



*Processes Do Not Adequately Reduce the
Risk That Outside Employment Activities Will
Conflict With Employees' Official Duties*

September 25, 2019

Reference Number: 2019-10-080

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.

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HIGHLIGHTS

PROCESSES DO NOT ADEQUATELY REDUCE THE RISK THAT OUTSIDE EMPLOYMENT ACTIVITIES WILL CONFLICT WITH EMPLOYEES' OFFICIAL DUTIES

Highlights

Final Report issued on
September 25, 2019

Highlights of Reference Number: 2019-10-080
to the Commissioner of Internal Revenue.

IMPACT ON TAXPAYERS

The *Standards of Ethical Conduct for Employees of the Executive Branch* specifically prohibit Executive Branch employees from engaging in outside employment or any other outside activity that conflicts with their official duties. Conflict of interest can compromise the integrity of tax administration and erode public confidence that the IRS administers the Nation's tax laws fairly and equitably.

WHY TIGTA DID THE AUDIT

TIGTA previously reported that approximately 50 percent of full-time IRS employees who had outside employment reported on Form W-2, *Wage and Tax Statement*, or Form 1040, *U.S. Individual Income Tax Return*, Schedule C, *Profit or Loss From Business*, did not have approval or the activities were not documented in the Outside Employment System (OES). This audit was initiated to determine whether the IRS has implemented controls to provide reasonable assurance that outside employment activities are approved, tracked, and reviewed for potential conflicts of interest.

WHAT TIGTA FOUND

The IRS does not have processes to identify employees with unapproved prohibited outside employment. TIGTA identified 167 employees who potentially engaged in prohibited activities such as tax preparation, and 2,196 employees who hold positions that, depending on the nature of the outside employment activity, have a

higher risk for a real or perceived conflict of interest.

In addition, the OES does not ensure that employees comply with outside employment requirements. The Human Capital Office does not perform regular quality reviews of the system to ensure its accuracy. Managers also did not review or timely review 9,063 (64 percent) of the 14,155 employee requests in the OES in Tax Year 2018 as required.

Lastly, the system that contains the OES will no longer be available. The IRS is still unsure where the OES will be housed in the future.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Director, Workforce Relations Division, review the employees identified by TIGTA and ensure that appropriate action is taken to address any prohibited activities or conflicts of interest; work with the IRS's Office of Chief Counsel to evaluate whether a legislative proposal is needed to enable the IRS to use tax data to identify employees engaged in outside employment activities that involve potentially prohibited activities; require employees to submit all outside employment requests using the OES and resubmit all requests for approval during a designated time frame; and create a plan for housing the OES or create a new database to track outside employment activities.

In their response, IRS management agreed or partially agreed with most of the recommendations. Management could not commit to requiring bargaining unit employees to submit outside employment requests using the OES because such a change must be negotiated and included in the National Agreement.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 25, 2019

MEMORANDUM FOR COMMISSIONER OF INTERNAL REVENUE

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Processes Do Not Adequately Reduce the Risk That Outside Employment Activities Will Conflict With Employees' Official Duties (Audit # 201810025)

The report presents the results of our review to determine whether the Internal Revenue Service (IRS) has implemented controls to provide reasonable assurance that outside employment activities are approved, tracked, and reviewed for potential conflicts of interest. This is a follow up to a prior Treasury Inspector General for Tax Administration audit.¹ This review is included in our Fiscal Year 2019 Annual Audit Plan and addresses the major management challenge of Security Over Taxpayer Data and Protection of IRS Resources.

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 Heather Hill, Acting Assistant Inspector General for Audit (Management Services and Exempt Organizations).

¹ Treasury Inspector General for Tax Administration, Ref. No. 2014-10-073, *Controls Over Outside Employment Are Not Sufficient to Prevent or Detect Conflicts of Interest* (Sept. 2014).



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Abbreviations

C.F.R.	Code of Federal Regulations
HCO	Human Capital Office
IRS	Internal Revenue Service
OES	Outside Employment System
TIGTA	Treasury Inspector General for Tax Administration
TY	Tax Year



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Background

The *Standards of Ethical Conduct for Employees of the Executive Branch* (hereafter referred to as the Standards of Ethical Conduct)¹ generally require Executive Branch employees to be free of conflicts of interest, either actual or perceived, that can impair their ability to carry out their official duties. The Standards of Ethical Conduct specifically prohibit Executive Branch employees from engaging in outside employment or any other outside activity that conflicts with their official duties.² According to the Standards of Ethical Conduct, an activity conflicts with an employee's official duties if:

- (a) It is prohibited by statute or by an agency supplemental regulation or
- (b) It would require an employee to disqualify himself or herself from matters so central to or critical to the employee's official duties that the employee's ability to perform those duties would be materially impaired.³

In addition to the prohibitions in the Standards of Ethical Conduct, the Code of Federal Regulations (C.F.R.) prohibit Internal Revenue Service (IRS) employees from receiving outside compensation for performing legal and tax-related activities.⁴ Bookkeeping or accounting activities related to tax determination matters are also generally prohibited.⁵

The *Ethics Handbook* requires IRS employees to obtain prior approval before engaging in most outside employment or business activities (hereafter referred to as outside employment).⁶ Outside employment that does not require approval includes activities such as serving in a union, in the National Guard or Reserves, or on a homeowner's association; renting property; serving as a notary public; or performing minor services for friends, family, or neighbors.

IRS employees wishing to engage in outside employment may submit their request through the Outside Employment System (OES). The OES serves as a single repository for information related to IRS employees' outside employment. Employees may also submit a completed Form 7995, *Outside Employment or Business Activity Request*, to their manager for approval. Upon receipt, the employee's manager is required to input the Form 7995 information into the OES. The OES contained 14,155 requests for outside employment as of August 22, 2018.

