Reduced Budgets and Collection Resources Have Resulted in Declines in Taxpayer Service, Case Closures, and Dollars Collected

May 8, 2015

Reference Number: 2015-30-035

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REDUCED BUDGETS AND COLLECTION RESOURCES HAVE RESULTED IN DECLINES IN TAXPAYER SERVICE, CASE CLOSURES, AND DOLLARS COLLECTED

Highlights

Final Report issued on May 8, 2015

Highlights of Reference Number: 2015-30-035 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

Since Fiscal Year 2010, decreases in the budget have resulted in the reduction of 21 percent of Automated Collection Service (ACS) contact representatives and 28 percent of Field Collection revenue officers. The availability of these key collection employees directly affects taxpayer service and the IRS's ability to take appropriate enforcement action on delinquent taxpayers.

WHY TIGTA DID THE AUDIT

Between Fiscal Years 2010 and 2015, the IRS's budget has been reduced by more than $1.2 billion. This audit was initiated to determine the impact that IRS budget reductions have had on collection programs and employees.

WHAT TIGTA FOUND

Collection employees are important because their technical skills are needed to fulfill the IRS's mission of collecting unpaid taxes. Although management made extensive cuts to non-labor costs, significant collection personnel reductions were still necessary.

This has resulted in the ACS answering 25 percent fewer taxpayer telephone calls since 2011, because there were fewer ACS contact representatives available to answer them. Taxpayers whose calls were answered spent an average of eight minutes (97 percent) longer waiting for a contact representative. Taxpayers may become frustrated and remain noncompliant if they are unable to reach a contact representative to resolve their tax issues. In addition, ACS inventory grew and became older, and more cases were not resolved and were transferred to the Queue.

In FY 2014, revenue officers collected $222 million (7 percent) less than in FY 2011. In addition, they closed 34 percent fewer cases. This was primarily due to the decrease in the number of revenue officers and downtime that resulted from revenue officers' computer problems. In FY 2014, revenue officers' computer downtime reached 66,448 hours, the equivalent to losing 32 full-time employees for the year.

Many lower graded revenue officers are more experienced because budget limitations have restricted their promotion opportunities. As a result, Field Collection may be able to mitigate further risk to tax administration by assigning revenue officers' inventory closer to full capacity. In addition, higher graded revenue officers could be assigned a higher percentage of high-risk complex cases. The number of unassigned highly complex cases grew by more than 180 percent since Fiscal Year 2012. This is important because the average amount collected on the most complex cases was more than three times the next highest average amount collected.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS: 1) ensure that revenue officer inventory levels are maintained at close to full capacity while ensuring the inventory levels are commensurate with the complexity of the cases; and 2) ensure that General Schedule-13 grade revenue officers are working appropriate cases, and when possible, increase the percentage of General Schedule-13 grade cases assigned to General Schedule-13 grade revenue officers.

IRS management agreed with the recommendations and plans to take corrective actions.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

May 8, 2015

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Reduced Budgets and Collection Resources Have Resulted in Declines in Taxpayer Service, Case Closures, and Dollars Collected (Audit # 201330010)

This report presents the results of our review to determine the impact that Internal Revenue Service (IRS) budget reductions have had on collection programs and employees. This audit is included in our Fiscal Year 2015 Annual Audit Plan and addresses the major management challenge of Tax Compliance Initiatives.

Management's complete response to the draft report is included as Appendix VII.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. If you have any questions, please contact me or Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations).

Table of Contents

Abbreviations

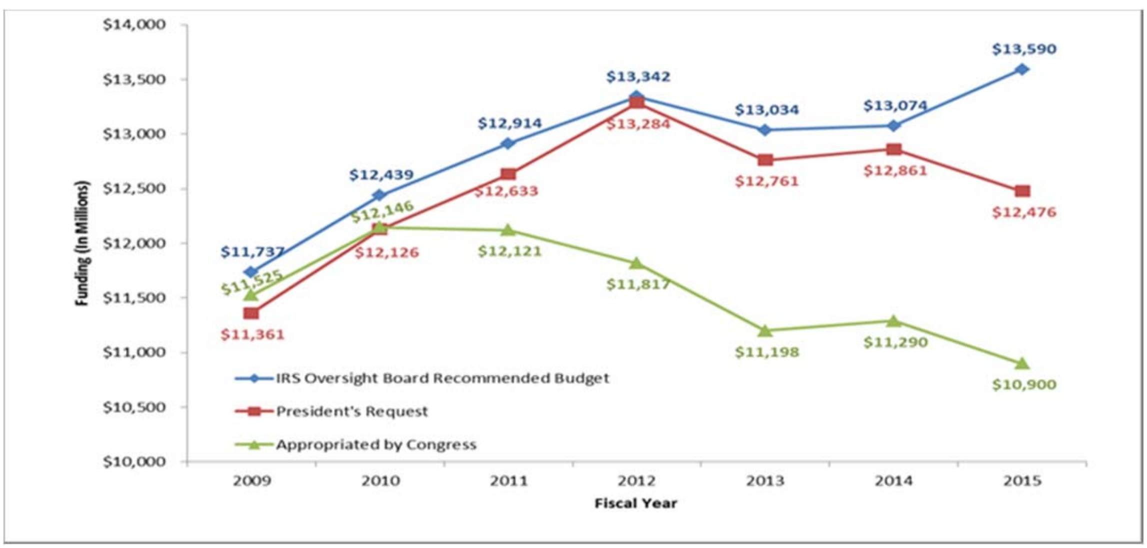
ACS	Automated Collection System
FY	Fiscal Year
GS	General Schedule
IRS	Internal Revenue Service
TDA	Taxpayer Delinquent Account
TDI	Taxpayer Delinquency Investigation
TIGTA	Treasury Inspector General for Tax Administration

Background

The Internal Revenue Service (IRS) continues to encounter a number of formidable budgetary challenges. Due to delays in enacting Federal budgets for the past several years, Continuing Resolutions[1] have been passed to keep the Government operating. As such, the full-year operating budget has not been known until well into the fiscal year. Additionally, the impact of the sequestration provisions in the Balanced Budget and Emergency Deficit Control Act, as amended by the Budget Control Act of 2011,[2] significantly affected the IRS. During Fiscal Year (FY) 2013, the IRS operated under a Continuing Resolution, in addition to sequestration rules, that funded the agency at just less than $11.2 billion. That amount was significantly lower than both the President's and the IRS Oversight Board's FY 2013 recommendations, approximately $948 million less than the FY 2010 budget. The IRS's FY 2015 enacted budget of $10.9 billion was more than $1.2 billion (10 percent) less than the FY 2010 enacted budget.

Figure 1 shows the IRS's enacted budgets since FY 2009 in comparison to the amounts requested in the President's budgets and the amounts recommended by the IRS Oversight Board. The enacted amounts have dropped significantly since FY 2011.

Figure 1: The IRS's Recommended, Requested, and Appropriated Budgets From FY 2009 to FY 2015



Source: IRS Oversight Board's FY 2015 IRS Budget Recommendation Special Report.

[1] See Appendix VI for a glossary of terms.
[2] Pub. L. No. 112-25, 125 Stat. 240 (2011).

In its FY 2015 IRS Budget Recommendation Special Report, the IRS Oversight Board expressed concern that the cuts have forced the IRS to find major cost efficiencies and implement significant spending cuts. This has led to dramatic curtailments in training, travel, office space, and outside contracts. The IRS has also been forced to significantly reduce the size of its workforce. In FY 2012, the agency offered buyouts to 7,000 of its employees, with more than 1,200 accepting. The IRS also instituted an "exception-only" hiring freeze, leaving many vacancies unfilled. Between FY 2010 and the end of FY 2014, the number of IRS employees has been reduced by approximately 13,000 full-time positions, with about 9,500 coming from front-line enforcement personnel.

The IRS Collection program has the primary responsibility for collecting delinquent taxes and tax returns while ensuring that taxpayer rights are protected. Specifically, the mission of the IRS Collection function is:

> *To collect delinquent taxes and secure delinquent tax returns through the fair and equitable application of the tax laws, including the use of enforcement tools when appropriate, provide education to customers to enable future compliance, and thereby protect and promote public confidence in the American tax system.*

This is a significant operation within the IRS because of the extent of noncompliance in both delinquent tax liabilities and delinquent tax returns. The IRS estimates that the annual Tax Gap ($450 billion) includes $46 billion in delinquent tax liabilities and $28 billion in unfiled tax returns.[3] The Automated Collection System (ACS) and Field Collection are two critical parts of the IRS's overall Collection program and perform a vital role in collecting delinquent taxes and tax returns. Their work with delinquent taxpayers is a major factor in determining the Collection program's success in meeting its mission.

The ACS has 15 call sites in the Small Business/Self-Employed Division. The Small Business/Self-Employed Division also has a total of five ACS support sites that support the call sites. Four of these ACS support sites resolve written correspondence from taxpayers, taxpayer representatives, and/or third-party contacts. Contact representatives at the ACS call sites are responsible for answering incoming taxpayer calls and working the inventory of Taxpayer Delinquent Accounts (TDA) and Taxpayer Delinquency Investigations (TDI). TDAs and TDIs in ACS inventory are created after prior efforts to collect unpaid balances via notices have been unsuccessful.

There are more than 400 Field Collection offices across the country from which revenue officers contact taxpayers in person to collect unpaid taxes and secure tax returns from delinquent

[3] The Tax Gap is the difference between what taxpayers should have paid and what they paid timely. The largest portion ($376 billion) of the Tax Gap is based on taxpayers underreporting taxes. A smaller portion ($46 billion) is based on taxpayers not fully paying their tax liabilities. The final portion ($28 billion) is based on those taxpayers not filing tax returns. In January 2012, the IRS reported these updated Tax Gap figures that represent Tax Year 2006 tax return data.

taxpayers who have not complied with previous notices or contacts by the ACS. Revenue officers also take enforcement actions, including levies, liens, and seizures of property.

