



United States Government Accountability Office
Washington, DC 20548

May 3, 2013

The Honorable Frank Lautenberg
Chairman
The Honorable Mike Johanns
Ranking Member
Subcommittee on Financial Services and General Government
Committee on Appropriations
United States Senate

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

Internal Revenue Service: Preliminary Observations on the Fiscal Year 2014 Budget Request

This letter transmits briefing slides based on our work to date in response to your requests for a preliminary review of the fiscal year 2014 budget request for the Internal Revenue Service (IRS). See appendix I and appendix II for the briefing slides that include the information used to brief your staff in April 2013, and were subsequently updated.

Our briefing objectives were to (1) describe the fiscal year 2013 budget for IRS and potential reductions resulting from sequestration; (2) describe IRS's budget data and trends from fiscal years 2010 through 2014 and the fiscal year 2014 new program initiatives, return on investment (ROI) information, and major information technology (IT) investments; (3) list any analyses we have done related to legislative proposals highlighted in the congressional budget justification; and (4) identify our open matters for Congress and recommendations to IRS with a potential financial benefit.

To conduct this work, we summarized the President's budgets and IRS congressional budget justifications from fiscal years 2010 through 2014, reviewed Office of Management and Budget guidance on sequestration, reviewed revenue estimates from the Department of Treasury's Green Book, and interviewed IRS officials in the offices of the Chief Financial Officer and Corporate Budget. We

interviewed IRS officials and determined that the data presented in this briefing were sufficiently reliable for our purposes.

We conducted this performance audit from April to May 2013 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.

In summary,

- The fiscal year 2013 annualized continuing resolution rate shown in the fiscal year 2014 budget (\$11.9 billion) is not the enacted funding level, and the actual amount is \$689 million lower.
- For fiscal year 2014, the President's Budget requests an increase for IRS of 9 percent (\$1,044 million) in discretionary funding over the fiscal year 2012 appropriation and an increase of 8 percent (6,732 full-time equivalents) in staffing over fiscal year 2012 actual levels. In addition, the funding request includes:
 - Twelve new program initiatives related to enforcement activities and 6 new program initiatives related to taxpayer service, infrastructure, or other activities.
 - New information on actual return on investment for enforcement activities, and expanded information on IT investments, such as lifecycle costs, projected useful life of the current asset, and anticipated benefits.
- The request includes 33 legislative proposals, including 12 related to our prior work.
- As of March 2013, 39 of our products contained 10 matters for congressional consideration and 88 recommendations to IRS with a potential financial benefit that have not been addressed. Since March 2012, IRS has implemented 24 recommendations with a potential financial benefit. See appendix III for a complete listing of all 39 products.

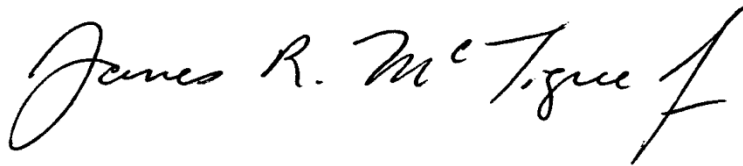
Agency Comments

On May 1, 2013, IRS provided technical comments on our findings, which we have incorporated where appropriate.

As arranged with your office, unless you publically announce the contents of this report earlier, we plan no further distribution until 5 days after the date of this report. At that time, we will send copies of this report to other Chairmen and Ranking Members of Senate and House committees and subcommittees that have appropriation and oversight responsibilities for IRS. We also will be sending copies to the Acting Commissioner of Internal Revenue, the Secretary of the Treasury, and the Chairman of the IRS Oversight Board. Copies also are available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staffs have any questions about this report, please contact us at (202) 512-9110 or mctiguej@gao.gov. Contact points for our offices of Congressional Relations and Public Affairs are on the last page of this report. GAO staff members who made major contributions to this report are listed in appendix IV.

Sincerely yours,

A handwritten signature in black ink that reads "James R. McTigue, Jr." followed by a stylized flourish.

James R. McTigue, Jr.
Director, Tax Issues
Strategic Issues



Internal Revenue Service: Preliminary Observations on the Fiscal Year 2014 Budget Request

**Prepared for the Subcommittee on Oversight, Committee
on Ways and Means, U.S. House of Representatives (April
23, 2013) and the Subcommittee on Financial Services and
General Government, Committee on Appropriations, U.S.
Senate (April 25, 2013)**

Updated May 3, 2013



Briefing Objectives

You requested preliminary information on the fiscal year 2014 budget for IRS. This briefing:

- describes the fiscal year 2013 budget for IRS and potential reductions resulting from sequestration;
- describes IRS's budget data and trends from fiscal years 2010 through 2014, and the fiscal year 2014 new program initiatives, return on investment (ROI) information, and major information technology (IT) investments;
- lists any analyses we have done related to legislative proposals highlighted in the congressional budget justification; and
- identifies our open matters for Congress and recommendations to IRS with a potential financial benefit.

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Scope and Methodology

To conduct this work, for each objective, we:

- summarized the President's budgets and IRS congressional justifications from fiscal years 2010 through 2014, reviewed Office of Management and Budget (OMB) guidance on sequestration, reviewed revenue estimates from the Department of Treasury's Green Book, and interviewed IRS officials in the offices of the Chief Financial Officer and Corporate Budget. We interviewed IRS officials and determined that the data presented in this briefing were sufficiently reliable for our purposes.

We conducted this performance audit from April to May 2013 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.



Results in Brief

In summary,

- The fiscal year 2013 annualized continuing resolution rate shown in the fiscal year 2014 budget (\$11.9 billion) is not the enacted funding level, and the actual amount is \$689 million lower.
- For fiscal year 2014, the President's Budget requests an increase for IRS of 9 percent (\$1,044 million) in discretionary funding over the fiscal year 2012 appropriation and an increase of 8 percent (6,732 full-time equivalents (FTEs)) in staffing over fiscal year 2012 actual levels. In addition, the funding request includes:
 - Twelve new program initiatives related to enforcement activities and 6 new program initiatives related to taxpayer service, infrastructure, or other activities.
 - New information on actual return on investment for enforcement activities, and expanded information on information technology (IT) investments, such as lifecycle costs, projected useful life of the current asset, and anticipated benefits.
- The request includes 33 legislative proposals, including 12 related to our prior work.
- As of March 2013, 39 of our products contained 10 matters for congressional consideration and 88 recommendations to IRS with a potential financial benefit that have not been addressed. Since March 2012, IRS has implemented 24 recommendations with a potential financial benefit.