¹ See Appendix VI for a glossary of terms.

² 5 Code of Federal Regulations (C.F.R.) § 2635.802.

³ Conditions that require disqualification are provided in C.F.R. §§ 2635.402 and 2635.502 of the Standards of Ethical Conduct.

⁴ 5 C.F.R. § 3101.106.

⁵ Additional information about the general rules for outside employment and business activities is included in Appendix V.

⁶ IRS, Document 12011, *IRS Ethics Handbook*, Chapter 10 (July 2018).



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Managers are to review the outside employment request and approve or deny the request within 10 business days of receipt. Managers are also required to review previously approved requests annually to:

- Ensure that the information is still accurate.
- Ensure that the approved activity does not conflict with the employee's current IRS duties.
- Determine if the approval should be continued, rescinded, or resubmitted.

If there are no changes, the supervisor must enter the review date on the OES. If there have been any changes to the employee's position or duties at either the IRS or the outside employment activity, or the employee is no longer performing the outside employment or business activity, managers must update and delete the previously approved request(s) in the OES.⁷

The *IRS Manager's Guide to Penalty Determinations* establishes the suggested range of penalties for IRS employees who fail to get approval prior to participating in outside employment or engaging in prohibited outside employment activities.⁸ The penalties range from admonishment for a first offense to suspension or removal for multiple offenses.

In September 2014, the Treasury Inspector General for Tax Administration (TIGTA) reported that nearly 3,000 (approximately 50 percent) of the more than 6,000 full-time, active IRS employees who received income reported on Form W-2, *Wage and Tax Statement*, and Form 1040, *U.S. Individual Income Tax Return*, Schedule C *Profit or Loss*, during Calendar Year 2011 from a source other than the IRS did not have approval for outside employment or the activities were not documented in the OES.⁹ TIGTA also determined that the OES database is ineffective for identifying potential conflicts of interest due to incomplete or out-of-date records. Finally, TIGTA found that the IRS had no processes to identify employees who were engaged in unapproved outside employment activities.

In response to our recommendations, IRS management agreed to require submission of all outside employment requests through the OES and assigned oversight and responsibility of the OES to the Human Capital Office (HCO) Workforce Relations Division.¹⁰ The IRS also performed a one-time cleanup of the OES. However, IRS management disagreed with our recommendation that the HCO work with the IRS's Office of Chief Counsel to evaluate whether a legislative proposal is needed to amend Internal Revenue Code Section (§) 6103 to enable the

⁷ Deleted requests are moved to OES historic files.

⁸ IRS, Document 11500, *IRS Manager's Guide to Penalty Determinations* (Aug. 2012).

⁹ TIGTA, Ref. No. 2014-10-073, *Controls Over Outside Employment Are Not Sufficient to Prevent or Detect Conflicts of Interest* (Sept. 2014).

¹⁰ IRS employees have the option to request outside employment electronically using the OES or to use the Form 7995. Managers must record the Form 7995 requests in the OES.



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IRS to use tax data to identify employees who are engaging in outside employment without approval.

This review was performed with information obtained from the HCO and the HCO Workforce Relations Division located in Nashville, Tennessee, and from the Official Personnel File Consolidated Site in Lee's Summit, Missouri, during the period June 2018 through July 2019. 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.



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Results of Review

**Employees Were Potentially Engaged in Prohibited Outside
Employment Activities**

Our review of Tax Year (TY) 2016 income tax data identified 167 employees who were potentially engaged in a prohibited employment activity and did not have an approved request in the OES. In addition, we identified 2,196 employees with outside employment activity who hold IRS positions that have a high risk of an actual or perceived conflict of interest as a result of the outside employment but did not have an approved outside employment request. Federal regulations prohibit employees from engaging in activities such as tax and accounting services because these activities have a higher risk of creating a conflict of interest. These policies specifically prohibit IRS employees from preparing taxes for compensation. Certain positions within the IRS have a higher risk for a conflict of interest than other positions due to the nature of their official duties. As a result, an actual or perceived conflict can arise if these employees are asked to examine or investigate their outside employer. Employees who have an actual or perceived conflict of interest can compromise the integrity of tax administration and erode public confidence that the IRS administers the Nation's tax laws fairly and equitably.

**Employees were potentially engaging in prohibited activities that conflict with
their tax administration responsibilities**

We identified 167 employees who were potentially engaged in a prohibited employment activity.¹¹ We determined that these employees did not have approval to engage in outside employment. We also identified three employees who have an active Preparer Tax Identification Number that was used on one or more tax returns indicating that the employee was paid to prepare the tax return. In addition, some of the employees we identified worked for organizations whose primary business involves prohibited employment activity. For example, five employees received income from the tax preparation service company H&R Block. Figure 1 shows the number of employees who are potentially engaged in a prohibited activity.¹²

¹¹ Six employees had income records for multiple business categories.

¹² The tax information is not conclusive evidence of prohibited activity because it does not describe the employee's duties or responsibilities. This analysis was limited to tax information reported by organizations whose primary business is a prohibited activity.



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**Figure 1: IRS Employees Potentially Engaged
in Prohibited Employment Activity**

Outside Employment Type	Number of Employees
Accounting	51
Legal Services	45
Financial Services ¹³	30
Bookkeeping	25
Taxation	22

Source: TIGTA analysis of TY 2016 tax return information.¹⁴

A significant number of employees in positions with a high risk of a conflict of interest are engaged in unapproved outside employment activities

Certain IRS employees hold positions that have a high risk of an actual or perceived conflict of interest as a result of outside employment. For example, revenue agents and criminal investigators examine taxpayer returns for compliance with the tax laws or investigate potential taxpayer fraud. In addition, employees in these positions have knowledge of the IRS's internal processes and dollar value thresholds that can be used to benefit another employer. We categorized more than 45,000 IRS employees as holding positions that would have a high risk of an actual or perceived conflict of interest if those employees engaged in outside employment. Our analysis determined that more than 3,700 (8 percent) of these employees engaged in outside employment in TY 2016. Of these 3,700 employees, approximately 42 percent had an approved outside employment request on file with the IRS. The remaining 2,196 employees earned income in TY 2016, but did not have an approved outside employment request. We found that revenue agents had more unapproved outside employment activities than any other IRS position. Figure 2 shows the IRS positions we identified with the highest occurrence of unapproved outside employment activity.

