Compliance With the Internal Revenue Service Restructuring and Reform Act of 1998 Section 1204 Has Not Yet Been Achieved

September 2001

Reference Number: 2001-10-178

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

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

September 27, 2001

MEMORANDUM FOR COMMISSIONER ROSSOTTI

Pamela J. Gardiner

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Compliance With the Internal Revenue Service Restructuring and Reform Act of 1998 Section 1204 Has Not Yet Been Achieved

This report presents the results of our review of restrictions on the use of enforcement statistics. The overall objective of this review was to determine if the Internal Revenue Service (IRS) complied with legal guidelines set forth in the IRS Restructuring and Reform Act of 1998 (RRA 98)[1] Section (§) 1204.

RRA 98 § 1204 (a) prohibits the IRS from using a record of tax enforcement results (ROTER) to evaluate employees or to impose or suggest production quotas or goals. Section 1204 (b) requires that employees be evaluated using the fair and equitable treatment of taxpayers as a performance standard. The IRS' procedures require all managers of enforcement employees to complete the RRA 98 § 1204 Manager's Self-Certification Form for each quarter and require appropriate supervisors to maintain an office file of the certifications. The Treasury Inspector General for Tax Administration is required under 26 U.S.C. § 7803(d)(1)(A)(i) (1999) to annually evaluate the IRS' compliance with the provisions of RRA 98 § 1204.

In summary, we found that the IRS has not yet achieved compliance with RRA 98 § 1204. Potential violations of RRA 98 §§ 1204 (a) and (b) were identified in 16 of

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[1] Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

the 200 sampled enforcement employees' performance or related supervisory documentation.

- ROTERs, production quotas, or goals were identified in performance and related supervisory files for 2 of the 200 sampled enforcement employees. These potential violations occurred because some IRS managers either misunderstood or did not follow IRS procedures.
- IRS managers could not substantiate use of the fair and equitable treatment of taxpayers as a performance standard to evaluate 14 of 200 sampled enforcement employees. This occurred because the IRS has not yet incorporated this performance standard into the appraisal form for all employees. The IRS plans to update the appraisal forms by October 2001.

Management's Response: Organizational Performance Division (OPD) management agreed to take appropriate action on the potential violations reported. In addition, they offered clarification of their self-certification procedures and a concern that the precision values in our statistical projections are understated. Management's complete response to the draft report is included as Appendix V.

Office of Audit Comment: We agree with IRS management's comment regarding their guidelines which require § 1204 first-line mangers to complete quarterly self-certifications and forward them to their § 1204 appropriate supervisor. However, neither the first-line supervisors nor any other level of IRS management, including at least 1 appropriate supervisor, could provide copies of self-certifications in 46 instances for 25 sampled employees. OPD management requested that we work with the IRS Commissioner's Representative in the local IRS offices. We attempted to locate these self-certifications through the first-line supervisors and the IRS Commissioner's Representatives (some of whom are appropriate supervisors), and we provided the opportunity, through August 30, 2001, for the OPD to locate the missing self-certifications.

In addition, our statistical projections and precision values were developed in consultation with a professional statistician according to sound statistical principles.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendation. Please contact me at (202) 622-6510 if you have questions or John R. Wright, Acting Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

Table of Contents

Compliance With the Internal Revenue Service Restructuring and Reform Act of 1998 Section 1204 Has Not Yet Been Achieved

Background

On July 22, 1998, the President signed the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)[1] into law.

- RRA 98 § 1204 (a) prohibits the IRS from using a record of tax enforcement results (ROTER) to evaluate employees or to impose or suggest production quotas or goals.
- RRA 98 § 1204 (b) requires that employees be evaluated using the fair and equitable treatment of taxpayers as a performance standard.
- RRA 98 § 1204 (c) requires each appropriate supervisor to certify quarterly whether tax enforcement results were used in a prohibited manner. The IRS defines an appropriate supervisor as the highest ranking executive in a distinct organizational unit that supervises directly or indirectly one or more Section 1204 employees.[2]

  IRS procedures require that, beginning with first-line managers of § 1204 employees, each level of management must self-certify that they have not used records of tax enforcement results in a manner prohibited by RRA 98 § 1204. This information is forwarded to the appropriate supervisor for each office. The appropriate supervisor is required to maintain an office file of the certifications.

