

December 2012

2012 TAX FILING

IRS Faces Challenges Providing Service to Taxpayers and Could Collect Balances Due More Effectively



G A O

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Why GAO Did This Study

The tax filing season is an enormous undertaking during which the IRS processes millions of tax returns, issues billions of dollars in refunds and provides service to millions of taxpayers over the phone, online, and face-to-face. It also identifies taxpayers who owe additional taxes and begins the process of collecting their balance due. GAO was asked to review IRS's performance during the 2012 filing season. Among other things, this report (1) assesses IRS's performance in processing returns, issuing refunds, and providing service to taxpayers over the phone, online, and in-person; and (2) describes what is known about taxpayers who filed returns with a balance due for tax year 2010 and assesses IRS's efforts to ensure timely payment. To conduct the analyses, GAO obtained and compared IRS data from 2007 through 2012, reviewed pertinent IRS documents, interviewed IRS officials and observed IRS operations, and interviewed other experts in tax administration, including from states and tax preparation firms.

What GAO Recommends

GAO recommends that IRS outline a strategy to improve taxpayer service, define appropriate levels of service, and describe how it intends to manage performance declines; clearly define the roles and responsibilities of those reviewing the notice phase; and pilot risk-based approaches for contacting taxpayers who have a balance due.

In response to GAO's first recommendation, IRS said it is pursuing some steps to improve service. IRS described plans to implement the other two recommendations.

View [GAO-13-156](#). For more information, contact James R. White at (202) 512-9110 or whitej@gao.gov.

2012 TAX FILING

IRS Faces Challenges Providing Service to Taxpayers and Could Collect Balances Due More Effectively

What GAO Found

While there have been efficiency gains and efforts to improve service, the Internal Revenue Service (IRS) faced challenges providing telephone service and responding to correspondence, continuing trends experienced in recent years. In 2012, 82 percent of individual taxpayers filed their returns electronically (e-filed), reducing IRS's processing costs. IRS also increased calls answered using automated service and added a variety of self service tools, which helped gain efficiencies. However, IRS's level of telephone service (the percentage of callers seeking live assistance who receive it) declined to 68 percent. In addition, of the 21 million pieces of paper correspondence IRS received, about 40 percent were considered overage (meaning that IRS did not respond within 45 days of receipt), an increase compared to last year. While IRS plans to continue to pursue efficiency gains, its strategy for future years does not specifically address how it plans to reverse these negative trends. Reversing the declines in telephone and correspondence services may require IRS to consider difficult tradeoffs, such as reassessing which phone calls IRS should answer with a live assistant and which it should not because automated services are available.

IRS Return Processing, Telephone Service, and Correspondence, 2007 through 2012 Filing Seasons

	2007	2008	2009	2010	2011	2012
Return processing (fiscal year)						
Returns processed (in millions)	135	151	139	137	140	142
Percent e-filed	58	59	67	71	78	82
Telephone service (as of June 30, each year)						
Percentage of callers seeking live assistance who receive it	81	57	68	76	72	68
Average wait time (in minutes)	4.6	8.6	8.4	9.5	11.7	17
Paper correspondence (end of fiscal year)						
Percentage of overage correspondence	17	23	25	27	35	40

Source: GAO analysis of IRS data.

GAO identified about 3.8 million returns where taxpayers self-acknowledged a balance due of \$13.8 billion for tax year 2010, the most recent data available. During IRS's notice phase, when IRS sends letters to taxpayers telling them how to pay the balance, the majority of this amount is either fully paid or accounted for through installment agreements. However, at least \$4.4 billion remained uncollected after IRS sent as many as four notices to taxpayers. These amounts become subject to more costly collections actions, such as phone or face-to-face contact. Best practices, such as risk-based approaches where contacts are tailored to the taxpayer, have helped increase collections in states such as New York and California. IRS has developed an analytics plan and uses some risk-based processes to identify which notices taxpayers will receive, but has not yet implemented the plan and management responsibilities are unclear. As a result, IRS has not tested more advanced risk-based approaches. This may lead to delayed collection of taxpayer debt, higher costs for IRS, and additional penalties for taxpayers who pay late.

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Abbreviations

CADE	Customer Account Data Engine
CFPB	Consumer Financial Protection Bureau
CONOP	Concept of Operations
CP	Computer Paragraph
CSR	Customer Service Representative
e-file	electronic filing
ETAAC	Electronic Tax Administration Advisory Committee
FTE	Full-Time Equivalent
IMF	Individual Master File
IRS	Internal Revenue Service
ITA	Interactive Tax Assistant
MeF	Modernized e-File
PPS	Practitioner Priority Service
RAC	Refund Anticipation Check
RAL	Refund Anticipation Loan
TAC	Taxpayer Assistance Center
TIGTA	Treasury Inspector General for Tax Administration
VITA	Volunteer Income Tax Assistance

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Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

December 18, 2012

The Honorable Max Baucus
Chairman
The Honorable Orrin Hatch
Ranking Member
Committee on Finance
United States Senate

The Honorable Charles W. Boustany
Chairman
The Honorable John Lewis
Ranking Member
Subcommittee on Oversight
Committee on Ways and Means
House of Representatives

Every tax filing season is an enormous undertaking during which the Internal Revenue Service (IRS) interacts with millions of taxpayers and hundreds of thousands of tax preparers by processing tax returns, issuing refunds, answering telephone calls, and providing other services, including those on its website. In recent years, IRS has taken a number of steps to improve return processing, provide faster refunds, and deliver better service. For example, IRS has added automated telephone lines and increased the number of self-service tools that taxpayers can use online. IRS also has a telephone line for professional tax return preparers.

More than three-quarters of taxpayers receive a refund, but some owe additional tax. Taxpayers who file a return showing additional tax owed, referred to as a balance due, are generally required to submit payment to the IRS by the tax filing deadline—usually April 15th. Paying on time is critical—taxpayers avoid interest and penalties associated with late payments and IRS avoids using limited compliance staff resources to collect taxes owed.

Taxpayers receiving refunds have a range of decisions to make about the best way to obtain refunds. Last year, we reported that taxpayers' use of controversial Refund Anticipation Loans (RAL)—high interest, short-term loans from tax preparers or banks that give quicker access to tax refunds than if taxpayers wait for a direct deposit or paper check—significantly decreased because RALs were no longer widely available. In contrast, taxpayers' use of Refund Anticipation Checks (RAC)—temporary bank

accounts set up by tax preparers allowing them to subtract tax preparation and other fees from taxpayers' refunds—has continued to increase.¹ Some tax industry experts and consumer protection organizations have expressed concerns that taxpayers do not always have information, especially about RAC fees, to make the best decisions about how to obtain their refund.

In this context, you asked us to review a number of issues related to IRS's 2012 tax filing services. Specifically, this report

1. Assesses IRS's performance in processing returns, delivering refunds, and providing telephone service and online and face-to-face assistance in comparison to its 2012 goals and prior years' performance;
2. Describes what is known about taxpayers who filed returns with a balance due for tax year 2010, but did not pay by the filing deadline, and assesses IRS's efforts to encourage timely payment; and
3. Summarizes the growth of RACs in recent years and the reasons taxpayers may obtain them, the manner in which RAC and other fees are disclosed to taxpayers in commonly used online tax return preparation software packages, and key stakeholder views regarding the transparency of RACs and associated fees.

To accomplish these objectives, we collected and analyzed data and documents from IRS and tax industry experts. We used these data to compare IRS's performance in 2012 to prior years and IRS's goals. We also interviewed IRS officials and tax industry experts to obtain different perspectives on IRS's performance during the 2012 filing season. To identify the number of returns and associated dollar amounts from returns where the taxpayer self-identified a balance due, as well as the amount IRS collected and resolved during the notice phase of collections, we matched IRS notice data with collections data and return transaction data.

Data limitations are discussed where appropriate. We reviewed IRS documentation, interviewed IRS officials about computer systems and data limitations, and compared those results to our standards of data reliability. We interviewed knowledgeable IRS collections and research

¹GAO, *2011 Tax Filing: Processing Gains, but Taxpayer Assistance Could Be Enhanced by More Self-Service Tools*, [GAO-12-176](#) (Washington, D.C.: Dec. 15, 2011).

staff, as well as Treasury Inspector General for Tax Administration (TIGTA) staff who worked on past reports relevant to this area to identify data sources and better interpret our data. We consider the data presented in this report to be sufficiently reliable for our purposes. We conducted our fieldwork primarily at IRS headquarters in Washington, D.C., and at the Wage and Investment Division headquarters in Atlanta, Georgia, as well as other sites with key IRS offices.

To identify RAC and associated fees with return preparation software, we prepared sample returns from each of the five most frequently used software packages that taxpayers used to self-prepare returns in 2012. We also interviewed tax industry experts, consumer advocacy representatives, and government officials, including from the IRS and the Consumer Financial Protection Bureau (CFPB), to determine what, if any, steps are being taken to make RAC, and return preparation fees generally, more transparent to taxpayers. Appendix I provides additional details on how we did our work.

We conducted this performance audit from February 2012 through December 2012 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. To conduct our analysis of the cost and features of RACs, we used investigative techniques. We conducted our related investigative work in accordance with investigation standards prescribed by the Council of the Inspectors General on Integrity and Efficiency.

Background

IRS processes paper and electronic tax returns and validates key pieces of information during the filing season. The majority of returns are now electronically-filed (e-filed). IRS is replacing its legacy e-file system with the Modernized e-File (MeF) system.² IRS is also transitioning from the antiquated Individual Master File (IMF) system to a more modern tax processing system known as the Customer Account Data Engine 2

²IRS cannot accept electronically filed returns directly from taxpayers. Rather, IRS authorizes e-file providers to transmit returns to IRS electronically using either the legacy e-file or MeF system.

(CADE 2), the systems IRS uses to process tax returns.³ CADE 2 allows IRS to provide quicker refunds and conduct more and better compliance checks before refunds are issued.