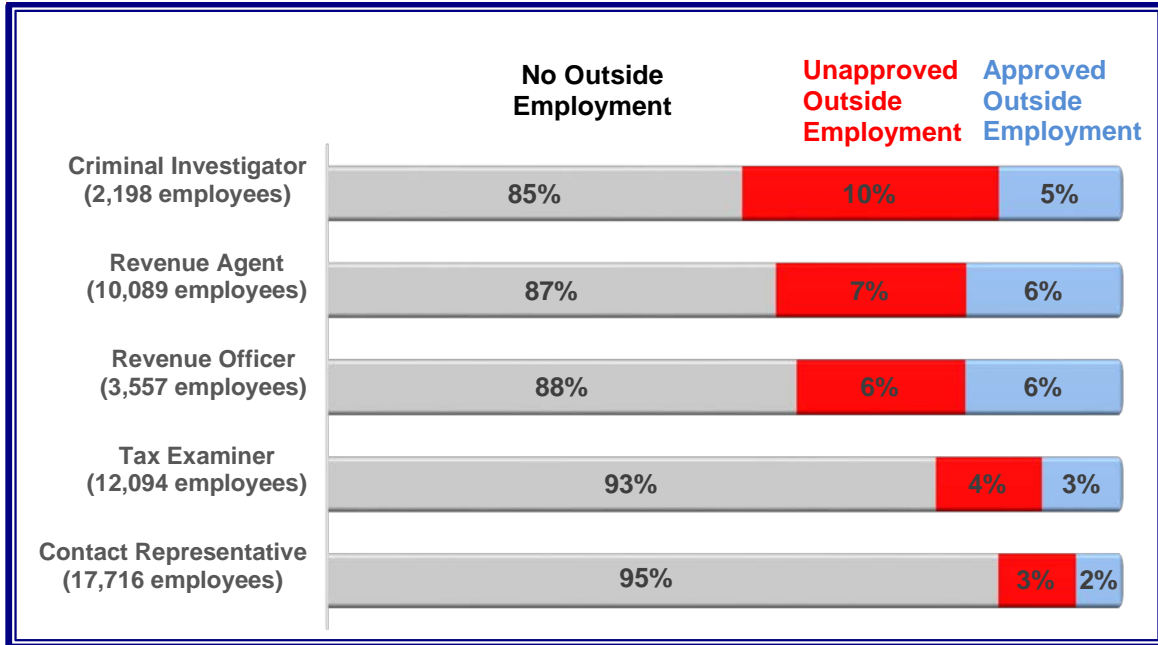
¹³ Financial services companies included Fidelity Investments, JPMorgan, Charles Schwab, and other small investment companies. IRS employees are prohibited from engaging in accounting or the use, analysis, and interpretation of financial records when such activity involves tax matters. Employment with financial services companies could constitute prohibited activity depending on the nature of the employment.

¹⁴ Tax return information included the IRS Individual Returns Transaction File, the Information Returns Master File, the OES, and the Treasury Integrated Management Information System.



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**Figure 2: IRS Positions With the Highest Occurrence of
Unapproved Outside Employment Activity**



Source: TIGTA analysis of TY 2016 tax return information.

Our analysis of TY 2016 IRS employee data showed that for all of these positions, more employees with outside employment did not have approval than those who had approval. In addition, the occurrence of employees who earned income without approval was high. For example, approximately 10 percent (211 employees) of all IRS criminal investigators earned some kind of outside income without approval. Similarly, approximately 7 percent (727 employees) of all IRS revenue agents engaged in unapproved outside employment activities.¹⁵

The IRS informs employees about its policies for outside employment at the time they are hired and reminds them annually of their responsibility to obtain prior approval for outside employment activities. However, this reminder is sent via e-mail and is included with other annual administrative reminders, some of which may not be applicable to all employees. As a result, the outside employment reminder may be overlooked.

Our review of IRS internal guidance also found that employees may misinterpret the *Outside Employment and Business Activity Guidelines*. The guidance provides the general requirements for requesting approval for outside employment. The guidelines also state employees do not need approval for:

¹⁵ We analyzed the “employee series” from the Treasury Integrated Management Information System.



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Membership and services (including holding of office) in civic, scout, religious, educational, fraternal, social, community, veteran, and charitable organizations, including corporations, where such office or services do not entail the management of a business-type activity such as the direct operation of a commercial type clubhouse.¹⁶

However, employees may not understand what activities involve the “*management of a business-type activity.*” For example, employees who engage in accounting services for a corporation may think they do not need permission for such activities because they are not in a management position or directly involved in the management of the business. IRS management confirmed that the guidance applies to entities that are corporations, and management provided “a home owner’s association” as an example of this provision. However, the guidance does not include this example, and an employee could incorrectly conclude that all corporations are included in the list of organizations for which an employee does not need prior approval for employment.

