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IRS BUSINESS OPERATIONS

Issues in Setting Priorities and Managing for Results

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Messrs. Chairmen and Members of the Commission:

I am pleased to be here to discuss the important role that the Commission can play in improving the Internal Revenue Service's (IRS) business operations. GAO has done extensive work detailing the substantial problems IRS has experienced, and our views on the pivotal actions that IRS should take to fully implement our many recommendations were summarized in a September 1996 report, which I am including for the record.[1] Today, I will focus on three issues the Commission should consider as part of its review of IRS' present practices and the improvements necessary to modernize its operations.

First, I would encourage the Commission to evaluate IRS' management operations and practices in light of recently enacted management reform legislation—the Chief Financial Officers Act of 1990, the Government Performance and Results Act of 1993, and the Clinger-Cohen Act of 1996. The Government Performance and Results Act, in particular, is intended to produce a realistic set of business goals and priorities for IRS and a discrete number of performance measures to permit the Congress to track IRS' progress and to hold it accountable for achieving results. The Commission has an opportunity to make excellent contributions in these areas. Second, emphasis needs to be placed on IRS' development of effective implementation strategies. The lack of solid implementation strategies has been a major achilles heel to attaining IRS' business vision and fixing known, long-standing problems. Finally, any effort to modernize IRS' operations requires reliable cost and performance information. Without good data, the Congress and the executive branch will not be in a good position to assess IRS' performance, its resource needs, and the need for remedial actions in a timely manner.

Setting Priorities and Performance Measures

The Congress' desire to enhance agencies' accountability for their performance is at the heart of three pieces of management reform legislation of the 1990s: the Chief Financial Officers Act (CFO) Act of 1990, the Government Performance and Results Act (GPRA) of 1993, and the Clinger-Cohen Act of 1996. These laws represent the Congress' efforts to modernize the operations of federal agencies and impose a strengthened framework for management and accountability.

[1]Internal Revenue Service: Business Operations Need Continued Improvement (GAO/AIMD/GGD-96-152, September 9, 1996).

The Congress enacted the CFO Act to remedy decades of serious neglect in federal financial management by establishing chief financial officers across government and requiring the preparation and audit of annual financial statements, among other things, to provide accountability. GPRA, which is directed at improving program performance, requires each agency to consult with the Congress and other stakeholders in developing its mission and strategic goals. The act also requires each agency to establish annual performance goals, measure performance against these goals, and report publicly on how well it is doing. Finally, the recently enacted Clinger-Cohen Act requires agencies to apply these principles—goal setting, performance measurement, and reporting—to their information technology investments.

Full and effective implementation of these management reforms will help address the fundamental problems impeding IRS' business operations. Most of GAO's specific recommendations to improve IRS' management are directed at promoting effective implementation of these essential management mandates of the Congress. I strongly encourage the Commission to use this framework in formulating its recommendations to help push IRS further toward successful implementation.

The GPRA mandate to submit strategic goals and performance measures in particular, offers a unique opportunity for the Commission. IRS is being required to submit a strategic plan and detailed performance measures with its fiscal year 1998 budget request. This submission will be deliberated upon by the Congress in the coming months. Consequently, the Commission has a natural window of opportunity to engage in, and further, this debate.

It would be most helpful, for example, if the Commission could express its views on the appropriate business priorities for IRS. While there are many management and technical reasons why IRS has not achieved its business vision, a reasonable hypothesis can be advanced that it took on too many ambitious business goals and did not set priorities, particularly given the unrelenting production demands of the annual tax filing season. Similarly, under the GPRA pilot program, IRS did not focus on a small number of critical areas. This lack of prioritization has plagued the tax system modernization effort as well.