In addition to processing tax returns, IRS provides a variety of taxpayer services through its telephone, website, and face-to-face operations.

Telephone and paper correspondence

- Taxpayers can call IRS to speak directly with a customer service representative (CSR) to obtain information about their accounts or ask tax law questions. Providing live assistance over the phones is expensive for IRS—according to IRS officials, the cost of answering telephone calls has risen from about \$26 per call in 2009 to about \$30 in 2011.⁴
- Taxpayers can also obtain some of the same information using automated telephone lines, including IRS's 149 Tele-tax lines for tax law topics and 10 phone lines for account information. In 2011, IRS officials said that it cost 36 cents to answer an automated phone call.
- In October 2009, IRS started using a speech analytics program called Contact Analytics to better understand why taxpayers call IRS and evaluate how CSRs interact with taxpayers. Contact Analytics is a sophisticated speech analytics program that converts speech, such as CSR conversations with taxpayers, into text for analysis.
- CSRs are also responsible for responding to paper correspondence from taxpayers. IRS tries to minimize the amount of overage paper correspondence—correspondence that IRS has not addressed within 45 days of receipt.
- In addition to answering calls from taxpayers, CSRs answer calls from paid preparers who call about taxpayer accounts through IRS's Practitioner Priority Service (PPS). We have reported that paid preparers prepare about 60 percent of tax returns and play a critical

³The IMF is the system IRS has used to process tax returns in the past. CADE 2 will eventually fully replace the IMF.

⁴Cost per call for 2009 is based on calls answered from January 1, 2009, through June 30, 2009, and January 1, 2011, through June 30, 2011, respectively.

role in answering taxpayers' questions and filing tax returns.⁵ Taxpayers who get their questions answered by a preparer may not need to call IRS.

Website

- IRS also provides service to taxpayers through its website, <http://www.IRS.gov>. For example, taxpayers can find information on the status of their refunds, request transcripts (which are copies of a taxpayer's account information), and pay account balances. Taxpayers can also download forms, instructions, and publications, and research tax law issues through interactive tools.

Face to face

- IRS staff provides face-to-face assistance at 397 Taxpayer Assistance Centers (TAC). Staff at TACs provide answers to basic tax law questions, review taxpayer accounts, and prepare returns for qualified taxpayers.⁶ IRS has begun pilot-testing virtual assistance, where IRS employees interact with walk-in clients through a video terminal, at a small number of TACs and partner sites.
- IRS also has volunteer partners that staff more than 13,000 volunteer sites. These Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly sites prepare tax returns for traditionally underserved taxpayers. Some of these also serve as Facilitated Self-Assistance sites where volunteers guide taxpayers through simple tax returns.

Debt collection process and RACs

After tax returns are filed and processed, IRS begins the process of collecting unpaid tax debts. IRS attempts to collect unpaid tax debts in three phases: (1) notices sent through the mail, (2) telephone contact, and (3) face-to-face interactions.⁷ When a taxpayer files an individual return with a balance due but does not pay in full, IRS is statutorily required to send a letter detailing the proposed assessment of tax, penalty, and interest, and possible ways for the taxpayer to respond. If

⁵GAO, *Tax Preparer Regulation: IRS Needs a Documented Framework to Achieve Goal of Improving Taxpayer Compliance*, [GAO-11-336](#) (Washington, D.C.: Mar. 31, 2011).

⁶Taxpayers with annual incomes of \$50,000 or less can have their returns prepared at TACs.

⁷GAO, *Tax Debt Collection: IRS Has a Complex Process to Attempt to Collect Billions of Dollars in Unpaid Tax Debts*, [GAO-08-728](#) (Washington, D.C.: June 13, 2008).

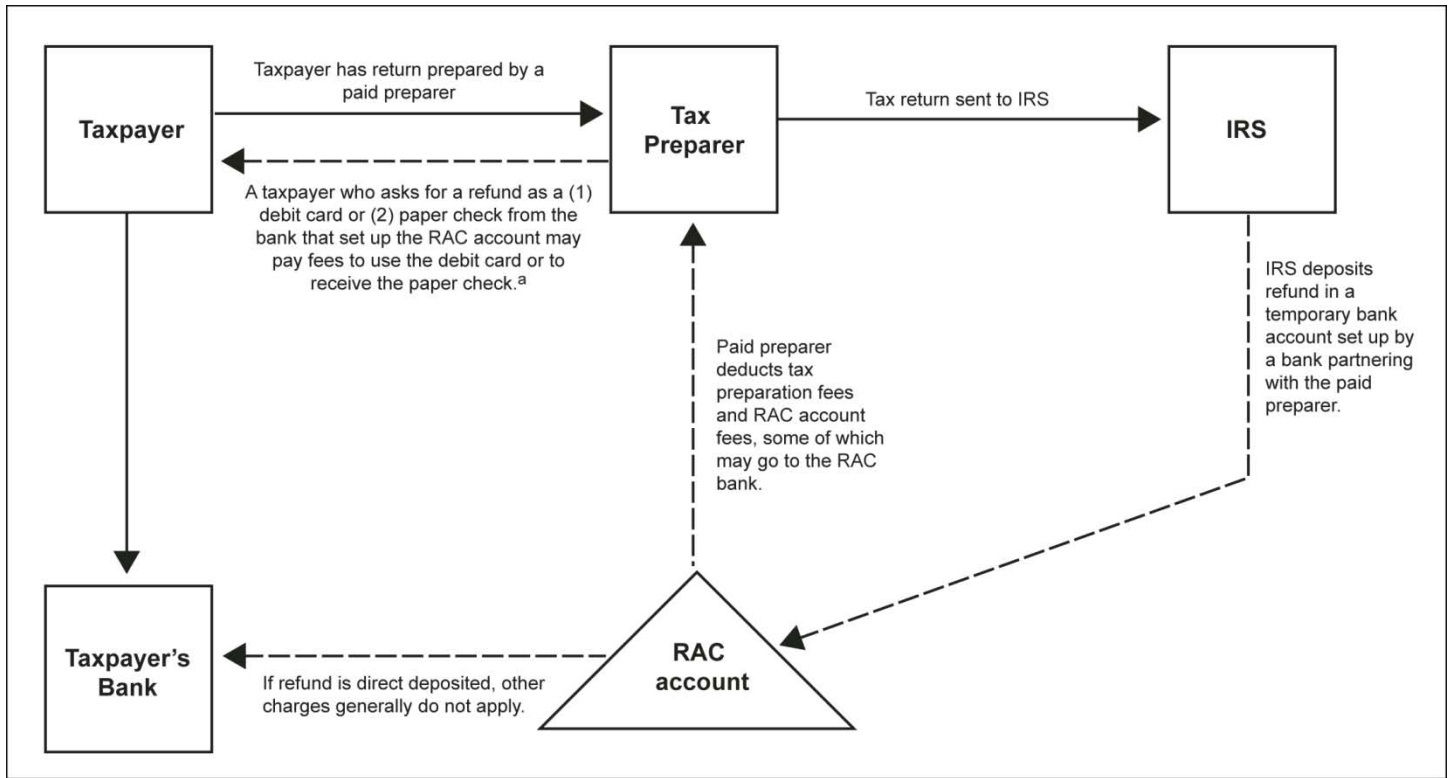
IRS does not receive a response within an allotted time, it is statutorily required to send a final notice prior to taking collection action such as levying wages on a bank account or filing a lien. Between the first and final notices, IRS may send up to two additional notices. Depending on the taxpayer, IRS could send a total of four notices before initiating other, more costly collection activities such as telephone calls to taxpayers or face-to-face interactions. Appendix II provides a more detailed summary of IRS's notices process.

Finally, in recent years, millions of taxpayers have chosen to obtain their tax refunds and pay for tax preparation services through a RAC obtained from tax software companies or paid preparers. With a RAC, paid preparers or software companies deduct any applicable fees from taxpayers' refunds. The remainder of the refund can be deposited (1) in a bank account created by a financial institution or paid preparer on behalf of the taxpayer, (2) in the taxpayers' own account, or (3) on a prepaid debit card issued by the paid preparer. In recent years, RACs have almost entirely replaced RALs.⁸ Figure 1 provides an example of potential fees incurred by taxpayers when filing a return and receiving a refund through a RAC.⁹

⁸In August 2010, IRS announced it would no longer provide return preparation companies with the debt indicator that had allowed preparers to observe whether taxpayers had other debts to the federal government or if the taxpayer would likely receive the full anticipated refund from IRS. As a result, most banks stopped funding RALs when banking regulators determined them to present too much risk to participating banks. IR-2010-89, August 5, 2010.

⁹[GAO-12-176](#).

Figure 1: Example of How a Taxpayer Receives a Refund Anticipation Check and When Fees May Be Incurred



Source: GAO analysis.

^aTaxpayers with bank accounts can generally cash or deposit their refund check without charge. If not, they may use an alternative provider and pay a fee to have the check cashed.

While IRS Has Made Efficiency Gains and Improved Performance in a Variety of Areas, It Faces Challenges Providing Service to Taxpayers

E-Filing Continued to Grow, MeF Contingency Plans Are Being Updated, and IRS Is Working to Improve Its Public Messaging Regarding Refund Turnaround Time

About 142 million individual income tax returns were filed in 2012, slightly up from last year. As table 1 shows, IRS achieved an 82 percent e-file rate for individual returns, surpassing the goal set by Congress for all returns in 1998—a significant accomplishment for IRS.¹⁰ E-filing has many benefits for taxpayers, including faster refunds and higher accuracy rates. It also provides IRS with significant cost savings by eliminating the need to manually transcribe data on paper returns. According to IRS, in fiscal year 2010, it cost 17 cents to process an e-filed return and \$3.66 for returns filed on paper.