The IRS still has not implemented processes to identify employees with potential conflicts of interest

We previously reported that the IRS did not have a process to identify employees who were not complying with the outside employment requirements. We recommended the IRS evaluate whether a legislative change was needed to authorize it to perform analyses of employee income information to identify employees with unapproved outside employment. IRS management disagreed with our recommendation stating that they did not feel it was appropriate for the IRS to use such information for this purpose. The IRS has taken no additional steps to implement a process to identify employees who have unapproved outside employment who were potentially engaged in a prohibited employment activity. However, HCO management stated that they are continuing to seek advice from their Chief Counsel on using income information to identify employees with unapproved outside employment. Our review of the Automated Labor and Employee Relation Tracking System used by the IRS to track the resolution of employee misconduct also shows that few IRS employees are disciplined for outside employment issues. Over the past five years, from 2014 to 2018, the IRS disciplined 40 employees for outside employment issues, and 13 were suspended or removed from service.¹⁷

¹⁶ IRS, *IRS Outside Employment and Business Activity Guidelines*, page 3 (July 2015).

¹⁷ We identified IRS employees with discipline for outside employment issues by reviewing the Automated Labor and Employee Relations Tracking System for issue code 23, Outside Employment.



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Recommendations

The Director, Workforce Relations Division, should:

Recommendation 1: Review the 2,196 employees who hold IRS positions that have responsibility for tax matters and the 167 employees who are potentially engaged in prohibited activity, who earned income in TY 2016 but did not have an approved outside employment request, and ensure that appropriate action is taken to address any prohibited activities or conflicts of interest.

Management's Response: The IRS partially agreed with this recommendation. Management will adjudicate the 167 issues referred for investigation upon receipt of these cases from TIGTA's Office of Investigations. However, IRS management does not believe monitoring employees' outside employment activity constitutes tax administration, and it therefore may not access the tax records for the 2,196 cases without a referral from TIGTA's Office of Investigations. Therefore, the IRS will refer these cases to TIGTA's Office of Investigations.

Office of Audit Comment: Management's planned corrective action meets the intent of the recommendation.

Recommendation 2: Update the outside employment guidelines to clarify what outside employment activities require approval.

Management's Response: The IRS agreed with this recommendation. The IRS will update the outside employment guidelines with the activities that require approval.

Recommendation 3: Work with the IRS's Office of Chief Counsel to evaluate whether a legislative proposal is needed to amend Internal Revenue Code § 6103 to enable the IRS to use tax data to perform analyses and identify employees engaged in outside employment activities that involve potentially prohibited activities.

Management's Response: The IRS Office of Chief Counsel has already advised that monitoring IRS employee outside employment is not a tax administration purpose and that as currently enacted Internal Revenue Code § 6103 does not permit the IRS to use employee return information to monitor employee outside employment. The IRS agreed to partner with its legal advisers, the Office of Chief Counsel, and the Department of the Treasury to evaluate whether the IRS should seek a statutory amendment to Internal Revenue Code § 6103 to allow the IRS to review employee tax returns to monitor outside employment.



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The Outside Employment System Is Ineffective in Ensuring That Employees Comply With Outside Employment Requirements

The IRS took several actions in response to our prior recommendations to improve the completeness and accuracy of the OES. However, the OES continues to be inaccurate and incomplete pertaining to outside employment activities. Specifically, we identified 9,063 requests that were not reviewed or not reviewed timely.¹⁸

IRS management uses the OES to facilitate its review of outside employment requests to ensure that they do not present a conflict of interest with an employee's official duties. As such, it is imperative that the IRS have sufficient controls in place to monitor and update employment requests, particularly when IRS employees change positions after their outside employment was approved.

In response to our prior recommendations, the IRS assigned oversight of the OES to the Workforce Relations Division within the HCO. After our review, the HCO performed a one-time cleanup of the OES Active File and removed almost 12,000 inaccurate or outdated requests. However, the IRS has not established processes to perform regular reviews of the OES to ensure its accuracy. Rather the IRS relies on its managers to ensure that the OES is accurate and complete. The IRS still allows employees to submit paper requests and relies on the employee's manager to enter paper requests into the OES and ensure that approved requests are still valid.

Managers are not reviewing outside employment requests as required

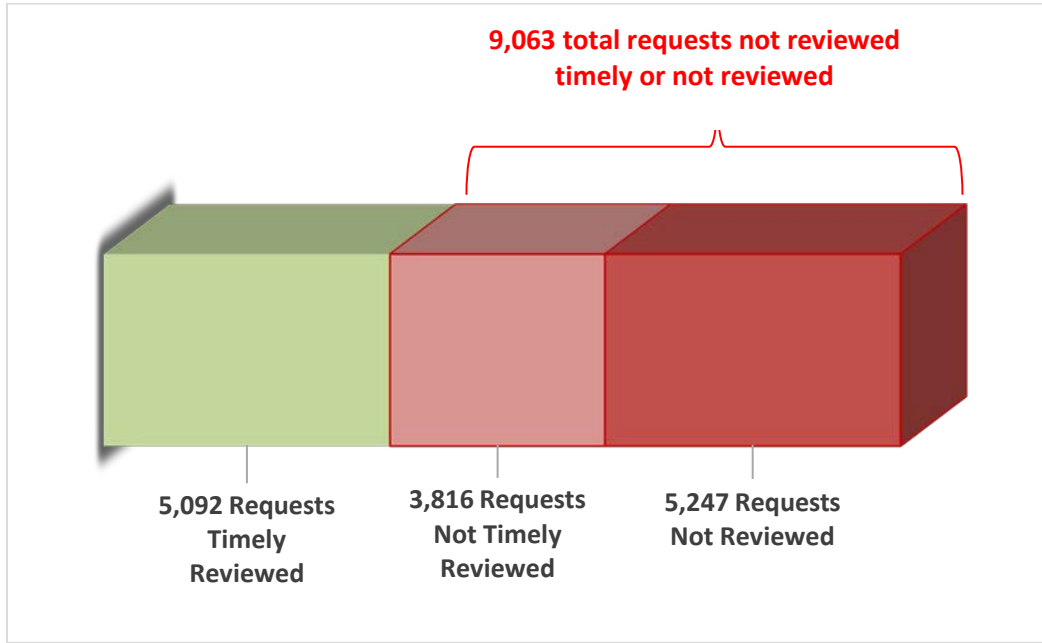
The IRS does not limit the period for which an approved outside employment request is valid. In addition, employees are not required to update their outside employment requests periodically. Instead, IRS managers are required to review previously approved requests annually to ensure that the request is still valid and does not present a conflict with the employee's current duties. We found that managers are not conducting the annual reviews as required. Our review of the 14,155 active requests in the OES as of August 2018 found that 9,063 (64 percent) requests were not reviewed or were not reviewed timely. Figure 5 shows the number of active outside employment requests that were reviewed as of August 2018.