The IRS defines ROTERs as data, statistics, compilations of information, or other numerical or quantitative recordations of the tax enforcement results reached in one or more cases. ROTERs do not include the tax enforcement results of individual cases when used to determine whether an employee exercised appropriate judgment in pursuing enforcement of the tax laws based upon a review of the

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[1] Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

[2] An enforcement employee (1204 employee) is an employee who exercises judgment in recommending or determining whether or how the IRS should pursue enforcement of the tax laws.

employee's work on that individual case. Examples of ROTERs include information such as the amount of dollars collected or assessed, the number of fraud referrals, and the number of seizures conducted.

The 26 U.S.C. § 7803 (d)(1)(A)(i) (1999) requires the Treasury Inspector General for Tax Administration (TIGTA) to determine annually whether the IRS is in compliance with restrictions on the use of enforcement statistics. The TIGTA previously evaluated the IRS' compliance with RRA 98 § 1204 provisions in both Fiscal Years (FY) 1999 and 2000.

- In FY 1999,[3] the TIGTA reported that the IRS had controls in place to identify and report violations; however, there were still instances when ROTERs were used to evaluate employees or to impose or suggest production quotas or goals.
- In FY 2000,[4] the TIGTA reported that most employee evaluations and management documents did not contain tax enforcement results and did not impose production quotas and goals. However, employees were not always provided with or evaluated on the performance standard requiring the fair and equitable treatment of taxpayers.

IRS management is still implementing corrective actions from the TIGTA FY 2000 report. These actions, when completed, should improve the IRS' compliance with the requirements of RRA 98 § 1204.

The audit was performed between January and August 2001. It was conducted in accordance with *Government Auditing Standards*. The sample of enforcement employees included in our review had the opportunity to be selected from any

[3] *The Internal Revenue Service Should Continue Its Efforts to Achieve Full Compliance with Restrictions on the Use of Enforcement Statistics* (Reference Number 1999-10-073, dated September 1999).

[4] *Further Improvements Are Needed in Processes That Control and Report Misuse of Enforcement Statistics* (Reference Number 2000-10-118, dated September 2000).

IRS office within the continental United States.[5] Our sampling methodology prevented us from fully testing the IRS' compliance with RRA 98 § 1204 (c). However, we did perform tests of the IRS' procedures used to ensure compliance with RRA 98 § 1204 (c). Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

The Internal Revenue Service Has Not Yet Achieved Compliance With RRA 98 Section 1204 and Its Own Procedures

The IRS has not yet achieved compliance with RRA 98 § 1204. Potential violations of RRA 98 § 1204 were identified in 16 of the 200 sampled enforcement employees' performance or related supervisory documentation. In addition, IRS managers of enforcement employees could not substantiate compliance with the IRS' procedures by providing proof that they completed the RRA 98 § 1204 Manager's Self-Certification Form in 46 instances affecting 25 employees. Documentation reviewed included Employee Personnel Files (EPF), consisting of documents, such as annual and mid-year performance appraisals, self-assessments, drop files, workload reviews, and award narratives.

In addition, related supervisory documents, such as read files, minutes of meetings, local procedures, and guidance, were reviewed when available. IRS procedures do not require managers to maintain these documents.

Records of tax enforcement results were used to evaluate employees or to impose production quotas or goals

ROTERs, production quotas, or goals were identified in performance and related supervisory files for 2 of the 200 sampled enforcement employees.[6] These potential RRA 98 § 1204 (a) violations include the following:

- A manager wrote in an employee's workload review that part of the District's Business Plan is to try to increase

[5] The locations included in our sample were California, Georgia, Kentucky, Maryland, Minnesota, Tennessee, Texas, and West Virginia.