Table 1: Individual Income Tax Returns Processed from 2007 to 2012

	2007	2008 ^a	2009	2010	2011	2012	Percent change from 2011 to 2012 ^b
Number of individual tax returns processed (in millions)	135	151	139	137	140	142	2
Electronic	79	89	94	97	109	116	6
Paper	56	62	45	40	30	26	-13
Percentage e-filed	58	59	67	71	78	82	5
Number of refunds issued (millions)	103	105	109	107	107	108	1
Amount of refunds issued (dollars in billions)	\$234	\$248	\$298	\$312	\$303	\$295	-3
Average refund amount	\$2,259	\$2,350	\$2,725	\$2,915	\$2,836	\$2,726	-4

Source: GAO analysis of IRS data.

¹⁰IRS has yet to reach the 80 percent e-file goal for some types of returns other than individual income tax returns.

Notes: Data are from January 1 through September 28, 2007; January 1 and October 3, 2008; January 1 and October 2, 2009; January 1 and October 1, 2010; January 1 and September 30, 2011; and January 1 and September 28, 2012.

^aThe Economic Stimulus Act of 2008 mandated that IRS send stimulus payments to over 100 million households, many of which would not otherwise have needed to file a tax return.

^bThe numbers in the table are rounded, but the percent change was calculated using exact values. Therefore, in some cases, the percent change is slightly different than it would be if it were calculated using the rounded values in the table.

In March 2012, we reported that IRS experienced problems with its MeF processing system, for which it had implemented important changes. Given these problems, we recommended that IRS review its contingency plan for MeF and update it in time for the 2013 filing season.¹¹ We also reported that IRS officials told us they had problems with a fraud detection process being unable to function properly in the daily processing environment. In June 2012, IRS officials told us that these problems were not detected due to limited testing before implementing the systems. Based on the experiences with MeF this year, and recommendations we and the Electronic Tax Administration Advisory Committee (ETAAC) made, IRS announced that it plans to keep legacy e-file available in a limited capacity in case of a catastrophic MeF failure.¹²

In addition, IRS officials said they were concerned that MeF may not be able to handle peak volume during the 2013 filing season. To mitigate these risks, IRS is more fully testing MeF, making necessary adjustments, and updating its MeF Contingency Plan again in January 2013. IRS is working with industry experts to identify which states, preparers, and transmitters will support both systems.

For 2012, IRS's public messaging for refund timeliness noted that most taxpayers could receive their refunds within 10 to 21 days of filing. According to tax industry experts, they conveyed IRS's timeframe to taxpayers, but delays due to processing errors or otherwise unmet

¹¹GAO, *Internal Revenue Service: Interim Results of 2012 Tax Filing Season and Summary of the Fiscal Year 2013 Budget Request*, [GAO-12-566](#) (Washington, D.C.: Mar. 20, 2012).

¹²ETAAC is a committee of tax industry experts with the primary purpose of providing input to the IRS on the development and implementation of IRS's strategic plan for electronic tax administration. In 2012, ETAAC issued a report that agreed with our recommendation and went further to suggest that IRS retain the capability to roll out its legacy e-file system in the event of a major MeF system failure.

expectations resulted in preparers receiving a significant number of phone calls from clients. For 2013, IRS officials indicated they may change IRS's public messaging to tell taxpayers to expect refunds in 21 days or less. However, they added that they would consult the tax preparation industry before setting refund timeliness expectations for the public.

New Self-Service Tools on IRS's Website and Further Development of an Online Services Strategy May Produce Efficiency Gains

IRS's website (<http://www.irs.gov>) had 297 million visits in 2012, an increase of almost 19 percent over 2011. The use of self-service tools available on the website has continued to grow, with the greatest increases coming from use of Interactive Tax Assistant (ITA) tools and Where's My Refund.¹³ For more information on website use, see appendix III.

IRS officials indicated that the website could be used to offer additional services. IRS is planning to develop more self-service tools so taxpayers can research tax law and account information.¹⁴ For example, in 2013, IRS plans to implement a Where's My Amended Return online tool where taxpayers can check whether their amended returns have been received by IRS. Online services give taxpayers access to information without calling IRS, which, as previously discussed, is expensive. We are conducting a separate evaluation of IRS's efforts to develop its website.

Expanded Self-Service and Virtual Service Programs at TAC and Volunteer Sites Have Helped IRS Serve Taxpayers

Although far fewer taxpayers visit TAC and volunteer sites than call IRS or use its website, these sites provide a significant service. As of April 30, 2012, IRS received 2.77 million taxpayer contacts at TACs, as compared to 2.85 million contacts this time in 2011. The accuracy of responses to account and tax law questions provided at TACs increased compared to previous years, as shown in table 2.

¹³ITA provides information on certain tax law topics by taking taxpayers through a series of questions. Where's My Refund provides taxpayers with information on the expected refund date. Additionally, appendix III shows that Online Payment Agreements had a significant increase in usage. However, this may be due to a programming error that led to a decrease in the number of completed agreements in 2011.

¹⁴In December 2011, we recommended that IRS develop a strategy for determining which self-service tools it will offer online. Since our recommendation, IRS has provided more details, such as an assessment of costs and benefits for some new services identified and time frames for when these online services would be created. See [GAO-12-176](#).

Table 2: IRS Walk-in Site Accuracy, 2008 through 2012 Filing Seasons

Accuracy measure (in percent)	2008 actual	2009 actual	2010 actual	2011 actual	2012 actual	2012 goal
Accounts assistance	85%	86%	91%	88%	92%	91%
	+/-2.30	+/-1.93	+/-1.66	+/-1.94	+/-1.61	
Tax law assistance	66	76	81	82	85	83
	+/-2.73	+/-1.97	+/-1.83	+/-1.83	+/-1.70	
Return preparation assistance ^a	n/a	n/a	82	83	89	n/a
			+/-3.82	+/-3.45	+/-2.86	

Legend: n/a = not applicable.

Source: GAO analysis of IRS data.

Note: Actual data for each year are from January 1 through April 30. IRS does not have comparable accuracy data available for the years prior to 2008.

^aReturn preparation assistance data were not available before 2010.

IRS expanded self-service and virtual service at both TAC and volunteer sites to increase access, reduce wait time, and extend the effectiveness of its employees. IRS piloted the Virtual Service Delivery program at 10 TACs and 2 external partner sites and plans to expand this program to an additional 10 to 20 sites nationwide in 2013. Through Virtual Service Delivery, IRS employees interact with walk-in clients through a video terminal when the employees are not occupied at their home site. For the first time beginning in 2012, IRS was able to track wait time data on a nationwide basis at TAC locations.¹⁵ For 2012, 74 percent of taxpayers waited less than 30 minutes for TAC service.

IRS partnered with 3,930 community-based organizations operating over 13,000 volunteer sites, staffed by about 99,000 volunteers in 2012.¹⁶ The number of returns prepared by volunteers increased slightly to 3.15 million in 2012, up from 3.07 million in 2011 (a 2.3 percent increase).¹⁷ IRS expanded the number of Facilitated Self-Assistance sites (computer kiosks) from 102 in 2011 to 496 in 2012, and plans to increase the

¹⁵The wait time is calculated from the time a ticket is issued to the time service begins.

¹⁶This is an increase from almost 88,500 volunteers in 2011, or about 12 percent.

¹⁷IRS officials said that increase in the number of returns prepared by volunteers for 2012 was not commensurate with increase in the number of volunteers because the increase in volunteers was due to more accurate accounting.

number of sites to 1,000 nationally by the end of the 2013 filing season. IRS also expanded the number of Virtual VITA sites, where taxpayers at remote locations can obtain service over fax, internet, and video connection, from 34 to 61. For more information on the services performed at IRS walk-in and volunteer sites, see appendix IV.

Access to Live Telephone Assistance Continues to Decline

In 2012, call volume increased, and as of June 30, 2012, IRS had received 98 million calls, an 18 percent increase over 2011. IRS answered about 50 million of these calls through automation, a 36 percent increase from 2011. IRS officials attributed the increase in automated calls answered to refund inquiries caused, in part, by refund delays early in the filing season and requests for transcripts. At the same time, there was a 52 percent increase in busy signals and cases where IRS determines that the best course of action is to disconnect the call before answering (due to wait times for the taxpayer or other reasons). For more information on calls to IRS by call type, see appendix V.

While calls answered through automation have increased, the number of CSR answered calls declined by about 14 percent (19.4 million calls compared to 22.6 million calls in 2011). However, IRS officials said that as more automated telephone features are added, the calls that CSRs actually answer have increased in complexity. For example, questions about topics such as identity theft, an increasingly important topic, take longer to resolve than inquiries about refunds and other, more basic services.¹⁸ Consequently, the average length of a CSR answered call has also increased by about 19 percent since 2009. IRS had about the same amount of CSR resources to answer calls and respond to paper correspondence in 2012 as in 2011—about 13,500 full-time equivalents (FTE) in both years. These CSRs are responsible for not only answering calls but also responding to paper correspondence (which we discuss below).¹⁹

¹⁸GAO, *Identity Theft: Total Extent of Refund Fraud Using Stolen Identities is Unknown*, [GAO-13-132T](#) (Washington, D.C.: Nov. 29, 2012).

¹⁹In the past, IRS has had more FTEs dedicated to telephone service and paper correspondence. For example, in 2010, IRS had over 15,000 FTEs dedicated to these services.

Taken together, these factors explain, at least in part, why IRS's performance in providing live assistance has declined in recent years even though fewer calls were answered by live assistors. In 2012, IRS's level of service, the percentage of callers seeking live assistance who receive it, was 68 percent, down from 81 percent in 2007, as is shown in table 3. The average wait time increased to 17 minutes in 2012, up from 4.6 minutes in 2007. While IRS exceeded its 2012 level of service and wait time goals, those goals were the lowest IRS has established in recent years.

Table 3: IRS's Telephone Service Goals and Performance, 2007 through 2012 Filing Seasons

Access measure		2007	2008	2009	2010	2011	2012	Percent change from 2011 to 2012 ^a
Percentage of callers seeking live help who received it	Goal	82%	82% ^b	77% ^c	71%	71%	61%	-14.1%
	Actual	81	57	68	76	72	68	-5.6
Average wait time (in minutes)	Goal	4.3	4.5	10.4 ^d	11.6	11.6	19	62.1
	Actual	4.6	8.6	8.4	9.5	11.7	17	42.7

Source: GAO analysis of IRS data.