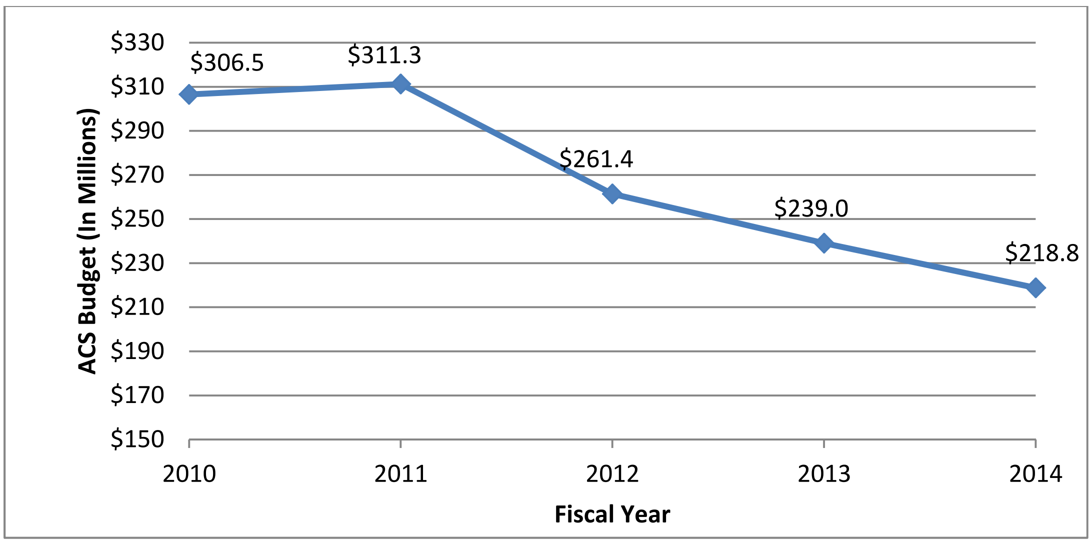
This review was performed at the Small Business/Self-Employed Division Headquarters in New Carrollton, Maryland; the Philadelphia Campus in Philadelphia, Pennsylvania; Field Collection offices in Oakland, California; Denver Colorado; Springfield, Illinois; and Seattle, Washington, during the period November 2013 through November 2014. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Results of Review

Budget Reductions Have Resulted in a Decrease in Automated Collection System and Field Collection Personnel

The IRS budget for FY 2014 was nearly $1 billion less than the FY 2010 budget. During that same period, the budgets for the ACS and Field Collection were reduced by more than $269 million. Figure 2 shows the changes in the ACS budget from FY 2010 to FY 2014. Since FY 2011, the ACS budget decreased more than $92 million (30 percent) from $311.3 million to $218.8 million.

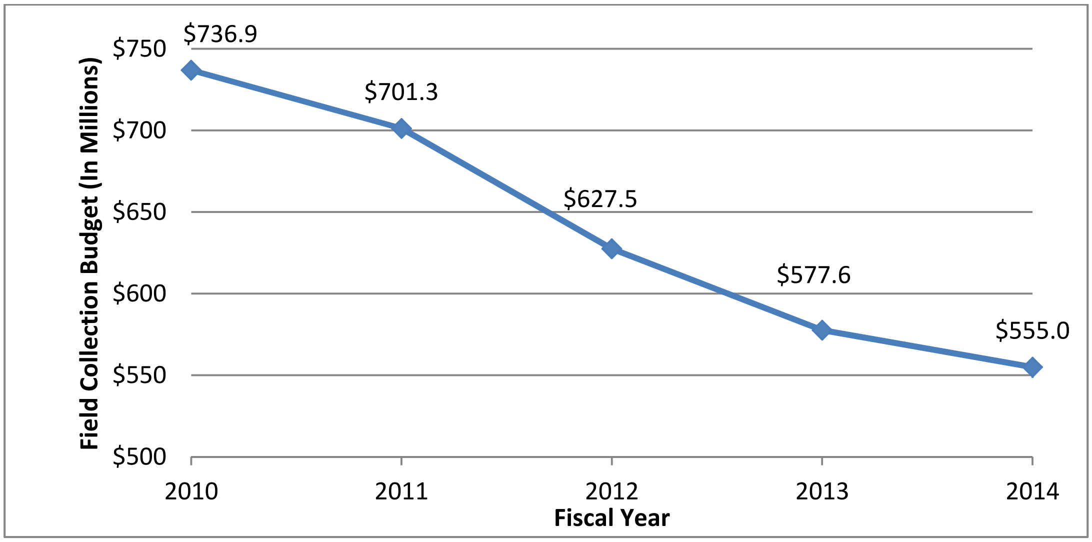
Figure 2: ACS Budget From FY 2010 to FY 2014



Source: Treasury Inspector General for Tax Administration (TIGTA) analysis of the 2010 through 2014 Monthly Summary of Resources Reports and Dollars and Sense Reports.

Figure 3 shows the changes in the Field Collection budget from FY 2010 to FY 2014. Since FY 2010, the Field Collection budget decreased more than $181 million (25 percent) from $736.9 million to $555.0 million.

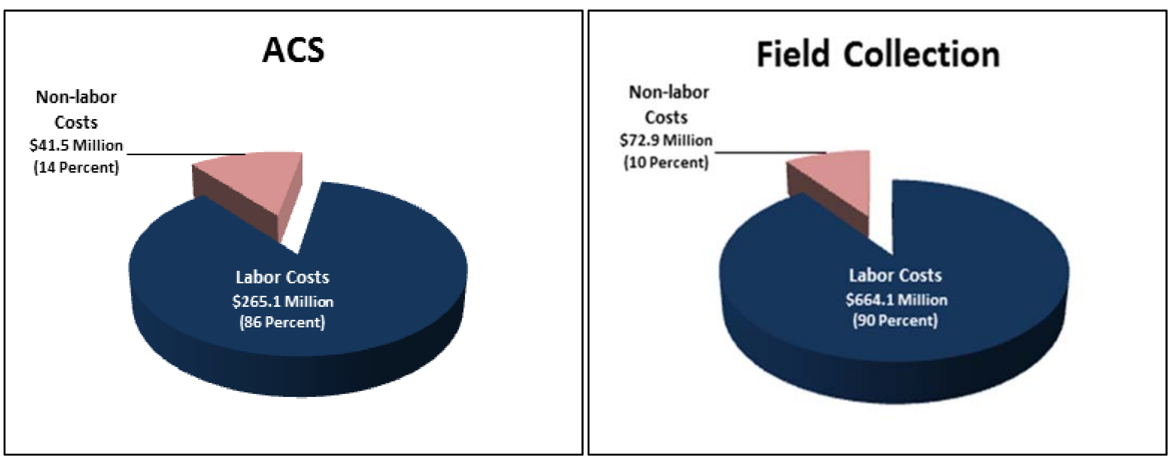
Figure 3: Field Collection Budget From FY 2010 to FY 2014



Source: TIGTA analysis of the 2010 through 2014 Monthly Summary of Resources Reports and Dollars and Sense Reports.

Similar to the other functions of the IRS, the largest portions of the ACS and Field Collection budgets are spent on labor costs. Figure 4 shows that in FY 2010, the majority of the ACS and Field Collection budgets was devoted to labor costs.

Figure 4: ACS and Field Collection FY 2010 Budget Allocations

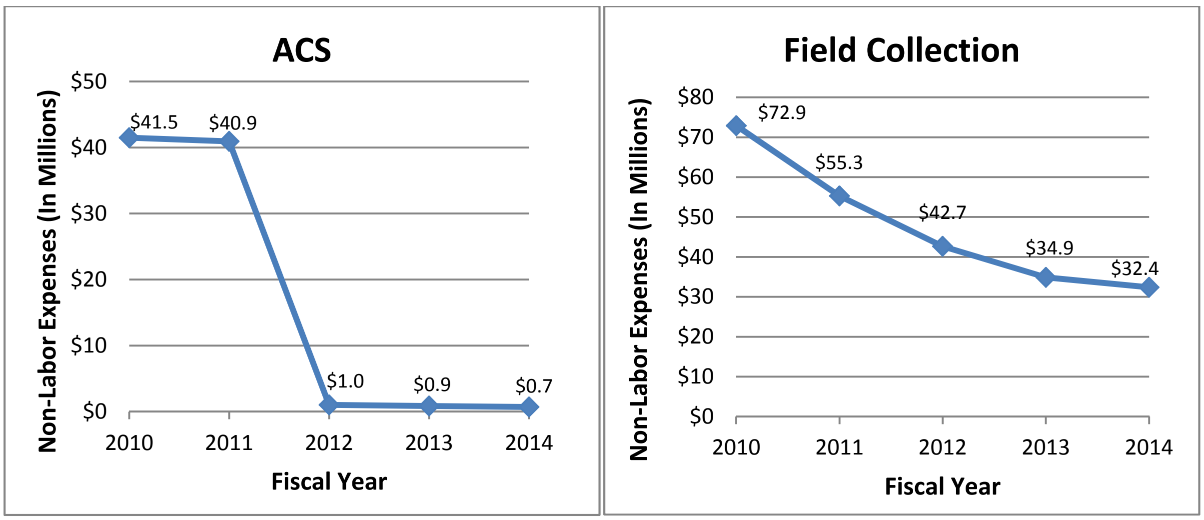


Source: TIGTA analysis of the 2010 Monthly Summary of Resources Reports and Dollars and Sense Reports.

Management recognized the importance of keeping employees available to work with taxpayers and work inventory. Therefore, management reduced non-labor expenses, such as training, travel, services, and supply expenses, proportionally more than labor expenses. Figure 5 shows the decrease in non-labor expenses in the ACS and Field Collection between FY 2010 and

FY 2014. Specifically, ACS non-labor expenses were reduced by $40.8 million (98 percent) and Field Collection non-labor expenses were reduced by $40.5 million (56 percent).

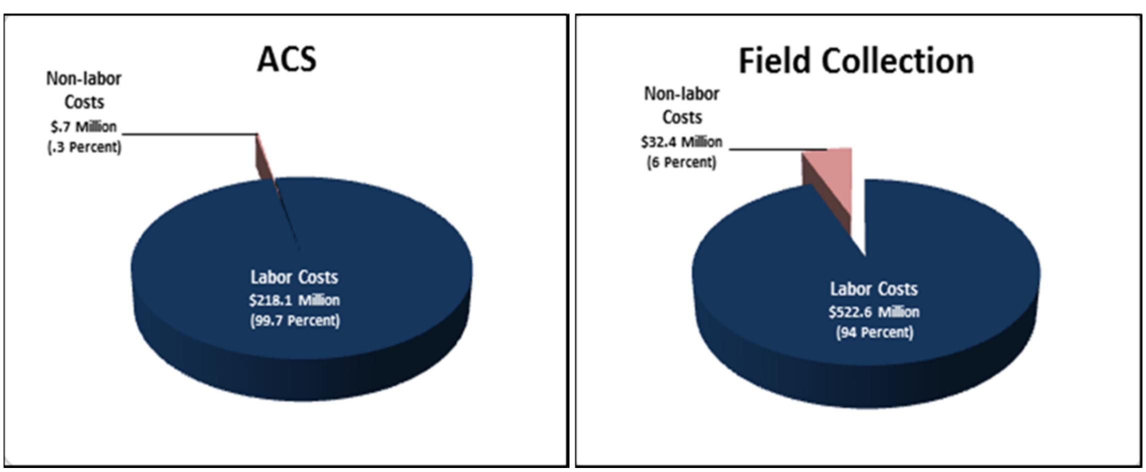
Figure 5: ACS and Field Collection Non-Labor Expenses From FY 2010 to FY 2014



Source: TIGTA analysis of the 2010 through 2014 Monthly Summary of Resources Reports and Dollars and Sense Reports.

All non-labor costs could not be eliminated because some of these costs are necessary. For example, revenue officers often incur travel expenses when visiting taxpayer locations. However, by FY 2014, the proportion of the budget that was dedicated to labor costs had increased. Figure 6 shows the FY 2014 ACS and Field Collection budget allocations.