[6] Projected across the estimated population of 45,288 enforcement employees, similar violations could affect 452 employees in the continental United States.

efforts to secure full payment or installment agreements on closed cases. In another workload review for this employee, the manager wrote similar comments about the District's Business Plan.

The district had no such plan at the time of the evaluation and the manager simply made an error by "cutting and pasting" information from a prior document. However, this could be perceived by the employee as setting quotas or goals. RRA 98 § 1204 (a) prohibits imposing or suggesting production quotas or goals.

- Another manager mentioned in an employee's annual performance appraisal that the employee had finalized a major investigation in which the employee recommended tax charges against two individuals.

  It was clear that the employee was not evaluated using this information; however, it is a potential technical violation of RRA 98 § 1204 (a). IRS guidelines define the number of indictments and investigations recommended for prosecution as a ROTER. The IRS also identified this as a ROTER during the self-certification process. However, it was never removed from the employee's evaluation.

The two potential violations that we identified occurred because IRS managers either misunderstood or did not follow IRS procedures. Although, one of the two potential violations was identified by IRS management during the self-certification process, the manager did not correct the violation by eliminating the ROTER from the employee's evaluation. The evaluation in the EPF was the original one containing the ROTER, and the manager was unable to provide us with a copy of the revised evaluation. One of these two employees was not selected for review as part of the IRS' independent review. We could not determine if the other employee was part of the independent review.

The use of enforcement statistics in performance and related supervisory files could be perceived by IRS employees as a method of suggesting production quotas or goals. Although we identified only two potential violations, the IRS reported a total of 186 violations identified through the Independent Review and the Self-Certification process.[7] These violations can increase the risk that employees will focus on achieving perceived goals through inappropriate or abusive enforcement actions, such as unwarranted seizures or unreasonable tax assessments, rather than creating a quality work product. Inappropriate or abusive enforcement actions could lead to potential violations of taxpayer rights.

IRS management is revising its independent review process guidelines and will conduct a special assurance review of the independent review process. These actions were in response to our FY 2000 report and should improve the IRS' ability to detect and correct violations of RRA 98 § 1204. These corrective actions are not scheduled for full completion until the third quarter of FY 2002.

Use of the fair and equitable treatment of taxpayers performance standard could not always be substantiated

IRS managers could not substantiate use of the fair and equitable treatment of taxpayers as a performance standard when evaluating 14 of 200 sampled enforcement employees.[8] This provision was enacted to provide assurance that employee performance is focused on providing quality service to taxpayers instead of achieving enforcement results.

In most instances, this performance standard was distributed as a separate document and managers either misplaced or forgot to complete it when evaluating employees during FY 2000. This occurred because the IRS has not yet incorporated this performance standard into the appraisal form for all employees. As a result, the IRS could not always validate its compliance with RRA 98 § 1204 (b).

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[7] The period for the Independent Review was July 1, 1999, through June 30, 2000. Violations of the Self-Certification process are for the FY 2000.

[8] Projected across the estimated population of 45,288 enforcement employees, similar violations could affect 3,170 employees in the continental United States.

The TIGTA FY 2000 report recommended that the IRS incorporate the standard into the Critical Job Elements of non-managerial employees. This is scheduled for full implementation on October 1, 2001. When completed, this should greatly reduce or eliminate the recurrence of these potential violations.

We projected our findings to the estimated population of 45,288 enforcement employees as of October 7, 2000. According to the projection, potential violations of RRA 98 § 1204 (a) or (b) could affect an estimated 3,623 enforcement employees (± 5.9 percent). We are 95 percent confident that the range of enforcement employees affected by similar occurrences is between 969 and 6,277.

Managers could not always substantiate completion of quarterly self-certifications

IRS managers of employees in our sample could not substantiate that they certified whether tax enforcement results were used in a prohibited manner in 46 instances for 25 of the sampled employees.[9] For 45 of these instances, the managers stated that they complied with IRS procedures but could not provide us with copies of their self-certifications. One of the managers for an employee in our sample did not forward a self-certification for the employee to the appropriate supervisor.

In some instances, managers could not provide copies of self-certifications for 1 of the 4 quarters in FY 2000. In other instances, copies of certifications could not be provided for all 4 quarters.