¹⁸ The 14,155 active requests includes full-time, part-time, and seasonal employees. These requests are from TY 2018 and are different than the requests from TY 2016.



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Figure 3: Timeliness of Review Dates in the OES as of August 2018



Source: TIGTA analysis of the OES Active File.¹⁹

Although the HCO requires all requests be entered into the OES, it places the responsibility of maintaining the data on IRS managers. When employees use paper Forms 7995 to request approval, managers must transcribe the information into the OES for them. Employees are not required to resubmit requests for outside employment activities each year. Instead, it is incumbent upon managers to remember when a year has passed for each employee, and those anniversaries can occur anytime throughout the year. Currently, there are no automated reminders in the OES to remind managers when a request is due for recertification. IRS management stated that they do not have the resources to designate a person to monitor due dates, which is one reason annual reviews are missed. Management stated that future OES enhancements expected in September 2019 will include automated reminders.

In response to our prior recommendation, the IRS updated the outside employment guidance to require using the OES to request and approve outside employment requests. However, the IRS still allows employees to submit a paper Form 7995 to their manager. The manager is required to review the request for approval and transcribe the Form 7995 into the OES. This creates a lack of separation of duties within the outside employment process. In addition, it is possible that managers would overlook entering a paper outside employment request into the OES given their many other responsibilities. By requiring employees to only submit outside employment requests in the OES, the IRS can separate the duties for recording and reviewing the requests and

¹⁹ The OES Active File used for our analysis was last updated August 22, 2018.



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allow management to focus on their responsibility to ensure that the requested employment does not conflict with the employee's official duties.

The OES's future is uncertain

Workforce Relations Division management stated that the OES will no longer be housed on the Totally Automated Personnel System which also houses the IRS's Single Entry Time Reporting system. The IRS plans to migrate the time reporting system from the Totally Automated Personnel System to a new supporting system. As of July 2019, IRS management was still unsure about where the OES will be housed after the existing system is closed.

As noted previously, there were 14,155 requests for outside employment in the OES as of August 2018. Each of these requests represents a potential for a conflict of interest with the employee's official duties. The OES enables the IRS to track employees outside employment and ensure that the employment does not compromise an employee's ability to fulfill his or her duties for the IRS. While the OES continues to need improvement, it is still a more efficient and effective process than trying to manage the thousands of employee outside employment requests manually.

Recommendations

The Director, Workforce Relations Division, should:

Recommendation 4: Establish processes to conduct periodic quality reviews to ensure that the OES is accurate.

Management's Response: The IRS agreed with this recommendation. The IRS will revise the Internal Revenue Manual by adding responsibilities for employees, managers and business unit points of contact, such as periodic quality reviews. Points of contact will receive training and meet on a recurring basis.

Recommendation 5: Remove the paper Form 7995 as an option to request outside employment and require IRS employees to submit all outside employment requests through the OES.

Management's Response: The IRS stated that it is unable to agree with this recommendation at this time. While non-bargaining unit employees are required to submit requests in the OES, the IRS stated that it may not unilaterally require bargaining unit employees to submit all outside employment requests through the OES. IRS management will instead need to negotiate a change to the National Agreement before requiring electronic submission of requests.

Office of Audit Comment: TIGTA believes the topic of mandatory electronic outside employment requests should be included in future bargaining negotiations and National Agreements.



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Recommendation 6: Revise internal outside employment guidelines to require employees to resubmit their outside employment requests at least annually and modify the OES to allow for the systemic closure of all requests for which a renewal was not timely received. OES modifications should include the ability to notify any employees whose request was closed.

Management's Response: The IRS agreed to consider having all employees resubmit their requests annually and having systemic closure of requests if the annual review is not timely, after bargaining obligations are determined. The IRS will request a system modification to generate e-mail notifications to employees when their request is closed.

Recommendation 7: Work with the IRS Information Technology organization to create a plan for housing the OES or to create a new database to ensure that outside employment requests are tracked after the Totally Automated Personnel System is shut down.

Management's Response: The IRS agreed with this recommendation. IRS management will continue meeting with the Department of the Treasury for options to replace the Totally Automated Personnel System. Pending replacement, the IRS will continue to make improvements to the system, which will remain operational until a decision is made for an alternate system.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective of this audit was to determine whether the IRS has implemented controls to provide reasonable assurance that outside employment activities are approved, tracked, and reviewed for potential conflicts of interest. To accomplish our objective, we:

