02	<i>Management Advisory Report: Network Penetration Study of Internal Revenue Service Systems</i>
2002-20-059	03/01/02	<i>The Business Systems Modernization Office Needs to Strengthen Its Processes for Overseeing the Work of the PRIME Contractor</i>
2002-40-058	03/05/02	<i>The Wage and Investment Division Properly Planned for the 2002 Toll-Free Telephone Operation</i>
2002-10-065	03/08/02	<i>Management Advisory Report: Follow-On Review of Lost or Stolen Sensitive Items of Inventory at the Internal Revenue Service</i>
2002-30-062	03/12/02	<i>The Internal Revenue Service Continues to Owe Millions of Dollars in Interest to Taxpayers with Frozen Refunds (Funds Put to Better Use: \$12,900,000) Note: Monetary benefit projected over a five-year period.</i>
2002-40-046	03/12/02	<i>Improvements Need to Be Made to Publications and Instructions to Assist Taxpayers in Successfully Signing Their Tax Returns Electronically (Taxpayer Burden: 26,000,000 taxpayers who filed electronically but did not sign with an electronic signature.)</i>
2002-30-060	03/15/02	<i>Improvements Are Needed to Enable the National Non-filer Strategy to Achieve Its Objectives</i>
2002-40-067	03/26/02	<i>Management Advisory Report: Numerous Efforts Are Taken to Educate Taxpayers on Innocent Spouse Eligibility Requirements (Taxpayer Burden: 1,250,000 taxpayers who received two publications containing insufficient information.)</i>
2002-10-068	03/27/02	<i>Appeals Is Generally Complying With the Requirements of the Law for Lien and Levy Appeals Cases (Taxpayer Rights and Entitlements: 39 Appeals hearings and 98 determination letters did not follow all the provisions of the law or follow established Appeals guidelines.)</i>

Reference Number	Issued	Report Title
2002-10-069	03/27/02	<i>Management Advisory Report: The Internal Revenue Service's Federal Financial Management Improvement Act Remediation Plan Complies With Reporting Requirements</i>
2002-10-072	03/27/02	<i>The Large and Mid-Size Business Division's Risk Analysis Process Complies With Legal Guidelines, but Its Use Should Be Clarified</i>
2002-10-079	03/28/02	<i>Taxpayer Advocate Service Employees Made Adjustments to Taxpayer Accounts Without Proper Authorization</i>
2002-20-063	03/28/02	<i>Controls Over the LexisNexis Connection Should Be Improved to Better Deter and Detect External Attacks</i>
2002-30-071	03/28/02	<i>Computer Programming Can Be Used to More Effectively Stop Refunds on Illegal Claims for Repairs Credits (Revenue Protection: \$90,731,930 for 2,880 accounts.) Note: Monetary benefit projected over a five-year period.</i>
2002-30-076	03/28/02	<i>Interim Actions Can Be Taken to Determine Partnerships' Compliance in Withholding Taxes on Foreign Partners</i>
2002-10-070	03/29/02	<i>Taxpayers Should Be Informed of the Benefits of the Fast Track Mediation Program (Taxpayer Burden: 26,000 taxpayers not offered Fast Track Mediation.)</i>
2002-10-077	03/29/02	<i>Taxpayer Burden Can Be Reduced By Ensuring That Taxpayers Have Accurate Information for Submitting Power of Attorney Forms</i>
2002-10-078	03/29/02	<i>The Internal Revenue Service's Levy Process Can Be Improved to Ensure Compliance With the Internal Revenue Code (Improper release of levies increasing Taxpayer Burden for 13 accounts and affecting Taxpayer Rights and Entitlements for 4 accounts; Reliability of Information: 37 accounts erroneously closed and 197 accounts with payments erroneously coded.)</i>
2002-20-074	03/29/02	<i>Sensitive Information on Excessed Computers Needs To Be More Effectively Safeguarded (Funds Put to Better Use: \$4,650)</i>
2002-20-075	03/29/02	<i>User Activity on Most Sensitive Computer Systems Is Not Monitored</i>
2002-40-080	03/29/02	<i>The Internal Revenue Service Certifies Its Readiness to Process Individual Income Tax Returns in 2002</i>

