

# TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



## **Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed**

December 23, 2020

Report Number: 2021-10-005

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# HIGHLIGHTS: Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed



Final Audit Report issued on December 23, 2020  
Report Number 202110005

## Why TIGTA Did This Audit

In May 2017, the Tax Exempt and Government Entities (TE/GE) Division realigned the issue identification, planning, classification, and case delivery functions into a centralized Compliance Planning and Classification (CP&C) function to address concerns that current processes were not sustainable in a “no-hire” environment.

The overall objective of this review was to determine the effectiveness of the TE/GE Division’s implementation of the CP&C function to consolidate examination identification, planning, assignment, and monitoring.

## Impact on Taxpayers

The CP&C function now identifies and assigns examinations for review based on a new data-focused identification strategy. However, if this process did not improve the identification of productive examination cases, examiners could still contact compliant taxpayers unnecessarily, which places an unnecessary burden on them.

## What TIGTA Found

The creation of the CP&C function centralized how noncompliance issues are identified, developed, approved, classified, and monitored for all five TE/GE Division functions. This reorganization changed how the TE/GE Division identifies examination projects, processes referrals, and tracks examinations results. However, because management did not develop performance metrics to measure progress towards achieving reorganization goals, TE/GE Division leadership cannot determine if the CP&C function improved the effectiveness and efficiency of identifying, planning, classifying, and monitoring examination workload.

Further, TE/GE Division management did not establish reorganization goals and outcomes, have a dedicated implementation team in place for the duration of the reorganization, involve all key stakeholders, effectively communicate with affected employees, or provide adequate project management oversight to ensure timely implementation of all necessary actions. This resulted in employee confusion and compromised the initial success of the reorganization.

Finally, TIGTA’s analysis showed that the CP&C function has had mixed results reducing the number of unnecessary contacts with compliant taxpayers and identifying more productive examinations. Specifically, between Fiscal Years 2016 and 2019, the number of examinations closed without any changes favorably decreased for two of the five TE/GE functions, but increased by 36, 40, and 31 percent for the other three functions. Further, the overall number of cases closed without full examination (surveyed) favorably decreased by 5 percent, but increased by 468 percent for the Indian Tribal Government function.

The reorganization helped create additional benefits, such as reducing the potential for bias in case selection. In addition, the CP&C function implemented processing changes that decreased processing time for Exempt Organization function referrals by 37 percent, and began implementing a tracking system for all assigned inventory in September 2020.

## What TIGTA Recommended

TIGTA made six recommendations, including the Director, CP&C, should develop performance metrics and explore process improvements for validating identified cases to ensure that they include the identified issues prior to assignment. In addition, the Commissioner, TE/GE Division, should determine the feasibility of reassigning resources from compliance functions to improve the efficiency of identifying, classifying, and monitoring productive examination workloads. Management agreed or partially agreed with five of the recommendations, but disagreed to explore process improvements to ensure that selected cases include identified issues prior to issuance. TIGTA believes this action could help reduce the number of assigned cases that employees close without examination.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

**U.S. DEPARTMENT OF THE TREASURY**

**WASHINGTON, D.C. 20220**

December 23, 2020

**MEMORANDUM FOR:** COMMISSIONER OF INTERNAL REVENUE

M. Weir for

**FROM:**

Michael E. McKenney  
Deputy Inspector General for Audit

**SUBJECT:**

Final Audit Report – Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed (Audit # 201910022)

The overall objective of this review was to determine the effectiveness of the Tax Exempt and Government Entities Division's implementation of the Compliance Planning and Classification function to consolidate examination identification, planning, assignment, and monitoring. This review was part of our Fiscal Year 2021 Annual Audit Plan and addresses the major management and performance challenge of *Achieving Operational Efficiencies*.

Management's complete response is included as Appendix V.

If you have questions, please contact me or Heather Hill, Assistant Inspector General for Audit (Management Services and Exempt Organizations).



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## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

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### Background

The mission of the Tax Exempt and Government Entities (TE/GE) Division is to provide TE/GE Division customers top quality service by helping them understand and comply with applicable tax laws and to protect the public interest by applying the tax law with integrity and fairness to all. The TE/GE Division has important responsibilities for both the oversight of regulatory compliance as well as compliance with tax requirements. The Division serves charities, small local community organizations, major universities, large pension funds, small business retirement plans, State and local governments, participants in complex tax-exempt bond transactions, and Indian tribal governments and tribal associations.

In past years, the examination classification and case delivery units within the various TE/GE functions identified and prepared approximately 15,000 cases for examination each year.<sup>1</sup> However, according to TE/GE Division leadership, given the available limited resources, it was increasingly difficult to maintain quality, meet requirements, and create consistent processes. To address these concerns, in September 2015 the former Commissioner, TE/GE Division, requested an evaluation to identify potential efficiencies by standardizing the processes for all five TE/GE functions. The evaluation concluded that processes were not sustainable in a “no-hire” environment. In addition, the evaluation found:

- Each function within the TE/GE Division used a different methodology to identify taxpayer returns for examination.
- Separation of duties did not exist between examination and classification because the team that selected the work and the team that examined the taxpayers were in the same function.

TE/GE Division leadership believed they could realize additional efficiencies by consolidating the development of the annual work plan and by developing a compliance strategy process to improve strategic planning effectiveness.<sup>2</sup> They also believed that consolidating similar tasks from each TE/GE function into the same units would foster knowledge sharing.

On May 1, 2017, the TE/GE Division realigned the issue identification, planning, classification, and case delivery functions that were previously embedded within the Employee Plans (EP), Exempt Organizations (EO), and Government Entities (including Federal, State, and Local (FSL), Indian Tribal Governments (ITG), and Tax Exempt Bonds (TEB) functions), into the centralized Compliance Planning and Classification (CP&C) function. The new CP&C function includes three units:

- **Issue Identification and Special Review** – Issue Identification specialists interact with various TE/GE functions to develop compliance strategy proposals. The group also conducts research to identify compliance gaps and patterns in data that reveal opportunities for improvement. The Special Review groups perform quality reviews of randomly selected EO and EP closed examination cases.

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<sup>1</sup> Classification is the process of determining whether a return should be selected for compliance activities, what issues should be the primary focus of the compliance activity, and the type of compliance activity that should be conducted.

<sup>2</sup> Compliance strategies are issues approved by TE/GE Division’s Compliance Governance Board to identify, prioritize, and allocate resources within the TE/GE Division filing population.



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- **Planning and Monitoring (P&M)** – Employees develop work plans using ongoing projects and programs and newly identified issues from the Issue Identification unit. The P&M unit also closes completed examinations on a case management system and develops automated management reports for all TE/GE Division Examination units to ensure consistency and accuracy. In addition, the P&M unit monitors closing results and shares findings with the Issue Identification unit and TE/GE Division leadership.
- **Classification and Case Assignment** – Includes employees responsible for:
  - Performing congressionally mandated reviews of tax-exempt hospitals.<sup>3</sup>
  - Processing, classifying, and maintaining all incoming referrals, whistleblower cases, claims [for refunds or abatements] and other types of work.<sup>4</sup>
  - Replenishing unassigned inventory on the TE/GE Division case management system (*i.e.*, the “Virtual Shelf”).<sup>5</sup>

The creation of the CP&C function centralized how noncompliance issues are identified, developed, approved, classified, and monitored for all five TE/GE Division functions. This altered the organizational structure of the TE/GE Division, especially the examination units within each function.

**The CP&C function now selects and assigns all examination cases for every TE/GE function.**

The Government Accountability Office recently issued a report on the use of data analytics to identify workload, particularly for the EO function.<sup>6</sup> Consequently, we did not review the CP&C function’s examination workload identification process during this review.

## Results of Review

### The Tax Exempt and Government Entities Division’s Reorganization Efforts Were Not Always Consistent With Best Practices for Effective Agency Reform

The steps taken to plan and implement the reorganization that created the CP&C function were not consistent with Government Accountability Office best practices for implementing agency reforms (hereafter referred to as Federal best practices).<sup>7</sup> For example, TE/GE Division management did not establish reorganization goals and outcomes, have a dedicated

<sup>3</sup> The *Patient Protection and Affordable Care Act* (Public Law 111–148) requires the IRS to perform reviews of tax-exempt hospitals to ensure that they meet the community benefit requirements for maintaining their tax-exempt status.