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Fiscal Year 2013 and Sequestration

Funding Levels Down Again, while Demands on Resources Increase with Implementation of Four New Laws

- The fiscal year 2013 annualized continuing resolution rate shown in the fiscal year 2014 budget (\$11.9 billion) is not the enacted funding level, and the actual amount is \$689 million lower due to sequestration (\$594 million), the final continuing resolution adjustment (\$71 million), and a 0.2 percent rescission (\$24 million).
 - According to IRS budget officials, IRS adjusted its fiscal year 2013 operating plans to reflect these reductions, which are described in the operating plan for fiscal year 2013, released on April 30, 2013.
 - As a result, comparisons in the congressional justification are based on fiscal year 2012 instead of fiscal year 2013.
- The fiscal year 2013 decrease follows a fiscal year 2012 cut of \$305 million.
- IRS has been implementing four new laws, relating to (1) the Patient Protection and Affordable Care Act (PPACA),¹ (2) merchant card transaction,² (3) basis reporting,³ and (4) the Foreign Account Tax Compliance Act (FATCA),⁴ which have resulted in additional demands for its existing resources.

¹PPACA, Pub. L. No. 111-148, 124 Stat. 119 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act (HCERA), Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010). All references to PPACA include amendments by HCERA.

²Housing Assistance Tax Act of 2008, Pub. L. No. 110-289, div. C, § 3091, 122 Stat. 2654, 2908-2911 (July 30, 2008).

³Energy Improvement and Extension Act of 2008, Pub. L. No. 110-343, div. B, § 403, 122 Stat. 3765, 3854-3860 (Oct. 3, 2008).

⁴Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, Title V, 124 Stat. 71, 97-117 (Mar. 18, 2010).

Fiscal Year 2013 and Sequestration

Sequestration Reduces Fiscal Year 2013 Budget Levels for IRS

According to the Acting IRS Commissioner, as a result of sequestration, IRS may plan to

- continue to operate under a hiring freeze;
- reduce funding for grants and other expenditures;
- cut costs in areas such as travel, training, facilities, and supplies;
- review contract spending to ensure only the most critical and mandatory requirements are fully funded; and
- furlough all staff for a total of 5 to 7 days after the filing season ends.⁵

Table 1: IRS Funding Subject to Sequestration and Subsequent Reductions to Discretionary IRS Appropriation Accounts for Fiscal Year 2013^a

Discretionary appropriation accounts	Total sequestrable budget authority amount (in millions)	Sequester percentage	Total sequester amount (in millions)
Enforcement	\$5,348	5%	\$267
Operations support	3,983	5	199
Taxpayer services	2,271	5	113
Business Systems Modernization (BSM)	332	5	17
Total discretionary	\$11,934^b	--	\$594

Source: GAO analysis of OMB and IRS data.

Note: Numbers may not add due to rounding.

^aDiscretionary appropriations are budgetary resources that are provided in appropriations acts, and do not fund mandatory programs. Sequestration also requires reductions of 5.1 percent to other nonexempt nondefense mandatory programs. IRS has eight appropriation accounts, such as the IRS Miscellaneous Retained Fees account, that fall into this category. The total sequester amount for those appropriation accounts is \$232 million.

^bThis amount includes reimbursables (\$46 million) and the final continuing resolution adjustment (\$71 million).

⁵The Acting IRS Commissioner announced 5 furlough days, including May 24, 2013, June 14, 2013, July 5, 2013, July 22, 2013, and August 30, 2013, and that two other furlough days may be scheduled in August and September 2013.

Fiscal Year 2013 and Sequestration

Cost Saving Actions Taken in Fiscal Year 2012 Resulted in a Lower Base Budget for Fiscal Year 2013

- IRS realized \$426 million in savings in fiscal year 2012.
 - Savings and efficiencies resulted from, for example:
 - Reducing FTEs by 3.4 percent (\$206 million) through targeted buyouts, attrition, and hiring freezes;
 - transferring lock box fees to taxpayers as part of their installment agreements;⁶
 - reducing IT infrastructure costs (e.g., renegotiating contracts);
 - reducing printing and postage (e.g., stopped weekly mailings of Publication 15, *Employer's Tax Guide*); and
 - reducing travel and training.
 - The savings were \$236 million more than IRS projected for fiscal year 2012.
 - According to IRS budget officials, some savings from fiscal year 2012 are being used in fiscal year 2013 to cover implementation of legislative mandates and sequestration.

⁶A lockbox is a post office box established by a financial institution to receive payments made to the IRS.

Fiscal Year 2014 Budget Data and Trends

Summary of Key Budget and FTE Data

- The fiscal year 2014 budget request for IRS is \$12.9 billion and 96,218 FTEs.
 - The budget shows a:
 - 9 percent increase (\$1,044 million) over the fiscal year 2012 appropriation.
 - 8 percent increase (6,732 FTEs) in staffing over fiscal year 2012 actual levels.
 - In fiscal year 2014, IRS expects to gain base budget savings and efficiencies of \$217 million from cost reduction strategies, such as hiring restrictions, space consolidations, and savings resulting from more electronically filed tax returns.⁷
 - The requested increases include:
 - Twelve new enforcement initiatives, such as a request for \$101 million to improve identification and prevention of refund fraud and identity theft.
 - Six taxpayer service, infrastructure, and other initiatives, such as \$306 million to implement IT changes to deliver tax credits and other requirements for PPACA.

⁷The savings and efficiencies of \$217 million include a net reinvestment of \$37.5 million.

Fiscal Year 2014 Budget Data and Trends

Dollars by Appropriation Account, Fiscal Years 2010 through 2014

Table 2: IRS Fiscal Years 2010 through 2014 Budget by Appropriation Account (Dollars in Millions)

Appropriation account	Fiscal year 2010 enacted	Fiscal year 2011 enacted	Fiscal year 2012 enacted	Fiscal year 2013 annualized continuing resolution ^a	Fiscal year 2014 requested	Dollar change fiscal year 2012 enacted compared to fiscal year 2014 requested	Percent change fiscal year 2012 enacted compared to fiscal year 2014 requested
Enforcement	\$5,504	\$5,493	\$5,299	\$5,331	\$5,667	\$367	7%
Operations support	4,084	4,057	3,947	3,971	4,481	533	14
Taxpayer services	2,279	2,293	2,240	2,254	2,413	173	8
BSM	264	263	330	332	301	-29	-9
Health Insurance Tax Credit Administration (HITCA) ^b	16	15	-- ^b	-- ^b	-- ^b	n/a	n/a
Subtotal	12,146	12,122	11,817	11,888	12,861	1,044	9
Other resources, such as user fees	539	655	695	905	497	-198	-29
Total funding available for obligation	\$12,686	\$12,777	\$12,512	\$12,793	\$13,358	\$846	7%

Legend: n/a = not applicable.

Source: Fiscal year 2012, 2013, and 2014 congressional budget justifications for IRS.

Note: Dollars are nominal and not adjusted for inflation, and numbers may not add due to rounding.

^aA full-year 2013 appropriation for this account was not enacted at the time the budget was prepared; therefore, the budget assumes this account is operating under the Continuing Appropriations Resolution, 2013 (P.L. 112-175). The amounts included for 2013 reflect the annualized level provided by the continuing resolution and do not include reductions due to sequestration.