Notes: Actual data are from January 1 through June 30, while goals are for the entire fiscal year. We believe comparing performance during the filing season to fiscal year goals is appropriate as IRS's filing season performance is an indicator of its performance for the entire year.

^aNumbers in the table are rounded, but percentage change was calculated using exact values. Therefore, in some cases, the percentage change is slightly different than it would be if it were calculated using the rounded values in the table.

^bIRS revised its original fiscal year goal of 82 percent down to 74 percent because of high call volume due to economic stimulus-related calls.

^cIRS revised its original fiscal year goal of 77 percent down to 70 percent because of high call volume from taxpayers requesting e-filing authentication information and asking stimulus-related questions.

^dIRS determines its wait time goals based on anticipated call volume and resource availability. IRS significantly raised its wait time goal for 2009 compared to 2008 in light of anticipated increased call volume related to tax law changes.

In 2010, we recommended that IRS take steps to define what appropriate levels of telephone service would be, determine a standard for telephone service, and identify the resources required to achieve this standard. However, IRS disagreed with this recommendation, saying that its current process of developing a planned level of telephone service takes into consideration many factors, including budget and assumptions about potential call volume. The IRS Oversight Board has said that an acceptable level of service should be about 80 percent.

Performance on IRS's Practitioner Priority Service, where paid preparers can call IRS, telephone lines also declined. As shown in table 4, the level of service for the paid preparer telephone line decreased to 73 percent in 2012, down from 91 percent in 2007. Over the same period, the average wait time for the paid preparer line increased from 2.8 minutes to 22.1 minutes. Officials said that paid preparers are willing to wait longer than taxpayers because paid preparers are attempting to get answers for their clients. Like phone service for taxpayers, IRS lowered the level of service goal for the Practitioner Priority Service in 2012.

Table 4: Practitioner Priority Service Goals and Performance, Fiscal Years 2007 through 2012

Access measure		2007	2008	2009	2010	2011	2012	Percent change from 2011 ^{a,b}
		Percentage of tax preparers seeking live assistance who received it	Goal	87%	87%	82%	76%	
	Actual	91	86	88	80	78	73	-6.4 ^a
Average wait time (in minutes)	Goal	4.9	4.5	6.5	10.0	10.7	26.2	145.4
	Actual	2.8	5.2	4.7	10.5	13.3	22.1	65.8

Source: GAO analysis of IRS data.

^aThe difference is 5 percentage points between actual performance in 2011 and 2012 and 6 percentage points between fiscal year 2011 and 2012 goals.

^bThe numbers in the table are rounded, but the percent change was calculated using exact values. Therefore, in some cases, the percent change is slightly different than it would be if it were calculated using the rounded values in the table.

The continued accuracy of the CSRs' answers represents a positive aspect of IRS's telephone service. As shown in table 5, IRS's accuracy rate for CSR answered calls remained well over 90 percent. We have reported that IRS officials attributed the high accuracy rate to automated interactive tax assistance tools that CSRs use to provide answers to taxpayers as well as use of Contact Analytics.²⁰

²⁰ [GAO-12-176](#).

Table 5: Accuracy of Telephone Service, 2007 through 2012 Filing Seasons

Accuracy measures ^a	2007	2008	2009	2010	2011	2012
Tax law rate (in percent) ^b	90.7% +/-0.9	90.3% +/-0.9	92.5% +/-0.8	92.4% +/-0.8	92.9% +/-0.6	92.5% +/-0.7
Account accuracy Rate (in percent) ^b	93.2 +/-0.5	93.5 +/-0.4	95.1 +/-0.4	95.6 +/-0.4	96 +/-0.3	95.4 +/-0.3

Source: IRS data.

^aBased on representative samples of phone calls selected by IRS from January 1 through June 30.

^bThe percentage of calls in which CSRs provided accurate answers for the call type and took the appropriate actions, with a 90 percent confidence interval.

Overage Paper Correspondence Increased

As shown in table 6, while the amount of paper correspondence in 2012 increased by 5 percent from 2011, the percentage of overage taxpayer correspondence increased by 14 percent over the same period. Providing a timely response to paper correspondence is important because if IRS's response takes too long taxpayers may write again or call IRS.

Table 6: IRS Taxpayer Correspondence Performance, Fiscal Years 2007 through 2012

	Fiscal Year						Percent Change from fiscal year 2011 to 2012
	2007	2008	2009	2010	2011	2012	
Correspondence received (in millions) ^a	16	18	19	20	20	21	5%
Percentage of taxpayer correspondence overage ^b	17%	23%	25%	27%	35%	40%	14%

Source: GAO analysis of IRS data.

Note: Aggregate data are from Accounts Management and Submission Processing, which jointly responds to IRS's taxpayer correspondence.

^aData cover equivalent periods for each fiscal year with slight variation in the exact dates depending on the year and data source.

^bIRS generally considers paper correspondence that is not resolved within 45 days to be overage. Data from 2007 and 2008 data do not include overage data for correspondence processed by submission processing as submission processing began tracking overage data in 2009.

IRS Does Not Have a Strategy to Reverse Declines in Service

IRS has taken a multi pronged approach to improve taxpayer service and better manage call volumes. For example, in 2012, to reduce the time CSRs spend on phone calls, IRS implemented personal identification numbers that taxpayers who are transferred to a new CSR can provide to

eliminate the re-authentication process. To increase the number of calls answered by CSRs, IRS also implemented a new procedure where the CSR is automatically connected to the next caller after finishing the current call. To better manage call volume, pre-empt taxpayer questions, and identify which services could be provided through automation, IRS is using Contact Analytics to identify trends in taxpayers' calls and update information on IRS.gov. Additionally, in response to our previous recommendation in 2009, IRS deployed an online VITA locator during 2012 where taxpayers can enter their ZIP codes to find VITA sites close to their location.²¹

The numerous efficiency initiatives IRS has implemented to date have not kept pace with call or correspondence volume. IRS's current Concept of Operations (CONOP) outlines a 3- to 5-year strategic plan for providing taxpayer services. The plan acknowledges that IRS will experience declining levels of service absent aggressive action and outlines potential actions that IRS could take to deflect demand and improve efficiency of operations. However, the potential actions generally continue the approach IRS has followed in recent years seeking incremental efficiency gains. The federal government's tight budget environment makes any meaningful increase in resources for taxpayer service unlikely. Further, IRS officials said that the actions and time frames presented in the CONOP would be difficult for IRS to meet. Without a more strategic approach that recognizes the inability of efficiency initiatives to keep up with call volume and call complexity, as well as the reality of IRS's resources and capabilities, telephone service and response time to paper correspondence is at risk of further decline.

Given the above, reversing the declines in telephone and correspondence services may require IRS to consider difficult tradeoffs. Rather than limiting access through long wait times, other ways of reducing demand might be considered. One option might be reassessing which phone calls IRS should answer with a CSR and which it should not because automated services are readily available—either online or over the phones. Although limiting access to CSRs for certain callers is not an optimal solution, it might help better target taxpayer assistance to those for whom live assistance is the only option. Another option might be to

²¹GAO, *Tax Administration: Opportunities Exist for IRS to Enhance Taxpayer Service and Enforcement for the 2010 Filing Season*, [GAO-09-1026](#) (Washington, D.C.: Sept. 23, 2009).

consider whether certain types of questions should be directed to paid preparers or tax software companies. Identifying options, assessing their pros and cons, and deciding on a course of action would need to be part of a more extensive strategy than the currently existing CONOP.

IRS Could More Effectively Apply Risk-Based Approaches to Collect Balances Due

For tax year 2010, the most recent year with available data, we found about \$13.8 billion on returns where taxpayers filed with a self-acknowledged balance due that was not paid on time. State officials we interviewed described some best practices for collecting balances due, including earlier contact based on the characteristics and behaviors of individual taxpayers and more extensive use of complex data analytics and modeling. IRS has adopted some risk-based approaches to its notice phase, such as determining which taxpayers will receive which notices (IRS sends up to four notices), based on factors such as the size of the amount owed. However, a lack of clarity in the roles and responsibilities of IRS officials in charge of sending notices to taxpayers impedes IRS's ability to best identify and implement risk-based approaches for resolving balances due. Although IRS has developed a data analytics plan for managing its balance due process, the plan has not yet been implemented. Further, IRS has not pilot tested other, more extensive risk-based approaches being used in some states.

For Tax Year 2010, Taxpayers Self-Assessed Balances Due for Billions of Dollars

As table 7 shows, about 3.8 million returns were filed where taxpayers self-assessed unpaid balances owed for tax year 2010, meaning that they filed a return where they acknowledged that they owe additional tax and did not pay in full by the filing deadline. These taxpayers owed a total of about \$13.8 billion.²²

²²We calculated \$13.8 billion based on the amount listed on the first notice sent to taxpayers who filed an individual return with a balance due but did not pay in full.

Table 7: Balance Due Accounted for During Notice Process or Sent on to Collections, Tax Year 2010

Dollars in billions

Description	Total amount due on first notice	Number of returns (millions)
Balance due returns resolved during the notice process	\$9.4	3.2
Balance due returns sent to collections	4.4	0.6
Total	\$13.8	3.8

Source: GAO analysis of IRS data.

As shown in table 8, of those taxpayers that had a balance due at the filing deadline, almost two-thirds eventually paid in full or entered into installment agreements, which are payment plans where the taxpayer can repay the debt owed in scheduled increments (usually monthly). However, IRS was unable to collect at least \$4.4 billion in balances through notices and these returns progressed to later collections stages. Additionally, an unknown amount of tax owed remained uncollected in cases where the taxpayer defaulted on an installment agreement. According to IRS officials, about 18 percent of taxpayers default on installment agreements, resulting in IRS eventually sending these taxpayers to collections.²³ Unpaid balances due result in IRS using more expensive resources, such as phone contact and field visits, to collect the taxes. In addition, taxpayers may face additional interest and penalties.