<sup>4</sup> Referrals are alleged noncompliance by a TE/GE Division entity received from internal (*e.g.*, other IRS operating divisions) and external (*e.g.*, members of Congress, taxpayers) sources.

<sup>5</sup> The Virtual Shelf is the unassigned case inventory ready for assignment to an examiner.

<sup>6</sup> Government Accountability Office, GAO-20-454, *Tax Exempt Organizations: IRS Increasingly Uses Data in Examination Selection, but Could Further Improve Selection Processes* (June 16, 2020).

<sup>7</sup> Government Accountability Office, GAO-18-427, *Government Reorganization: Key Questions to Assess Agency Reform Efforts* (June 13, 2018).



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implementation team in place for the duration of the reorganization, involve all key stakeholders, effectively communicate with affected employees, or provide adequate project management oversight to ensure timely implementation of all necessary actions. This resulted in the TE/GE Division's inability to monitor progress towards reorganization goals, created confusion for employees, and may have reduced the effectiveness and efficiency of compliance efforts.

According to Internal Revenue Service (IRS) procedures, all organizational changes should begin with an identified need for change, gathering and analyzing appropriate data, considering alternatives, and preparing a business case (written proposal) to fully inform the approving official.<sup>8</sup> The initiating office should prepare a written proposal describing the proposed changes and expected effect, and define how the change will be implemented and evaluated. Written proposals should comply with individual business unit guidance. For example, the IRS's Wage and Investment and Small Business/Self-Employed Divisions each have specific guidance for reorganizations.<sup>9</sup> However, the TE/GE Division lacks business-unit specific guidance for implementing organizational changes.

### Establishing goals and outcomes

According to Federal best practices for organizational realignment, reorganization efforts require agreement on the goals and the means for achieving them. The TE/GE Division established broad goals for the reorganization.

- Select the most important issues of noncompliance.
- Minimize unnecessary contacts with compliant taxpayers.
- Eliminate redundancies or duplication in current processes.
- Increase awareness for overall issue treatment strategy for TE/GE Division leadership.
- Consolidate oversight for all compliance monitoring, planning, and closing activities.
- Address span of control issues.

However, the TE/GE Division did not establish performance measures for determining whether these goals were achieved. The *Reorganization Request for the Realignment of Tax Exempt and Government Entities* states, "...we will implement a control plan that will both monitor and evaluate the success of the project/organizational change." In addition, TE/GE Division's *Business Performance Review Fiscal Year (FY) 2017 (Third Quarter)* reported that, "Future deliverables will include more consistent reporting of metrics for EP, EO, and ITG/TEB, as well as a proposal for performance measures for the new CP&C function."<sup>10</sup> Yet more than three years after implementation, TE/GE Division leadership is still missing all necessary information to determine if the CP&C function improved the effectiveness and efficiency of identifying, planning, classifying, and monitoring examination workload. Such information would help TE/GE Division leadership determine if they should make additional changes to achieve the desired results.

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<sup>8</sup> Internal Revenue Manual 1.1.4, *Organizational Planning* (Aug. 2013).

<sup>9</sup> Internal Revenue Manual 1.55.2, *Wage and Investment; Organizational Changes* (Nov. 2018); Internal Revenue Manual 1.53.1, *Managing Organizational Change, Small Business/Self-Employed Division* (Aug. 2007).

<sup>10</sup> 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.



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Prior to CP&C function standup, the reorganization implementation team provided TE/GE Division management with suggested metrics for the new CP&C function, including:

- Frequency of contact with compliant taxpayers.
- Incorporation of approved compliance issues in the work plans.<sup>11</sup>

Although process changes related to these metrics have occurred, management never developed performance metrics to measure progress towards achieving them. One former Director, CP&C, stated that several procedural changes since reorganization, such as triaging EO referrals (discussed later in the report), have made it difficult to measure whether the CP&C function achieved its goals. In addition, CP&C function management stated they instead are developing new performance metrics related to the compliance strategy development process and new case evaluation processes (discussed later in this report).

IRS business units are expected to support IRS's strategic and operational goals, and each organization is responsible for periodically updating its performance measures to ensure effectiveness.<sup>12</sup> In addition, Executive Order 13781 explains that reorganizations should reduce duplication and redundancy and improve efficiency and effectiveness.<sup>13</sup>

**Recommendation 1:** The Commissioner, TE/GE Division, should develop reorganization guidance that includes the requirement for measurable metrics and data collection for future reorganizations and use the results to identify needed improvements.

**Management's Response:** The IRS partially agreed with this recommendation stating that, in the event of a future reorganization, the TE/GE Division will develop appropriate metrics and data collection.

**Office of Audit Comment:** Although the IRS agreed to develop metrics and data collection, it did not address the development of reorganization guidance. Based on prior history, the TE/GE Division will likely experience future reorganizations. The Treasury Inspector General for Tax Administration (TIGTA) believes the TE/GE Division should develop guidance to improve the reorganization process prior to any future reorganizations, not when the reorganization is occurring. As discussed in the report, other IRS business units have such guidance available in the Internal Revenue Manual. Developing a framework for future reorganizations, including the requirement of measurable metrics for use in identifying additional improvements, would help the TE/GE Division meet its reorganization goals.

**Recommendation 2:** The Director, CP&C, should develop performance metrics and data collection methods to measure progress towards current business unit goals that support the IRS's strategic objectives and use this information to improve processes.

**Management's Response:** The IRS agreed with this recommendation. The Director, CP&C, will develop performance metrics for the CP&C function and data collection

<sup>11</sup> See Appendix II for a complete list of potential metrics developed by the reorganization team in FY 2017.

<sup>12</sup> Internal Revenue Manual 1.5.1, *Managing Statistics in a Balanced Measurement System, The IRS Balanced Performance Measurement System*, (May 2019).

<sup>13</sup> Executive Order 13781, *Comprehensive Plan for Reorganizing the Executive Branch*, March 13, 2017.



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methods to measure progress towards current business unit goals that support the IRS's strategic objectives.

### Dedicated implementation team

According to Federal best practices for organizational realignments, organizational transformation should be led by a dedicated team of high-performing leaders within the agency. However, frequent management changes at all levels within the CP&C function since standup may have impeded the development and implementation of metrics. For example, there have been four different Directors, CP&C, since the reorganization took effect on May 1, 2017, with the most recent Director change occurring in May 2020.

### Involvement of key stakeholders

According to Federal best practices, successful reforms require agencies to involve their employees, Congress, and key stakeholders in the development of any major reforms. Involving employees helps to incorporate insights from a front-line perspective and increases acceptance of changes. During the course of our review, we interviewed 64 managers and employees judgmentally selected from the CP&C function and the five other TE/GE Division functions.<sup>14</sup> Per TE/GE Division leadership, employees were given the opportunity to participate and provide input on the reorganization. For example, the reorganization team coordinated with the National Treasury Employees Union and solicited subject matter experts to assist with developing new processes for the CP&C function. However, many employees expressed frustration with various aspects of the reorganization, especially training, communication, and the ability to provide input prior to and after implementation.<sup>15</sup> Figure 1 highlights the most common reorganization implementation concerns raised to us by employees.<sup>16</sup>

**Figure 1: TE/GE Division Reorganization Implementation – Employee Concerns**



Source: TIGTA interviews with TE/GE Division employees.

<sup>14</sup> A judgmental sample is a nonprobability sample, the results of which cannot be used to project to the population.

<sup>15</sup> We tailored the questions to the employees' functions and positions, so not all employees were asked the same questions. In addition, the same employee may be included in the counts of more than one issue.

<sup>16</sup> See Appendix III for additional concerns raised during our interviews.



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Numerous concerns existed before and after the reorganization and some are still affecting operations more than three years later. For example, communication between TE/GE Division management and field employees continues to be a concern for many employees. Specifically, eight of 13 interviewed CP&C function employees and six of seven current and former CP&C function directors and unit managers felt better communication is needed.

### Communication efforts

Per the *Reorganization Request for the Realignment of Tax Exempt and Government Entities (TE/GE)*, TE/GE Division leadership made several efforts to communicate with employees before the reorganization, including:

- Two group sessions with the potentially affected employees to communicate project progress during planning. The sessions described the need for process and organizational changes in order to make the TE/GE Division more sustainable in the “no-hire” environment. How the alignment of TE/GE Division’s activities would support the IRS Future State Goals was included in these discussions.
- TE/GE Connect newsletter updates.
- Working with the employee union to solicit and select subject matter experts to assist with process and organizational redesign.