- I. Determined whether the IRS implemented corrective actions in response to the recommendations from the previous report on outside employment.¹
 - A. Reviewed the OES² to ensure that a one-time cleanup of the OES took place to remove outdated records and to determine whether supervisors are performing an annual recertification of existing outside employment requests.
 - B. Validated OES data and prepared a Data Reliability Assessment. We reviewed the OES data and confirmed the validity of the data with the IRS and determined the data to be sufficiently reliable for our purposes.
- II. Determined if the IRS has controls in place to reasonably assure that outside employment activities do not potentially conflict with employees' official duties.
 - A. Determined the IRS's guidelines regarding employees engaging in prohibited outside employment or activities that conflict with their IRS duties. We determined how these guidelines are communicated to IRS employees.
 - B. Determined if IRS employees have any indications of potential conflicts of interest or prohibited outside employment.
 1. Identified the population of IRS employees with outside sources of income in Calendar Year 2016. We used the TIGTA Data Center Warehouse to compare current IRS employees who were full-time or part-time for all of Calendar Year 2016 to their TY 2016 tax return data (Form W-2, *Wage and Tax Statement*; Form 1099-K, *Payment Card and Third Party Network Transactions*; Form 1099-Misc, *Miscellaneous Income*; Form 1040, *U.S. Individual Income Tax Return, Schedule C, Profit or Loss From Business*, and Schedule F, *Profit or Loss From Farming*). We validated the tax return data and prepared a Data Reliability Assessment. We also reviewed the tax return

¹ TIGTA, Ref. No. 2014-10-073, *Controls Over Outside Employment Are Not Sufficient to Prevent or Detect Conflicts of Interest* (Sept. 2014).

² See Appendix VI for a glossary of terms.



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information and compared it to the Integrated Data Retrieval System and determined the data to be sufficiently reliable.

2. Identified the population of employees engaging in potentially unapproved prohibited outside employment by reviewing relevant forms for certain key words, as well as certain business activity codes.
3. Matched the employee Social Security Numbers to the Automated Labor Employee Relations Tracking System to determine if there are indications of potential conflicts of interest from outside employment.³
4. Matched the populations from Step II.B.2. to the OES to determine which employees had an outside employment request that was approved and which did not.

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: Department of the Treasury regulations and IRS policies, procedures, and practices for reviewing, approving, and monitoring employee requests for outside employment and business activities. We evaluated these controls by reviewing applicable documentation; interviewing management about the process for reviewing, approving, and maintaining records of outside employment requests; testing the accuracy of the system for maintaining records of outside employment requests; and analyzing data for selected employees with multiple sources of income.

³ We looked at Automated Labor Employee Relations Tracking System records for which the employee had unauthorized accesses to tax return data, may have misused their badge/credentials, or had attendance issues. In these cases, we searched narrative fields for indications that these actions may be related to the employees' outside employment.



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Appendix II

Major Contributors to This Report

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David M. Bueter, Audit Manager
Jeffery R. Stieritz, Acting Audit Manager
John M. Jarvis Jr., Lead Auditor
Nicole J. Blank, Auditor



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Appendix III

Report Distribution List

Deputy Commissioner for Operations Support
Human Capital Officer
Director, Workforce Relations Division
Director, Office of Legislative Affairs
Director, Enterprise Audit Management



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Appendix IV

Outcome Measure

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

Type and Value of Outcome Measure:

- Reliability of Information – Potential; 9,063 outside employment requests that were potentially outdated and inaccurate (see page 9).

Methodology Used to Measure the Reported Benefit:

Our review of the 14,155 active OES file records as of August 2018 identified 9,063 (64 percent) of the requests on the OES active file that were outdated and potentially inaccurate outside employment requests. Specifically, 3,816 requests were not reviewed as required in the past 12 months and 5,247 requests had no review date at all. IRS supervisors are required to review all their employees' OES records to determine if there are any changes in the employees' outside employment or business activities. If there have been any changes to an employee's position or duties at either the IRS or the outside employment activity, or if the employee is no longer performing the outside employment or business activity, the manager must update and delete the previously approved request(s) in the OES.



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Appendix V

*General Rules for Outside Employment
Requests and Approvals*

<i>Prohibited Activities¹</i>
Legal services involving Federal, State, or local tax matters.
Appearing on behalf of any taxpayer before any Federal, State, or local governmental agency in an action involving a tax matter, except with the written authorization of the Commissioner of the IRS.
Outside activity (unless otherwise permitted) that deals directly with any tax-related matter. However, employees may engage in bookkeeping and accounting that is directly related to a tax determination in the following situations: keeping the books for a firm owned or run by immediate family and prospects for a conflict of interest are remote; engaging in the activity for a civic, religious, educational, or charitable nonprofit organization in which the employee is not paid for the work; or engaging in business with your spouse with permission.
<i>Allowed Activities Must:</i>
Conform to the general ethical requirements in the Office of Government Ethics Standards.
Not conflict with the employee's official duties.
Not be prohibited by statute or an agency supplemental regulation.
Not require that the employee disqualify themselves from matters so central and critical to the performance of their IRS duties as to materially impair their ability to perform those duties.
Not result in improper use of Government property.
Not result in the use or disclosure of nonpublic official information obtained in connection with the employee's Government duties or position.
Not impact the employee's effectiveness on the job.

¹ If the activity is prohibited, the employee may not do it indirectly, that is in the name of, or through family members. In addition, an employee may not advertise their employment with the IRS to generate business.



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Allowed Activities Not Requiring Written Approval

Outside activities that are not considered employment or business.

Membership and services in civic, scout, religious, educational, fraternal, social, community, veteran, and charitable organizations in which such office or services do not entail the management of a business-type activity, *e.g.*, direct operation of commercial-type clubhouse.

Membership and services (including holding office) in the local office of a credit union, which may include paid bookkeeping work performed by the treasurer, or part-time clerical or teller services.

Services as a notary public.

Minor services and odd jobs for friends, relatives, or neighbors that is not for compensation as an employee or for a business.

Furnishing advice and assistance in the preparation of tax returns for which no fee or other consideration is accepted.

Unpaid bookkeeping, preparation of tax returns and other forms required by the IRS, and maintenance of other records for civic, religious, educational, and charitable nonprofit organizations that are exempt from Federal income tax.