²³According to IRS, the default rate for IMF installment agreements was 18 percent in fiscal year 2012 and 17 percent for fiscal year 2011.

Table 8: Actions Taken by IRS or Taxpayers on Balance Due Returns by Amount Owed and Percentage, Tax Year 2010

Dollars in billions

Action Taken	Amount	Percentage of amount owed	Percentage of returns
Installment agreement	\$5.5	40%	33%
Full paid	3.1	23	39
Sent to collections	4.4	32	16
Other ^a	0.7	5	12
Total	\$13.8^b	100%	100%

Source: GAO analysis of IRS data.

^aThe other categories include a range of taxpayers, including those that IRS determines are currently unable to pay and taxpayers whose returns have been referred for criminal investigation.

^bNumbers do not add due to rounding.

Some States Have Implemented Risk-Based Approaches to Debt Collection That Are Considered Best Practices

States have employed risk-based approaches to help them collect uncollected taxes that provide options that may be appropriate for IRS to also consider. Representatives from three states with advanced collection approaches (identified by the Federation of Tax Administrators, an organization that represents state tax administration agencies) we spoke with identified two best practices for collections strategies:

- applying risk-based approaches to collections strategies, including risk-based analytics such as risk scores based on taxpayer data, and
- initiating timely contact of taxpayers who owe debts. Both we and the Treasury Inspector General for Tax Administration (TIGTA) have reported on the success of timely contact with debtors, and it is an accepted debt collection best practice.²⁴

Risk-based approaches use data on taxpayers' filing status, payment history, public records such as bankruptcies, and payment behaviors to determine for a given taxpayer which collections methods will produce the best results. Risk-based analytics have been in use by IRS and other tax agencies for many years, but mostly in fraud detection and prevention.

²⁴GAO-08-728 and TIGTA, *Reducing the Processing Time Between Balance Due Notices Could Increase Collections* (Sept. 26, 2011).

For example, IRS applies a risk score to returns during its screening process to estimate the risk of fraud. IRS sometimes audits taxpayers who submit returns with scores that exceed certain thresholds, which are those returns predicted most likely to be fraudulent. The use of such tools in early phases of collecting balances owed by taxpayers is an emerging best practice and can (1) increase amounts of debt collected if applied to taxpayers who do not respond quickly and (2) save resources by identifying taxpayers who may not require intervention (those who are likely to comply or tend to self-resolve their debts without intervention from the IRS).

According to experts we interviewed, some taxpayers may respond better to multiple notices sent more quickly or a phone call shortly after a notice, while others may respond to a single notice. According to state level officials we interviewed, data analysis sometimes showed that certain taxpayers are likely to pay without further intervention from the tax agency and that collection activities should be focused elsewhere.

New York State Department of Taxation and Finance officials reported that although they had fewer available collections resources, they collected an additional \$83 million in 2010, an increase of 8 percent, during the first year using their revenue-based analytics collections program. According to New York State officials we interviewed, the program uses data analytics to determine the collection actions most likely to generate the greatest amount of revenue at a given point in time, within certain resource constraints. New York State officials reported that they believe the program has been instrumental in helping increase collections.

Officials from two other state revenue agencies, California's Franchise Tax Board and North Carolina's Department of Revenue, told us that they have seen some improvement in collection rates as they implement risk-based approaches and other strategies to contact taxpayers who owe debt, but they cannot quantify how much of the improvement is related to these activities as they are part of a comprehensive change in collections processes. California's Franchise Tax Board experienced an 18 percent increase in collections revenue from fiscal years 2010 to 2011, which officials there attribute to the implementation of new tools, including risk-based analytics and proactive call center strategies.

In all three states, these activities are part of broad changes in collections processes. According to representatives from the New York State Department of Taxation and Finance, in their experience, the initial

investment and set up of a revenue-based analytics collections program required both time and resources. The maintenance of this system also requires continuous updates as new events occur. For example, one of the most challenging parts of implementing the New York State system was to develop a way to correctly adhere to all of the state's laws and policies that affected collections and at the same time not to restrict the analytics engine so much that it cannot make the right choices. However, tax administration experts at the three states we interviewed and the Federation of Tax Administrators generally agreed that the benefits should outweigh the costs.

IRS Uses Some Risk-Based Approaches in the Notice Process but the Rationale and Management Responsibilities Are Unclear

IRS applies business rules, which determine the sequence of notices sent to a taxpayer, in an attempt to apply a risk-based approach to its notice process. IRS officials told us that they have some basic criteria, including taxpayers who repeatedly pay late, owe larger dollar amounts, or owe other taxes to the IRS, to determine which taxpayers receive which notices. However, we previously reported that IRS lacked information describing what the business rules for balance due notices are, specifically finding that IRS did not meet our criteria for internal controls for this process.²⁵ For example, although guidance for federal internal control standards states that managers should have information in forms to ensure the effectiveness of operations, IRS officials lacked documentation for the business rules of the notice phase and how the rules operated. We recommended that IRS document rationales for the business rules for managers. At the time of this review, IRS was still unable to provide us with clear documentation of these business rules that would meet internal control requirements.

IRS does not have well-documented, risk-based business rules, in part because of a lack of clear management responsibility for administering

²⁵In [GAO-09-976](#), *Tax Debt Collection: IRS Needs To Better Manage Collection Notices Sent to Individuals*, (Washington, D.C.: Sept. 30, 2009), we cited the Internal Control and Management Evaluation Tool ([GAO-01-1008G](#)) which specifies criteria for a well run program that includes: written documentation covering the agency's internal control structure and for all significant transactions and events; the documentation is readily available for examination; documentation, whether in paper or electronic form, is useful to managers in controlling their operations and to any others involved in evaluating or analyzing operations; and, pertinent information is identified, captured, and distributed to the right people in sufficient detail, in the right form, and at the appropriate time to carry out their duties and responsibilities efficiently and effectively.

parts of the collection notice process. This is partly because of the substantial reorganizations at IRS over the last 2 years, including the creation of an Enterprise Collection Strategy (ECS) and a Return Integrity Correspondence Service (RICS).²⁶ RICS officials told us that they have authority over the development and revision of balance due notices but that ECS is responsible for most of the analytics for the collections process. However, ECS officials told us that they were still determining the scope of their authority, but that IRS's Wage and Investment division has the majority of responsibility over the balance due notices process.²⁷ Lack of clarity in the roles and responsibilities of IRS officials responsible for sending notices to taxpayers impedes IRS's ability to best identify and implement risk-based approaches for resolving balances due.

IRS Has Not Implemented More Advanced Risk-Based Approaches Early in Its Collections Process

More effective risk-based analytics could benefit taxpayers by making them aware of payment options earlier and allowing them to avoid interest and penalties. For example, IRS does not contact taxpayers who e-file and have a balance due but do not pay in full until mid-May—IRS contacts taxpayers who file on paper as soon as the balance due is identified. Other approaches may also allow IRS to reduce costs by applying collections resources in a more targeted and effective manner. In recent comments, the Commissioner of Internal Revenue indicated that leveraging data analytics to continually improve IRS's operations is one of the agency's next major priorities.²⁸ IRS officials told us that they have a proposal, referred to as their Advanced Consolidated Data Analytics Plan, to apply a risk-based approach to determine to the extent to which each taxpayer who files a balance due and does not pay in full on time is contacted. The plan includes routing some taxpayers directly to phone

²⁶ECS is a unit within the IRS Small Business and Self-Employed division to centralize more of the collections functions. ECS became active in October 2011 and is currently developing a mission statement and strategy based on the IRS Collections Process Strategy issued in 2010. The IRS Return Integrity and Correspondence Services began its operations in October 2011, bringing together the Accounts Management Taxpayer Assurance Program, Earned Income Tax Credit and Health Coverage Tax Credit offices, and the Office of Taxpayer Correspondence under one umbrella. This consolidation is part of a strategy to address rising concerns about refundable credits and refund fraud.

²⁷According to GAO's *Standards for Internal Control in the Federal Government*, a good internal control environment requires that the agency's organizational structure clearly define key areas of authority and responsibility. [GAO/AIMD-00-21.3.1](#).

²⁸Prepared Remarks of IRS Commissioner Doug Shulman before the American Institute of Certified Public Accountants. Washington, D.C. IR-2012-89, November 7, 2012.

and field collections after the first notice is issued. However, due to other priorities, IRS has not scheduled implementation of the plan.

Potential additional risk-based approaches to collecting balances due range from relatively simple steps to more robust data analytics similar to what some states have implemented. While earlier contact with taxpayers based on payment history, or other indicators that they are not likely to pay on time, is an example of a relatively simple risk-based approach, options exist to test more complex approaches, similar to those described earlier and being used by some states. Such approaches involve more complex statistical analysis and help better determine which communication strategies are likely to work the best for a given taxpayer and yield the most revenue.

Use of RACs Has Increased Significantly and IRS and Others Are Beginning to Address Questions About the Transparency of RAC and Other Fees

As of September 30, 2012, taxpayers had requested more than 20 million RACs, which is about the same as 2010, but more than double the roughly 10 million RACs issued in 2005. Stakeholders we interviewed from both consumer protection groups and the tax industry generally agreed the primary benefits of RACs are allowing taxpayers to deduct return preparation fees from their refunds and ensuring some taxpayers receive refunds faster. Tax industry professionals said that RACs offer taxpayers flexibility that might otherwise not be available. For example, taxpayers may want to obtain a RAC if they do not have a personal bank account or lack sufficient funds to pay tax preparation fees in advance. Taxpayers can obtain a RAC through either use of a tax software package or paid preparer.

IRS data shows that nearly 40 percent of taxpayers who obtain a RAC use a software package to help self-prepare their returns. Our analysis of the five most frequently used tax software packages, 4 of which offered a RAC, found that

- three of the four RAC providers charged about \$30 for a RAC, which is consistent with findings from an Urban Institute study released in 2010,²⁹ and

²⁹Urban Institute, *Who Needs Credit at Tax Time and Why: A Look at Refund Anticipation Loans and Refund Anticipation Checks* (Washington, D.C.: November 2010).