Despite communication efforts, interviewed employees were frustrated because management did not provide specific details about the reorganization, such as who their new managers and coworkers would be, or what their new responsibilities were, until shortly before implementation.<sup>17</sup> Affected employees stated that the communication two weeks before standup did not provide enough time for employees to accept the changes or raise concerns for resolution. In addition, five employees cited concerns that the implementation was rushed and not well planned. However, TE/GE Division leadership stated that agreements with the National Treasury Employees Union stipulate limitations on when and how management may communicate with affected employees.

Per Federal best practices, reorganizations need to have a two-way continuing communications strategy that listens and responds to concerns of employees regarding the effects of potential reforms. Agencies should engage employees and employee unions in developing the reforms (*e.g.*, through surveys, focus groups) to gain their ownership for the proposed changes.

TE/GE Division leadership believes they appropriately communicated overall plans and current developments with all employees through newsletters and other contacts, such as group meetings, during reorganization development. TE/GE Division leadership reasoned that there was never going to be a perfect time to implement changes, and the best way to identify and resolve issues was to take action.

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<sup>17</sup> TE/GE Division management did provide 36 employees the opportunity to select which office they preferred to be moved into at standup. Each was given at least two choices to rank in order of preference.



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**Recommendation 3:** The Commissioner, TE/GE Division, should include in its business unit-specific reorganization guidance, pursuant to Recommendation 1, a comprehensive communication strategy and the expectation for a designated, dedicated leader responsible for implementation of proposed reforms during the transition.

**Management's Response:** The IRS partially agreed to this recommendation stating that in the event of a future reorganization, the TE/GE Division will provide a comprehensive communication strategy and the expectation for a designated, dedicated leader responsible for implementation of proposed reforms.

**Office of Audit Comment:** Although the IRS agreed to provide a comprehensive communication strategy in the event of a future reorganization, it did not address the development of reorganization guidance. Based on prior history, the TE/GE Division will likely experience future reorganizations. TIGTA believes the TE/GE Division should develop guidance to improve the reorganization process prior to any future reorganizations, not when the reorganization is occurring. As discussed in the report, other IRS business units have such guidance available in the Internal Revenue Manual. Developing a framework for future reorganizations, including a comprehensive communication strategy and the expectation for a designated, dedicated leader responsible for implementation of proposed reforms during the transition, would help the TE/GE Division meet its reorganization goals.

### Project management of reorganization efforts

According to Federal best practices, it is important for organizations to develop an implementation plan with key milestones and deliverables to track implementation progress. The CP&C reorganization team developed an overall transition plan with key actions needed for a successful reorganization, including completion target dates through February 1, 2018. In addition, several transition teams were established to oversee specific areas of change. However, the CP&C function could not provide finalized documentation showing that the plans were used to track implementation progress. This condition may have led to delays in completion of the identified deliverables. Figure 2 shows the timeliness status of key overall transition goals.<sup>18</sup>

<sup>18</sup> See Appendix IV for the remaining list of transition goals.



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**Figure 2: Timeliness of Transition Goals**

Transition Goal	Due Date	Status
Capability to monitor the work plan and fulfill all reporting requests	May 1, 2017	●
Sufficient inventory during transition	May 1, 2017	●
Issue ID starts developing new issues using the Issue ID tool <sup>19</sup>	August 1, 2017	●
Classification and Case Assignment tests Virtual Shelf fulfillment process and starts classifying and case assignment using the new process	August 1, 2017	●
Charters and Issue governance document complete	September 30, 2017	●
Issue ID Tool roll-out	September 30, 2017	●
Finalize interim guidance for all newly created organizations	September 30, 2017	●
Planning and Monitoring will implement more efficient reporting <sup>20</sup>	September 30, 2017	●
Internal Revenue Manuals updated (all new organizations)	February 1, 2018	●
<span style="color: green;">●</span> Timely Implemented <span style="color: yellow;">●</span> Partially Timely Implemented <span style="color: red;">●</span> Not Implemented Timely		

*Source: Transition Plan – Big Picture, March 23, 2017 - PowerPoint and TIGTA analyses of documentation.*

Less than one-half of the listed transition goals were timely completed, and deadlines for some significant goals were missed. For example, the issuance of some interim guidance memorandums did not occur until November 2017, more than one month after their due dates and five months after CP&C function standup. In addition, Internal Revenue Manuals were not finalized until September 2019, more than two years after standup. According to interviewed employees, this delay sometimes resulted in confusion and frustration because employees were developing guidance while processing cases. IRS procedures allow the immediate issuance of emergency interim guidance memorandums to employees when a delay in issuance would result in a work stoppage, incorrect processing of account data, or severely affect taxpayer actions. However, management did not issue any emergency interim guidance during the delay. Five employees we interviewed raised concerns with inadequate procedures at CP&C function standup. For example, EP function employees recounted confusion with processing taxpayer claims and a need for guidance after CP&C function standup.

In addition, as of May 2020, there were still separate, distinct processing and project codes for each function on the case management system. For example, the same status code may mean something different for each of the five functions. In September 2019, the TE/GE Division developed standard processing and project codes for all the functions; however, the new codes will not be implemented until FY 2021. Inconsistent case management codes hinder efficiently closing cases on the system and the ability to produce standardized reports. In addition, this

<sup>19</sup> The Issue ID Tool later became known as the Compliance Issue Submission Portal, where employees submit ideas for compliance strategies.

<sup>20</sup> Efficient reporting includes consistent coding.



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condition makes it difficult to cross-train P&M unit employees to share responsibility for closing multiple functions' cases on the case management system (discussed later in the report).

Additional reorganizations continue to affect operations within the TE/GE Division, and management could be vulnerable to continuing information gaps unless corrective actions are taken. For example, the TE/GE Division stood up a new Tax Exempt Compliance Unit in October 2018 and completed another reorganization in November 2019 to split the combined ITG/TEB function into two separate offices. Although we did not review the specifics of these subsequent organizational changes, management should ensure that they have the information necessary to identify areas needing improvement and the capacity to implement these large-scale changes, while also continuing to deliver on day-to-day services, before proceeding with future reorganizations.

### The Tax Exempt and Government Entities Division Partially Achieved the Goals of Its Reorganization

Because management never implemented specific performance metrics to assess the CP&C function's progress, we used available data to independently assess progress towards achieving TE/GE Division's six identified goals. Figure 3 shows the goals and our assessment of efforts to achieve them.

**Figure 3: Goals of the CP&C Function**

TE/GE Division Identified Goals	
<span style="color: green;">●</span> <b>Goals met</b>	
	Increase awareness for our overall issue treatment strategy for TE/GE Division leadership.
	Consolidate oversight for all compliance monitoring, planning, and closing activities.
	Address span of control issues.
<span style="color: yellow;">●</span> <b>Goal was partially met</b>	
	Minimize unnecessary contacts with compliant taxpayers.
	Eliminate redundancies for duplication in current processes.
<span style="color: orange;">●</span> <b>Status indeterminable</b>	
	Consistently select the most important noncompliance issues.

*Source: TIGTA analysis of the Reorganization Request for the Realignment of Tax Exempt and Government Entities.*

Our results showed mixed success. The CP&C function met one-half of the identified goals, but only partially met two of the three remaining goals. We could not determine the status of one goal because management did not define it in quantitative terms.