Figure 6: ACS and Field Collection FY 2014 Budget Allocations



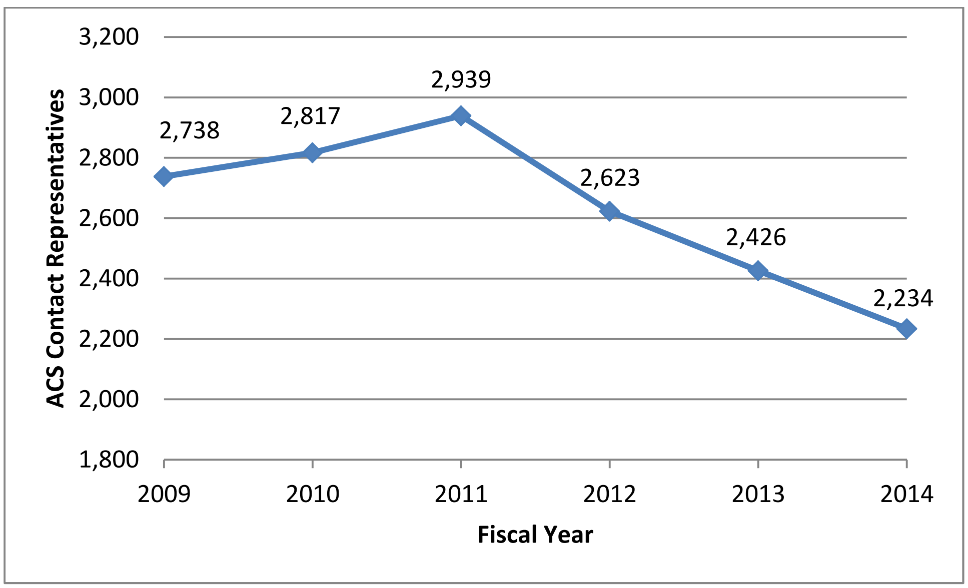
Source: TIGTA analysis of Monthly Summary of Resources Reports and Dollars and Sense Reports.

Even though ACS and Field Collection management were able to lower the labor costs' proportional share of the budget reduction compared with other costs, labor cost reductions were unavoidable because the budget reduction was more than all non-labor costs combined. Specifically, in the ACS, the budget reduction was $46 million more than all non-labor costs combined, and in Field Collection, the budget reduction was $109 million more than all non-labor costs combined. As a result, both the ACS and Field Collection reduced staff.

ACS staffing has been reduced 24 percent since FY 2011

The ACS began FY 2014 with 705 (24 percent) fewer contact representatives than it started with in FY 2011. Figure 7 shows the change in contact representatives from FY 2009 to FY 2014.

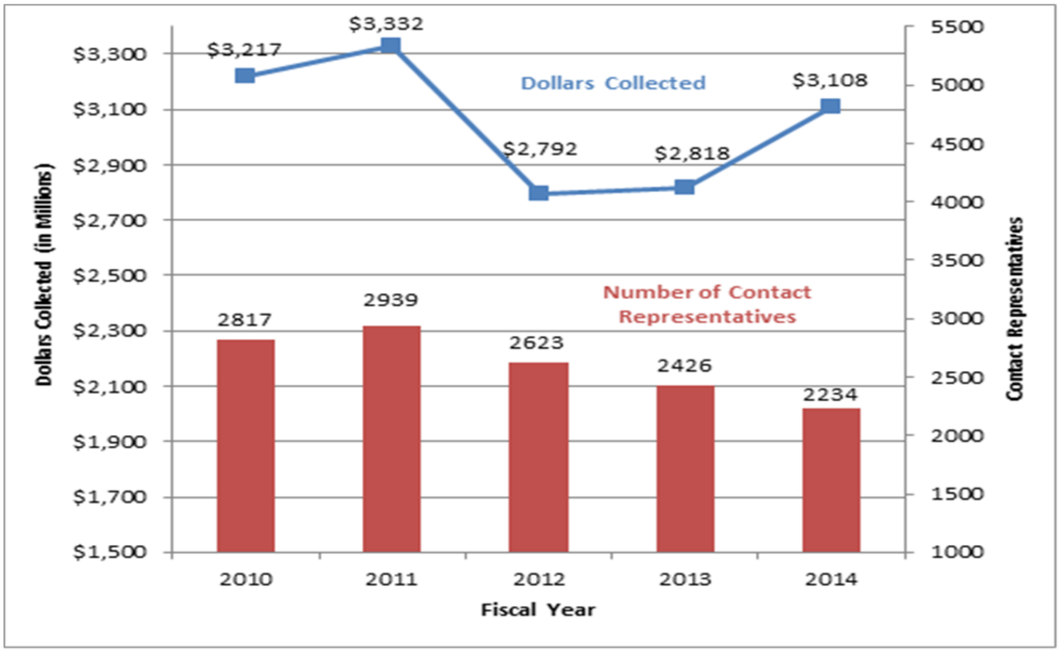
Figure 7: Number of ACS Contact Representatives From FY 2009 to FY 2014



Source: TIGTA analysis of ACS call site staffing data.

In addition, three ACS call sites were taken offline in February 2013 to work Accounts Management function inventory. Management made this decision to free up Accounts Management function resources to address the IRS's growing inventory of identity theft cases. The initiative was originally scheduled to continue for three months, but was subsequently extended until June 2014. This reallocation was the equivalent of losing an additional 410 contact representatives because the employees in these three ACS call sites were now answering taxpayer questions rather than working ACS inventory. As a result, from FY 2011 to FY 2013, the number of ACS contact representatives was reduced by 31 percent. Figure 8 shows how the amount of ACS dollars collected was affected during that time frame.

Figure 8: Dollars Collected Compared With Contact Representatives From FY 2010 to FY 2014



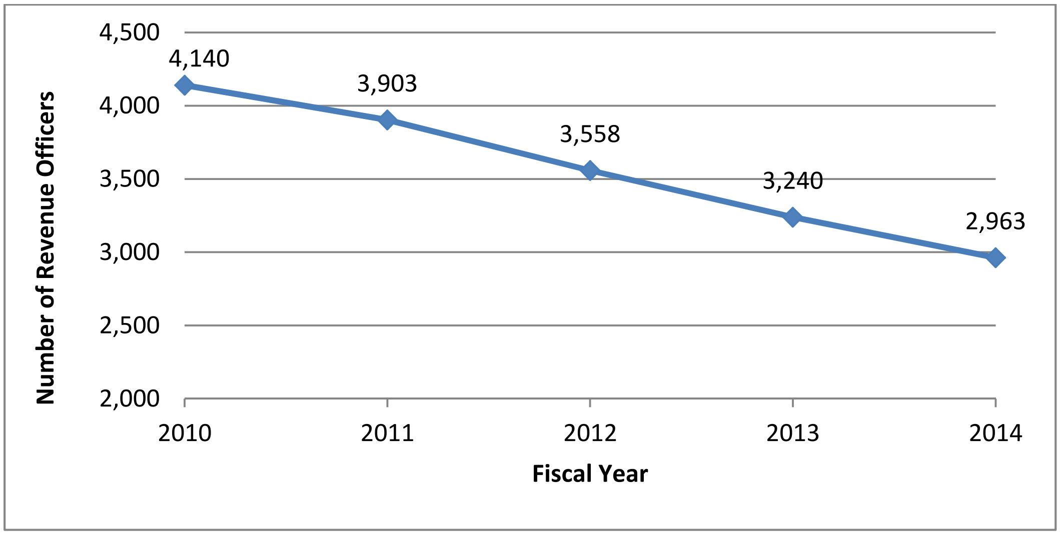
Source: TIGTA analysis of FY 2010 through 2014 Collection Activity Reports and ACS staffing data.

Despite the decline in ACS contact representatives, dollars collected by ACS started to trend upward in FY 2013. In FY 2014, dollars collected by ACS increased $316 million (11 percent) from FY 2012. IRS management believes the levels in FY 2012 and FY 2013 were low because of reduced staffing levels and interruptions to ACS systemic levy processing. An improving economy and the return of detailed ACS staff in the second half of FY 2014 helped, in part, to return revenues closer to levels collected before FY 2012. However, the $3.1 billion collected in FY 2014 is still slightly less than the $3.2 billion collected in FY 2010.

The number of revenue officers has decreased by 28 percent since FY 2010

Since FY 2010, 1,177 (28 percent) revenue officers have been lost due to attrition or reassignment. Figure 9 shows the change in the number of revenue officers from FY 2010 to FY 2014.

Figure 9: Number of Revenue Officers From FY 2010 to FY 2014



Source: TIGTA analysis of Collection reports.

Retirement eligibility data indicate that declines in the number of ACS contact representatives and Field Collection revenue officers may continue. In FY 2015, 16 percent of ACS contact representatives and nearly one-quarter of Field Collection revenue officers are eligible to retire. By the end of FY 2016, 24 percent of the ACS contact representatives and 33 percent of Field Collection revenue officers will be eligible to retire.

ACS contact representatives and Field Collection revenue officers are important because their technical skills are needed to fulfill the Collection function's mission of collecting unpaid taxes. Contact representatives at the ACS call sites are responsible for answering incoming taxpayer calls and working the inventory of TDAs and TDIs. Revenue officers contact taxpayers in person to collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices or contacts by the ACS. These are the key resources needed to address the Collection function's portion of the Tax Gap and to work the inventory of delinquent accounts to ensure equitable treatment for the majority of taxpayers who timely and fully pay their taxes.

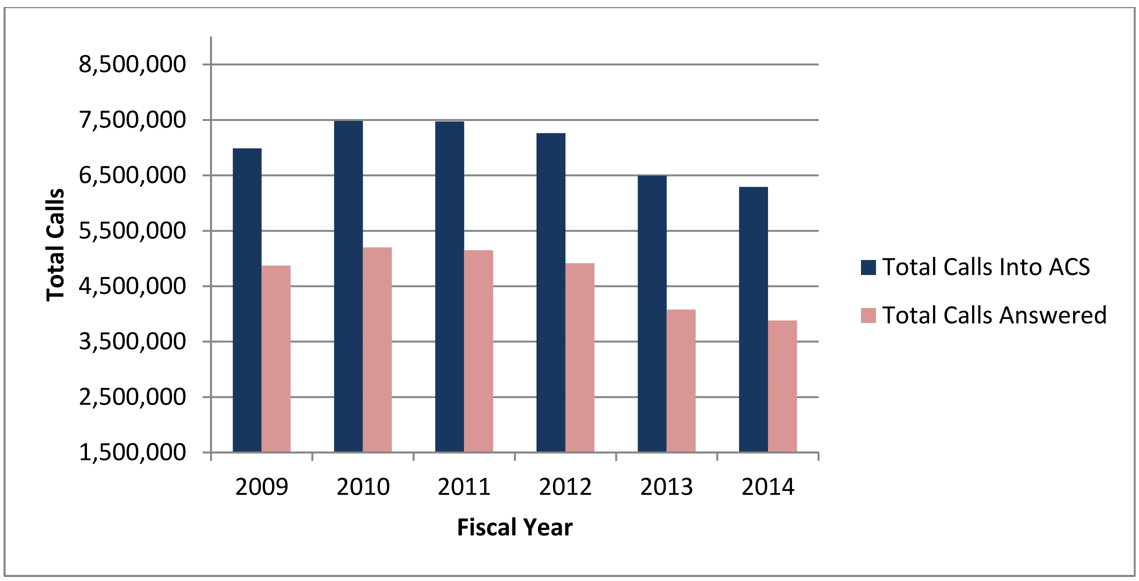
In addition to working the inventory of delinquent taxpayers, revenue officers also serve as a deterrent to potentially delinquent taxpayers. With fewer resources available to administer tax collections, both the ACS and Field Collection have experienced unfavorable trends in some key customer service (ACS call handling) and business results. Further, replacing lost employees will potentially create a further strain on the IRS's ability to work the delinquent taxpayer inventory because experienced employees will need to be taken from their regular duties to train any new employees.