IRS procedures require that each enforcement manager must complete the RRA 98 Section 1204 Manager's Self-Certification Form each quarter and forward the form to the next level of management. Each level of management

[9] Projected across the estimated population of 45,288 enforcement employees, similar violations could affect 5,661 employees in the continental United States.

reports a cumulative number of violations identified by the lower level of management.

Appropriate supervisors are required by RRA 98 § 1204 (c) to certify quarterly whether tax enforcement results were used in a prohibited manner. They report the total cumulative number of violations reported by the subordinate managers and are also required to maintain an office file of their self-certifications and the certifications of their subordinate managers.

Examples of appropriate supervisors include the former District Directors, who were responsible for maintaining all the forms for managers in their districts. On October 1, 2000, the IRS reorganized, eliminating District and Regional offices and replacing them with business units, such as the Wage and Investment Division and the Small Business/Self-Employed Division. The restructuring also eliminated management positions, such as District Directors and Regional Commissioners.

Elimination of the management positions contributed to the unavailability of most of the 46 instances where self-certifications were not available because the first-line managers forwarded the documents to District and Regional Offices that no longer existed. Many of the local managers stated that the transition to the new organization was the reason the forms could not be located and that they were not sure who had responsibility for retaining these documents.

We did not test for legal compliance with RRA 98 § 1204 (c); to verify that would have required us to review each level of management below the appropriate supervisor. IRS management determined that they complied with RRA 98 § 1204 (c) because all appropriate supervisors properly certified.

Although we did not specifically test for this condition, our audit tests reviewed the process that IRS management uses to ensure compliance with RRA 98 § 1204 (c). IRS management cannot be assured that their process for certifying RRA 98 § 1204 (c) was effective because neither TIGTA nor IRS management could locate all self-certifications of managers for employees in our sample;

and because we identified one instance where a manager did not complete a self-certification, yet the appropriate supervisor certified as having received the self-certification from the lower level manager.

We projected our findings to the estimated population of 45,288 enforcement employees as of October 7, 2000. According to the projections, potential violations of IRS procedures could affect 5,661 enforcement employees (± 10.6 percent). We are 95 percent confident that the range of enforcement employees affected by similar procedural violations is between 848 and 10,474.[10]

Recommendation

1. The Commissioner, Small Business/Self-Employed Division, and Chief, Criminal Investigation, should review the performance and related supervisory files that we identified as containing potential violations of RRA 98 § 1204 (a). The potential violations should be discussed with the managers to prevent recurrence of the violations. Where appropriate, the documents should be revised.

Management's Response: The Director for the Organizational Performance Division (OPD) will contact the respective division and functional unit to ensure that the potential violations of RRA 98 § 1204 (a) identified in the report are reviewed. These organizational units will discuss the potential violations with the managers and take appropriate action.

In addition, OPD management offered clarification of their self-certification procedures and a concern that the precision values in our statistical projections are understated.

Office of Audit Comment: We agree with IRS management's comment regarding their guidelines which require § 1204 first-line managers to complete quarterly self-certifications and forward them to their § 1204 appropriate supervisor. However, neither the first-line

[10] See Appendix IV for an explanation of our projections.

supervisors nor any other level of IRS management, including at least 1 appropriate supervisor, could provide copies of self-certifications in 46 instances for 25 sampled employees. OPD management requested that we work with the IRS Commissioner's Representative in the local IRS offices. We attempted to locate these self-certifications through the first-line supervisors and the IRS Commissioner's Representatives (some of whom are appropriate supervisors), and we provided the opportunity, through August 30, 2001, for the OPD to locate the missing self-certifications.

In addition, our statistical projections and precision values were developed in consultation with a professional statistician according to sound statistical principles.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine if the Internal Revenue Service (IRS) complied with legal guidelines set forth in the IRS Restructuring and Reform Act of 1998 (RRA 98)[1] Section (§) 1204. We performed the following work:

I. Identified current national and local office procedures and guidelines for achieving compliance with RRA 98 § 1204.

   A. Interviewed Organizational Performance Division personnel to identify the procedures used to ensure compliance with the provisions of RRA 98 § 1204.