^bIn fiscal year 2012, administrative resources for HITCA were moved to the taxpayer services appropriation under the Consolidated Appropriations Act, 2012 (Pub. L. No. 112-74).

Fiscal Year 2014 Budget Data and Trends

Staffing by Appropriation Account, Fiscal Years 2010 through 2014

Table 3: Fiscal Years 2010 through 2014 Full-Time Equivalents (FTEs) by Appropriation Account

Appropriation account	Fiscal year 2010 actual	Fiscal year 2011 actual	Fiscal year 2012 actual	Fiscal year 2013 annualized continuing resolution ^a	Fiscal year 2014 requested	FTE change fiscal year 2012 actual compared to fiscal year 2014 requested	Percent change fiscal year 2012 actual compared to fiscal year 2014 requested
Enforcement	50,400	49,920	47,189	46,702	49,987	2,798	6%
Operations support	12,262	12,103	11,499	12,240	13,143	1,644	14%
Taxpayer services	31,607	31,574	30,236	30,402	32,575	2,339	8%
BSM	337	309	562	513	513	-49	-9%
HITCA ^b	12	0	0	0	0	n/a	n/a
Subtotal	94,618	93,906	89,486	89,857	96,218	6,732	8%
Other resources, such as user fees	752	1,003	2,185	1,698	1,093	-1,092	-50%
Total FTEs	95,370	94,909	91,671	91,555	97,311	5,640	6%

Legend: n/a = not applicable.

Source: Fiscal year 2012, 2013 and 2014 congressional budget justifications for IRS.

^aA full-year 2013 appropriation for this account was not enacted at the time the budget was prepared; therefore, the budget assumes this account is operating under the Continuing Appropriations Resolution, 2013 (P.L. 112-175). The amounts included for 2013 reflect the annualized level provided by the continuing resolution and do not include reductions due to sequestration.

^bIn fiscal year 2012, administrative resources for HITCA were moved to the taxpayer services appropriation under the Consolidated Appropriations Act, 2012 (Pub. L. No. 112-74).

Fiscal Year 2014 Budget Data and Trends

Unobligated Balances by Appropriation Account Fiscal Years 2010 through 2014

- Funds showed an expected decline in unobligated balances from fiscal years 2012 to 2014.
- IRS's unobligated balances are primarily resulting from no-year, multi-year, and carryover funding and transfers from IRS's Miscellaneous Retained Fee Fund (e.g., user fees) to its discretionary appropriation accounts.
- Fiscal years 2013 and 2014 unobligated balances represent estimates of multi-year and user fee balances for future years.

Table 4: Fiscal Years 2010 to 2014 Unobligated Balances for IRS Appropriation Accounts (Dollars in Millions)

Appropriation account	Fiscal year 2010	Fiscal year 2011	Fiscal year 2012	Fiscal year 2013 estimated	Fiscal year 2014 estimated
Enforcement	\$11	\$16	\$30	\$43	\$18
Operations support	97	142	178	291	22
Taxpayer services	150	148	192	205	158
BSM	119	179	119	97	104
Total	\$377	\$485	\$519	\$636	\$302

Source: GAO analysis of IRS data.

Fiscal Year 2014 Budget Data and Trends

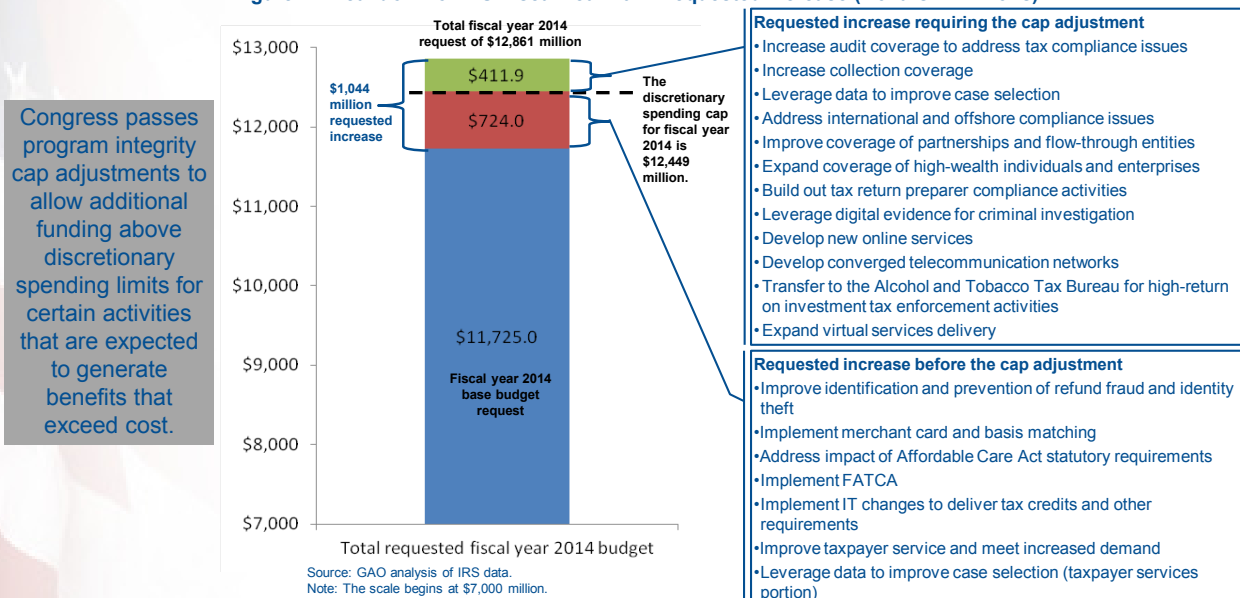
\$217 Million in Net Savings and Efficiencies Projected for Fiscal Year 2014

- The fiscal year 2014 budget request for IRS continues efforts to seek savings through:
 - Agency-wide strategies:
 - Hiring restrictions (e.g., not replacing attrited staff) (\$78 million)
 - Reducing IT infrastructure (\$58 million)
 - Reducing costs and streamlining operations in the human capital function (\$8 million)
 - Consolidating and closing offices (\$39 million (net))
 - Space optimization (e.g., close, consolidate, or reduce 123 of 648 offices) (\$77 million)
 - One-time reinvestment to implement space optimization, which requires building and consolidating space and relocating employees (\$38 million)
 - Program strategies:
 - Savings related to increases in electronically filed returns (\$5 million)
 - Reduction in funding to BSM (\$30 million)

Fiscal Year 2014 Budget Data and Trends

The Administration Requested a Program Integrity Cap Adjustment of \$412 Million for IRS

Figure 1: Breakdown of IRS Fiscal Year 2014 Requested Increase (Dollars in Millions)



New Initiatives and Return on Investment

IRS Proposed 12 Enforcement Initiatives, Totaling \$605 Million

Table 5: Funding Requested for Enforcement Initiatives (Dollars in Millions)