Collection Program Performance Trends Have Declined

ACS call handling performance has declined due to fewer ACS contact representatives

ACS management places a high priority on answering incoming taxpayer telephone calls because communication with taxpayers helps resolve delinquencies and brings taxpayers into compliance with their tax obligations. The ACS's primary measure of telephone effectiveness is the Level of Service, which is a measure of the callers' abilities to connect with ACS contact representatives. However, with fewer contact representatives to answer telephone calls, the ACS was unable to maintain the same Level of Service that it achieved in prior years. Although IRS management took steps to reduce the number of incoming telephone calls by reducing the number of liens and levies, contact representatives could not keep up with the number of incoming calls. Specifically, although total calls into the ACS have decreased by 16 percent since FY 2011, ACS contact representatives answered 25 percent fewer telephone calls. Figure 10 compares the number of calls received and answered from FY 2009 to FY 2014.

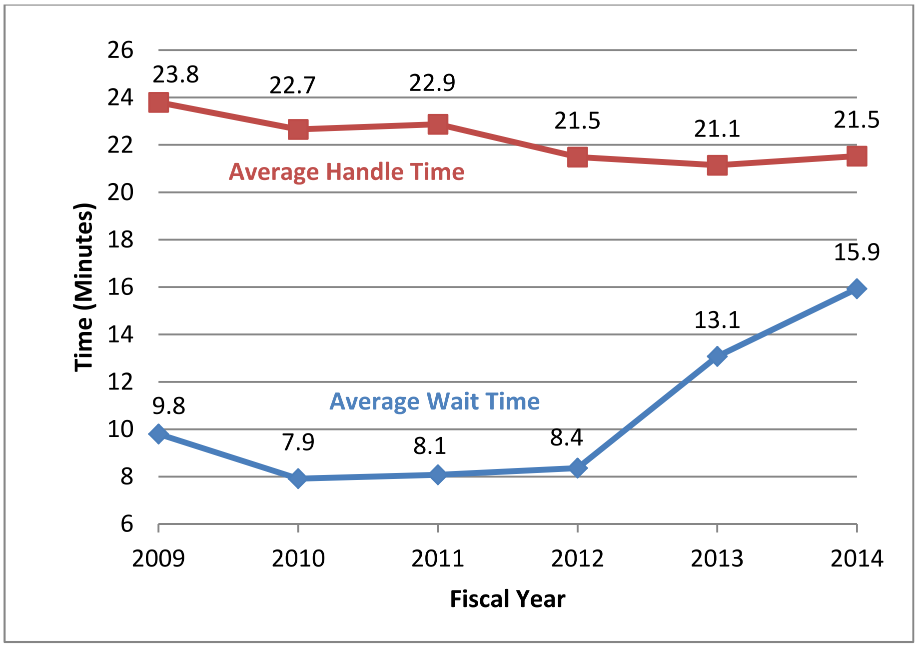
Figure 10: ACS Calls Received and Answered From FY 2009 to FY 2014



Source: TIGTA analysis of ACS call site data.

In addition, the taxpayers who reach a contact representative are experiencing much longer wait times. In FY 2014, the average time to reach an ACS contact representative increased by approximately eight minutes (97 percent) compared with FY 2011. Conversely, the average time that contact representatives spent resolving taxpayer questions has decreased since FY 2011. On average, ACS employees spent 6 percent less time handling taxpayer telephone calls in FY 2014 than they did in FY 2011. TIGTA previously reported[4] that ACS management information does not capture the complete results of its call handling operations. As a result, ACS management cannot determine the reasons why there was a decrease in the average time it took to handle each taxpayer call. Figure 11 shows wait times increased as handle times decreased from FY 2009 to FY 2014.

Figure 11: ACS Telephone Average Wait Time and Average Handle Time From FY 2009 to FY 2014

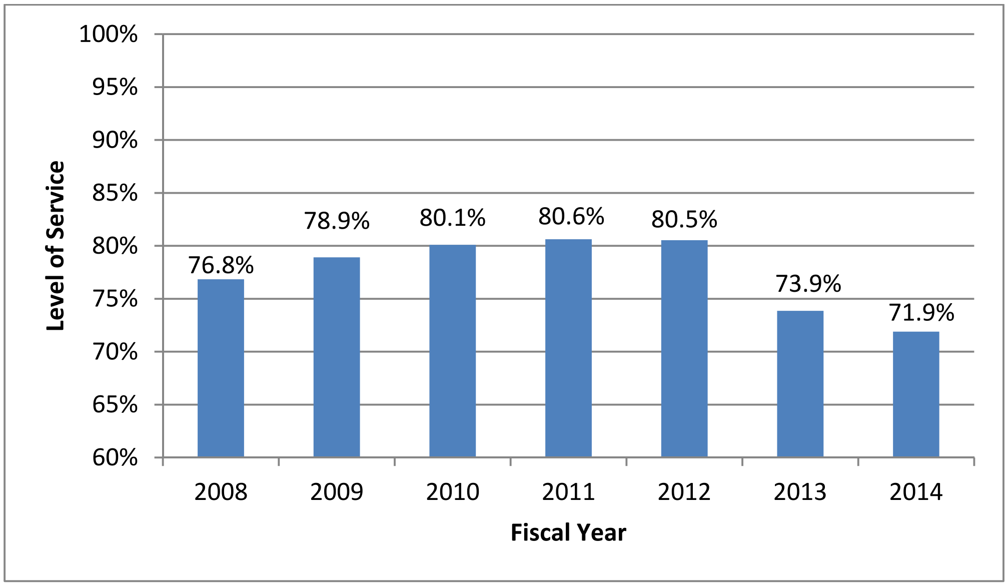


Source: TIGTA analysis of ACS call site data.

The Level of Service also declined in FY 2014. Figure 12 shows that although the average Level of Service stayed near 80 percent from FY 2009 to FY 2012, it decreased to less than 72 percent in FY 2014.

[4] TIGTA, Ref. No. 2014-30-080, *Declining Resources Have Contributed to Unfavorable Trends in Several Key Automated Collection System Business Results* (Sept. 2014).

Figure 12: ACS Level of Service From FY 2008 to FY 2014



Source: TIGTA analysis of ACS Level of Service data.

If this trend continues, these conditions could lead to taxpayer frustration as many taxpayers receiving IRS notices, *e.g.*, Notice to File Federal Tax Lien and Notice of Levy, will find it difficult to reach a contact representative to resolve their tax issues.

Several key ACS business results showed unfavorable trends

In addition to unfavorable trends in providing service to taxpayers by answering telephone calls, TIGTA previously reported[5] that ACS business results have been affected by declining resources in the following ways:

- New inventory is outpacing case closures, so the inventory is growing.
- Inventory is taking longer to close, thus cases in inventory are aging.
- More, and older, cases were transferred to the Queue, which reduces the probability of collection by the field.

See Appendix IV for the details and analysis of the affected ACS business results previously reported by TIGTA.

[5] TIGTA, Ref. No. 2014-30-080, *Declining Resources Have Contributed to Unfavorable Trends in Several Key Automated Collection System Business Results* (Sept. 2014).

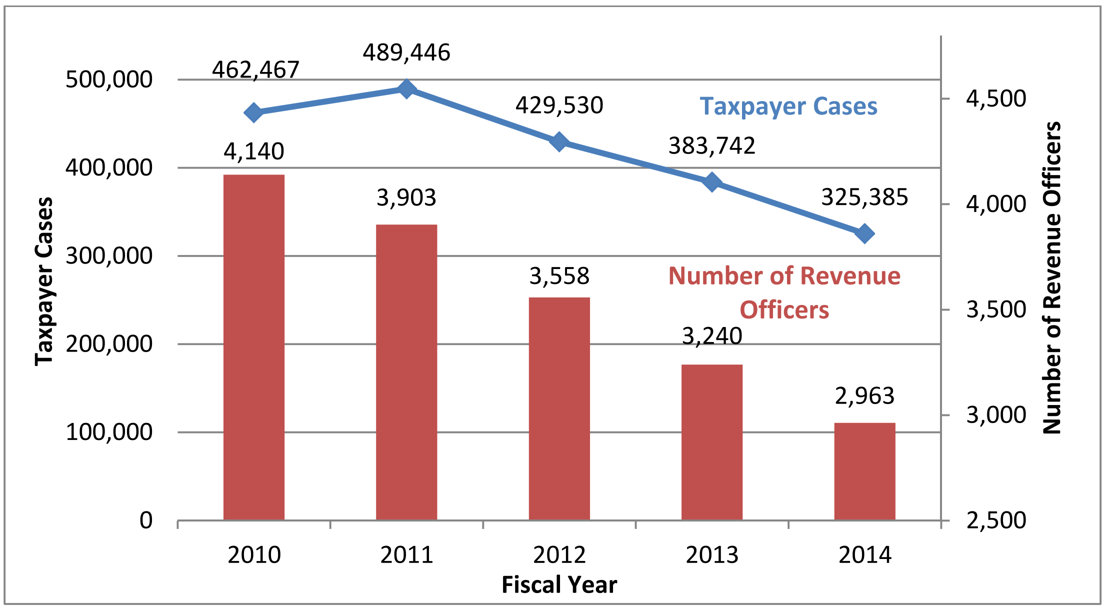
The number of cases closed by Field Collection has decreased

In FY 2014, revenue officers closed 164,061 (34 percent) fewer cases than in FY 2011. We determined that the decline in case closures was due in large part to the decrease in the number of revenue officers and downtime resulting from revenue officers' computer problems.

The 28 percent reduction in the number of revenue officers correlated with a 34 percent decrease in case closures

Figure 13 shows that from FY 2010 to FY 2014, the number of cases closed by revenue officers correlated with the number of revenue officers.

Figure 13: Case Closures and Number of Revenue Officers From FY 2010 to FY 2014



Source: TIGTA analysis of Director Collection Reports and Collection Activity Reports.