TIGTA audit reports are available online at <http://treas.gov/tigta>

Appendix V – Statutory TIGTA Reporting Requirements

In FY 2001, TIGTA completed its third round of statutory reviews that are required annually by *RRA 98*. The following table reflects the status of the FY 2002 *RRA 98* statutory reviews. Eleven statutory audit reports that dealt with the adequacy and security of IRS technology were issued during this reporting period.¹

Reference to Statutory Coverage	Explanation of the Provision	Comments/TIGTA Audit Status
Enforcement Statistics <i>I.R.C. § 7803(d)(1)(A)(i)</i>	An evaluation of IRS' compliance with restrictions under Section 1204 of <i>RRA 98</i> on the use of enforcement statistics to evaluate IRS employees.	Audit fieldwork in process.
Restrictions on Directly Contacting Taxpayers <i>I.R.C. § 7803(d)(1)(A)(ii)</i>	An evaluation of IRS' compliance with restrictions under <i>I.R.C. § 7521</i> on directly contacting taxpayers who have indicated that they prefer their representatives be contacted.	Audit has not yet been initiated.
Filing of a Notice of Lien <i>I.R.C. § 7803(d)(1)(A)(iii)</i>	An evaluation of IRS' compliance with required procedures under <i>I.R.C. § 6320 (Supp. IV 1998)</i> upon the filing of a notice of lien.	Audit fieldwork in process.
Levies <i>I.R.C. § 7803(d)(1)(A)(iv)</i>	An evaluation of IRS' compliance with required procedures under <i>I.R.C. § 6330 (Supp. IV 1998)</i> regarding levies.	Audit fieldwork in process.

¹ This includes 6 audit reports on the security of IRS technology, and 5 audit reports on IRS information technology. All information technology program reviews are considered statutory based on the *RRA 98* requirement to report annually on the adequacy and security of IRS technology.

Reference to Statutory Coverage	Explanation of the Provision	Comments/TIGTA Audit Status
Collection Due Process <i>I.R.C. § 7803(d)(1)(A)(iii) and (iv)</i>	An evaluation of IRS' compliance with required procedures under <i>I.R.C. §§ 6320 and 6330 (Supp. IV 1998)</i> regarding the taxpayers' rights to appeal lien or levy actions.	<p><i>Reference Number 2002-10-068, March 2002.</i></p> <p>In 85 of the 87 cases reviewed (98 percent), the IRS generally complied with the requirements of the law and ensured taxpayers' appeal rights were protected. However, in 2 of the 87 cases, the IRS did not always follow all the requirements of the law. In these instances, Appeals Officers either did not adequately balance the efficiency of the proposed collection action against the taxpayer's legitimate concerns that the action be no more intrusive than necessary or did not obtain adequate verification from the IRS that all regulations had been met. OA does not believe that in either of these cases the noncompliance resulted in a legal violation of the taxpayer's Collection Due Process rights since no collection actions were ever initiated.</p> <p>Additionally, in 82 of the 87 cases, Appeals appropriately communicated the decision to taxpayers. These results indicate an improvement in communicating Appeals' decisions to taxpayers when compared to the prior year's audit. Ensuring all determination letters completely outline all the provisions of the law considered in the decision and by ensuring all established guidelines are followed could make further improvements. The <i>Code of Federal Regulations (CFR)</i>, 26 <i>CFR 301.6330-1T(e)(Q-E7)</i>, and Appeals procedures state that the letters must address all issues raised by the taxpayer and whether the IRS followed all the applicable rules and administrative procedures and balanced tax collection with the taxpayers' legitimate concerns. The IRS guidelines also require the letters to provide information concerning which court the taxpayer must file his/her request for judicial review, as well as information about any agreements reached during the hearing and the actions to be taken by the IRS or the taxpayer.</p>
Seizures <i>I.R.C. § 7803(d)(1)(A)(iv)</i>	An evaluation of IRS' compliance with required procedures under <i>Subchapter D of Chapter 64</i> for seizure of property for collection of taxes.	Audit fieldwork in process.
Taxpayer Designations – Illegal Tax Protester Designation and Nonfiler Designation <i>I.R.C. § 7803(d)(1)(A)(v)</i>	An evaluation of IRS' compliance with restrictions under <i>Section 3707 of RRA 98</i> on designation of taxpayers.	Audit fieldwork in process.