Description of budget adjustments	Fiscal year 2014 funding requested, by appropriation account				Total ^a	Projected ROI for fiscal year 2016 ^b
	Taxpayer services account	Enforcement account	Operations support account	BSM account		
New enforcement initiatives	\$38	\$365	\$202	-	\$605	n/a
▲ Increase audit coverage to address tax compliance issues	-	71	39	-	111	3.2
Improve identification and prevention of refund fraud and identity theft	19	48	33	-	101	14.4
▲ Increase collection coverage	-	36	24	-	60	9.3
▲ Leverage data to improve case selection ^c	10	4	37	-	52	1.5
Implement merchant card and basis matching	8	30	12	-	50	8.5
▲ Address international and offshore compliance issues	-	43	6	-	49	4.5
▲ Improve coverage of partnerships and flow-through entities	-	39	6	-	45	7.7
Address impact of Patient Protection and Affordable Care Act statutory requirements	1	26	17	-	44	1.9
Implement Foreign Account Tax Compliance Act	-	20	16	-	35	3.7
▲ Expand coverage of high-wealth individuals and enterprises	-	29	5	-	34	13.4
▲ Build out tax return preparer compliance activities	-	16	2	-	18	... ^d
▲ Leverage digital evidence for criminal investigation	-	1	4	-	5	... ^d
New nonenforcement initiatives	130	8	392	-	531	n/a
Inflation adjustment and pay raises	22	51	52	1	126	n/a
Savings and efficiencies, net reinvestment	-18	-57	-113	-30	-217	n/a
Total appropriations adjustment	\$173	\$367	\$533	\$-29	\$1,044^a	n/a

Legend: ▲ = requested increase would require a program integrity cap adjustment; n/a = not applicable

Source: Fiscal year 2014 congressional budget justification for IRS.

Notes: Numbers may not add due to rounding.

^aThe total does not include the final continuing resolution adjustment of \$71 million.

^bAccording to IRS, new fiscal year 2014 hires will reach full potential in fiscal year 2016. See appendix II for more information on ROI.

^cThe taxpayer services portion of this initiative (\$10 million) would not require a program integrity cap adjustment.

^dIRS does not have assurance that the Build Out Tax Return Preparer Compliance and Leverage Digital Evidence for Criminal Investigations initiatives will produce direct revenue.

New Initiatives and Return on Investment

IRS Proposed Six Taxpayer Service, Infrastructure, and Other Initiatives, Totaling \$531 Million

Table 6: Funding Requested for Taxpayer Service, Infrastructure, and Other Initiatives (Dollars in Millions)

Description of budget adjustments	Fiscal year 2014 funding requested, by appropriation account				Total ^a
	Taxpayer services account	Enforcement account	Operations support account	BSM account	
New enforcement initiatives	\$38	\$365	\$202	-	\$605
New nonenforcement initiatives	130	8	392	-	531
Implement IT changes to deliver tax credits and other requirements	-	-	306	-	306
Improve taxpayer service and meet increased demand	130	3	44	-	177
▲ Develop new online services	-	-	24	-	24
▲ Develop converged telecommunication networks	-	-	15	-	15
▲ Transfer to the Alcohol and Tobacco Tax and Trade Bureau for high return-on-investment tax enforcement activities	-	5	-	-	5
▲ Expand virtual services delivery	-	-	4	-	4
Inflation adjustment and pay raises	22	51	52	1	126
Savings and efficiencies, net reinvestment	-18	-57	-113	-30	-217
Total appropriations adjustment	\$173	\$367	\$533	\$-29	\$1,044^a

Legend: ▲ = requested increase would require a program integrity cap adjustment.

Source: Fiscal year 2014 congressional budget justification for IRS.

Notes: Numbers may not add due to rounding.

IRS does not calculate ROI for nonenforcement initiatives.

^aThe total does not include the final continuing resolution adjustment of \$71 million.

New Initiatives and Return on Investment

\$440 Million and 1,954 FTEs Proposed to Implement PPACA in Fiscal Year 2014

Table 7: Fiscal Year 2014 PPACA Budget Request (Dollars in Millions)

Initiatives	Taxpayer services		Enforcement		Operations support		Total	
	Dollars	FTEs	Dollars	FTEs	Dollars	FTEs	Dollars	FTEs
Improve taxpayer service and meet increased demand (PPACA portion of initiative)	\$70	908	\$3	32	\$16	9	\$90	949
Address impact of PPACA statutory requirements	1	8	26	223	17	52	44	283
Implement IT changes to deliver tax credits and other requirements					306	722	306	722
Total fiscal year 2014 PPACA budget request	\$71	916	\$29	255	\$339	783	\$440	1,954

Source: Fiscal year 2014 congressional budget justification for IRS.
Note: Numbers may not add due to rounding.

- In fiscal year 2014, PPACA funding is included in three of IRS's new funding initiatives.
- In fiscal year 2013, IRS requested \$360 million to implement PPACA, but did not receive it.
- In fiscal years 2010 through 2012, IRS received a total of \$488 million and 1,272 FTEs to implement PPACA from the Department of Health and Human Services' Health Insurance Reform Implementation Fund (HIRIF).

Table 8: IRS HIRIF Funding for PPACA, Fiscal Years 2010 Through 2012 (Dollars in Millions)

Fiscal year	FY 2010	FY 2011	FY 2012	Total
Dollars (in millions)	\$21	\$168	\$299	\$488
FTEs	31	577	664	1,272

Source: Fiscal year 2014 congressional budget justification for IRS.
Note: Numbers may not add due to rounding.

New Initiatives and Return on Investment

IRS Reported Actual Return on Investment Data for Three Enforcement Programs for the First Time

Table 9: Actual ROI for Major IRS Enforcement Programs (Dollars in Millions)

Enforcement program	Fiscal year 2009				Fiscal year 2010				Fiscal year 2011				Fiscal year 2012		
	Cost	Revenue	ROI		Cost	Revenue	ROI		Cost	Revenue	ROI		Cost	Revenue	ROI
Examination	\$3,965	\$17,446	4.4		\$4,371	\$23,563	5.4		4,333	\$18,924	4.4		\$4,232	\$14,476	3.4
Collection	1,880	26,871	14.3		1,948	29,105	14.9		1,939	31,060	16.0		1,742	30,442	17.5
Automated Underreporter	223	4,569	20.5		262	4,924	18.8		270	5,245	19.4		267	5,269	19.7
IRS total	\$6,068	\$48,886	8.1		\$6,581	\$57,592	8.8		\$6,543	\$55,229	8.4		\$6,242	\$50,187	8.0

Source: Fiscal year 2014 congressional budget justification for IRS.

Note: Numbers may not add due to rounding.