   B. Reviewed the RRA 98, the Internal Revenue Code, the Internal Revenue Manuals, IRS memoranda, and other documentation to identify the legal requirements as well as the procedures used to ensure compliance with RRA 98 § 1204.

II. Determined if the IRS complied with the provisions of RRA 98 § 1204 through a review of employee appraisals, Employee Performance Files (EPF), drop files, performance plans, organizational read files, and any other pertinent documentation created during Fiscal Year (FY) 2000.

   A. Selected a statistically valid random sample of enforcement employees for review.

      1. Obtained a computer download of Treasury Integrated Management Information System (TIMIS) records for the pay period covering the 2-week period September 24 through October 7, 2000.

      2. Validated the accuracy and completeness of the TIMIS database by a comparison with IRS Masterfile[2] records.

      3. Extracted a nationwide listing of 58,874 enforcement employees from the TIMIS database obtained in sub-objective II.A.1.

      4. Selected a random sample of 400 enforcement employees from the database in sub-objective II.A.3. using a two-stage, weighted sampling technique with a 95 percent Confidence Level, a 4 percent Precision Rate, and a 5 percent Occurrence Rate.

[1] Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

[2] Masterfile is a magnetic tape record that contains taxpayer account information.

The selection of audit sites was limited to states in the continental United States (U.S.) (including Washington, D.C.) and was weighted based on the population of enforcement employees in each location. Locations with larger populations had a greater chance of being selected, and it was possible for locations to be selected multiple times. The first stage of the sampling technique identified 10 locations, including California, Georgia, Kentucky, Maryland, Minnesota, Tennessee, Texas, and West Virginia. California and Texas were each selected twice; therefore, two separate samples were selected for these locations.

In the second stage of the sampling technique, we selected a random sample of 40 employees for each audit location. Two samples each were selected for California and Texas. The sampling criteria required the review of 20 enforcement employees for each location. We over-sampled because there was a high probability that our population included employees who were not enforcement employees during our sample period (October 1, 1999, to September 30, 2000). During case reviews, we eliminated and replaced non-enforcement employees from our sample until the first 20 enforcement employees in our sample for each location were identified.

B. Reviewed the EPFs, drop files, performance plans, organizational read files, and any other pertinent documentation for a statistically valid random sample of 200 enforcement employees to determine compliance with RRA 98 § 1204.

1. Determined if records of tax enforcement results (ROTER) were used in evaluating the sampled employees or to impose production quotas or goals.
2. Determined if the fair and equitable treatment of taxpayers was used as a performance standard for evaluating the sampled employees' performance.
3. Determined if the supervisor of each of the sampled employees certified quarterly by letter whether tax enforcement results were used in a manner prohibited by RRA 98 § 1204(a).
4. Interviewed the employee's manager for any exception cases to determine why the potential violation occurred.
5. Discussed potential RRA 98 § 1204 violation cases with Organizational Performance Division personnel.
6. Obtained interpretations from Treasury Inspector General for Tax Administration (TIGTA) Office of Chief Counsel on all cases with potential legal violations.

C. Determined if the IRS' review processes detected the exception cases that were identified during the review of the sample cases in sub-objective II.B.

1. Obtained copies of the FY 2000 quarterly self-certifications and the results of IRS management's independent reviews for the offices visited in sub-objective II.B.

2. Determined if the IRS review processes identified these same exception cases during either the FY 2000 quarterly self-certifications or during the IRS' independent reviews.

D. Projected the results of the sample review to the estimated population of actual enforcement employees in the continental U.S. and verified the validity of the projection with a professional statistician.

III. Determined the status of IRS corrective actions taken as a result of recommendations in the TIGTA FY 2000 Report[3] and if they will enable the IRS to improve compliance with RRA 98 § 1204.

[3] *Further Improvements Are Needed in Processes That Control and Report Misuse of Enforcement Statistics* (Reference Number 2000-10-118, dated September 2000).