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- three of the four software packages offering RACs required taxpayers to have a bank account to receive the remainder of the refund once all the fees, including the RAC fee, had been paid. This is noteworthy because helping taxpayers without bank accounts receive refunds is one of the major stated benefits of RACs.

In addition to RAC fees, we found that taxpayers may incur other fees related to the receipt of their refund. For example, if taxpayers choose to receive their refund on a prepaid debit card, they may incur fees for using the card or making withdrawals. Our analysis showed that cash withdrawal, monthly maintenance, and balance inquiry fees generally applied to the prepaid debit cards. Appendix VI includes more information on the fee structure of the software packages we reviewed.

We also found that, in general, RACs and associated fees varied, and the tax preparation software packages we reviewed included the required disclosures to taxpayers about the product. However, we were not able to evaluate the extent to which taxpayers read and understand the disclosures.³⁰ Further, we did not analyze how paid preparers operating commercial stores offered RACs to taxpayers or otherwise presented tax preparation fees.

Convincing empirical evidence about whether taxpayers are aware of and understand RACs and associated fees does not exist. Although we found that the fee structure and disclosures were included in tax software packages we reviewed, interested parties have expressed concerns about the transparency and cost of RACs. For example, we found that:

- Representatives from consumer protection groups we interviewed have noted that the fees associated with a RAC may be high, lack transparency, and taxpayers may not fully understand alternatives for receiving their refunds.³¹ These representatives noted that taxpayers

³⁰We have previously reported that disclosures related to some credit cards and mortgages are difficult for people to understand. GAO, *Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers*, [GAO-06-929](#) (Washington, D.C.: Sept. 12, 2006); and *Alternative Mortgage Products: Impact on Defaults Remains Unclear, but Disclosure of Risks to Borrowers Could Be Improved*, [GAO-06-1021](#) (Washington, D.C.: Sept. 19, 2006).

³¹See also, National Consumer Law Center, *End of the Rapid Rip-Off: An Epilogue For Quickie Tax Loans* (February 2011).

who have bank accounts and access to credit should have little need for a RAC.

- Industry participants stated that, in some cases, RAC and other fees could be more effectively disclosed to taxpayers. Tax industry representatives told us they have made proposals to policy makers and regulators to enhance return preparation and bank fee disclosures, monitor third-party vendors, and develop marketing requirements and other agreed upon prohibited and best practices.
- Some states have enacted legislation governing paid tax preparers that offer RACs. The state laws that have been enacted require the disclosure of fees and the posting of a fee schedule.³² In some cases, the required disclosures include informing the taxpayer that the taxpayer has the right to not obtain a RAL or RAC.³³ Some states have taken the additional step of placing restrictions on the fees a tax preparer can charge when providing a RAC. For example, Illinois law prohibits tax preparers from charging any additional fee to obtain a RAC apart from that charged by the financial institution providing the RAC.³⁴

Finally, IRS officials told us that because a RAC is a bank product it would be more appropriate for banking regulators, who also played a key role in eliminating RALs, to determine whether further steps need to be taken to address issues that have been raised with respect to the transparency of RACs.³⁵ The Bureau of Consumer Financial Protection, commonly referred to as the Consumer Financial Protection Bureau (CFPB), examines short-term, small-dollar lending, which could include

³²See, for example, Ark. Code §§ 4-116-101 to 4-116-108 (2012); Conn. Gen. Stat. Ann. § 42-480 (2012); Me. Rev. Stat. tit. 9-A, § 10-310 (2012); Tex. Fin. Code § 352.001 (West 2012).

³³See, for example, Cal. Bus. & Prof. Code §§ 22251 and 22253 (2012); Md. Code, Com. Law, §§ 14-3806; Mich. Comp. Laws Ann. § 446.111, et. seq.

³⁴Tax Refund Anticipation Loan Reform Act, 2012 Ill. Laws P.A. 97-849.

³⁵The Office of Professional Responsibility governs paid preparers in accordance with Circular 230, which includes unreasonable fees and misleading or false advertising by paid preparers. See [GAO-12-176](#) for an explanation of the role banking regulators played in limiting the use of RALs.

RACs; however, CFPB has not done extensive work with RACs.³⁶ CFPB officials said that they do not have specific jurisdiction over return preparation fees. Recently, in response to increased interest about RAC and other tax preparation fees, IRS and CFPB have begun discussing whether there is a need for further regulation of RAC and other fees or if additional steps need to be taken to help taxpayers understand return preparation fees. As IRS is beginning to work with consumer and regulatory groups on these issues, we are not making any recommendations to IRS at this time.

Conclusion

IRS deserves credit for achieving noticeable efficiency gains in processing returns and providing taxpayer services over recent years. In an era of tight budgets, such gains are vital for keeping up with an expanding workload and improving outcomes for taxpayers. However, while IRS has realized efficiency gains, it is still struggling in its efforts to give taxpayers access to telephone assistors and provide timely responses to correspondence. The efficiency gains have been more than offset by increases in demand for services. While further improvements, as envisioned in IRS's CONOP are desirable, recent history provides little prospect of such gains reversing the service declines. Without a more dramatic revision in strategy, the recent declines in access and correspondence services seem likely to continue.

While processing returns and issuing refunds to taxpayers, IRS also collects taxes owed to the government. New analytical, risk-based tools are helping state tax administration agencies better determine when and how to contact taxpayers who file a return with a balance due but do not pay the government when they file their returns. However, IRS has yet to experiment with implementing such tools during the notice phase before more expensive methods of collection, including telephone calls and face-to-face visits to taxpayers, are necessary. This is due, in part, to IRS's lack of clearly defined responsibilities for administering the notice phase. Resolving payment issues early on also helps taxpayers avoid paying interest and penalties on their remaining balances.

³⁶The CFPB was created in 2010 to ensure that consumers get the information they need to make the financial decisions they believe are best for themselves. Consumer Financial Protection Act of 2010, Pub. L. No. 111-203, title X, 124 Stat. 1955.

Recommendations for Executive Action:

We recommend that the Acting Commissioner of Internal Revenue take the following actions:

1. Outline a strategy that defines appropriate levels of telephone and correspondence service and wait time and lists specific steps to manage service based on an assessment of time frames, demand, capabilities, and resources.
2. Clearly define and document the roles and responsibilities of IRS offices administering the notice phase, such as in resolving tax debts.
3. Tailor appropriate and timely interventions with taxpayers who file balance due returns, by pilot testing risk-based approaches that could include
 - implementing the Advanced Consolidated Data Analytics plan, and
 - using more data driven methods to identify the most appropriate method for contacting a taxpayer.

Agency Comments and Our Evaluation

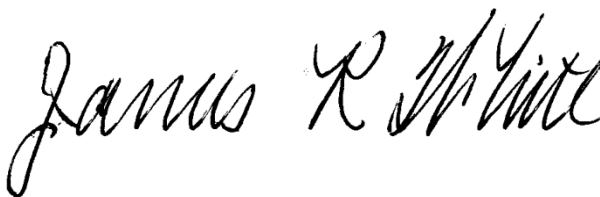
We provided a draft of this report to the Acting Commissioner of Internal Revenue. He provided written comments on a draft of the report, which are reprinted in appendix VII. IRS also suggested technical changes to the report, which we incorporated where appropriate.

IRS neither agreed nor disagreed with our first recommendation. IRS said it already has an objective of providing taxpayers with access to accurate services while managing demand and that this will be achieved by improving contact center efficiency, providing issue resolution alternatives to reduce demand, and equipping the workforce with additional tools. However, as we stated in the draft, in recent years, IRS has realized efficiency gains and provided alternative types of services, including more automated services. Notwithstanding these efforts, IRS has not kept up with the demand for service. Its service to taxpayers has continued to decline—the percentage of calls answered by a CSR has decreased and telephone wait times and the percentage of overage paper correspondence have increased. Because IRS's efforts to date have not reversed these declines in taxpayer service, we believe our recommendation to outline a strategy that defines appropriate levels of service and lists specific steps to manage service that would reverse recent trends remains valid. As the draft stated, a strategy to reverse the trends may require difficult tradeoffs.

Regarding our other two recommendations, IRS described its plans to implement them.

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to the Chairmen and Ranking Members of other Senate and House committees and subcommittees that have appropriation, authorization, and oversight responsibilities for IRS. We will also send copies to the Acting Commissioner of Internal Revenue, the Secretary of the Treasury, the Chairman of the IRS Oversight Board, and the Deputy Director for Management of the Office of Management and Budget. In addition, the report will be available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at (202) 512-9110 or whitej@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix VIII.

A handwritten signature in black ink that reads "James R. White". The signature is written in a cursive, flowing style.

James R. White
Director, Tax Issues
Strategic Issues

Appendix I: Objectives, Scope, and Methodology

This report

1. Assesses the Internal Revenue Service's (IRS) performance in processing returns, delivering refunds, and providing telephone service and online and face-to-face assistance in comparison to its 2012 goals and prior years' performance;
2. Describes what is known about taxpayers who filed returns and had a balance due for tax year 2010 but did not pay on or before the filing deadline, and assesses IRS's efforts to encourage timely payment; and
3. Summarizes the growth of Refund Anticipation Checks (RAC) in recent years and the reasons taxpayers may obtain them, the manner in which RAC and other fees are disclosed to taxpayers in commonly used online tax return preparation software packages, and key stakeholder views regarding the transparency of RACs and associated fees.