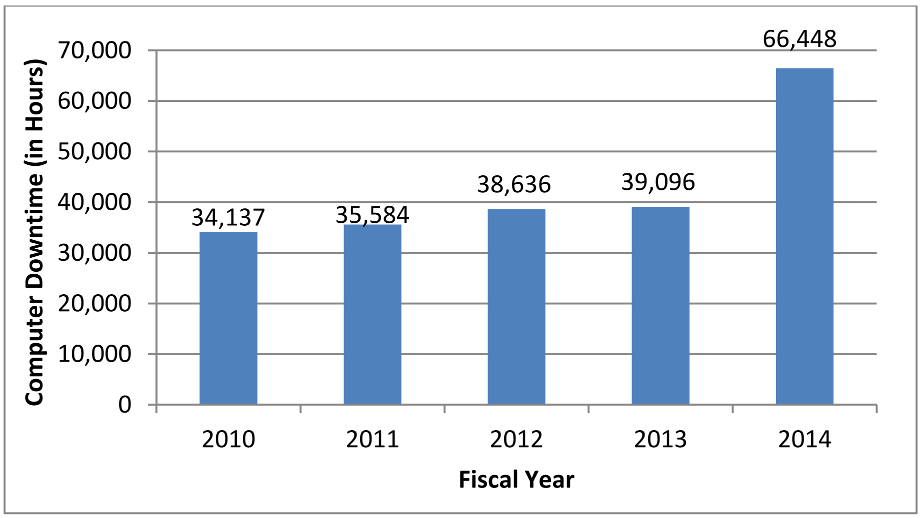
The number of TDAs[6] closed by revenue officers is a component in determining the Collection coverage rate.[7] The collection coverage rate measures how well the IRS is keeping up with new inventory. Between FY 2008 and FY 2013, the coverage rate has declined from 55.2 percent to 47.0 percent. For FY 2014, the IRS established the coverage rate target at 42.7 percent. The decline in coverage rate is another indication that revenue officers are not keeping up with new receipts of TDAs.

[6] A revenue officer case can include multiple TDAs pertaining to one taxpayer.
[7] The collection coverage rate compares the number of collection cases disposed of to the cases available. Cases available are calculated as the beginning inventory of cases plus any new cases.

Delayed laptop roll-out led to computer downtime

In addition to having fewer revenue officers to work cases, a delay in issuing new laptops to revenue officers may have contributed to the decrease in Field Collection case closures. The IRS was unable to make many technological enhancements due to budget reductions. As a result, many revenue officers had to work on outdated laptops using outdated software, which led to computer downtime. During our interviews, group managers expressed concern with outdated technology because their employees were not fully productive as a direct result of these computer issues. Specifically, even though there were fewer revenue officers in FY 2014 than FY 2010, computer downtime increased 95 percent. Figure 14 shows that computer downtime increased from 34,137 hours in FY 2010 to 66,448 hours in FY 2014.

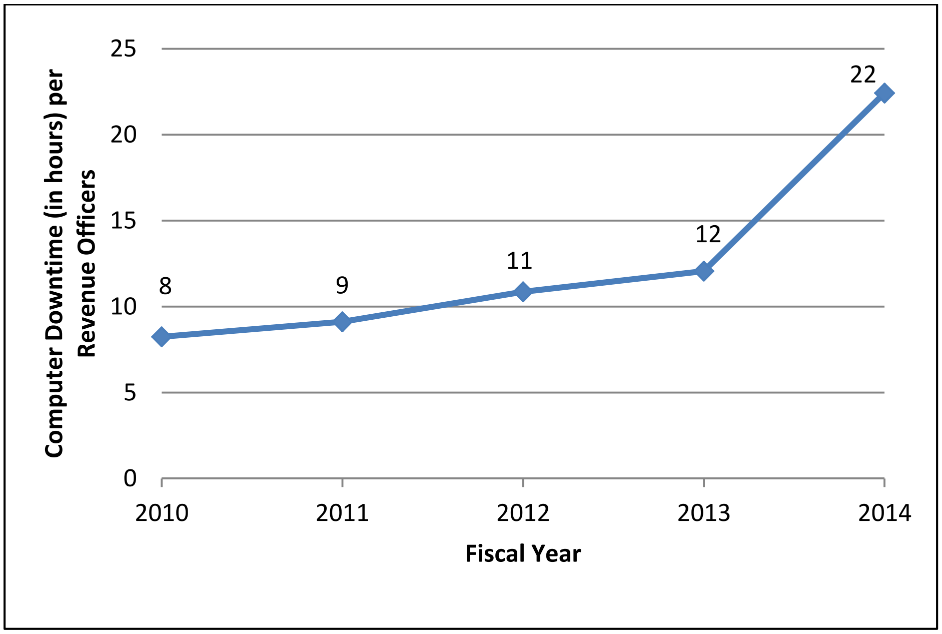
Figure 14: Revenue Officer Computer Downtime From FY 2010 to FY 2014



Source: FYs 2010 through 2014 Collection Activity Reports.

In FY 2014, revenue officers' computer downtime reached 66,448 hours, the equivalent to losing 32 full-time employees for the year. Figure 15 shows the increase in the average number of downtime hours charged per revenue officer. As the number of revenue officers declined 28 percent from FY 2010 to FY 2014, average computer downtime increased 175 percent per revenue officer.

Figure 15: Average Number of Downtime Hours per Revenue Officer From FY 2010 to FY 2014

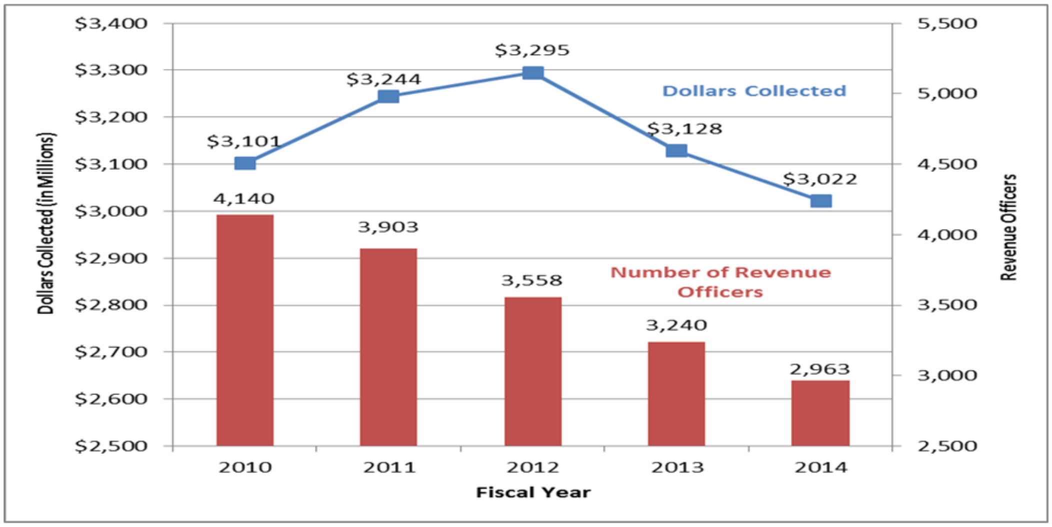


Source: TIGTA analysis of FYs 2010 through 2014 Collection Activity Reports.

The number of dollars collected has decreased as fewer revenue officers are closing cases

In FY 2014, Field Collection collected $222 million (7 percent) less than FY 2011. This is due, in part, to the decline in revenue officers. Figure 16 shows that starting in FY 2013, dollars collected correlated with the decrease in the number of revenue officers.

Figure 16: Dollars Collected Compared With Revenue Officers From FY 2010 to FY 2014



Source: TIGTA analysis of Director Collection Reports and Collection Activity Reports.

In addition, fewer cases are being closed by each revenue officer. In FY 2011, revenue officers closed an average of 125 cases; while in FY 2014, revenue officers closed an average of 110 cases. However, revenue officers have collected more dollars per case which may explain why dollars collected have not declined more. In FY 2014, revenue officers collected approximately $2,700 (40 percent) more per case than FY 2011. Overall, revenue officers collected 36 percent more dollars per revenue officer in FY 2014 than in FY 2010. General Schedule (GS)-13 grade revenue officers collected an average of $4.4 million each in FY 2014 and $159 million (162 percent) more dollars total in FY 2014 than in FY 2011.

There Are Opportunities for Field Collection to Mitigate the Risks Resulting From the Decline in the Number of Revenue Officers

Despite the billions of dollars collected by revenue officers in Field Collection, additional steps can be taken to reduce the risks posed by the declining number of revenue officers and case closures.

Revenue officers' assigned inventories are not at full capacity

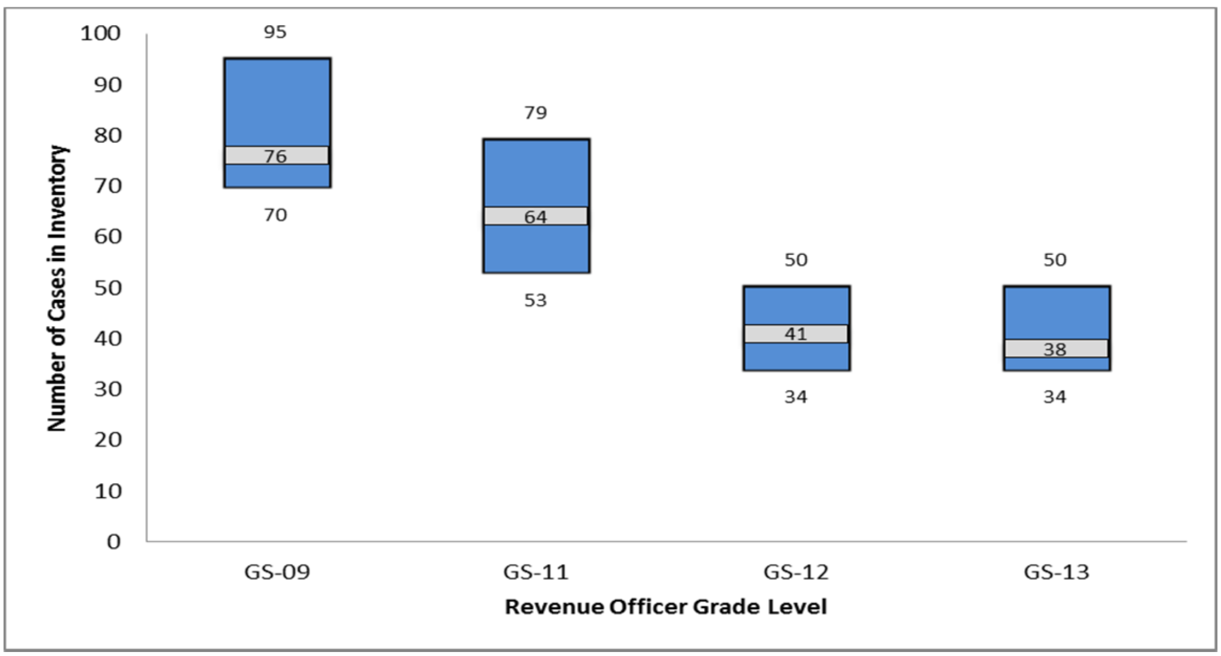
The IRS established target inventory levels for each revenue officer grade in order to obtain maximum productivity without affecting Field Collection quality. The inventory levels also provide a measure of uniformity among the Field Collection offices. The following target inventory ranges are required for each revenue officer grade:

- GS-13 — 34 to 50 taxpayer cases

- GS-12 — 34 to 50 taxpayer cases
- GS-11 — 53 to 79 taxpayer cases
- GS-09 — 70 to 95 taxpayer cases

By establishing ranges, management has some flexibility in how many cases are assigned to each revenue officer. Field Collection inventory reports provide a snapshot of the total number of cases assigned to each revenue officer and a breakdown of the assigned cases by grade level. We analyzed the collection inventory report for September 30, 2014 (end of FY 2014). Figure 17 shows the average inventory level for each revenue officer grade in comparison to their upper and lower inventory ranges.