Operating under its charter from the Congress, the Commission also can help further the essential process of obtaining consensus on IRS' business goals and performance measures among the administration and key congressional committees. The GPRA process was intended to help achieve this result; however, it will require much consultation and deliberation. For example, the conference report accompanying IRS' appropriations bill for fiscal year 1997 underscored concerns about past problems in measuring IRS' performance, especially in the areas of taxpayer service and assistance, tax collection, and compliance. The conferees stressed the need for valid performance measures and called for a strategic plan and detailed performance measures to be submitted with IRS' fiscal year 1998 budget request.

Ensuring Effective Implementation Strategies

While establishing business goals and priorities is an essential point of departure for improving IRS' operations, the expected results from this process will not be achieved without effective implementation strategies. IRS has set a business vision for itself that has been refined over time, but the differences between IRS' current operations and those proposed in its vision are great. One of the primary reasons for this is the absence of well defined strategies for making IRS' business vision a reality.

This problem is clearly illustrated by the fact that although increasing electronic filing has been a mainstay of IRS' business vision for some time, IRS does not yet have a comprehensive business strategy to reach or exceed its goal of 80 million electronic filings by 2001. IRS' estimates and projections for individual and business returns suggest that by 2001, as few as 39 million returns may be submitted electronically—less than half of IRS' goal and only about 17 percent of all returns expected to be filed.

We have reported that IRS' business strategy would not maximize electronic filings because it primarily targeted taxpayers who use a third party to prepare and/or transmit simple returns, are willing to pay a fee to file their returns electronically, and are expecting refunds. Focusing on this limited taxpaying population overlooks most taxpayers, including those who prepare their own tax returns using personal computers, have more complicated returns, owe tax balances, and/or are unwilling to pay a fee to a third party to file a return electronically.

To date, most of the returns filed electronically are ones that, if filed on paper, could be filed on forms (like the 1040EZ) that are among the least costly paper returns to process. Also, IRS has not yet successfully addressed one of the major impediments to the expansion of electronic filing—its cost to the taxpayers. IRS has taken a number of actions to address these concerns and is currently preparing a revised strategy that it plans to have ready this fall.

Another major goal of IRS' vision is to increase taxpayer service and compliance, which is dependent in large measure on increasing the use of, and implementing, new information systems. However, IRS has not fully defined business requirements for those systems and lacks a cost-effective strategy for accessing taxpayer data that may be needed for customer service and compliance. For instance, making it easier for taxpayers to reach IRS by telephone is of limited value if IRS employees on the other end of the line do not have access to the data needed to help the taxpayers.

No goal or priority for improving IRS' business operations will be met successfully without effective implementation strategies and sufficient management follow-through, not only by IRS but also by the Department of the Treasury and the Office of Management and Budget (OMB). While the Commission obviously cannot, and should not, focus on this level of detail, it needs to address directly the importance of these management tasks being carried out. Treasury, in particular, has recently become more active in oversight. While that is a positive development, Treasury's continued focus on monitoring IRS' corrective actions will be a key factor in ensuring progress. OMB needs to emphasize its leadership and oversight roles in resolving these matters as well.

The good work of this Commission, as well as critical mandates from the Congress and the administration, will hinge largely upon the executive branch's capacity to demonstrate effective implementation and dedicated follow-through. This has been lacking in the past and should be addressed by the Commission in its recommendations.

Requiring Reliable Cost and Performance Information

IRS continues to be plagued by the poor quality of its cost and performance information. Measuring performance becomes very difficult if baseline data are lacking or unreliable, as is the case at IRS. Under the CFO Act, IRS began preparing financial statements for the first time beginning with fiscal year 1992. We have audited these statements for fiscal years 1992 to 1995 and have been unable to express an opinion on their reliability. We have identified persistent, fundamental problems, including difficulties in reconciling the amount of total revenue collected with taxpayer records in the aggregate, substantiating the amounts of various types of taxes collected (social security, income, and excise taxes, for example), and accurately reporting correct amounts for valid and collectable accounts receivable. In addition, a significant portion of IRS' reported $3 billion in nonpayroll operating expenses has not been able to be verified.