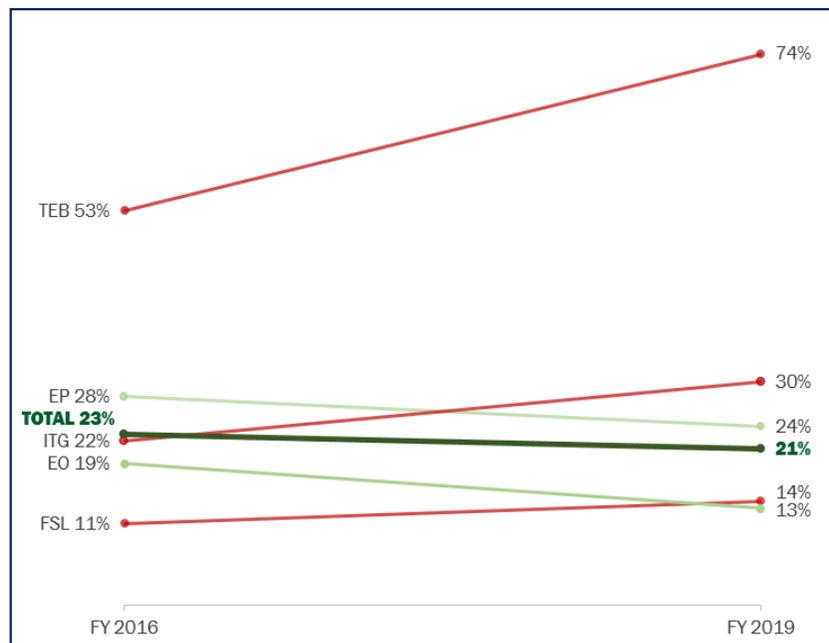
## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

### Goal partially met: Minimize unnecessary contacts with compliant taxpayers

Compliance strategies and data-driven models developed by the CP&C function to select cases for examination have resulted in improved productive workload identification for the TE/GE Division overall.<sup>21</sup> As a result, examiners are contacting fewer compliant taxpayers and spending fewer resources on unproductive cases. However, action can be taken to improve the selection of more productive workload for all functions going forward.

The IRS generally measures unproductive work by the “no-change rate,” which is the percentage of examinations that the examiner closed with no actions taken. The IRS associates a high percentage of examined returns with recommended adjustments as being more productive than examinations that result in no changes. Such work causes unnecessary burden on taxpayers and IRS resources. Figure 4 shows mixed results in reducing unnecessary contacts with compliant taxpayers after the CP&C function assumed responsibility for case selection.<sup>22</sup>

**Figure 4: Change in Percentage of Examinations Closed as No Change Between FY 2016 and FY 2019<sup>23</sup>**



Source: TIGTA analysis of Returns Inventory and Classification System data.

While fluctuations in the no-change rate occurred from year to year, overall, no-change closures have favorably decreased by 11 percent (2.6 percentage points) for the TE/GE Division. However, while the no-change rate decreased for two of the five functions; it increased by 36, 40, and 31 percent for the other three functions. These results could be an indication that the CP&C function is identifying less productive compliance work for the TEB, ITG, and FSL functions

<sup>21</sup> Data-Driven Approaches use data, models, and queries to select work based on quantitative criteria.

<sup>22</sup> It is possible that some closed cases were selected prior to the CP&C function’s involvement, but the CP&C function was unable to provide information to determine if this occurred.

<sup>23</sup> Percentages were calculated using actual results and rounded to the nearest whole number.

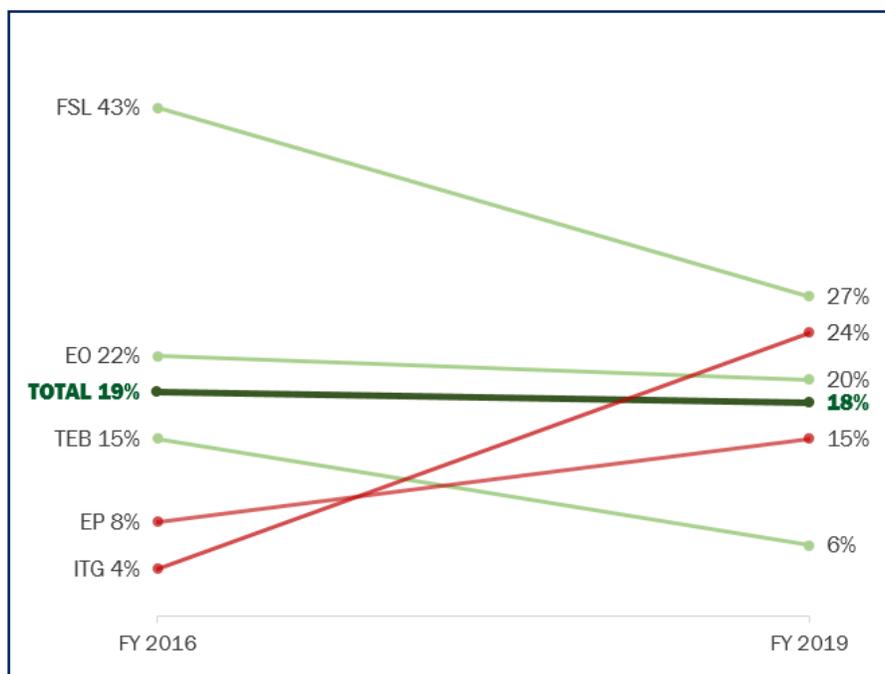


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than when the individual functions were identifying their own examination workloads. This creates an unnecessary burden on compliant organizations.

In addition, examiners may decide to close an assigned case without examining it, referred to as a “survey” closure, when research indicates, for example, that the expected noncompliant issue(s) is not present.<sup>24</sup> These cases are also generally considered unproductive because classifiers, group managers, and examiners spend time on cases that are never examined. Figure 5 shows the change in percentage of non-examined returns since the CP&C function began identifying compliance workload.

**Figure 5: Change in Percentage of Non-Examined Closures Between FY 2016 and FY 2019<sup>25</sup>**



Source: TIGTA analysis of Returns Inventory and Classification System data.

Overall, non-examined closures have decreased by 5 percent (1 percentage point) for the TE/GE Division. Non-examined closures decreased in three of the five functions, but substantially increased for EP and ITG cases, by 89 and 468 percent, respectively. Management stated these large increases were a result of errors in a sampling query that established cases incorrectly, a delay in the receipt of data from another business unit that caused an increase of non-examined closures due to short statute dates, and closures of established training cases that were not processed due to other priorities.

Of the five TE/GE functions, only the EO function had decreases in both the number of no-change and non-examined closures. The remaining four functions had increases in either the no-change rate or the number of non-examined closures.

<sup>24</sup> Surveying cases can occur before or after assignment to an examiner, with or without contacting the taxpayer.

<sup>25</sup> Percentages were calculated using actual results and rounded to the nearest whole number.



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IRS leadership stated that they consider no-change and survey closures successful cases because they can learn from them, and expressed that metrics need to be qualitative and not just quantitative. Furthermore, IRS leadership emphasized that the TE/GE Division and the CP&C function are gaining insights as to why cases were closed without change, and based on feedback, they are altering the scope of the compliance strategies.

One strategy to consistently decrease the no-change and survey rates for all functions could be to review the validity of compliance strategy and data-driven project cases to ensure that the suspected noncompliant activity is present prior to case assignment. Such a review would help determine if the methodology for identifying cases is constructive or needs refinement, potentially resulting in both more productive casework for the examiners and a reduction in the number of unnecessary contacts with compliant taxpayers.

**Recommendation 4:** The Director, CP&C, should explore a process improvement to determine if it is feasible and cost effective to validate whether cases include the identified issues prior to assignment.

**Management's Response:** The IRS disagreed with this recommendation stating that without a detailed review of books and records, there is no way to "validate" that an issue exists before a case is sent to an examiner. The methodology that is in place for development of strategies is designed to identify the compliance issues prior to assignment to the extent possible. Based on the amount of research analysis and development that is completed and presented to the TE/GE Division's CP&C function Governance Board, the IRS stated that it has a high confidence level of the compliance issue. According to the IRS, when possible, strategies are rolled out in phases to allow the agency to "test" results and modify the strategy if needed.

**Office of Audit Comment:** TIGTA believes it would be prudent for management to explore options for determining if subject matter experts' involvement is feasible and cost effective, before concluding it is not possible. Subject matter experts' involvement prior to assignment for examination, especially in functions for which the Issue Identification unit does not have adequate representation, would improve the selection of productive workload. Interviewed TE/GE Division employees told TIGTA that certain approved projects, including one TEB function compliance strategy, resulted in identifying little noncompliance because the suspected issues were not present in the cases assigned and examined.

### **Goal status indeterminable: Promote consistent selection of the most important noncompliance issues**

Management did not establish a quantifiable definition or methodology for measuring the importance of noncompliance issues during CP&C function standup, so it is difficult to assess progress towards achieving this goal. One component of importance could be the prevalence of specific noncompliant issues among organizations, which could be measured by the no-change rate previously discussed. By that measure, the CP&C function may not always select cases with the most important noncompliance issues. In addition, another component of importance could be the dollars assessed because these cases result in potential revenue. Cases with high assessments offer a return on investment of IRS resources, address potentially



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egregious noncompliant activity, and help close the \$441 billion Tax Gap.<sup>26</sup> However, according to TE/GE Division leadership, examination workload is not based on the potential additional tax assessments, but rather compliance with the tax law. As a result, examination assessments may vary greatly from year-to-year based on the mix of cases reviewed.