Figure 17: Average Inventory Level by Revenue Officer Grade



Source: TIGTA analysis of Field Collection inventory report ending on September 30, 2014.

At the end of FY 2014, the average number of cases assigned to each revenue officer grade was between 76 and 83 percent of their full capacity. For example, the average number of cases assigned to Grade 12 revenue officers was 41 cases, which is 82 percent of their full capacity of 50 cases. In addition, 12 of the 59 GS-13 grade revenue officers had adjustments[8] to their inventory levels. Of the 47 GS-13 grade revenue officers that did not have adjustments to their inventory levels, nine (19 percent) did not have a sufficient number (less than 34) of cases assigned to them. In May 2011, the Director, Field Collection, issued guidance that provided

[8] GS-13 grade revenue officers may have their inventory levels adjusted for a variety of reasons such as temporary assignments, medical conditions, assignment of collateral duties, *etc*.

that the inventories of field revenue officers should generally not exceed 85 percent of the top of the inventory ranges. However, the average inventory levels for each revenue officer grade shown in Figure 17 are less than 85 percent of the top of the respective inventory ranges.

The May 2011 guidance considered factors such as cycle time, mix of inventory, and resources in establishing the 85 percent. However, the current budget environment has limited the career advancement of lower grade revenue officers so most of the revenue officers hired in FY 2009 and FY 2010 at the GS-07 and GS-09 grade levels have remained at the GS-09 and GS-11 grade levels since FY 2011. As a result, the experience level of GS-09 and GS-11 grade revenue officers is generally higher than it has been in prior years.

Because target inventory levels were established to obtain maximum productivity, Field Collection could potentially increase productivity and case closures by using the target inventory range flexibility to assign revenue officers' inventories closer to full capacity. An IRS optimization study[9] concluded that increases in revenue officer inventory levels are associated with higher revenue officer productivity.

The decline in the number of higher grade revenue officers has affected the type of taxpayer cases worked

The decline in the number of revenue officers has affected the experience level of Field Collection. Figure 18 shows how the grade of revenue officers who were assigned inventory has changed over the last five years.

Figure 18: Number of Revenue Officers by Grade From FY 2010 to FY 2014

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	Percentage Change Since FY 2010
GS-13	76	71	60	57	59	-22%
GS-12	1,412	1,328	1,245	1,122	1,030	-27%
GS-11	954	921	988	931	853	-11%
GS-09	1,194	1,374	1,075	1,022	864	-28%

Source: TIGTA analysis of FYs 2010 through 2014 Collection Activity Reports.

From FY 2010 to FY 2014, Field Collection lost a significant percentage of its most experienced revenue officers. At the end of FY 2014, there were 27 percent fewer GS-12 grade revenue officers and 22 percent fewer GS-13 grade revenue officers working cases than in FY 2010. The

[9] Small Business/Self-Employed Division Research New Carrollton/Richmond Project ID: NCH0124: *Revenue Officer Target Inventory Level Study: Analysis of Inventory Levels and the Impact on Productivity, Cycle Days and Quality* (September 2009).

GS-13 grade revenue officer position was established in July 2006 to address the most complex collection cases. However, the IRS placed a freeze on promotions to the GS-13 grade level in FY 2012 due to the declining budget. The number of GS-09 and GS-11 grade revenue officers has also decreased, by 28 and 11 percent, respectively. These revenue officers were unable to advance to higher grades because of budget limits until the last quarter of FY 2014. IRS management advised us that some revenue officers were promoted to GS-11 and GS-12 between July 2014 and September 2014.

The significant decrease in the number of GS-12 and GS-13 grade revenue officers affects the complexity of the collection cases that are assigned and worked. TDAs and TDIs are issued with a case grade of GS-09, GS-11, GS-12, or GS-13. These case grade levels correspond to the anticipated level of difficulty of the case. The complexity associated with each grade level is also considered in the number of cases each revenue officer should carry in his or her inventory. Higher graded (more experienced) revenue officers are needed to work the more complex cases. These cases involve more sophisticated taxpayers and significantly larger delinquent tax amounts. Appendix V shows a comparison of the GS-09, GS-12, and GS-13 grade case attributes based on case-grading criteria.

The decrease in GS-13 grade revenue officers has affected the composition of TDA inventory in the Queue. Since FY 2010, the Queue has decreased 26 percent, due in part to the shelving of a large number of cases. Meanwhile, GS-13 grade unassigned inventory has increased 180 percent, from 5,617 TDAs in FY 2012 to 15,702 TDAs in FY 2014. Figure 19 shows how TDA inventory in the Queue has changed since FY 2012.

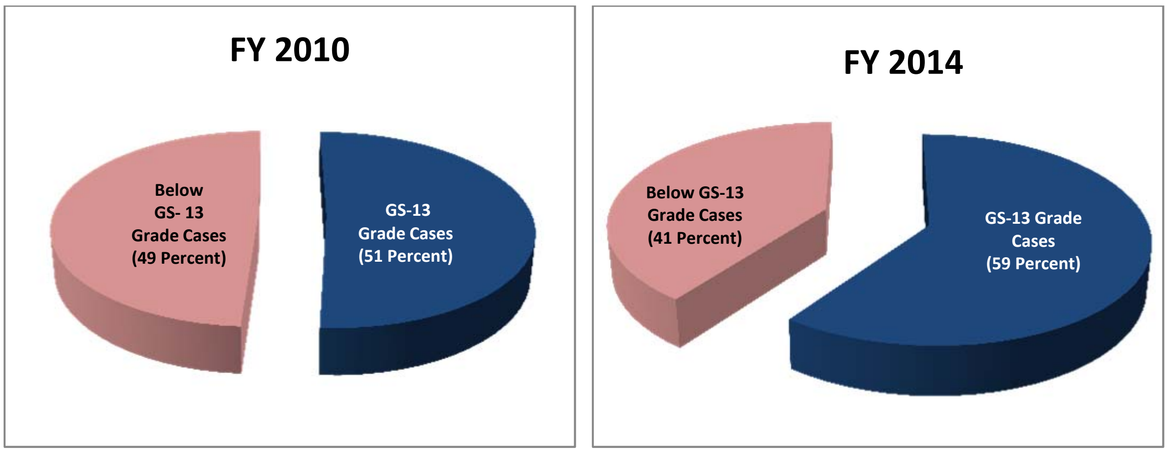
Figure 19: TDA Inventory in the Queue Between FYs 2012 and 2014

	FY 2012	FY 2013	FY 2014	Percentage Change Since FY 2012
Total TDA Inventory	1,135,911	848,239	840,492	-26%
GS-13 Grade	5,617	12,166	15,702	180%
GS 12 Grade	224,073	110,502	115,016	-49%
GS-11 Grade	354,150	220,807	218,428	-38%
GS-09 Grade	552,071	504,764	491,346	-11%

Source: TIGTA analysis of FYs 2010 through 2014 Collection Activity Reports (NO-5000).

In October 2012, the case-grading system in the Inventory Delivery System was enhanced to systemically grade cases as GS-13 cases. Prior to this enhancement, all GS-13 cases were manually graded. Management believes that the growth in GS-13 grade inventory in the Queue is related primarily to the case-grading enhancements rather than the decline in GS-13 grade revenue officers. However, even as the number of GS-13 grade cases increased and the number of GS-13 grade revenue officers declined, GS-13 grade revenue officers were assigned a significant number of lower grade cases. We analyzed the September 30th collection inventory reports for FYs 2010 through 2014. Figure 20 shows that at the end of FY 2010 and FY 2014, the percentage of assigned cases graded below the GS-13 grade level had decreased from 49 percent to 41 percent.

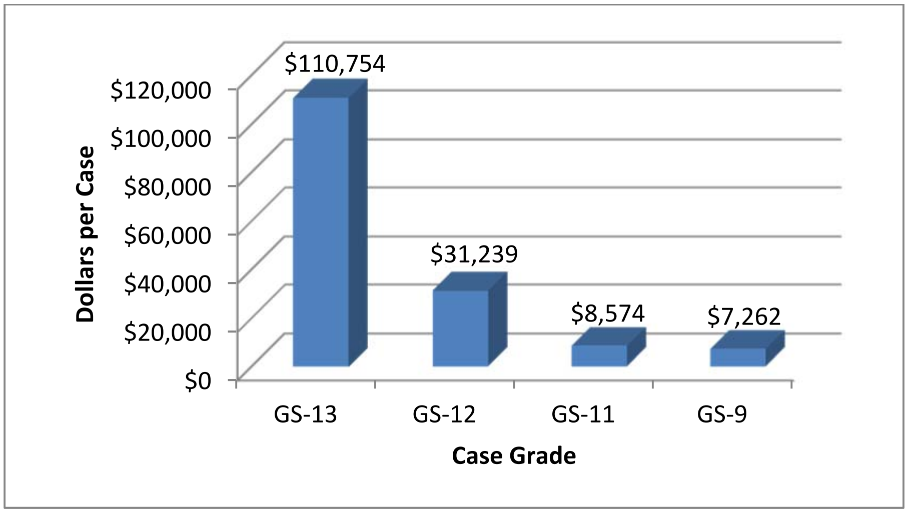
Figure 20: Inventory Mix Assigned to GS-13 Grade Revenue Officers



Source: TIGTA analysis of Field Collection inventory reports ending on September 30, 2010, and September 30, 2014.

This is a positive trend and we believe that there are benefits to increasing GS-13 grade revenue officers' inventories with more GS-13 grade cases. Closing more GS-13 grade cases may increase collections. In FY 2014, the average dollars collected per GS-13 grade case was more than $110,000. Figure 21 shows the average dollars collected on GS-13 grade cases compared with GS-12, GS-11, and GS-09 grade cases. The average amount collected on GS-13 grade cases is more than three times the amount collected on the next highest average amount collected.

Figure 21: Average Dollars Collected per Case by Case Grade in FY 2014



Source: TIGTA analysis of FY 2014 Collection Activity Reports (NO-5000).

By not assigning more GS-13 grade cases, the IRS may be more vulnerable to more sophisticated tax schemes and not work as many high-risk, high-dollar delinquencies. This could not only reduce revenue collected in the short-term, but also negatively affect future compliance.

Recommendations

Recommendation 1: The Director, Collection, Small Business/Self-Employed Division, should ensure that revenue officer inventory levels are maintained at close to full capacity while ensuring the inventory levels are commensurate with the complexity of the cases.

> **Management's Response:** IRS management agreed with this recommendation and will issue a memorandum reminding Field Collection group managers to ensure that their revenue officer inventory levels are within current inventory levels and appropriate, taking into account the complexity of the cases. IRS management will also evaluate whether the current inventory levels for revenue officers are appropriate as part of their ongoing study in the complexity of Field Collection cases.