IRS has made some progress in responding to these problems. Over the past 4 years, we have made 59 recommendations to improve IRS' financial management. In our assessment this year, we determined that IRS had completed action on 17 of these recommendations and efforts are underway to address the remaining areas.

However, many difficult problems remain to be corrected. With our assistance, IRS is working on a plan to solve these problems, with a goal of having certain issues resolved in time for the fiscal year 1996 financial statement audit. For some areas, however, especially in accounting for revenue, IRS will need to make more sweeping changes to fully address system problems.

Follow-through by IRS is essential. Solving these problems is essential to provide reliable financial information and assure taxpayers that their tax dollars are properly accounted for. The accuracy of IRS' financial statements is also key to both IRS and the Congress for (1) ensuring adequate accountability for IRS programs, (2) assessing the impact of tax policies, and (3) measuring IRS' performance and cost effectiveness in carrying out its numerous tax enforcement, customer service, and collection activities.

Any effort to improve and modernize IRS' operations requires at a minimum the ability to generate accurate, timely, and reliable financial information that withstands audit scrutiny. The conference report accompanying IRS' appropriations bill for fiscal year 1997 expresses concerns about the inability of IRS to prepare auditable financial statements and directs the IRS to submit a report to the Appropriations Committees by March 1, 1997, which presents a plan to correct the serious financial and reporting deficiencies identified through our financial audits. The Commission can play an important role by recommending priorities and time frames for corrective actions in this critical area.

Messrs. Chairmen and Members of the Commission, this concludes my statement. The work of the Commission will be an important impetus to improving IRS' business operations. To assist the Commission in using the GPRA framework, we have provided GAO's Executive Guide: Effectively Implementing the Government Performance and Results Act

(GAO/GGD-96-118, June 1996), which has been distributed throughout the executive branch to help promote successful GPRA implementation. I am also providing a list of recent GAO reports and testimonies, which I believe the Commission will find useful in framing the issues and focusing on needed solutions.

We will be pleased to assist the Commission as it continues its work.

Selected Recent GAO Products

Financial Audit: Examination of IRS' Fiscal Year 1992 Financial Statements (GAO/AIMD-93-2, June 30, 1993).

Financial Audit: Examination of IRS' Fiscal Year 1993 Financial Statements (GAO/AIMD-94-120, June 15, 1994).

Financial Audit: Examination of IRS' Fiscal Year 1994 Financial Statements (GAO/AIMD-95-141, August 4, 1995).

IRS Operations: Significant Challenges in Financial Management and Systems Modernization (GAO/T-AIMD-96-56, March 6, 1996).

Tax Systems Modernization: Management and Technical Weaknesses Must Be Overcome To Achieve Success (GAO/T-AIMD-96-75, March 26, 1996).

Tax Systems Modernization: Progress in Achieving IRS' Business Vision (GAO/T-GGD-96-123, May 9, 1996).

Financial Audit: Actions Needed to Improve IRS Financial Management (GAO/T-AIMD-96-96, June 6, 1996).

Tax Systems Modernization: Actions Underway But IRS Has Not Yet Corrected Management and Technical Weaknesses (GAO/AIMD-96-106, June 7, 1996).

Tax Systems Modernization: Cyberfile Project Was Poorly Planned and Managed (GAO/AIMD-96-140, August 26, 1996).

Internal Revenue Service: Business Operations Need Continued Improvement (GAO/AIMD/GGD-96-152, September 9, 1996).

Internal Revenue Service: Critical Need to Continue Improving Core Business Practices (GAO/T-AIMD/GGD-96-188, September 10, 1996).

IRS Financial Audits: Status of Efforts to Resolve Financial Management Weaknesses (GAO/T-AIMD-96-170, September 19, 1996).

Financial Audit: Examination of IRS' Fiscal Year 1995 Financial Statements (GAO/AIMD-96-101, July 11, 1996).

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