Because the word “important” is a subjective term and management did not establish a quantifiable definition or methodology for measuring it, improvements to no-change rates or assessment amounts might not accurately reflect progress towards achieving the goal. Employees we interviewed raised concerns with the quality of cases received for examination, as well as other quality concerns. Figure 6 shows the concerns raised by employees regarding quality, including subpar cases assigned to the field, and insufficient workload and case development.<sup>27</sup>

**Figure 6: TE/GE Division Reorganization Case Quality – Employee Concerns**



Source: TIGTA interviews with TE/GE Division employees.

Despite TE/GE Division efforts to communicate changes about the reorganization, numerous concerns existed before and after the establishment of the CP&C function and some are still affecting operations more than three years later.

### Goal met: Increase awareness for overall issue treatment strategy for TE/GE Division leadership

In May 2017, the Commissioner, TE/GE Division, established the Compliance Governance Board, which is comprised of six voting members representing all TE/GE functions and Division Counsel. It serves as the governing body over the identification, selection, assignment, and allocation of resources for all TE/GE Division compliance and enforcement activities and ensures that all compliance strategy proposals are reviewed and discussed prior to any case selection. Instead of selecting individual cases with potential noncompliance for examination, compliance

<sup>26</sup> IRS, Publication 1415, *Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2011–2013* (Sept. 2019). Like the Tax Year 2008 through 2010 estimates, these estimates reflect an estimated average compliance rate and associated average annual Tax Gap covering a time frame of three tax years. The annual gross Tax Gap was estimated to be \$394 billion in Tax Years 2008 through 2010 and \$441 billion in Tax Years 2011 through 2013.

<sup>27</sup> See Appendix III for additional concerns raised during our interviews.



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strategies identify a group of cases with the same potential noncompliant issue to address a common area of concern across the tax-exempt sector.

The Compliance Governance Board meets monthly and potential compliance strategies and projects are presented for approval. This process allows TE/GE Division leadership an opportunity to provide input into the types of compliance work completed and updates them on the latest areas of concern throughout the year. According to the IRS, this process also allows the TE/GE Division to address significant compliance and resource challenges through the strategic use of resources. It also helps the TE/GE Division focus on the highest risk cases and emerging issues using different treatment streams—from examinations and compliance contacts to educational letters and technical guidance. Once approved for a compliance treatment, these issues are considered priority work.

### **Goal partially met: Elimination of redundant and duplicate processes**

Per Federal best practices, agencies should conduct strategic workforce planning to determine whether they will have the needed resources and capacity, including the skills and competencies, in place for the proposed reorganization. In addition, agencies should address areas of fragmentation, overlap, and duplication in developing their reform proposals. The *Reorganization Request for the Realignment of Tax Exempt and Government Entities* included an expected outcome related to organizational redundancies. It states "...aligning similar processes, functions, and resources will promote efficiencies across our classification programs to include [elimination of] redundancies or duplication in current processes."

Although management transferred employees from various functions into the new consolidated CP&C units, many employees and managers we interviewed stated that some of these transferred employees still perform the same function-specific work related to the TE/GE function from which they were transferred. Employees also stated that while some attempts to cross-train were completed or ongoing, many had not been trained or the training provided was inadequate. Interviewed employees also expressed concerns that examiners in the business units were traveling unnecessarily because the CP&C function does not consider geography when assigning cases.

**Staffing.** In May 2017, the TE/GE Division transferred 165 employees from the existing functions to the new CP&C function. Figure 7 summarizes the initial employee reassignments.<sup>28</sup>

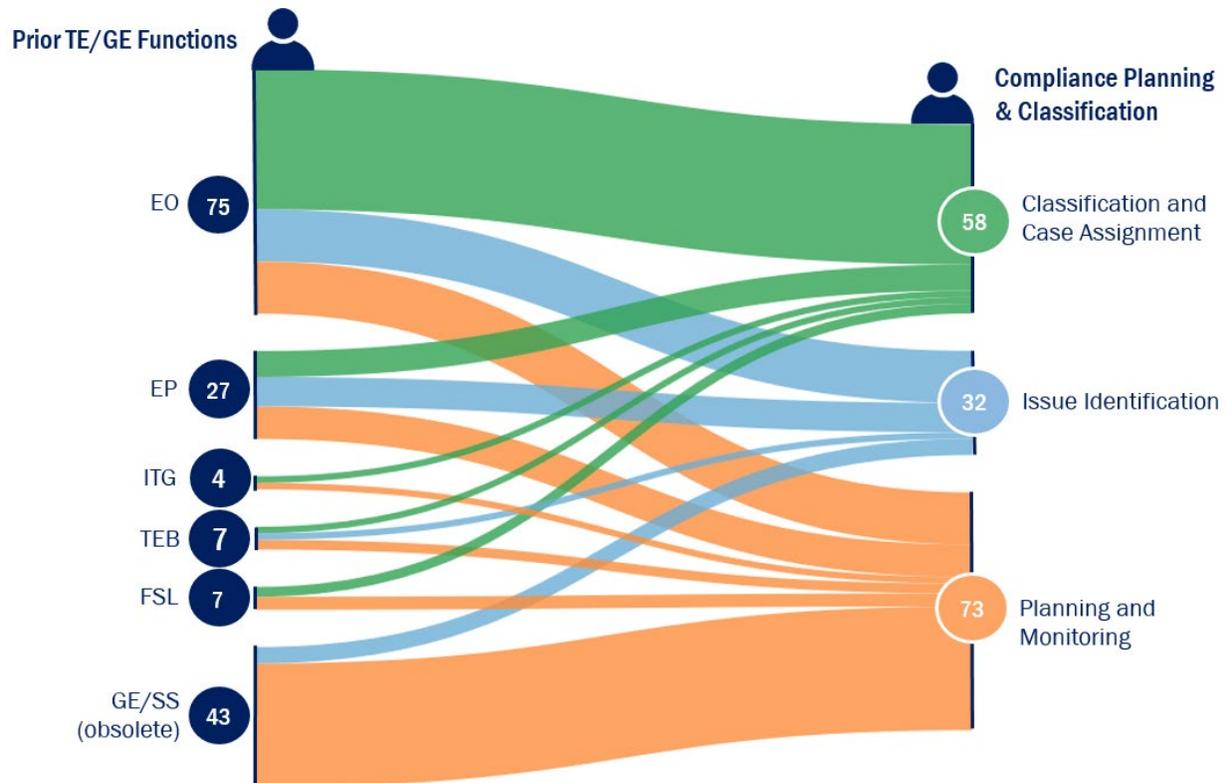
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<sup>28</sup> We did not include in Figure 7 two staff assistants transferred to the CP&C function.



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

Figure 7: Employee Reassignments to the CP&C Function



Source: TIGTA analysis of reorganization planning documentation.

Note: GE/SS was Government Entities and Shared Services, which was eliminated during a subsequent reorganization.

TE/GE Division leadership hoped reassigning employees from across TE/GE's functions into consolidated CP&C units would allow knowledge sharing between the functions and improve efficiency by standardizing similar workload. However, leadership did not establish a process to track progress towards these goals, so they do not have information to make decisions about the need for additional changes.

The TE/GE Division does not track CP&C function staff positions or work performed by specific functions (*e.g.*, EP function), so we could not quantify whether employees were spending time on cross-functional work. However, CP&C function employees we interviewed stated that they exclusively worked function-specific issues that mirrored the TE/GE functions for which they had previously worked. Similar positions from the five TE/GE functions transferred to the CP&C function require specialized knowledge to properly oversee them and are not interchangeable. In addition, management did not initially transfer employees possessing unique skills to the appropriate positions, such as those needed in the Issue Identification unit for the ITG function. This created a skills gap that resulted in a reduction of available examination work that the ITG function acknowledged in TE/GE Division's *FY 2017 Third Quarter Business Performance Review*. It states, "The nature of next best case work selection has produced fewer examinations and compliance checks than projected in the original FY 2017 Workplan."