To assess IRS's performance in 2012 relative to its goals and prior years' performance we:

- Obtained and analyzed IRS documents and data, including performance and workload data, reports, testimonies, budget submissions, and internal studies of programs, and compared these to IRS's 2012 goals and prior years' performance to identify trends and anomalies.
- Reviewed various other criteria, including industry standards, federal requirements, and best practices to assess IRS's performance in key areas.
- Observed operations at IRS's Joint Operations Center (which manages telephone services) and listened to calls from taxpayers with telephone Customer Service Representatives (CSR). We also observed operations at a walk-in site located in Richmond, Virginia, including virtual service delivery.
- Interviewed IRS officials responsible for tax return processing, taxpayer services, and online services.
- Collected data from and interviewed key external stakeholders who frequently interact with IRS on key aspects of the filing season,

including representatives from major tax return preparation companies.

To describe what is known about taxpayers who filed returns with a balance due in tax year 2010 but did not pay on or before the filing deadline, and to assess IRS's efforts to encourage timely payment, we:

- Reviewed IRS's process and organizational structure for contacting taxpayers who submit returns and owe a balance to the IRS but do not pay before the deadline. This included obtaining documentation from IRS and interviewing IRS officials responsible for this process.
- Analyzed IRS data on the number of taxpayers who file returns with a balance due in tax year 2010, the most recent year for which complete data are available. We also analyzed IRS data on the dollar amounts associated with these balances and the manner in which the balances were resolved. For our analysis, the amount on the first notice sent to the taxpayer, including any interest and penalties, is the amount owed.
- Determined the amounts owed by the taxpayer through matching data on notices sent to taxpayers against data from returns entering IRS's collections process across databases using the Taxpayer Identification Number, to assure that our population included only those who received a notice for a self-assessed balance due.
- Analyzed the amount and distribution of returns for the types of notices received and whether and how they were resolved or entered later collection phases.
- Interviewed representatives from state tax administration agencies, other experts in tax administration, and private industry experts in collecting balances owed to identify criteria and best practices, such as the use of risk-based approaches and timely contact, for getting taxpayers to pay balances owed on time. An organization that represents state tax administration agencies provided contact information for states with advanced collection practices. Experts from those states directed us to knowledgeable private industry experts.

To summarize the growth of RACs in recent years and the reasons taxpayers may obtain them, the manner in which RAC and other fees are disclosed to taxpayers in commonly used online tax return preparation software packages, and key stakeholder views regarding the transparency of RACs and associated fees, we:

- Obtained data from IRS's return preparer office identifying the five most frequently used software packages by taxpayers who self-prepare returns. We analyzed information regarding RACs from the largest online tax preparation software companies to identify RAC fees and the manner in which they are presented to taxpayers preparing returns.
- Interviewed consumer protection experts, tax return preparation industry experts, and officials from cognizant government agencies, including the IRS and Consumer Financial Protection Bureau (CFPB). We identified these experts to interview based on our prior reports involving consumer protection and tax administration issues and in consultation with organizations representing tax return preparation and related financial services companies. We conducted these interviews to obtain a range of views on the need for RACs, return preparation fees more generally, and whether additional actions are needed to regulate RACs and other associated fees.

When data were available, we compared IRS's performance to its 2012 goals and performance from fiscal years 2007 through 2011. IRS officials noted that since 2008, varying degrees of tax law changes and other factors have affected the agency's performance. This report discusses numerous filing season and performance measures and data covering the quality, accessibility, and timeliness of IRS's services. Where estimates are presented, we used 90 percent confidence intervals and 10 percent levels of statistical significance, the same used by IRS. To the extent possible, we corroborated information from interviews with documentation and data, and where not possible, attributed the information to IRS officials. We reviewed IRS documentation, interviewed IRS officials about computer systems and data limitations, and compared those results to our standards of data reliability.¹ We determined that the data presented in this report are sufficiently reliable for our purposes.

We conducted this performance audit from February 2012 through December 2012 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 objectives. We

¹GAO, *Assessing the Reliability of Computer-Processed Data*, [GAO-09-680G](#) (Washington, D.C.: July 2009).

believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. To conduct our analysis of the cost and features of RACs, we used investigative techniques. We conducted our related investigative work in accordance with investigation standards prescribed by the Council of the Inspectors General on Integrity and Efficiency.

Appendix II: Balance Due Notice Process

IRS is required by law to send at least two notices to taxpayers who have a balance due on their taxes—the first notice (known as computer paragraph or CP-14) and a final notice (CP-504). IRS may also send up to two other discretionary notices (known as CP-501 and CP-503) between the first and final notices. IRS uses business rules embedded in the programming of its computer systems to determine the number and type of notices sent to a taxpayer. IRS officials told us that business rules impact the notice path for taxpayers who meet certain criteria, including taxpayers who repeatedly pay late and owe larger dollar amounts. However, these business rules are static and IRS does not otherwise tailor its contact methods to individual taxpayers during the notice phase. (See table 9).

Table 9: Description of Balance Due Notices for Individual Filers of Self-Assessed Balance Due Returns

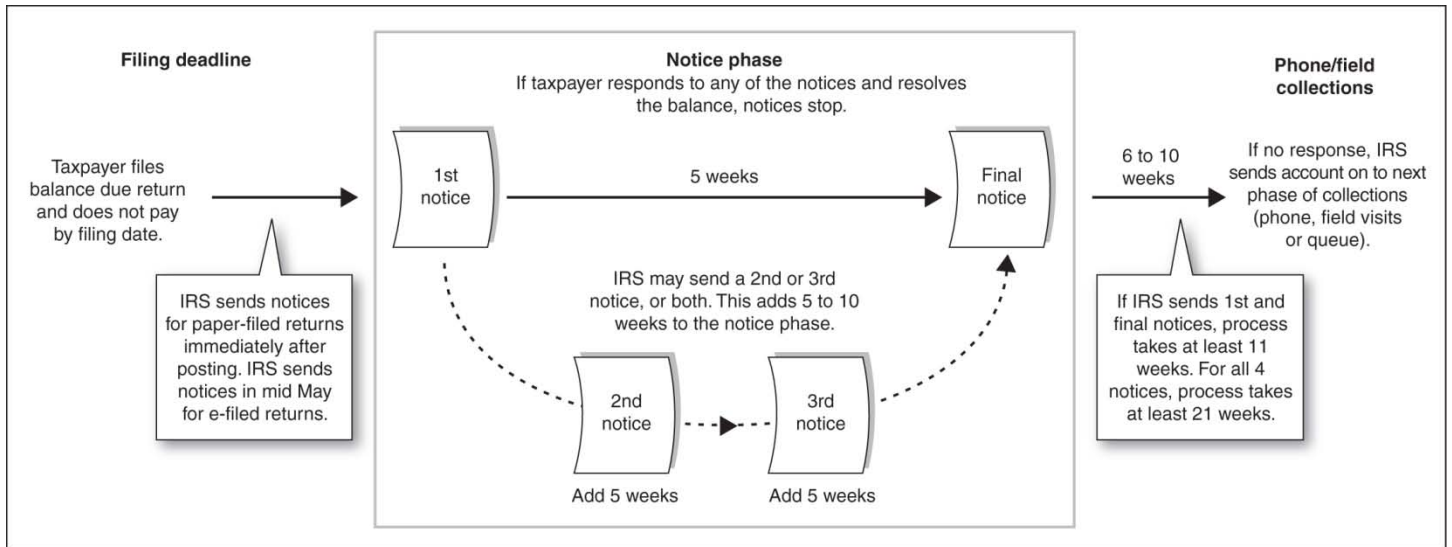
Name	CP	Explanation
First notice	CP-14	Issued as a first notice to inform a taxpayer of a balance due of \$5.00 or more, no math error. It tells taxpayers they have unpaid taxes, lists the amount due, the amount of penalties and interest assessed, and how to contact IRS to dispute the amount or to pay. This notice is required by law.
Second notice	CP-501	Second notice sent to taxpayer if no response after CP-14 notice. This notice is discretionary.
Third notice	CP-503	Third notice sent to taxpayer if no response to CP-14 or to second notice. This notice is discretionary.
Final notice	CP-504	Final notice issued to taxpayers informing them that IRS intends to issue a levy against the taxpayer's state tax refund because there is still a balance due on one or more of their tax accounts. Also, it informs the taxpayers that the IRS will begin searching for other assets on which to issue a levy and that the IRS may also file a federal tax lien. This notice is required by law.

Source: GAO analysis of TIGTA and IRS data.

Figure 2 shows that IRS's balance due notice process for a taxpayer receiving all four notices is at least 21 weeks. IRS allows 5 weeks between notices to give the taxpayer a chance to respond. If the taxpayer does not respond to the final notice within 6 to 10 weeks to make arrangements to settle the balance, then IRS sends the account to phone or field collections or the queue, where IRS holds some accounts to determine what actions to take later.

IRS does not typically contact taxpayers beyond the standard two to four notices during the notice phase.

Figure 2: Balance Due Notice Process for Individual Tax Return Filers



Source: GAO analysis of IRS information.

Appendix III: Use of IRS Website and Online Services

Taxpayers are increasingly using <http://www.IRS.gov> to download forms and publications and to check refund status. In 2012, IRS increased the number of Interactive Tax Assistant (ITA) topics from 11 to 19, which IRS officials said contributed to an 83 percent increase in ITA usage. Taxpayers' use of the Where's My Refund tool increased by almost 73 percent in 2012, which IRS officials said may be attributed to processing issues that affected when estimated refund dates were posted and programming errors which provided visitors with erroneous messages.

Table 10: Website Use from the 2008 through 2012 Filing Seasons

	2008	2009	2010	2011	2012	Percent change from 2011 to 2012 ^a
Total visits to IRS.gov (in millions) ^b	292	235	239	250	297	18.8
Taxpayer forms, publications, and instructions downloads (in millions)	136	137	157	166	259 ^c	56.0
Searches (in millions) ^d	125	263	277	312	290	-7.1
Volunteer site list (in thousands) ^e	n/a	n/a	48 ^f	152 ^g	152 ^h	0
Self-Service Tools						
Where's My Refund? (completion in millions)	38	53	64	73	126	72.6
Electronic Filing Pin Request (completion in millions)	n/a	n/a	5	10	12	20.0
Online Payment Agreement (completion in thousands)	19	34	43	26 ⁱ	64	146.2
Interactive Tax Assistance Tools (completion in thousands) ^j	n/a	n/a	42 ^k	212	388	83.0

Source: GAO analysis of IRS data.