Recommendation 2: The Director, Field Collection, Small Business/Self-Employed Division, should ensure that GS-13 grade revenue officers are working appropriate cases, and when possible, increase the percentage of GS-13 grade cases assigned to GS-13 grade revenue officers.

> **Management's Response:** IRS management agreed with this recommendation and will issue a memorandum reminding Field Collection group managers to ensure that their

GS-13 grade revenue officers are assigned appropriate cases, and when possible, increase the percentage of GS-13 grade cases assigned to GS-13 grade revenue officers.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine the impact that IRS budget reductions have had on collection programs and employees. To accomplish our objective, we:

I. Determined how the IRS budget cuts have affected the ACS[1] and Field Collection.

   A. Compiled and analyzed trends in IRS, ACS, and Field Collection budgets for FY 2009 through FY 2014.

   B. Compiled and analyzed trends in ACS and Field Collection staffing and business results.

      1. Analyzed ACS contact representatives' and Field Collection revenue officers' staffing levels and grade levels for FY 2010 through FY 2014.

      2. Analyzed Collection program business results from FY 2010 through FY 2014 using Collection Activity Reports and Director Collection Reports.

      3. Analyzed Collection Target Inventory Reports for the periods September 30, 2010, 2011, 2012, 2013, and 2014.

      4. Analyzed TDA inventory levels in the Queue for FY 2010 through FY 2014.

      5. Reviewed the TIGTA final report[2] on ACS inventory management.

   C. Identified any correlation between ACS contact representative staffing levels with call handling performance.

   D. Identified any correlation between Field Collection revenue officer staffing levels and case closures.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: collection target inventory levels established to ensure that revenue officers maximize productivity without a cost to quality

[1] See Appendix VI for a glossary of terms.
[2] TIGTA, Ref. No. 2014-30-080, *Declining Resources Have Contributed to Unfavorable Trends in Several Key Automated Collection System Business Results* (Sept. 2014).

and customer service, and call handling performance metrics established to measure the performance of the ACS telephone operations. We evaluated these controls by reviewing Target Inventory reports to determine whether each grade of revenue officer had a sufficient number of cases assigned and whether the cases assigned were at the proper grade level. We also analyzed ACS call handling performance metrics to assess the performance of its telephone operations.

Appendix II

Major Contributors to This Report

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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Director, Campus Collection, Small Business/Self-Employed Division SE:S:CC
Director, Collection, Small Business/Self-Employed Division SE:S:C
Director, Field Collection, Small Business/Self-Employed Division SE:S:FC
Director, Collection Policy, Small Business/Self-Employed Division SE:S:C:CP
Director, Headquarters Collection, Small Business/Self-Employed Division SE:S:C:HQ
Chief Counsel CC
National Taxpayer Advocate TA
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Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Commissioner, Small Business/Self-Employed Division SE:S

Appendix IV

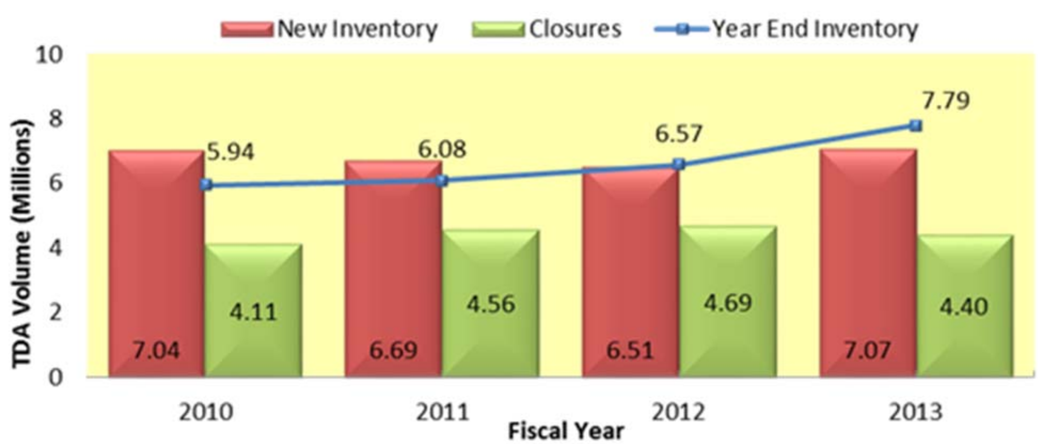
Automated Collection System Business Results

TIGTA previously reported[1] the following details and analysis of the affected ACS[2] business results. From FY 2010 to FY 2013, the number of ACS contact representatives has decreased by 39 percent. Because resources are still needed to answer taxpayer telephone calls, fewer resources are available to work new TDA and TDI inventory. This has contributed to unfavorable trends in several key business results over the past four years.

Inventory is growing

During FYs 2012 and 2013, the ACS received approximately 6.51 million and 7.07 million new TDAs, respectively. Figure 1 shows that ACS TDA open inventory grew from 5.94 million to 7.79 million (31 percent) from FY 2010 to FY 2013.

Figure 1: Modules in TDA Year-End Inventory for FYs 2010 Through 2013



Source: FYs 2010 through 2013 Collection Activity Reports (NO-5000).

Between FYs 2012 and 2013, the gap between new TDA receipts and closures increased by 47 percent. Specifically, in FY 2012, new TDAs (6.51 million) outpaced delinquent account closures (4.69 million) by 1.82 million. In FY 2013, new TDAs (7.07 million) outpaced delinquent account closures (4.40 million) by 2.67 million. Figure 2 shows that the dollar value associated with the open TDA inventory has also increased.

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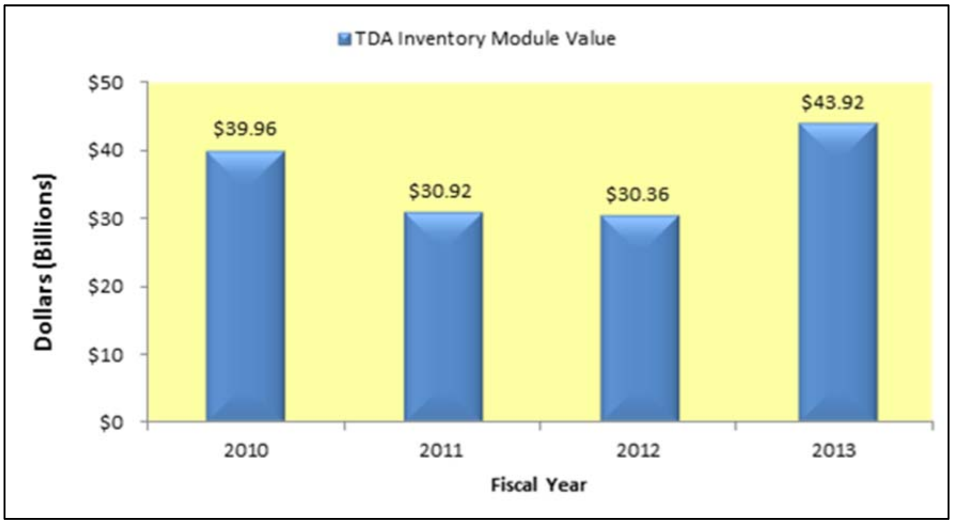
[1] TIGTA, Ref. No. 2014-30-080, *Declining Resources Have Contributed to Unfavorable Trends in Several Key Automated Collection System Business Results* (Sept. 2014).

[2] See Appendix VI for a glossary of terms.

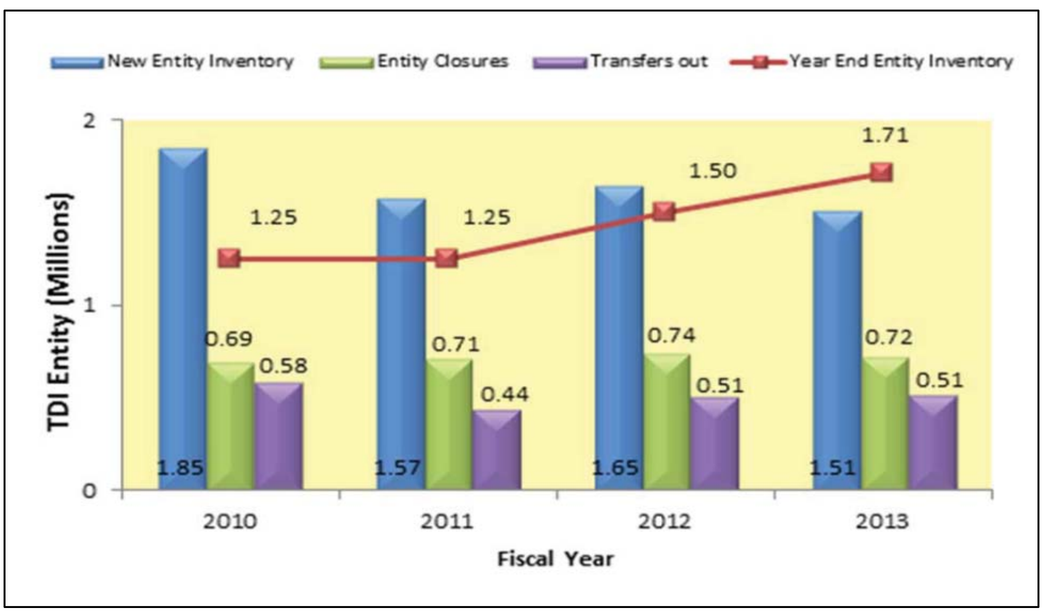
Figure 2: Value of TDA Year-End Inventory for FYs 2010 Through 2013



Source: FYs 2010 through 2013 Collection Activity Reports (NO-5000).

After decreasing from $39.96 billion in FY 2010 to $30.36 billion in FY 2012, the dollar value of the open inventory grew to $43.92 billion (45 percent) between FYs 2012 and 2013. Similarly, Figure 3 shows that the number of entities with open TDIs in ACS inventory has also increased since FY 2010.

Figure 3: Entities in TDI Year-End Inventory for FYs 2010 Through 2013

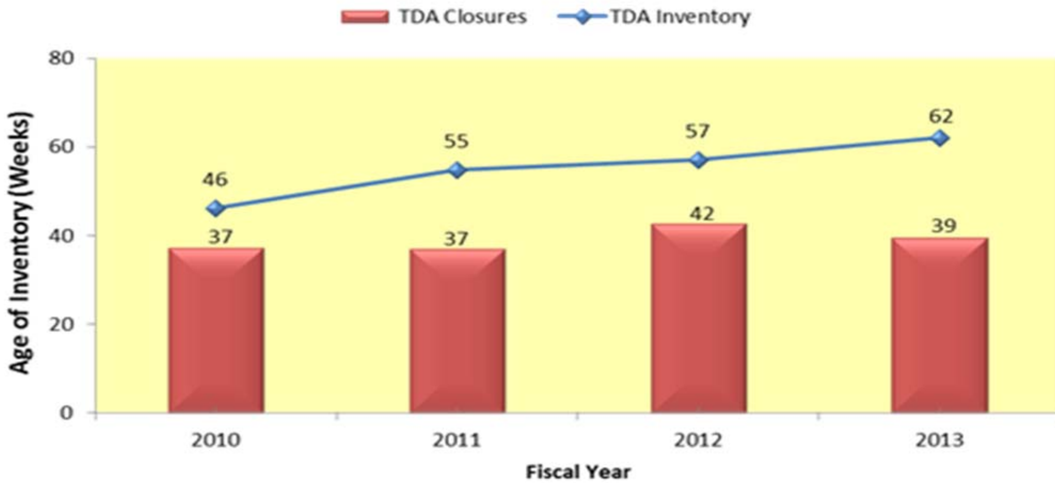


Source: FYs 2010 through 2013 Collection Activity Reports (NO-5000).