- IRS made significant progress by calculating average direct actual ROI for the Examination, Collection, and Automated Underreporter programs, as shown in table 9.
- IRS is not yet able to calculate ROI data that measure the marginal revenue produced by additional spending, such as program initiatives, or that include indirect effects of enforcement on voluntary compliance.
- IRS stated that developing actual ROI at the program initiative (marginal) level is challenging. As we reported in December 2012, developing a methodology and using data to improve the allocation of IRS enforcement resources could result in a significant increase in direct revenue.⁸

⁸See GAO, *Tax Gap: IRS Could Significantly Increase Revenues by Better Targeting Enforcement Resources*, GAO-13-151 (Washington, D.C.: Dec. 5, 2012).

Fiscal Year 2014 IT Investments

\$2.6 Billion Requested for IT in Fiscal Year 2014 and IRS Expanded Information on IT Investments

- Of the \$2.6 billion requested,
 - \$1.5 billion is planned to fund 18 major IT investments.⁹ The funding for major IT investments comes from multiple sources:
 - \$1.2 billion from the operations support appropriation account,
 - \$260 million from the BSM appropriation account,
 - \$40 million from operations support user fees, and
 - \$12 million from other funding sources.¹⁰
 - \$1.1 billion is planned to fund nonmajor IT investments.
- IRS included expanded information on its IT investments in the fiscal year 2014 budget request, including lifecycle costs, projected useful life of the current asset, anticipated benefits and how performance will be measured.

⁹According to IRS, major investments are defined by Treasury as those that cost \$10 million in either the current year or budget year, or \$50 million over the 5-year period extending from the prior year through budget year +2. Last year, IRS reported 20 major IT systems. The Current Customer Account Data Engine (Current CADE) and Affordable Care Act (ACA), the IT investment supporting IRS's implementation of the PPACA requirements) are no longer on the list. Current CADE was terminated in December 2011. According to IRS, ACA will now be reported as separate nonmajor investments instead of one major investment.

¹⁰Other funding sources include, for example, IRS Operations Support Reimbursables.

Fiscal Year 2014 IT Investments

Major IT Investments' Planned Cost

Table 10: Cost Information for IRS's Major IT Investments (Dollars in Millions)

Investment name	Fiscal year 2013 funding type ^a	Fiscal year 2013 to 2014 cost ^b	Lifecycle costs	Projected useful life of the current asset (estimated)
Account Management Services (AMS) Enhances customer support by providing applications that enable IRS employees to access, validate, and update individual taxpayer accounts on demand.	O&M	\$44	\$212	2019
Customer Account Data Engine 2 (CADE 2) Provides timely access to authoritative individual taxpayer account information and enhances IRS's ability to address technology, security, financial material weaknesses, and long-term architectural planning and viability.	O&M and DME	\$496	\$1,479	2019
Electronic Fraud Detection System (EFDS) Assists in detecting fraud at the time that tax returns are filed in order to eliminate the issuance of fraudulent tax refunds.	O&M	\$38	\$150	2015
e-Services (e-SVS) Comprises several web-based self-assisted services that are intended to allow authorized individuals to do business with the IRS electronically.	O&M and DME	\$24	\$211	2019
Foreign Account Tax Compliance Act (FATCA) Intended to implement provisions of the Foreign Account Tax Compliance Act regarding financial institutions reporting to IRS information about financial accounts held by U.S. taxpayers, or foreign entities in which U.S. taxpayers hold a substantial ownership interest.	DME	\$32	\$91	2019
Implement Return Review Program (RRP) (Replaces EFDS) Currently under development, is intended to maximize fraud detection at the time that tax returns are filed to eliminate issuance of questionable refunds.	DME	\$75	\$169	2019
Individual Master File (IMF) Represents the authoritative data source for individual tax account data. All other IRS information systems that process IMF data depend on output from this source. This investment is a critical component of IRS's ability to process tax returns.	O&M and DME	\$18	\$108	2019
Information Reporting and Document Matching (IRDM) Intended to establish a new business information matching program in order to increase voluntary compliance and accurate income reporting.	O&M and DME	\$46	\$186	2019
Integrated Customer Communication Environment (ICCE) Includes several projects that are intended to simplify voluntary compliance using voice response, Internet, and other computer technology such as the Modernized Internet Employee Identification Number, which allows third parties to act on the behalf of taxpayers.	O&M and DME	\$33	\$534	2019

Source: GAO analysis of fiscal year 2014 congressional budget justification for IRS.

Notes:

^aO&M= Operations and Maintenance; DME = Development/Modernization/Enhancement.

^bThe fiscal year 2013 to 2014 cost is defined as the base fiscal year 2013 budget plus the fiscal year 2014 request.

Fiscal Year 2014 IT Investments

Major IT Investments' Planned Cost (continued)

Table 10: cont'd: Cost Information for IRS's Major IT Investments (Dollars in Millions)

Investment name	Fiscal year 2013 funding type ^a	Fiscal year 2013 to 2014 cost ^b	Lifecycle costs	Projected useful life of the current asset (estimated)
Integrated Data Retrieval System (IDRS) Intended to provide systemic review, improve consistency in case control, alleviate staffing needs, issue notices to taxpayers, and allow taxpayers to see status of refunds. It is a mission-critical system used by 60,000 IRS employees.	O&M and DME	\$37	\$322	2019
Integrated Financial System/CORE Financial System (IFS) Used by IRS for budget, payroll, accounts payable/receivable, general ledger functions, and financial reporting; also used to report on the cost of operations and to manage budgets by fiscal year.	O&M and DME	\$32	\$483	2019
Integrated Submission and Remittance Processing System (ISRP) Processes paper tax returns, and updates tax forms to comply with tax law changes.	O&M and DME	\$24	\$192	2019
IRS End User Systems and Services (EUSS) Supports products and services necessary for daily functions for over 100,000 IRS employees at headquarters and field sites.	O&M	\$381	\$1,684	2025
IRS Main Frames and Servers Services and Support (MSSS) Intended to support the design, development, and deployment of server storage infrastructures, software, databases, and operating systems.	O&M	\$810	\$6,016	2025
IRS Telecommunications Systems and Support (TSS) Supports IRS's broad and local network infrastructure such as servers, and switches for voice, data, and video servicing of about 1,000 IRS sites.	O&M	\$594	\$2,583	2021
IRS.Gov - Portal Environment Provides web-based services such as tax filing and refund tracking, to internal and external users, such as IRS employees and other government agencies, taxpayers, and business partners.	O&M and DME	\$131	\$612	2020
Modernized e-File (MeF) Provides a secure web-based platform for electronic tax filing of individual and business tax and information returns by registered Electronic Return Originators.	O&M and DME	\$140	\$575	2019
Service Center Recognition/Image Processing System (SCRIPS) Used as a data capture, management, and image storage system using high-speed scanning and digital imaging to convert data from the 940, 941, K-1, and paper returns from Information Returns Processing into electronic format.	O&M and DME	\$19	\$195	2019

Source: GAO analysis of fiscal year 2014 congressional budget justification for IRS.