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Because management has still not established performance measures or developed a methodology to assess progress at reducing organizational redundancies, TE/GE Division leadership cannot determine if additional actions are necessary. TIGTA believes management should evaluate the staffing alignment within each CP&C function unit to assess needed changes to improve efficiencies.

**Cross-training.** Successfully cross-training employees was a significant factor in obtaining efficiencies with the CP&C function consolidation, and the CP&C function provided cross-training for certain CP&C units. For example, Issue Identification unit employees were cross-trained on how to develop employment tax issues. In addition, management was in the process of training P&M unit employees to perform case closings for both the EO and EP functions during our fieldwork.

However, affected employees stated that attempts to cross-train other CP&C function employees were generally unsuccessful. For example, seven CP&C function employees stated that they had received inadequate or no cross-training since moving to the CP&C function, including all interviewed Classification and Case Assignment unit employees.

Interviewed employees stated that attempts to cross-train employees to gain efficiencies and eliminate redundancies and duplication were not successful because each function's work is unique, and experience in each area is necessary for successful identification, development, and classification of examination workload. A manager also stated that because some TE/GE Division work is highly specialized and involves unique laws, the effectiveness of cross-training for productive case selection is limited. TE/GE Division leadership stated that consolidation of the functions allowed the development of consistent processes, even if certain staff, like classifiers, cannot be cross-trained to improve efficiency. Because of these challenges, further attempts to cross-train issue identification and classification employees may not result in additional efficiencies.

**Travel resources.** Prior to the reorganization, individual functions would assign cases based on geographical location, which allowed employees to work cases closer to their posts of duty and helped reduce funding needed for travel expenses. The CP&C function changed case assignment criteria by using the "next best case" inventory assignment process.<sup>29</sup> This process assigns cases based on the potential noncompliance identified rather than solely on where the examiner is located and personal preferences. For FY 2018, which was the first full fiscal year after the reorganization, TE/GE Division's overall enforcement travel costs increased to \$3.05 million (17 percent) compared to \$2.61 million in FY 2017. However, there were large variations in enforcement travel cost changes among the five functions, which could not be explained solely by inflation.

According to the IRS, since the establishment of the CP&C function, the case selection process for assignment to an examiner has changed. Each function now has a designated Functional Assignment Coordinator, who coordinates with the CP&C function to select cases for assignment when an examiner requires new casework. The Coordinator reviews the available case inventory and selects cases that match the request requirements, such as case grade, statute expiration, and a high potential for identifying noncompliance. According to management, the Functional Assignment Coordinator may also consider geography, by

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<sup>29</sup> The next best case is the term used for cases identified for assignment based on, for example, compliance strategies that will have the highest positive impact on voluntary compliance and tax administration.



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

selecting cases in close proximity to the examiner's location, in order to optimize the use of resources.

During interviews, 15 employees expressed concerns with the inventory assignment process, 16 employees raised concerns with increases in travel, and three group managers stated they consider the increase in travel unnecessary. Managers raised this concern during training in FY 2018 and TE/GE Division leadership told them to move inventory between themselves, if they wanted. Some managers we spoke with have traded cases to limit costly travel. Others have increased the number of examinations completed via telephone and mail instead of site visits. These practices may have contributed to a 17 percent reduction in enforcement travel costs in FY 2019. On average, enforcement travel costs for all five functions have increased 3 percent in the first two full years after reorganization compared to the two fiscal years prior to the reorganization.

The need to trade cases and alter the types of examinations completed leads to compliance activity inefficiencies. Improved case selection and assignment processes would reduce the time managers need to assess incoming inventory and allow examiners to perform more complete examinations, including site visits, while limiting travel costs.

The Commissioner, TE/GE Division, should:

**Recommendation 5:** Explore the feasibility of reassigning resources from compliance functions to the CP&C function to improve the efficiency of identifying, classifying, and monitoring productive examination workloads related to all TE/GE functions.

**Management's Response:** The IRS agreed with this recommendation stating that the Director, CP&C, will conduct an assessment within the CP&C function to determine the skills and staffing needed to improve the efficiency of identifying, classifying, and monitoring productive examination workloads related to all TE/GE functions. The Director, CP&C, will develop a hiring plan to acquire the appropriate resources.

**Recommendation 6:** Develop guidance for Functional Assignment Coordinators to minimize assigning cases involving excessive administrative actions and travel costs.

**Management's Response:** The IRS agreed with this recommendation stating that while the current case assignment process is deliberately designed to reduce the potential for bias in case selection, the TE/GE Division will review for possible process improvement a way to minimize assigning cases involving excessive administrative actions and travel costs. If a process improvement can be realized that does not negatively affect other factors, the CP&C function will develop or clarify guidance for Functional Assignment Coordinators to implement the process improvement.

### **Goal met: Consolidation of oversight for all compliance monitoring, planning, and closing activities**

The CP&C function has taken steps to consolidate oversight through the development of standardized management information reports for different audiences and standardized work plans. For example, the P&M unit developed a compliance strategy dashboard that includes planned and actual examination data across all functions for TE/GE Division leadership. In addition, the P&M unit prepares and distributes a more detailed monthly report to each TE/GE functions' Director, Examinations. This practice helps ensure consistency in data reporting for



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future planning efforts. Further, the P&M unit now develops examination work plans based on approved compliance strategies and data-driven models for all TE/GE functions, which also helps improve planning consistency.

### **Goal met: Normalization of spans of control for managers**

IRS policy requires organizations to establish and maintain effective spans of control, with particular emphasis on front-line and second-level managers.<sup>30</sup> An effective span of control entails, to the extent possible, assigning the maximum number of individuals to the fewest number of managers while ensuring achievement of organizational goals and program objectives. Per IRS guidance, the minimum number of direct reports in field offices should be 10 employees for front-line managers and seven employees for second-level managers.

The realignment of 165 employees from the five TE/GE functions into the CP&C function resolved existing span of control issues but created new ones for the remaining individual TE/GE functions. Numerous consolidations of groups outside the CP&C function occurred to maintain appropriate span of control levels. For example, management reduced the number of ITG and TEB field operations groups from six and five, respectively, to three each. In addition, management eliminated entire offices in some of the functions' examination units, but not all of the employees in those offices were moved to the CP&C function. The remaining employees were moved under other managers.

### **The Compliance Planning and Classification Function Improved Some Examination Processes**

The creation of the CP&C function changed how the TE/GE Division identifies examination projects, processes referrals, and tracks examination results. Specifically, it resulted in separation of duties, triaging of most EO referrals, and tracking the results of specific potential noncompliance issues.<sup>31</sup>

### **The CP&C function reduced potential and perceived bias in workload identification and selection**

The creation of a separate function independent of the examination units reduced potential and perceived bias in the identification and selection of examination workload. According to the IRS, the Issue Identification unit is now responsible for developing issues with potential high levels of noncompliance, using unbiased, data-driven approaches. In addition, prior to case selection, TE/GE Division executives now approve the noncompliance areas developed by the Issue Identification unit. Furthermore, independent of issue identification, the Classification and Case Assignment unit identifies and assigns examination work to the various TE/GE functions. Case assignments are now prioritized based on the "next best case," meaning cases with the

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<sup>30</sup> Internal Revenue Manual 6.511.1, *Position Management and Classification Policy and Operational Guidance*, (Mar. 2010).

<sup>31</sup> Separation of duties, sometimes referred to as segregation of duties, involves management dividing or segregating key duties and responsibilities among different people to reduce the risk of error, misuse, or fraud.



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

highest possibility of noncompliance, instead of focusing on, for example, the geographical location or examiners' personal preferences.<sup>32</sup>

### The CP&C function created a triage process for classifying EO function referrals

Most referrals received by the TE/GE Division relate to the EO function.<sup>33</sup> In September 2018, the CP&C function developed a triage process intended to efficiently separate EO function referrals with examination potential from those without potential, such as duplicates, junk mail, or misroutes (*i.e.*, those belonging to another IRS business unit). Prior to the triage process, the Classification group would establish all referrals on the case management system before the manager assigned them for review. However, this practice sometimes delayed the review of referrals with unique processing protocols, such as taxpayers under criminal investigation, whistleblower cases, and political campaign intervention, because they would have to be reassigned to designated classifiers responsible for the unique issues.