Note: Data are from January 1 to July 31 for each year unless otherwise noted.

^aNumbers in the table are rounded, but percentage change was calculated using exact values. Therefore, in some cases, the percentage change is slightly different than it would be if it were calculated using the rounded values in the table.

^bA visit is a series of actions that begins when a visitor views their first page from the server, and ends when the visitor leaves the site.

^cData is for January 1 to June 30, 2012.

^dPage views include both successful search results and search results not found.

^e2010's listing was on 1 page, with an index at the top. 2011's listing was split into 52 pages; one for each state, the District of Columbia, and Puerto Rico. For 2012, IRS created a volunteer site locator tool for searches using zip codes.

^fPage views data are for February 12 through July 31, 2010.

^gData are from January 1 through June 30, 2011.

^hData represents the number of visits to the disclaimer page where users leave IRS.gov to use the volunteer site locator application, hosted by the Department of Treasury.

Appendix III: Use of IRS Website and Online Services

ⁱA programming error led to a decrease in the number of completed agreements.

^jIRS introduced the interactive tax assistance tools in March 2010 and added more tools in 2011 and 2012. As a result, the time frames and available services are not comparable.

^kData are from March 7 through July 31, 2010.

Appendix IV: Visits to Taxpayer Assistance Center and Volunteer Income Tax Assistance Sites

The total number of contacts at Taxpayer Assistance Centers (TAC) staffed by IRS employees had decreased in 2012 as compared to 2010 and 2011. The total number of returns prepared at Volunteer Income Tax Assistance (VITA) sites for 2012 increased slightly compared to 2011, while 97 percent of the returns prepared at volunteer sites were electronically-filed.

Table 11: Services Performed at IRS TAC and VITA Sites, 2010 through 2012 Filing Seasons

	2010	2011	2012	Percent change from 2011 to 2012
TAC				
Total contacts	2,777,478	2,847,221	2,772,044	-2.6
Return preparation	222,624	201,413	148,075	-26.5
Tax law questions	177,002	153,398	128,746	-16.1
Account notices	1,217,383	1,327,406	1,446,413	9.0
Forms	440,417	457,839	378,051	-17.4
Other ^a	720,052	707,165	670,759	-5.1
VITA				
Return preparation	2,951,952	3,077,687	3,149,197	2.3
Percent of returns e-filed	95	96	97	n/a

Legend: n/a = not applicable.

Source: GAO analysis of IRS data.

Notes: Data for each calendar year are for January 1 through April 30.

^aOther contacts include responding to correspondence, scheduling appointments, and providing self-assistance services, which do not fall into the defined categories.

Appendix V: Description of Telephone Calls Answered by IRS

IRS receives millions of calls each year from taxpayers. As table 12 shows, while an increasingly large number of calls are answered through automation, the number of calls answered by customer service representatives (CSRs) has declined. Abandoned calls are those calls where the taxpayer hangs-up before receiving assistance.

Table 12: Calls to IRS by Call Type, 2007 through 2012 Filing Seasons

In millions							Percent change from 2011 to 2012 ^b
	2007	2008 ^a	2009	2010	2011	2012	
Automated calls answered	20.8	43.0	25.3	31.6	36.7	50.1	36
CSR calls answered	21.5	27.0	25.7	24.1	22.6	19.4	-14
Abandoned calls	13.3	34.4	21.4	20.5	22.7	27.3	20
Busies and IRS disconnects	1.0	13.6	5.3	1.2	1.1	1.6	52
Total calls received	56.6	118.0	77.6	77.4	83.1	98.4	18

Source: GAO analysis of IRS data.

Note: Data are from January 1 through June 30 for all years.

^aAccording to IRS officials, IRS received an unprecedented number of calls in 2008 primarily related to economic stimulus package payments.

^bThe numbers in the table are rounded, but the percent change was calculated using exact values. Therefore, in some cases, the percent change is slightly different than it would be if it were calculated using the rounded values in the table.

Appendix VI: Fees for Refund Anticipation Checks

As part of our review of Refund Anticipation Checks (RAC), we observed how RACs and the fees associated with them, including fees for prepaid debit cards, are presented to taxpayers. Table 13 summarizes our results.

Table 13: Comparisons of Fees and Refund Anticipation Check Options for Five Software Packages

	Software Package 1	Software Package 2	Software Package 3	Software package 4	Software package 5
Tax Return and RAC Fees					
Tax preparation fee	\$74.90	\$74.90	\$17.95	\$12.95	\$17.90
RAC fee	29.95	32.95	16.95	n/a	29.95
Pre-paid Card Fees					
ATM cash withdrawal one time	2.50	2.50	1.95	n/a	n/a
Over the counter withdrawal	2.50	25.00	5.00	n/a	n/a
ATM balance inquiry	0.50	1.00	0.50	n/a	n/a
Monthly maintenance fee	5.95 ^a	2.50 ^b	2.50 ^c	n/a	n/a

Legend: n/a = not applicable.

Source: GAO analysis.

^aThe maintenance fee is waived when available balance is \$50 or greater on the last day of billing cycle.

^bThis is a monthly inactivity fee (charged after 3 months consecutive with no activity).

^cThe maintenance fee is charged monthly, therefore the \$2.50 amount could increase depending on the length of card's activation.

Appendix VII: Comments from the Department of the Treasury



DEPUTY COMMISSIONER

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

December 13, 2012

Mr. James R. White
Director, Tax Issues
U.S. Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

Dear Mr. White:

I have reviewed your draft report entitled *2012 TAX FILING: IRS Faces Challenges Providing Service to Taxpayers and Could Collect Balances Due More Effectively*, and appreciate your acknowledgment of our efficiency gains in processing returns and providing taxpayer service in recent years. We delivered another successful filing season in 2012. The Modernized e-File (MeF) platform met all performance expectations. Although there were some issues with subordinate systems handling MeF return data and fraud detection processes early in the season, we took immediate steps to identify and resolve the problems. All tax returns were properly processed and the majority of taxpayers received refunds within 10 to 21 days. We expect to use the MeF as the sole platform for receiving electronic returns in 2013; however, as a precautionary measure, the legacy e-file system will remain available as a backup measure.

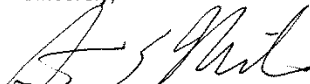
While significant gains in taxpayer service and collection of taxes have been achieved, more can be done in some areas noted in your report. For example, we are pursuing implementation of Advanced Consolidated Decision Analytics (ACDA) which will apply a risk-based approach to balance due returns, expediting taxpayer contact after the first notice. Successful implementation of ACDA will assist the IRS in collecting taxes due more efficiently and effectively. To address concerns about designated roles and responsibilities in the collection notice process, we will establish a cross functional team to review this area and document their determinations.

Regarding your first recommendation, the IRS is already using customer and stakeholder expectations, external factors, and capability analysis to segment recommendations into core improvement themes. The objective is to provide customers with easy access to accurate, user friendly tax law and account services, while proactively managing the increase in customer demand. This will be achieved by improving contact center efficiency, providing issue resolution alternatives to reduce customer demand, and equipping the workforce with the tools to be productive.

2

Responses to your specific recommendations are enclosed. If you have any questions, please contact Robin L. Canady, Director, Strategy and Finance, Wage and Investment Division, at (404) 338-8801.

Sincerely,



Steven T. Miller
Deputy Commissioner for
Services and Enforcement

Enclosure

Enclosure

We recommend that the Acting Commissioner of Internal Revenue take the following actions:

Recommendation

Outline a strategy that defines appropriate levels of telephone and correspondence service and wait time and lists specific steps to manage service based on an assessment of time frames, demand, capabilities, and resources.

Comment

The IRS is using customer and stakeholder expectations, external factors, and capability analysis to segment recommendations into core improvement themes. The objective is to provide customers with easy access to accurate, user friendly tax law and account services, while proactively managing the increase in customer demand. This will be achieved by improving contact center efficiency, providing issue resolution alternatives to reduce customer demand, and equipping the workforce with the tools to be productive.

It would be difficult to define a customer service telephone standard because, in practice, telephone plans are developed after consideration of many factors, including: historical demand adjusted for known anomalies; the types and anticipated lengths of calls we expect to receive; assumptions concerning upcoming events, such as known or pending legislation or trends in customer behavior; and the availability of existing or new automated and other alternative services. These plans are then matched with available or anticipated resources to determine the level of service that can be provided to generate the telephone program goals. Goals are finalized only after sharing projections with oversight functions including, the IRS Oversight Board, the Office of Management and Budget, and Treasury, and after consideration of the President's budget request by the House and Senate Appropriations Committees and congressional enactment of the Treasury budget.

Recommendation

Clearly define and document the roles and responsibilities of IRS offices administering the notice phase, such as in resolving tax debts.

Comment

A cross functional team will be formed to specifically define the roles and responsibilities of each operating division within the collection notice process.

Recommendation

Tailor appropriate and timely interventions with taxpayers who file balance due returns, by pilot testing risk-based approaches that could include implementing the Advanced Consolidated Data Analytics plan and using more data driven methods to identify the most appropriate method for contacting a taxpayer.

2

Comment

The Advanced Consolidated Decision Analytics (ACDA) proposal has recently been finalized and is currently under consideration for funding and prioritization. In the event full funding is not available, we will evaluate the effectiveness of incremental development and deployment of ACDA.

Appendix VIII: GAO Contact and Staff Acknowledgments

GAO Contact

James R. White, (202) 512-9110, whitej@gao.gov

Staff Acknowledgments

In addition to the individual named above, Joanna Stamatiades, Assistant Director; LaKeshia Allen Horner; Andrew Ching; David Fox; Tom Gilbert; Ron Jones; Inna Livits; Kirsten Lauber; Karen O'Connor; Albert Sim; Sabrina Streagle; Weifei Zheng; and John Zombro made key contributions to this report.

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