Source: TIGTA summary of The Office of Government Ethics Standards of Ethical Conduct for Employees of the Executive Branch, 5 CFR Part 2635, the Additional Rules for IRS Employees, 5 C.F.R. § 3101.106, and various IRS policies and procedures.



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Appendix VI

Glossary of Terms

Term	Definition
Automated Labor and Employee Relations Tracking System	A system used by the IRS to track the resolution of employee misconduct.
Code of Federal Regulations	The codification of the general and permanent rules published in the Federal Register by the executive departments and agencies of the Federal Government.
Contact Representative	Employees who provide administrative and technical assistance to individuals and businesses primarily over the telephone and/or in person.
Criminal Investigator	Conducts in-depth analysis of a wide variety of significant or highly sensitive law enforcement issues.
Data Center Warehouse	An online database maintained by TIGTA, which serves as a centralized data repository for Federal tax information and administrative data.
Individual Return Transaction File	A database that contains data transcribed from initial input of the original individual tax returns during return processing.
Information Returns Master File	IRS system that contains six years of information returns. Data can be obtained for all forms issued by a PAYER or all forms issued to a PAYEE.
Integrated Data Retrieval System	An IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.



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Term	Definition
Internal Revenue Manual	The Internal Revenue Manual enables the IRS to meet certain Federal requirements to document, publish, and maintain records of policies, authorities, procedures, and organizational operations. By law, Federal agencies are expected to document, publish, and maintain records of policies, authorities, procedures, and organizational operations. The Internal Revenue Manual is the source for the IRS.
Official Personnel File	An employee's official record of Federal employment. It contains the records the Government needs to make accurate employment decisions throughout the employee's Federal career.
Outside Employment System	Serves as a single repository for information related to IRS employees' outside employment.
Preparer Tax Identification Number	A number assigned to tax return preparers by the IRS. The Preparer Tax Identification Number, along with the tax return preparers' signature, must be included on all tax returns.
Revenue Agent	Employees who plan and conduct examinations using extensive and specialized knowledge of accounting techniques, practices, and investigative audit techniques to examine and resolve various tax issues of individuals and business organizations.
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.



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Term	Definition
Single Entry Time Reporting system	The Single Entry Time Reporting System is a computer-based system designed to accumulate time and attendance information for employees.
Standards of Ethical Conduct for Employees of the Executive Branch	A uniform set of standards applicable to all employees of the Executive Branch.
Tax Examiner	Employees who assist and advise taxpayers in meeting their Federal tax obligations.
Tax Year	The 12-month accounting period for keeping records of income and expenses used as the basis for calculating the annual taxes due.
Totally Automated Personnel System	The Totally Automated Personnel System consists of several personnel-related modules, including automated vacancy announcement and single-entry time reporting.
Treasury Integrated Management Information System	The Treasury Integrated Management Information System supports payroll and personnel processing and reporting requirements for the IRS.



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Appendix VII

Management's Response to the Draft Report



HUMAN CAPITAL OFFICE

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

September 20, 2019

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Robin D. Bailey, Jr. 
IRS Human Capital Officer

SUBJECT: Draft Audit Report – Processes Do Not Adequately Reduce the
Risk that Outside Employment Activities Will Conflict with
Employees' Official Duties (Audit #201810025)

Thank you for the opportunity to review TIGTA Draft Report #201810025, *Processes Do Not Adequately Reduce the Risk that Outside Employment Activities Will Conflict with Employees' Official Duties*, dated August 9, 2019. The IRS takes seriously our responsibility to ensure employees abide by the 14 General Principles of Ethical Conduct, as stated in Title 5 of the Code of Federal Regulations § 2635.101(b), and we are committed to improving our controls to provide reasonable assurance that outside employment activities are tracked and reviewed for potential conflicts of interest.

Of the seven recommendations in the Report, we agree with six, and disagree with one as specified in the attachment hereto. We agree that individual cases of potentially conflicting outside employment justify reviewing that individual's return information and properly addressing any conflicts. We look forward to implementing future technological changes that will alert management to update employee records, as appropriate.

We note that the method TIGTA used to identify employees with outside employment income is inconsistent with the longstanding interpretation by IRS Chief Counsel of the parameters of Internal Revenue Code § 6103 and what constitutes tax administration, as we have explained previously. As custodians of the nation's tax system, we have a duty to protect the privacy of taxpayers, and we do not agree that the Code authorizes the IRS to review IRS employees' federal tax returns or other return information to monitor outside employment.

We are seeking to employ technology to improve efficiency and reporting capabilities in many areas; accordingly, we agree in principle with recommendation 5 which recommends requiring all IRS employees to submit outside employment requests through the outside employment system (OES) exclusively. Article 6 of the 2019



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National Agreement requires employees to submit outside employment requests in writing and states that "[a]n employee will use the electronic or paper Form 7995 (Exhibit 6-1) when making a request for outside employment." Accordingly, the IRS may not unilaterally require that employees submit all requests electronically through the OES; instead, we will need to negotiate a change to this article.

We appreciate your support as we continue to improve our outside employment process. We believe increased oversight, recurring periodic reviews of system data, and automation enhancements will result in significant improvements. However, we continue to fundamentally disagree whether monitoring IRS employees' outside employment is a tax administration function. You may be interested to know the first phase of systemic automated email notifications is now in effect such that immediately after an outside employment request is added to the system, the employee's managers receive an email to process it.

We have attached our responses to your recommendations along with the corrective actions the IRS Human Capital Officer will take to address them.

If you have any questions, please contact me at 202-317-7600, or a member of your staff may contact Julia Caldwell, acting director, Workforce Relations Division, at 202-317-6289.