Inventory is aging and taking longer to close

Figure 4 shows that the ACS open inventory is aging and taking longer to close.

Figure 4: Age of TDA Inventory and Closures for FYs 2010 Through 2013



Source: FYs 2010 through 2013 Collection Activity Reports (NO-5000).

Between FYs 2010 and 2013, the average age of the TDAs in ACS inventory prior to being transferred out increased by 35 percent, from 46 weeks to 62 weeks. During the same period, the average time to close a delinquent account being actively worked in the ACS increased from 37 weeks to 39 weeks (5 percent). Also during the same period, TDAs 16 months[3] or older in open inventory increased by 98 percent from 1.3 million in FY 2010 to 2.57 million in FY 2013.

More cases were transferred to the Queue

Higher priority balance due accounts that are not successfully resolved by the ACS may be assigned to Field Collection for possible face-to-face contact with the taxpayer. However, because Field Collection does not have the resources to resolve all of the cases in the Queue, cases transferred to the Queue by the ACS may never be worked.

These unresolved cases may first be routed to the Queue for a significant period of time until a revenue officer can work them. Lower priority cases that are not successfully resolved by the ACS and need additional enforcement action are also assigned to the Queue, where they will remain in an inactive status until a change in the case status causes them to be reassigned to the ACS or assigned to a revenue officer. For example, a new balance due module issued on a current tax year can cause the prior period tax delinquency case to be reassigned to an active

[3] Sixteen months is the criterion the IRS uses to track the age of cases in ACS inventory.

status. As of the end of FY 2013, the Queue inventory included three million TDA tax modules involving 848,241 entities with balance due amounts totaling $49.9 billion.

Because fewer resources are working inventory, more cases are subsequently routed to the Queue. Specifically, the ACS sent 12 percent more cases to the Queue during FY 2013 than during FY 2012. As the Queue inventory grows, the number of cases that are removed from inventory and written off an uncollectible is also likely to increase. Cases can remain in the Queue until the 10-year statute of limitations[4] has expired. However, these cases become less collectible as they get older.

[4] Internal Revenue Code Section § 6502.

Appendix V

Comparison of Selected Case Attributes

Issue	GS-09 Grade	GS-12 Grade	GS-13 Grade
Taxpayer Total Positive Income	Less than $120,000	Greater than $185,000	Greater than $262,000
Financial Investigations	Basic financial investigations and analysis or routine verification of income and assets when income and assets are easy to identify.	Require in-depth, detailed financial investigations involving sophisticated and difficult issues, *e.g.*, electronic funds transfers between multiple accounts (Abusive Tax Avoidance Transactions cases included), when income and assets are difficult to trace, specialized, highly valuable, or unique.	Require investigation into complex subterfuges that conceal income and assets and delay collection. Examples include wire transfers; multiple sets of books; records from layered entities; Form 1040NR, *U.S. Nonresident Alien Income Tax Return*, filing; Abusive Tax Avoidance Transactions cases; and extensive Counsel involvement.
Enforcement Action Impact	No significant community or economic impact, *e.g.*, small business: action affecting less than 10 employees and is not expected to generate public interest.	Have a pronounced community or economic impact, *e.g.*, large-to-medium business: action affecting more than 31 employees, with the potential for media scrutiny and public reaction.	Have extensive economic impact including large business with assets more than $10 million involving more than 60 employees.
Types of Taxpayers	Deal with taxpayers and their representatives from small accounting firms or financial institutions.	Deal with representatives from large State and regional accounting firms, law firms, and financial institutions.	Require ongoing involvement with multiple suit, nominee, and transferee recommendations arising from a single case.

Source: TIGTA analysis of Internal Revenue Manual Exhibit 1.4.50-1 (Sept. 12, 2014).

Appendix VI

Glossary of Terms

Term	Definition
Automated Collection System	A telephone contact system through which telephone assistors collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.
Campus	The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.
Collection Activity Reports	Reports that provide Collection function activity information from the beginning of the fiscal year through the end of the current reporting month.
Continuing Resolution	A joint resolution enacted by Congress, when the new fiscal year is about to begin or has begun, to provide budget authority for Federal agencies and programs to continue in operation until the regular appropriations acts are enacted.
Field Collection	The unit in the Area Offices consisting of revenue officers who handle face-to-face contacts with taxpayers to collect delinquent accounts or secure unfiled returns.
Fiscal Year	Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.
IRS Oversight Board	A nine-member independent body charged to oversee the IRS in its administration, management, conduct, direction, and supervision of the execution and application of Internal Revenue laws and to provide experience, independence, and stability to the IRS so it may move forward in a cogent, focused direction.

Term	Definition
Level of Service	The percentage of calls answered compared to the number of calls attempted.
Queue	An automated holding file for unassigned inventory of delinquent cases for which employees in the Collection Field function are unable to be immediately assigned for contact due to limited resources.
Revenue Officer	Employees in the field who attempt to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses or the ACS.
Sequestration	When an amount of money equal to the difference between the cap set in the Budget Resolution and the amount actually appropriated is "sequestered" by the Department of the Treasury and not handed over to the agencies to which it was originally appropriated by Congress.
Tax Gap	The estimated difference between the amount of tax that taxpayers should pay and the amount that is paid voluntarily and on time.
Taxpayer Delinquency Investigation	An unfiled tax return(s) for a taxpayer. One taxpayer delinquency investigation is issued for each delinquent tax period for a taxpayer.
Taxpayer Delinquent Account	A balance due account of a taxpayer. One taxpayer delinquent account exists for all delinquent tax periods for a taxpayer.

Appendix VII

Management's Response to the Draft Report

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

COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

APR 16 2015

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Karen Schiller
Commissioner, Small Business/Self-Employed

SUBJECT: Draft Audit Report – Reduced Budgets and Collection Resources Have Resulted in Declines in Taxpayer Service, Case Closures and Dollars Collected (Audit # 201330010)

Thank you for the opportunity to review the subject draft report which examined the impact the IRS budget reductions have had on our collection programs and employees. We appreciate your acknowledgment of the "formidable budgetary challenges" confronting the IRS and our Collection program.

The IRS has sustained budget cuts for the last five years, resulting in our 2015 enacted budget being more than $1.2 billion below our 2010 enacted budget. The reality of these budget cuts required drastic curtailments across the agency. While non-labor costs (training, technological updates, supplies) sustained the most extensive cuts, reductions to our labor workforce were unavoidable. Indeed, since Fiscal Year 2010, our Automated Collection Service (ACS) collection representative staffing has decreased by 21 percent and the number of Field Collection revenue officers has decreased by 28 percent.

ACS and Field Collection are two critical parts of the IRS's overall collection program, and perform a vital role in collecting unpaid taxes from delinquent taxpayers, which in turn ensures equitable treatment for the majority of taxpayers who timely and fully pay their taxes and also promotes voluntary compliance by serving as a deterrent to potentially delinquent taxpayers. The cuts to our collection resources and program translate into a direct reduction in the nation's overall revenue collection, which in turn expands the tax gap and erodes taxpayer confidence in the voluntary compliance model. These are troubling trends that cannot be quickly and easily reversed.

Internally, the budget cuts have derailed our plans for updating some of our IT infrastructure and led to a delayed roll-out of updates to our employees' outdated laptops using outdated software. As your report points out, these computer issues negatively impacted productivity, and the resulting computer downtime was the equivalent of losing 32 full-time revenue officers for the year. To put this in context, that translates into a loss of 1% of our total revenue officer workforce and a lost opportunity cost of $32.6 million dollars (as the average amount collected per revenue officer is more than $1 million per year).

Despite these challenges, our Collection program continues to fulfill its mission to collect delinquent taxes and secure delinquent tax returns through the fair and equitable application of the tax laws. In Fiscal Year 2014, we updated our analytical models to identify and work our most productive inventory sooner. We also enhanced our online payment agreement system, allowing both individuals and certain businesses to use the system. In Fiscal Year 2015, we realigned the Agency Collection program entirely within the Small Business/Self-Employed Division. Our realigned Collection Organization provides streamlined leadership accountability, makes processes more efficient, reduces redundancies, and helps us to quickly identify emerging issues. Additionally, call site, campus, field, and headquarters organizations are now aligned to eliminate barriers and ensure that strategic decisions support collection-wide operational goals.

We will continue to look for ways to maintain taxpayer service and fulfill our mission of collecting unpaid taxes. But, as you acknowledge in your report, this will be increasingly difficult if staffing continues to decrease. We're hopeful that streamlining procedures and processes, engaging employees, and earlier intervention working productive cases will help us maximize our effectiveness.

Attached is a detailed response outlining our corrective actions. If you have any questions, please contact me, or a member of your staff may contact Scott Prentky, Director, Collection, at 954-423-7318.

Attachment

Attachment

RECOMMENDATION 1:
The Director, Collection, Small Business/Self-Employed Division, should ensure that revenue officer inventory levels are maintained at close to full capacity while ensuring the inventory levels are commensurate with the complexity of the cases.

CORRECTIVE ACTIONS:
1. We will issue a memorandum reminding our Field Collection group managers to ensure that their revenue officer inventory levels are within current inventory levels and appropriate, taking into account the complexity of the cases.
2. We also will evaluate whether the current inventory ranges for revenue officers are appropriate as part of our ongoing study on the complexity of Field Collection cases.

IMPLEMENTATION DATE:
1. September 15, 2015
2. April 15, 2016

RESPONSIBLE OFFICIALS:
1. Director, Field Collection, Small Business/Self-Employed Division
2. Director, Collection Policy, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:
We will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 2:
The Director, Field Collection, Small Business/Self-Employed Division, should ensure that GS-13 grade revenue officers are working appropriate cases, and when possible, increase the percentage of GS-13 grade cases assigned to GS-13 grade revenue officers.

CORRECTIVE ACTION:
We will issue a memorandum reminding our Field Collection group managers to ensure that their revenue officers are assigned and working appropriate cases. We will ask them to increase the percentage of Grade 13 cases assigned to Grade 13 revenue officers when possible.

IMPLEMENTATION DATE:
September 15, 2015

RESPONSIBLE OFFICIAL:
Director, Field Collection, Small Business/Self-Employed Division

2

CORRECTIVE ACTION MONITORING PLAN:
We will monitor this corrective action as part of our internal management system of controls.