Under the triage process, the Classification group manager now assigns EO referrals to a classifier for an initial review (*i.e.*, triage) prior to establishing the referral on the case management system. The classifier reviews the referral and conducts limited research to determine how to process the case. For referrals without examination potential, an administrative assistant establishes them on the case management system for immediate closure. Other referrals with unique issues (*e.g.*, taxpayers under criminal investigation) have specific processing procedures. Triage quickly identifies these types of referrals so the classifier can correctly route them for further action. For routine referrals that warrant further development, support staff establish them on the case management system for a determination of examination potential.

Although the CP&C function does not track which EO referrals were triaged, most go through the triage process. Our analysis of EO function referral data shows that since triaging began, the number of days from receipt to referral decision decreased 37 percent, from 265 days in FY 2018 to 167 days in FY 2019. These results suggest that triaging referrals has improved the efficiency of EO referral processing.

### Management has taken steps to collect issue-specific examination results

In August 2019, the CP&C function began piloting a data grid, which collects the results of examinations by each potential noncompliance issue reviewed. For every examination, the grid lists each potential noncompliance issue identified by the Issue Identification unit or the Classification and Case Assignment unit. In addition, examiners can add other issues identified during an examination. When examiners close cases, they indicate on the data grid the results for each identified issue, such as no change or assessment.

Before the pilot, examiners would close cases only at the summary level (*e.g.*, "adjustment"), with no information about the specific noncompliance issue(s) identified. As a result, the Issue Identification unit had no way of knowing if the potential issue(s) provided to the examiners resulted in an adjustment or if other issues identified during the examinations resulted in the

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<sup>32</sup> Although case identification and selection is completed by the CP&C function, examination group managers and examiners may elect to not process a case after the CP&C function assigns it to the group. This still provides the function's examination units a level of control over their workload.

<sup>33</sup> Other functions also receive referrals, but fewer in numbers.



## **Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed**

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change. This practice could lead to a mistaken belief that the CP&C function's methodology for identifying cases for examination led to a related finding of noncompliance.

For example, if the Issue Identification unit identified a possible employment tax issue, but the examination resulted in an unrelated change (such as the filing of a delinquent return), the overall case would be closed as a "change case," but the CP&C function would have no way of knowing that the employment tax issue was not substantiated. Using the completed data grid, the CP&C function can now compare examination results with the specific potential noncompliance issues initially identified and adjust the criteria used to detect potential noncompliance issues as necessary. The TE/GE Division began implementing the data grid for all assigned inventory in September 2020.



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

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# Appendix I

## Detailed Objective, Scope, and Methodology

Our overall objective was to determine the effectiveness of the TE/GE Division's implementation of the CP&C function to consolidate examination identification, planning, assignment, and monitoring. To accomplish our objective, we:

- Determined how the IRS planned for and implemented the CP&C function by reviewing available documentation from the reorganization team, interviewing reorganization team members, as well as current and former TE/GE Division Commissioners.
- Evaluated the effectiveness of the CP&C function's reorganization to address concerns regarding the separation of classification, workload selection and examination activities, and workload management.
- Interviewed a judgmental sample of 64 employees to determine the effect of the CP&C function's implementation on their work processes.<sup>1</sup> We could not reliably determine the population of employees and selected a judgmental sample because we did not plan to project our results. Additionally, we interviewed current and former CP&C Directors, as well as the current and former program managers for the three CP&C units (Issue Identification, P&M, and Classification and Case Assignment). Further, we interviewed Program Directors, Examination Directors, and Program Managers within the TE/GE Division.
- Determined whether the CP&C function established sufficient performance measures, whether it is progressing towards its goals, and if the anticipated effectiveness and efficiencies have been realized. We reviewed the performance measures and analyzed closed examinations and non-examined data.

### Performance of This Review

This review was performed at the TE/GE Headquarters in Washington, D.C., and the TE/GE function offices in Florence, Kentucky; Cincinnati, Ohio; and Dallas, Texas, during the period July 2019 through August 2020. 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.

Major contributors to the report were Heather M. Hill, Assistant Inspector General for Audit (Management Services and Exempt Organizations); Carl L. Aley, Director; Cheryl J. Medina, Audit Manager; Allison P. Sollisch, Lead Auditor; Michael A. McGovern, Auditor; and Vikram E. Singh, Auditor.

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<sup>1</sup> A judgmental sample is a nonprobability sample, the results of which cannot be used to project to the population.



## **Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed**

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### **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: the processes for identifying and classifying returns for examination and monitoring the results in the CP&C function. We evaluated these controls by reviewing IRS procedures, interviewing IRS employees, and analyzing examination statistics.



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## Appendix II

### Metrics Developed by the Reorganization Team With Suggested Measurement Methods

Objective	Measurement
Minimize/ avoid contact with compliant taxpayers	Compliance strategy issue realization rate (how often did we find the original issues that we were looking for)
Applies the most effective compliance treatments, which could include more than one compliance treatment	Impact (defined in compliance strategy) vs. compliance treatment hours
Counts what counts (focus on measuring “substantial noncompliance” treatment impact)	Substantial noncompliance (defined in compliance strategy) change count vs. number of treatments applied
Applies TE/ GE Division resources to change noncompliant taxpayer behavior rather than just develop a workplan for the number of agents available with a reasonable change rate	Issue reduction rate (start of treatment vs. 1st year, 2nd year, and 3rd year of treatment)
Ensures that the workplan is focused on the treatment of board directed issues	Percentage of in-process cases focused on original workplan issues
Efficient reporting on Compliance Program execution	Percentage of total reports that are self-serve
Keep fresh inventory on the Virtual Shelf	Inventory turns (average number of cases on shelf vs. total volume consumed each year)
Accurate claim, referral, Affordable Care Act, <i>etc.</i> Determinations	Claim, referral, Affordable Care Act, <i>etc.</i> (determination defect rate...check via sampling)
Keep Virtual Shelf fully stocked with cases that support the workplan	Percentage adherence to period stocking plan
Provides accurate and pertinent information in the case	Case defect rate (cases missing critical elements...check via sampling)
Provides a just-in-time inventory system; when you need a case, your manager can get one within a few days with updated research included	Fulfillment cycle time (75th percentile target = two days)

Source: Reorganization Team SharePoint Site.



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## Appendix III

### Additional Employee Concerns

Many employees expressed concerns with the reorganization during our interviews. Listed below are additional concerns multiple employees raised to us.

#### **TE/GE Division Reorganization Employee Concerns**

Concern	Number of Employees
<b>Scope of examinations is too narrow</b>	<b>9</b>
<b>Employees frustrated and demoralized due to no portal feedback</b>	<b>9</b>
<b>Workload does not match field employees' technical knowledge</b>	<b>6</b>
<b>Perception that CP&amp;C function standup was rushed and not well planned</b>	<b>5</b>
<b>Compliance project cases should be sampled to verify expected noncompliance issues exist prior to field assignment</b>	<b>5</b>
<b>Perception that centralization of classification activities is not more efficient</b>	<b>4</b>
<b>Perception that management values quick case closures more than the quality of examinations</b>	<b>3</b>

*Source: TE/GE Division employee interviews.*

In addition, TE/GE function management raised additional concerns.

#### **TE/GE Function Examination Management Concerns**

Concern	Number of Function Directors
<b>Inadequate workforce size</b>	<b>6</b>
<b>CP&amp;C function formation has not created efficiencies or improved effectiveness of the compliance program</b>	<b>5</b>
<b>Perception that CP&amp;C function employees lack the technical knowledge to fulfill their job responsibilities</b>	<b>4</b>
<b>Better CP&amp;C function communication needed</b>	<b>1</b>
<b>Perception that CP&amp;C function standup was rushed</b>	<b>1</b>

*Source: TE/GE Division Examination units' management interviews.*



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## Appendix IV

### Additional Compliance Planning and Classification Function Transition Goals

<b>Transition Goal</b>
<b>Ensure that all permissions are granted to close cases and create reports (Due May 1, 2017)</b>
<b>Continue delivery of immediate referrals and claims to the field (Due May 1, 2017)</b>
<b>CP&amp;C function leadership provides high-level introduction to the process (Due August 1, 2017)</b>
<b>Develop and deliver CP&amp;C function messaging plan (Due August 1, 2017)</b>
<b>Planning and Monitoring tests shelf monitoring process (Due August 1, 2017)</b>
<b>Classification and Case Assignment trains Functional Assignment Coordinators and starts classifying and case assignment using the new process (Due August 1, 2017)</b>
<b>New issue development process fully activated (Due September 30, 2017)</b>
<b>All new processes in place (Due February 1, 2018)</b>
<b>Training completed (Due February 1, 2018)</b>
<b>Identify the new reports needed to monitor issue success (Due February 1, 2018)</b>

*Source: Transition Plan – Big Picture, March 23, 2017 - PowerPoint.<sup>1</sup>*

<sup>1</sup> Includes minor editing changes for clarity.