Attachment



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Attachment

RECOMMENDATION 1:

Review the 2,196 employees that hold IRS positions that have responsibility for tax matters and the 167 employees who are potentially engaged in prohibited activity, who earned income in TY 2016, but did not have an approved outside employment request. Ensure appropriate action is taken to address any prohibited activities or conflicts of interest.

• **CORRECTIVE ACTION:**

We agree. We will adjudicate the 167 issues referred for investigation upon receipt of these cases from TIGTA. As stated previously, we find the method used by TIGTA to identify outside income is inconsistent with the longstanding interpretation by IRS Chief Counsel of the parameters of Internal Revenue Code § 6103 and what constitutes tax administration. Pursuant to Counsel guidance, monitoring IRS employees' outside employment is not a tax administration purpose. Therefore, we are unable to utilize the list of 2,196 employees identified by TIGTA's accessing employee return information without an official referral from TIGTA like that used for the 167 issues. To maintain the integrity of the process, we will refer the 2,196 employees identified by TIGTA to the office of investigations for their review. By June 15, 2020, we will provide a report regarding adjudication of 167 employees and the status of the 2,196 cases referred to the TIGTA office of investigations.

• **IMPLEMENTATION DATE:**

June 15, 2020

• **RESPONSIBLE OFFICIAL:**

Acting Director, Workforce Relations Division

• **CORRECTIVE ACTION MONITORING PLAN:**

We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it monthly until completed.

RECOMMENDATION 2:

Update the outside employment guidelines to clarify what outside employment activities require approval.

• **CORRECTIVE ACTION:**

We agree with this recommendation. We will update the outside employment guidelines with the activities that require approval.

• **IMPLEMENTATION DATE:**

January 15, 2020



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- **RESPONSIBLE OFFICIAL:**
Acting Director, Workforce Relations Division
- **CORRECTIVE ACTION MONITORING PLAN:**
We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it monthly until completed.

RECOMMENDATION 3:

Work with the IRS's Office of Chief Counsel to evaluate whether a legislative proposal is needed to amend Internal Revenue Code §6103 to enable the IRS to use tax data to perform analyses and identify employees engaged in outside employment activities that involve potentially prohibited activities.

- **CORRECTIVE ACTION:**
IRS Chief Counsel has already advised that monitoring IRS employee outside employment is not a tax administration purpose and that as currently enacted § 6103 does not permit the IRS to use employee return information to monitor employee outside employment. We agree to partner with our legal advisers, IRS Chief Counsel, and the Department of the Treasury, to evaluate whether the IRS should request a statutory amendment to Internal Revenue Code § 6103 to allow the IRS to review employee tax returns to monitor outside employment.
- **IMPLEMENTATION DATE:**
April 15, 2020
- **RESPONSIBLE OFFICIAL:**
Acting Director, Workforce Relations Division
- **CORRECTIVE ACTION MONITORING PLAN:**
We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it monthly until completed.

RECOMMENDATION 4:

Establish processes to conduct periodic quality reviews to ensure that the OES is accurate.

- **CORRECTIVE ACTION:**
We agree with this recommendation. We will revise Internal Revenue Manual 6.735, Ethics and Conduct Matters, by adding responsibilities for employees, managers and business unit points of contact (POCs), such as periodic quality reviews. POCs will receive training and meet on a recurring basis.



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- **IMPLEMENTATION DATE:**
March 15, 2020
- **RESPONSIBLE OFFICIAL:**
Acting Director, Workforce Relations Division
- **CORRECTIVE ACTION MONITORING PLAN:**
We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it monthly until completed.

RECOMMENDATION 5:

Remove the paper Form 7995 as an option to request outside employment and require IRS employees to submit all outside employment requests through the OES.

- **CORRECTIVE ACTION:**
We are unable to agree with this recommendation at this time. Non-bargaining unit employees are required to submit requests in the OES. However, Article 6 of the 2019 National Agreement requires bargaining unit employees to submit outside employment requests in writing and states that "[a]n employee will use the electronic or paper Form 7995 (Exhibit 6-1) when making a request for outside employment." Accordingly, the IRS may not unilaterally require that employees submit all requests electronically through the OES; instead, we will need to negotiate a change to this article before we may accept only electronic submissions.

RECOMMENDATION 6:

Revise internal outside employment guidelines to require employees to resubmit their outside employment requests at least annually and modify the OES to allow for the systemic closure of all requests for which a renewal was not timely received. The OES modifications should include the ability to notify any employees whose request was closed.

- **CORRECTIVE ACTION:**
We agree to consider having all employees resubmit their requests annually and having systemic closure of requests if the annual review is not timely. (Implementing that change will require renegotiating Article 6 of the 2019 Agreement and therefore the IRS may not do so unilaterally for bargaining-unit employees.) We will request a system modification to generate email notifications to employees when their requests are closed.



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- **IMPLEMENTATION DATE:**
June 15, 2020, to determine bargaining obligations
September 15, 2021, to implement system modification
- **RESPONSIBLE OFFICIAL:**
Acting Director, Workforce Relations Division
- **CORRECTIVE ACTION MONITORING PLAN:**
We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it monthly until completed.

RECOMMENDATION 7:

Work with the IRS Information Technology organization to create a plan for housing the OES or to create a new database to ensure that outside employment requests are tracked after the Totally Automated Personnel System (TAPS) is shut down.

- **CORRECTIVE ACTION:**
We agree with this recommendation. We will continue meeting with the Department of the Treasury for options to replace the TAPS system. Pending replacement, we will continue to make improvements to the TAPS system, which will remain operational until a decision is made for an alternate system.
- **IMPLEMENTATION DATE:**
September 15, 2021
- **RESPONSIBLE OFFICIAL:**
Acting Director, Workforce Relations Division
- **CORRECTIVE ACTION MONITORING PLAN:**
We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it monthly until completed.