Appendix II

Major Contributors to This Report

Maurice S. Moody, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)
Nancy A. Nakamura, Director
Gerald T. Hawkins, Audit Manager
Alan R. Beber, Senior Auditor
Catherine E. Cloudt, Senior Auditor
Deadra M. English, Senior Auditor
Mary L. Faulkner, Senior Auditor
Abraham B. Millado, Senior Auditor
Jeffery A. Smith, Senior Auditor
Yolanda D. Brown, Auditor
Andrew J. Burns, Auditor
Gwendolyn M. Green, Auditor

Appendix III

Report Distribution List

Assistant Deputy Commissioner N:ADC
Commissioner, Large and Mid-Size Business Division LM
Commissioner, Small Business/Self-Employed Division S
Commissioner, Tax Exempt and Government Entities Division T
Commissioner, Wage and Investment Division W
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- Commissioner, Tax Exempt and Government Entities Division T
- Commissioner, Wage and Investment Division W
- Chief, Appeals AP
- Chief, Criminal Investigation CI
- Director, Tax Administration Coordination N:ADC:T
- National Taxpayer Advocate TA
- Chief Counsel CC

Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to the Congress.

Type and Value of Outcome Measure:

- Protection of Taxpayer Rights – Potential; the performance or related supervisory documentation for an estimated 3,623 enforcement employees in the continental United States (U.S.) (± 5.9 percent) could contain violations of the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)[1] Section (§) 1204 (a) or (b). We are 95 percent confident that the range of enforcement employees affected by similar occurrences is between 969 and 6,277 (see page 3).

Methodology Used to Measure the Reported Benefit:

We obtained a computer download of Treasury Integrated Management Information System (TIMIS) data for all IRS employees for the period September 24, 2000, through October 7, 2000. We extracted from the TIMIS database a listing of 58,874 enforcement employees who worked in the continental U.S. from the TIMIS database. The enforcement employees included the following job series: 0501, 0512, 0526, 0592, 0920, 0930, 0962, 1101, 1169, 1171, and 1811.

We used a multi-stage attribute sampling technique that required sampling enforcement employees in 10 audit locations and reviewing the performance documentation of 20 employees in each location. We proposed a 95 percent Confidence Level, a 4 percent Precision Rate, and a 5 percent Occurrence Rate.

We used the Army Audit Sampling Program (computer program) to randomly select 10 of 49 potential audit locations (the 48 continental states and Washington, D.C.) in stage 1 of the sampling methodology. The selection of the audit locations was weighted based on the estimated population of enforcement employees in each location. Therefore, the larger the population of enforcement employees in a location, the greater the opportunity that the location would be selected. In addition, it was possible for a location to be selected multiple times. California and Texas were selected twice. Georgia, Kentucky, Maryland, Minnesota, Tennessee, and West Virginia were selected once.

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[1] Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

We then used the Army Audit Sampling Program to select 40 enforcement employees for each of these 10 locations in stage 2 of the sampling methodology. Although preliminary indications were that we would review the performance documentation of 20 employees in each of the 10 audit locations, we selected a sample of 40 employees for each location so that non-enforcement employees could be eliminated from the sample and replaced.

From the listing of 40 employees for each location, we reviewed the Fiscal Year (FY) 2000 performance and supervisory documentation for the first 20 enforcement employees. We reviewed the selected employees' performance documentation for compliance with the requirements of RRA 98 § 1204. We evaluated documentation for 260 employees and determined that 60 of these employees did not perform enforcement activities in FY 2000. These non-enforcement employees were eliminated from our sample and replaced. Potential violations of RRA 98 § 1204 (a) or (b) were identified in 16 of the 200 sampled enforcement employees' performance or related supervisory documentation.