Notes:

^aO&M= Operations and Maintenance; DME = Development/Modernization/Enhancement.

^bThe fiscal year 2013 to 2014 cost is defined as the base fiscal year 2013 budget plus the fiscal year 2014 request.

Legislative Proposals

GAO Conducted Analyses Related to 12 of the 33 Legislative Proposals in the Fiscal Year 2014 Budget

Table 11: Legislative Proposals Related to Prior GAO Work (in Millions)

IRS legislative proposals related to prior GAO work	Projected revenues over 10 years	Projected costs over 3 years	Related GAO reports
Modify reporting of tuition expenses and scholarships on Form 1098-T, Tuition Statement	\$1,095	Not available	GAO-10-225 GAO-13-279SP
Increase certainty about the rules pertaining to classification of employees as independent contractors	\$9,097	\$1.9	GAO-09-717
Extend IRS math error authority in certain circumstances	\$185	\$1.4	GAO-10-349 , GAO-10-225 GAO-11-481
Allow IRS to absorb credit and debit card processing fees for certain tax payments	\$19	\$9.6	GAO-10-11
Provide Treasury with the regulatory authority to require additional information to be included in electronically filed Form 5500, Annual Return/Report of Employee Benefit Plan, and electronic filing of certain other employee benefit plan reports	No revenue effect	\$11.2	GAO-05-491
Require taxpayers who prepare their returns electronically, but file their returns on paper, to print their returns with a two-dimensional bar code	No revenue effect	\$6.8	GAO-12-33 GAO-08-38
Require all Form 990 series tax and information returns be filed electronically and provide IRS with regulatory authority to make the electronically filed Form 990 series returns publicly available in a machine readable format in a timely manner	No revenue effect	Not available	GAO-02-526 , GAO-02-444 GAO-06-799
Restrict access to Death Master File	\$1,303	Not available	GAO-02-233T
Provide whistleblowers with protection from retaliation	Negligible revenue effect	Not available	GAO-11-683
Provide stronger protection from improper disclosure of taxpayer information in whistleblower actions	No revenue effect	Not available	GAO-11-683
Add tax crimes to the Aggravated Identity Theft Statute	Negligible revenue effect	Not available	GAO-13-132T , GAO-09-882 , GAO-02-766
Impose a civil penalty on tax identity theft crimes	Negligible revenue effect	Not available	GAO-13-132T , GAO-09-882 , GAO-02-766

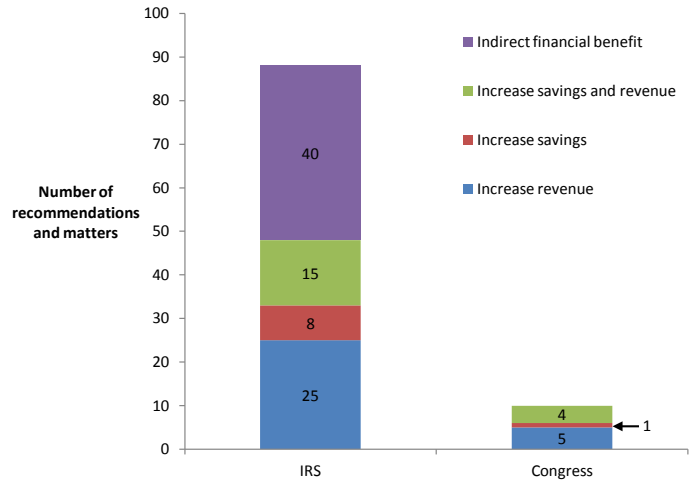
Source: IRS, Fiscal year 2014 congressional budget justification, and Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2014 Revenue Proposals* (Washington, D.C.: April 2013).

Open Matters and Recommendations

Implementing Open Matters for Congress and Recommendations to IRS Could Result in Financial Benefits

- We highlighted several areas where IRS could achieve cost savings and revenue enhancements in our duplication, overlap, and fragmentation reports.¹¹
- As of March 2013, 39 of our products contain 10 matters for congressional consideration and 88 recommendations to IRS with a potential financial benefit that have not been addressed. In addition, we have multiple other recommendations that could improve IRS operations if implemented. See appendix III for a list of products.
- Since March 2012, IRS has implemented 24 recommendations with a potential financial benefit.

Figure 2: Recommendations to IRS and Open Matters for Congress with a Financial Benefit

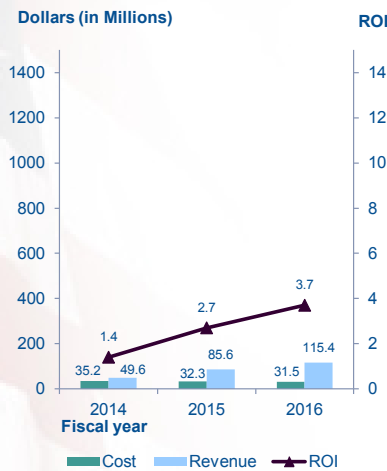


¹¹See GAO, 2013 Annual Report: Actions Needed to Reduce Fragmentation, Overlap, and Duplication and Achieve Other Financial Benefits, GAO-13-279SP (Washington, D.C.: Apr. 9, 2013), 2012 Annual Report: Opportunities to Reduce Duplication, Overlap and Fragmentation, Achieve Savings, and Enhance Revenue, GAO-12-342SP (Washington, D.C.: Feb. 28, 2012), and Opportunities to Reduce Potential Duplication in Government Programs, Save Tax Dollars, and Enhance Revenue, GAO-11-318SP (Washington, D.C.: Mar. 1, 2011).

Appendix II: Return on Investment Charts

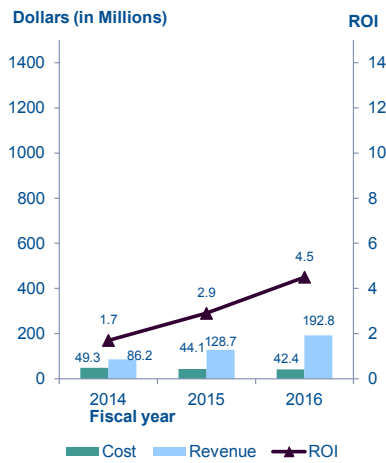
IRS Estimated Future ROI for 10 of the 12 New Enforcement Initiatives

Figure 3: Implement FATCA



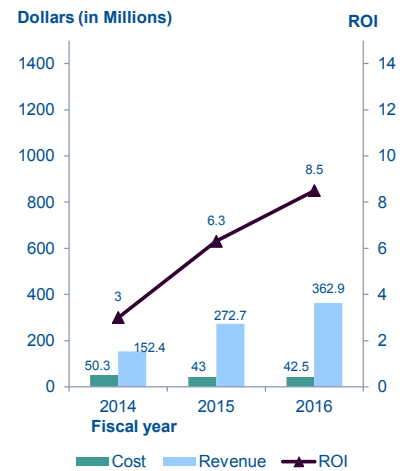
Source: GAO analysis of IRS data.