Reference to Statutory Coverage	Explanation of the Provision	Comments/TIGTA Audit Status
Disclosure of Collection Activities With Respect to Joint Returns <i>I.R.C. 7803(d)(1)(B)</i> <i>I.R.C. § 6103(e)(8)</i>	Review and certify whether or not IRS is complying with <i>I.R.C. § 6103(e)(8)</i> to disclose information to an individual filing a joint return on collection activity involving the other individual filing the return.	Audit is in planning process.
Taxpayer Complaints <i>I.R.C. § 7803(d)(2)(A)</i>	Requires TIGTA to include in each of its <i>Semiannual Reports to Congress</i> the number of taxpayer complaints received and the number of employee misconduct and taxpayer abuse allegations received by IRS or TIGTA from taxpayers, IRS employees and other sources.	Audit has not yet been initiated.
Administrative or Civil Actions With Respect to the Fair Debt Collection Practices Act of 1996 <i>I.R.C. § 7803(d)(1)(G)</i> <i>I.R.C. § 6304</i> <i>Section 3466 of RRA 98</i>	Include information regarding any administrative or civil actions with respect to violations of the fair debt collection provision of <i>I.R.C. § 6304</i> , including a summary of such actions, and any resulting judgments or awards granted.	Audit fieldwork in process.
Denial of Requests for Information <i>I.R.C. § 7803(d)(1)(F)</i> <i>I.R.C. § 7803(d)(3)(A)</i>	Include information regarding improper denial of requests for information from IRS based on a statistically valid sample of the total number of determinations made by IRS to deny written requests to disclose information to taxpayers on the basis of <i>I.R.C. § 6103</i> or <i>5 U.S.C. § 552(b)(7)</i> .	Draft report issued March 26, 2002.
Extensions of the Statute of Limitations for Assessment of Tax <i>I.R.C. § 7803(d)(1)(C)</i> <i>I.R.C. § 6501</i>	Include information regarding extensions of the statute of limitations for assessment of tax under <i>I.R.C. § 6501</i> and the provision of notice to taxpayers regarding the right to refuse or limit the extension to particular issues or a particular period of time.	Audit fieldwork in process.

Reference to Statutory Coverage	Explanation of the Provision	Comments/TIGTA Audit Status
<p>Adequacy and Security of the Technology of the IRS</p> <p><i>I.R.C. § 7803(d)(1)(D)</i></p>	<p>Evaluation of IRS' adequacy and security of its technology.</p>	<p>The consolidated status of IRS' adequacy and security of its technology for this reporting period is highlighted on pages 8-10.</p> <p><i>Security Reviews:</i></p> <p>Reference No. 2002-20-007, October 2001 Reference No. 2002-20-044, January 2002 Reference No. 2002-20-045, January 2002 Reference No. 2002-30-054, February 2002 Reference No. 2002-20-057, March 2002 Reference No. 2002-20-063, March 2002</p> <p><i>Information Technology:</i></p> <p>Reference No. 2002-20-025, November 2001 Reference No. 2002-20-026, November 2001 Reference No. 2002-20-043, January 2002 Reference No. 2002-20-056, March 2002 Reference No. 2002-20-059, March 2002</p>

Appendix VI - Section 1203 Standards

In general, the Commissioner of IRS shall terminate the employment of any employee of IRS if there is a final administrative or judicial determination that in the performance of official duties such employee committed the misconduct violations outlined below. Such termination shall be a removal for cause on charges of misconduct.