In order to project the results of our sample, we redefined the estimated population of enforcement employees in the continental U.S. The elimination of 60 non-enforcement employees from the sample resulted in the revision of our estimated population of enforcement employees in the continental U.S. to 45,288 as of October 7, 2000, as follows:

- 60 (enforcement employees removed from sample) / 260 (total employees reviewed) = .23076923 (non-enforcement employee revision factor).
- 23076923 (non-enforcement employee revision factor) * 58,874 (estimated population of enforcement employees) = 13,586 (estimated number of non-enforcement employees).
- 58,874 (estimated population of enforcement employees) – 13,586 (estimated number of non-enforcement employees) = 45,288 (revised estimate of population of enforcement employees).

We projected our results across the population of 45,288 enforcement employees. According to the projection, the performance or related supervisory documentation for an estimated 3,623 enforcement employees (± 5.9 percent) could contain violations of RRA 98 § 1204 (a) or (b). We are 95 percent confident that the range of enforcement employees affected by similar occurrences is between 969 and 6,277. This is based on a .05860272 precision rate calculated by the Army Audit Sampling Program.

- 16 (number of potential violations identified) / 200 (number of enforcement employees in the sample) * 45,288 (revised population of enforcement employees) = 3,623 (projected number of potential violations)
- 45,288 (revised population of enforcement employees) * .05860272 (precision rate) = 2,654 (precision of the projection)
- 3,623 (projected number of potential violations) - 2,654 (precision of the projection) = 969 (lower confidence limit)

- 3,623 (projected number of potential violations) + 2,654 (precision of the projection) = 6,277 (higher confidence limit)

A professional statistician reviewed our sampling methodology and our projections.

Appendix V

Management's Response to the Draft Report

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

CHIEF FINANCIAL OFFICER

SEP 20 2001

MEMORANDUM FOR PAMELA J. GARDINER
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: C. Spencer Nelms, Jr. CSN
Acting Director, Organizational Performance Division

SUBJECT: Treasury Inspector General of Tax Administration (TIGTA) Draft Audit Report - Compliance With the Internal Revenue Service Restructuring and Reform Act of 1998 Section 1204 Has Not Yet Been Achieved (Draft Audit Report No. 200110013)

Thank you for the opportunity to respond to your draft report (hereinafter "draft report" or "report") entitled, "Compliance with the Internal Revenue Service Restructuring and Reform Act of 1998 Section 1204 has not yet been Achieved." The draft report reviews our compliance with the IRS Restructuring and Reform Act of 1998 (RRA 98), Section 1204 which restricts the use of enforcement statistics to evaluate IRS employees or to impose or suggest production quotas or goals.

We concur with your recommendation that the two potential violations of RRA 98 Section 1204 (a) identified in your report should be discussed with the managers and documents revised as appropriate by the responsible division and functional unit. The respective operating divisions are reviewing the potential violations and will take the appropriate action.

More generally, we are pleased to report the following program enhancements which have recently been implemented for the Section 1204 certification and independent review processes based on feedback provided by the operating and findings of previous TIGTA reports. Specifically, the Section 1204 independent review process has been simplified and will be conducted for the full fiscal year. New Section 1204 independent review checklists (for review of employee performance folders and management activity) will provide standardized review methodology and will collect more extensive statistical information. These improvements will allow us to more accurately determine if problem areas exist and, if they do, in which part of the organization they are located.

The Section 1204 waiver process was also revised to require all non-Section 1204 executives to annually submit a waiver, which indicates that no Section 1204 activity was performed in any area within their organization. This raises the awareness of the RRA 98 Section 1204 legislation on the use of enforcement statistics Servicewide.

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As noted in your report, a National Special Assurance Review will also be conducted on the new independent review process by the third quarter of FY 2002. Other certification enhancements will be issued in the new IRM 1.5, Organization, Finance, and Management, Managing Statistics in a Balanced Measurement System Handbook, for FY 2002. Taken together, these efforts continue to improve and enhance our implementation of Section 1204.

Thank you again for the opportunity to comment on the draft report. Attachment 1 to this memorandum provides detailed comments and clarification on some of the other findings and technical aspects of the report. Attachment 2 contains the actions to be taken to address the recommendation. If you have any questions, please contact me at 202.622.4909.