Figure 4: Address International and Offshore Compliance Issues



Source: GAO analysis of IRS data.

Figure 5: Implement Merchant Card and Basis Matching

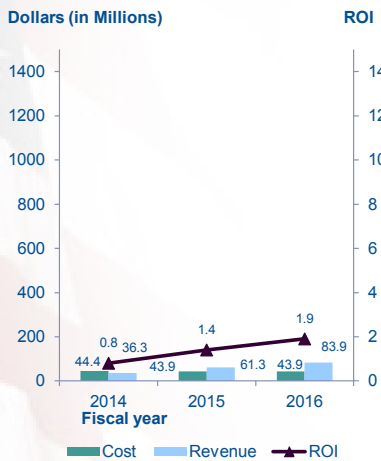


Source: GAO analysis of IRS data.

Appendix II: Return on Investment Charts

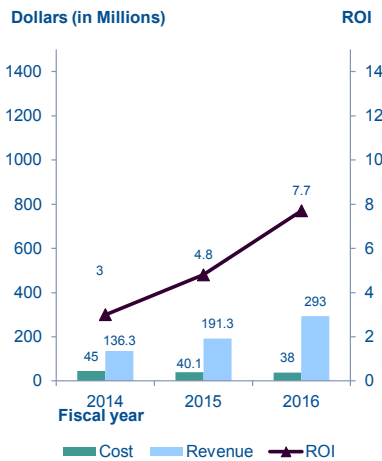
IRS Estimated Future ROI for 10 of the 12 New Enforcement Initiatives (continued)

Figure 6: Address Impact of PPACA Statutory Requirements



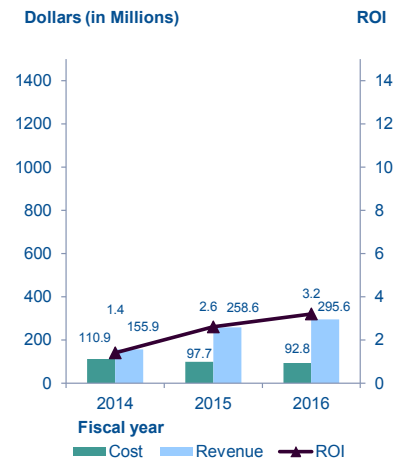
Source: GAO analysis of IRS data.

Figure 7: Improve Coverage of Partnerships and Flow-Through Entities



Source: GAO analysis of IRS data.

Figure 8: Increase Audit Coverage to Address Tax Compliance Issues

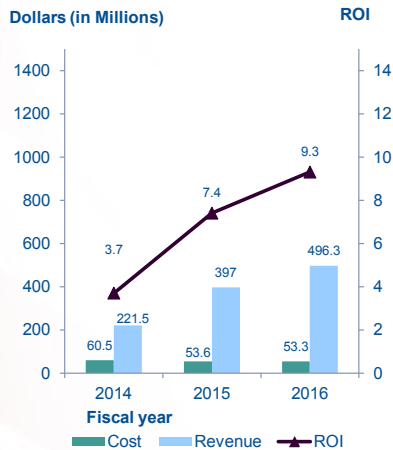


Source: GAO analysis of IRS data.

Appendix II: Return on Investment Charts

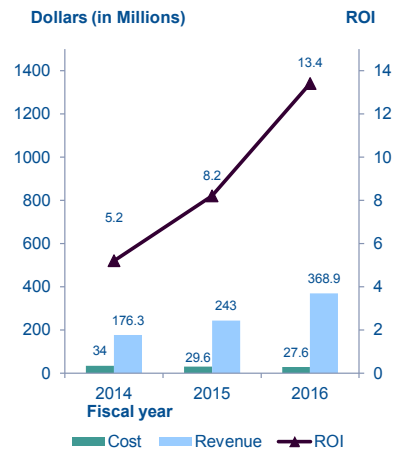
IRS Estimated Future ROI for 10 of the 12 New Enforcement Initiatives (continued)

Figure 9: Increase Collection Coverage



Source: GAO analysis of IRS data.

Figure 10: Expand Coverage of High-Wealth Individuals and Enterprises



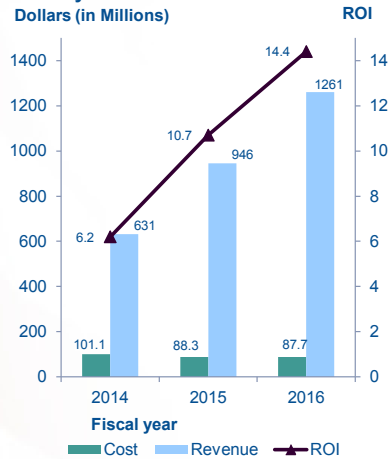
Source: GAO analysis of IRS data.

Appendix II: Return on Investment Charts

IRS Estimated Future ROI for 10 of the 12 New Enforcement Initiatives (continued)

Figure 11: Improve Identification and Prevention of Refund Fraud and Identity Theft

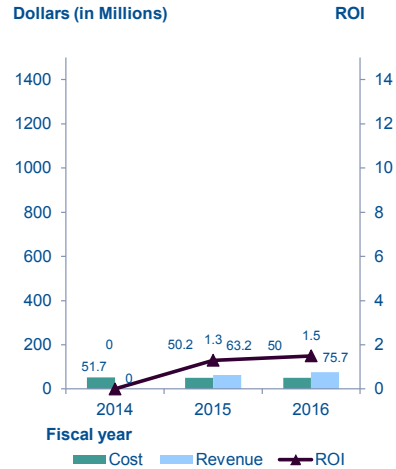
Dollars (in Millions)



Source: GAO analysis of IRS data.

Figure 12: Leverage Data to Improve Case Selection

Dollars (in Millions)



Source: GAO analysis of IRS data.

Note: Figures 11 and 12 do not use IRS's traditional ROI calculation. Figure 11 shows an initiative to protect revenue and Figure 12 shows an initiative to enhance revenue.

Appendix III: GAO Products with Open Matters for Congressional Consideration and Recommendations to IRS with a Potential Financial Benefit

39 GAO products contain 10 matters for Congressional consideration and 88 recommendations to IRS with a potential financial benefit that have not been addressed. Thirty have the potential to increase revenue (IR), 9 increase savings (IS), 19 increase both savings and revenue (ISR), and 40 may have indirect financial benefits (IFB).

Table 12: List of Open Matters for Congress and Recommendations to IRS That Could Result In Potential Savings or Increased Revenues or Both.