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**Appendix V**

**Management's Response to the Draft Report**



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

November 30, 2020

MEMORANDUM FOR MICHAEL E. MCKINNEY  
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Edward T. Killen *Edward T. Killen*  
Acting Commissioner  
Tax-Exempt and Government Entities Division (TE/GE)

SUBJECT: Draft Report – Consolidation of Examination Case Selection and  
Assignment in the Tax Exempt and Government Entities Division  
Created Benefits, but Additional Improvements Are Needed  
(Audit # 201910022)

Thank you for the opportunity to review your draft report titled: "Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed."

As you reported, the TE/GE Division has important responsibilities for both the oversight of regulatory compliance as well as compliance with tax requirements by charitable entities, small local community organizations, major universities, large pension funds, small business retirement plans, State and local governments, participants in complex tax-exempt bond transactions, and Indian tribal government and tribal associations, etc. Given the breadth and scope of work that TE/GE is responsible for and the limited resources available, improvements in the form of consolidated work processes were necessary. As you reported, "The evaluation concluded that processes were not sustainable in a 'no-hire' environment." For years, TE/GE has been unable to hire the staff needed to address the volume of work; staff are highly specialized in their field but are tasked with multiple jobs. Changes were made to gain efficiencies and sustain operations in case selection, referral processing, and tracking and monitoring examination results.

We appreciate your acknowledgement that the creation of the Compliance Planning and Classification (CP&C) function had many positive results:

- Reduced potential and perceived conflict of interest in the identification and selection of examination workload;



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- Prioritization of case assignments based on the highest possibility of noncompliance;
- Development of standardized management information reports for different audiences and standardized work plans; and
- Improved separation of duties, triaging of most EO referrals, and tracking the results of specific potential noncompliance issues.

While the recommendations include a “comprehensive communication strategy,” the draft reports on several communication efforts such as: “group sessions with the potentially affected employees to communicate project progress;” “newsletter updates;” and work “with the employee union to ... assist with ... organizational redesign.” Additionally, TE/GE conducted week-long face-to-face training on the CP&C function for all employees in the Division nationwide over the course of several months. That said, communication can always be amplified.

Moreover, CP&C created an issue portal that receives employee submissions of compliance issues. These issues can be developed into compliance strategies by an Issue Identification team that collaborates with the IRS Research, Applied Analytics & Statistics function. This team has also overhauled the data-driven case selection methods in the Division. As the report states: “Compliance strategies and data-driven models developed by the CP&C function to select cases for examinations have resulted in improved productive workload identification for the TE/GE Division overall.” Additionally, CP&C has been implementing a “data grid” that “can now compare examination results with the specific potential noncompliance issues initially identified and adjust the criteria used to detect potential noncompliance issues as necessary.” Nevertheless, we continuously endeavor to improve case selection.

We will strive to frame process improvements prior to making further organizational changes. We will ensure we have the information necessary to identify areas needing improvement and the capacity to implement large-scale changes while also continuing to deliver on day-to-day services before proceeding with future reorganizations.

We appreciate the opportunity to review and comment on the draft report. Attached is a detailed response to your recommendations. If you have any questions, you or your staff may contact me at (202) 317-8400 or Maria Hooke, Director, Compliance Planning & Classification, TE/GE, at (214) 413-5500.

Attachment



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

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Attachment

### Corrective Actions for TIGTA Audit Draft Report – Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed (Audit # 201910022)

#### **RECOMMENDATION 1:**

The Commissioner, TE/GE Division, should develop reorganization guidance that includes the requirement for measurable metrics and data collection for future reorganizations and use the results to identify needed improvements.

#### **CORRECTIVE ACTION:**

In the event of a future reorganization, the TE/GE Division will develop appropriate metrics and data collection.

#### **IMPLEMENTATION DATE:**

N/A

#### **RESPONSIBLE OFFICIAL(S):**

N/A

#### **CORRECTIVE ACTION MONITORING PLAN:**

N/A

#### **RECOMMENDATION 2:**

The Director, CP&C, should develop performance metrics and data collection methods to measure progress towards current business unit goals that support IRS's strategic objectives and use this information to improve processes.

#### **CORRECTIVE ACTION:**

The Director, CP&C, will develop performance metrics for CP&C and data collection methods to measure progress towards current business unit goals that support IRS's strategic objectives.

#### **IMPLEMENTATION DATE:**

October 15, 2021

#### **RESPONSIBLE OFFICIAL(S):**

Director, Compliance Planning & Classification, TE/GE

#### **CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

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### **RECOMMENDATION 3:**

The Commissioner, TE/GE Division, should include in its business-unit specific reorganization guidance pursuant to Recommendation 1, a comprehensive communication strategy and the expectation for a designated, dedicated leader responsible for implementation of proposed reforms during the transition.

### **CORRECTIVE ACTION:**

In the event of a future reorganization, TE/GE will provide a comprehensive communication strategy and the expectation for a designated, dedicated leader responsible for implementation of proposed reforms.

### **IMPLEMENTATION DATE:**

N/A

### **RESPONSIBLE OFFICIAL(S):**

N/A

### **CORRECTIVE ACTION MONITORING PLAN:**

N/A

### **RECOMMENDATION 4:**

The Director, CP&C, should explore a process improvement to determine if it is feasible and cost effective to validate whether cases include the identified issues prior to assignment.

### **CORRECTIVE ACTION:**

Without a detailed review of books and records, there is no way to “validate” that an issue exists before a case is sent to an examiner. The methodology that is in place for development of strategies is designed to identify the compliance issues prior to assignment to the extent possible. Based on the amount of research analysis and development that is completed and presented to the TE/GE CP&C Governance Board, we have a high confidence level of the compliance issue. When possible, we roll out strategies in phases to allow us to “test” results and modify the strategy if needed.

### **IMPLEMENTATION DATE:**

N/A

### **RESPONSIBLE OFFICIAL(S):**

N/A

### **CORRECTIVE ACTION MONITORING PLAN:**

N/A



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

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### **RECOMMENDATION 5:**

The Commissioner, TE/GE, should explore the feasibility of reassigning resources from compliance functions to CP&C to improve the efficiency of identifying, classifying and monitoring productive examinations workload related to all TEGE Functions.

### **CORRECTIVE ACTION:**

The CP&C Director will conduct an assessment within the CP&C function to determine the skills and staffing needed to improve the efficiency of identifying, classifying and monitoring productive examinations workload related to all TE/GE functions. The CP&C Director will develop a hiring plan to acquire the appropriate resources.

### **IMPLEMENTATION DATE:**

February 15, 2022

### **RESPONSIBLE OFFICIAL(S):**

Acting Commissioner, TE/GE

### **CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

### **RECOMMENDATION 6:**

The Commissioner, TE/GE, should develop guidance for Functional Assignment Coordinators to minimize assigning cases involving excessive administrative actions and travel costs.

### **CORRECTIVE ACTION:**

While the current case assignment process is deliberately designed to reduce the potential for bias in case selection, TE/GE will review for possible process improvement a way to minimize assigning cases involving excessive administrative actions and travel costs. If a process improvement can be realized that does not negatively impact other factors, CP&C will develop or clarify guidance for Functional Assignment Coordinators to implement the process improvement.

### **IMPLEMENTATION DATE:**

April 15, 2021

### **RESPONSIBLE OFFICIAL(S):**

Director, Compliance Planning & Classification, TE/GE

### **CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.



## Consolidation of Examination Case Selection and Assignment in the Tax Exempt and Government Entities Division Created Benefits, but Additional Improvements Are Needed

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## Appendix VI

### Abbreviations

CP&C	Compliance Planning and Classification
EO	Exempt Organizations
EP	Employee Plans
FSL	Federal, State, and Local
FY	Fiscal Year
IRS	Internal Revenue Service
ITG	Indian Tribal Governments
P&M	Planning and Monitoring
TEB	Tax Exempt Bonds
TE/GE	Tax Exempt and Government Entities
TIGTA	Treasury Inspector General for Tax Administration



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