Attachments

Attachment 1

Detailed Comments and Clarifications

Clarification of 1204 Procedures. Based on our review of its findings, we would like to provide clarification of Section 1204 procedural information referenced in your report. Specifically, it states that there was a procedural violation when certain IRS managers could not fully substantiate that they certified whether tax enforcement results were used in a prohibited manner. However, based on Internal Revenue Manual (IRM) 105.4 (9/15/99), Managing Statistics in a Balanced Measurement System Handbook, Sections 10.3.1 and 10.3.2, this does not reflect a procedural violation.

IRM guidelines require IRS Section 1204 first-line managers and higher-level managers to complete quarterly self-certifications and forward these to their Section 1204 Appropriate Supervisor. We concur with the statement in your report that "[e]limination of the management positions contributed to the unavailability of most of the 46 instances where self-certifications were not available." The Service's reorganization could have had a significant impact on the location of these self-certifications. However, it is each Appropriate Supervisor's responsibility to consolidate all individual self-certifications into the quarterly consolidated office certification and retain all self-certifications in his/her office file. Since your audit methodology did not include contacting the Appropriate Supervisor of each Section 1204 manager who was unable to provide copies of all of their quarterly self-certifications, it does not support the assertion that a procedural violation occurred.

Employee Retention Standard. Regarding Section 1204 (b), the Office of Strategic Human Resources reports that the retention standard became mandatory on July 1, 1999, and all Service employees received the separate retention standard for the fair and equitable treatment of taxpayers. Compliance with the standard must be (re)certified each year. The separate retention standard and receipt was incorporated into the Executive, Manager and Management Official Performance Agreements (Forms 12450, 12450-A and 12450-B) in December 1999, however, it remained separate for employees being evaluated on Form 6850, Performance Appraisal and Retention Standard Rating. The Service has completed impact and implementation negotiations regarding balanced measures Critical Job Elements (CJEs) with NTEU, and the retention standard for the fair and equitable treatment of taxpayers has been incorporated into the revised Form 6850. The revised Form 6850 and the balanced measures CJEs are currently being implemented throughout the Service.

Statistical Validation. We also have concerns with the information you present in Appendix IV, Outcome Measures, of your draft report. Using the documentation you provided during the course of this audit, we concur that your estimates of the number of Section 1204 enforcement employees for the various areas of noncompliance with Section 1204 are accurately computed based on the sampling methodology you used. However, we believe that the precision values for these estimates are understated. These precision values result in sample estimates that are very imprecise. This imprecision is magnified when we recomputed these values based on the formulas you provided. The imprecision of these estimates is evidenced by the fact that many of the 95% confidence intervals include either zero (0) or the total population number. This lack of precision of the primary estimates makes it difficult for us to use the information you provide to enhance our Section 1204 process.

After early discussions on sampling and estimation methodology, you provided a copy of the U.S. Army Audit Agency Statistical Sampling System (Version 6.3, August 1995), the computer software to be used to determine sample sizes, generate random numbers for sample selection, and compute the sample estimates and their corresponding precision. In order to validate the computations of this program, specifically the precision for the type of sample used for this audit, we requested documentation of the formulas used by this software. In response, you provided excerpts from the text, Elementary Sampling Theory, by Taro Yamana. Using these formulas, we attempted to verify the computations that were presented in your draft report. We were able to verify the sample estimates of the total number of Section 1204 enforcement employees that would be affected by the various areas of noncompliance that you reviewed. However, in every case, the precision values shown in your report are understated compared to the values we computed based on the formulas. This means that the sample estimates that you present in your draft report are less precise than are represented.

TOTAL P.05

Attachment 2

Actions to be Taken to Address the Recommendation

Implementation Date: January 1, 2002

Responsible Officials: Commissioner, Small Business/Self-Employed Division
Chief, Criminal Investigation

Corrective Action Monitoring Plan: The Director for the Organizational Performance Division will contact the respective division and functional unit to ensure that the potential violations of RRA 98 Section 1204 (a) identified in the report are reviewed. These organizational units will discuss the potential violations with the managers and take appropriate action. Officials will provide information to the Organizational Performance Division prior to January 1, 2002.