Misconduct violations include:

- Willful failure to obtain the required approval signatures on documents authorizing the seizure of a taxpayer's home, personal belongings, or business assets.
- Providing a false statement under oath with respect to a material matter involving a taxpayer or taxpayer representative.
- Violating, with respect to a taxpayer, taxpayer representative, or other employee of IRS,
 - any right under the *Constitution of the United States*, or
 - any civil right established under *Title VI or VII of the Civil Rights Act of 1964*,¹ *Title IX of the Education Amendments of 1972*,² *Age Discrimination in Employment Act of 1967*,³ *Age Discrimination Act of 1975*,⁴ *Section 501 or 504 of the Rehabilitation Act of 1973*,⁵ or *Title I of the Americans with Disabilities Act of 1990*.⁶
- Falsifying or destroying documents to conceal mistakes made by any employee with respect to a matter involving a taxpayer or taxpayer representative.
- Committing assault or battery on a taxpayer, taxpayer representative, or other employee of IRS, but only if there is a criminal conviction, or a final judgment by a court in a civil case, with respect to the assault or battery.
- Violating of the *Internal Revenue Code of 1986*, Treasury regulations, or policies of IRS (including the *Internal Revenue Manual*) for the purpose of retaliating against, or harassing a taxpayer, taxpayer representative, or other employee of IRS.
- Willfully misusing provisions of *Section 6103 of the Internal Revenue Code of 1986* for the purpose of concealing information from a congressional inquiry.

¹ *Pub. L. No. 88-352, 78 Stat. 241* (codified as amended in 42 U.S.C. § 2000e).

² 20 U.S.C. §§ 1681-1688 (1994).

³ 29 U.S.C. §§ 621-634 (1994 & Supp. IV 1998).

⁴ 42 U.S.C. §§ 6101-6107 (1994 & Supp. IV 1998).

⁵ *Pub. L. No. 93-112, 87 Stat. 355* (codified as amended in 29 U.S.C. §§ 701 & 794).

⁶ 42 U.S.C. §§ 12111 et seq. (1994 & Supp. IV 1998).

- Willfully failing to file any return of tax required under the *Internal Revenue Code of 1986* on or before the date prescribed therefor (including any extensions), unless such failure is due to reasonable cause and not to willful neglect.
- Willfully understating federal tax liability, unless such understatement is due to reasonable cause and not to willful neglect, and,
- Threatening to audit a taxpayer for the purpose of extracting personal gain or benefit.

In general, the IRS Commissioner may take a personnel action other than employment termination for the misconduct violations outlined above. The exercise of this authority shall be at the sole discretion of the Commissioner and may not be delegated to any other officer. The Commissioner, in his/her sole discretion, may establish a procedure which will be used to determine whether an individual should be referred to the Commissioner for a determination by the Commissioner. Any determination of the Commissioner in these matters may not be appealed in any administrative or judicial proceeding.

TIGTA HOTLINE

Reporting Fraud, Waste and Abuse - If you are aware of fraud, waste, mismanagement, and abuse in the IRS programs and operations, report it to the TIGTA Hotline!

Call

1-800-366-4484

Fax

(202) 927-7018

Write

**Treasury Inspector General for Tax Administration
P.O. Box 589
Ben Franklin Station
Washington, D.C. 20044-0589**

**Information is confidential and you may remain
anonymous**

**For Tax Problem Assistance
Call the IRS Taxpayer Advocate at:
1-877-777-4778**

DEPARTMENT OF THE TREASURY

Office of the Inspector General for Tax Administration

1125 15th Street, NW, Room 700A

Washington, D.C. 20005



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