Report title and number	Website for current status of matters and/or recommendations	Potential financial benefits
Addressing identify theft		
<i>Identify Theft: Total Extent of Refund Fraud Using Stolen Identities is Unknown</i> (GAO-13-132T)	http://www.gao.gov/products/GAO-13-132T	IFB
Detecting abusive tax avoidance transactions		
<i>Abusive Tax Avoidance Transactions: IRS Needs Better Data to Inform Decisions about Transactions</i> (GAO-11-493)	http://www.gao.gov/products/GAO-11-493	IR, IFB
Enhancing budget requests		
<i>IRS 2013 Budget: Continuing to Improve Information on Program Costs and Results Could Aid in Resource Decision Making</i> (GAO-12-603)	http://www.gao.gov/products/GAO-12-603	IS, IFB
<i>IRS Budget 2012: Extending Systematic Reviews of Spending Could Identify More Savings Over Time</i> (GAO-11-547)	http://www.gao.gov/products/GAO-11-547	IS
Enhancing collection of user fees		
<i>User Fees: Additional Guidance and Documentation Could Further Strengthen IRS's Biennial Review of Fees</i> (GAO-12-193)	http://www.gao.gov/products/GAO-12-193	IFB
Enhancing electronic filing		
<i>E-Filing Tax Returns: Penalty Authority and Digitizing More Paper Return Data Could Increase Benefits</i> (GAO-12-33)	http://www.gao.gov/products/GAO-12-33	IS, ISR, IFB
<i>Electronic Tax Return Filing: Improvements Can Be Made before Mandate Becomes Fully Implemented</i> (GAO-11-344)	http://www.gao.gov/products/GAO-11-344	IS
<i>Tax Administration: Opportunities Exist for IRS to Enhance Taxpayer Service and Enforcement for the 2010 Filing Season</i> (GAO-09-1026)	http://www.gao.gov/products/GAO-09-1026	ISR
Enhancing electronic filing and improving accuracy of paid preparers		
<i>Tax Administration: Many Taxpayers Rely on Tax Software and IRS Needs to Assess Associated Risks</i> (GAO-09-297)	http://www.gao.gov/products/GAO-09-297	IFB
Enhancing internal controls		
<i>Management Report: Improvements Are Needed to Enhance the Internal</i>	http://www.gao.gov/products/GAO-11-494R	IS, IFB

Appendix III: GAO Products with Open Matters for Congressional Consideration and Recommendations to IRS with a Potential Financial Benefit

<i>Revenue Service's Internal Controls and Operating Effectiveness (GAO-11-494R)</i>		
Enhancing taxpayer services		
<i>2012 Tax Filing: IRS Faces Challenges Providing Service to Taxpayers and Could Collect Balances Due More Effectively (GAO-13-156)</i>	http://www.gao.gov/products/GAO-13-156	ISR
<i>2011 Tax Filing: Processing Gains, but Taxpayer Assistance Could Be Enhanced by More Self-Service Tools (GAO-12-176)</i>	http://www.gao.gov/products/GAO-12-176	ISR
Enhancing treatment of appraisals issues		
<i>Appraised Values on Tax Returns: Burdens on Taxpayers Could Be Reduced and Selected Practices Improved (GAO-12-608)</i>	http://www.gao.gov/products/GAO-12-608	ISR
Expanding use of math error authority or third party data		
<i>2011 Tax Filing: IRS Dealt with Challenges to Date but Needs Additional Authority to Verify Compliance (GAO-11-481)</i>	http://www.gao.gov/products/GAO-11-481	IR
<i>Recovery Act: IRS Quickly Implemented Tax Provisions, but Reporting and Enforcement Improvements Are Needed (GAO-10-349)</i>	http://www.gao.gov/products/GAO-10-349	ISR
<i>2009 Tax Filing Season: IRS Met Many 2009 Goals, but Telephone Access Remained Low, and Taxpayer Service and Enforcement Could Be Improved (GAO-10-225)</i>	http://www.gao.gov/products/GAO-10-225	IR, ISR
<i>Tax Administration: IRS's 2008 Filing Season Generally Successful Despite Challenges, although IRS Could Expand Enforcement during Returns Processing (GAO-09-146)</i>	http://www.gao.gov/products/GAO-09-146	ISR
Implementing Information Reporting and Document Matching (IRDM) system		
<i>IRS Management: Cost Estimate for New Information Reporting System Needs to be Made More Reliable (GAO-12-59)</i>	http://www.gao.gov/products/GAO-12-59	IFB
<i>Information Reporting: IRS Could Improve Cost Basis and Transaction Settlement Reporting Implementation (GAO-11-557)</i>	http://www.gao.gov/products/GAO-11-557	IFB
Implementing Patient Protection and Affordable Care Act (PPACA)		
<i>Patient Protection and Affordable Care Act: IRS Managing Implementation Risks, but Its Approach Could Be Refined (GAO-12-690)</i>	http://www.gao.gov/products/GAO-12-690	IFB
<i>Patient Protection and Affordable Care Act: IRS Should Expand Its Strategic Approach to Implementation (GAO-11-719)</i>	http://www.gao.gov/products/GAO-11-719	IFB
Improving allocation of enforcement resources		
<i>Tax Gap: IRS Could Significantly</i>	http://www.gao.gov/products/GAO-13-151	IR

Appendix III: GAO Products with Open Matters for Congressional Consideration and Recommendations to IRS with a Potential Financial Benefit

<i>Increase Revenues by Better Targeting Enforcement Resources</i> (GAO-13-151)		
Improving collection of unpaid taxes from Medicaid providers		
<i>Medicaid: Providers in Three States with Unpaid Federal Taxes Received Over \$6 Billion in Medicaid Reimbursements</i> (GAO-12-857)	http://www.gao.gov/products/GAO-12-857	IS
Improving corporate tax compliance		
<i>Tax Gap: Actions Needed to Address Noncompliance with S Corporation Tax Rules</i> (GAO-10-195)	http://www.gao.gov/products/GAO-10-195	IR, IFB
Improving individual or corporate tax compliance		
<i>Financial Derivatives: Disparate Tax Treatment and Information Gaps Create Uncertainty and Potential Abuse</i> (GAO-11-750)	http://www.gao.gov/products/GAO-11-750	IFB
<i>Federal Tax Collection: Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes</i> (GAO-11-272)	http://www.gao.gov/products/GAO-11-272	IR
Improving management of information technology (IT) investments		
<i>Investment Management: IRS Has a Strong Oversight Process but Needs to Improve How It Continues Funding Ongoing Investments</i> (GAO-11-587)	http://www.gao.gov/products/GAO-11-587	IS, IFB
Improving offshore compliance		
<i>Offshore Tax Evasion: IRS Has Collected Billions of Dollars, but May be Missing Continued Evasion</i> (GAO-13-318) ^a	http://www.gao.gov/products/GAO-13-318	IR
Improving real estate tax compliance		
<i>Tax Administration: Expanded Information Reporting Could Help IRS Address Compliance Challenges with Forgiven Mortgage Debt</i> (GAO-10-997)	http://www.gao.gov/products/GAO-10-997	IR
<i>Home Mortgage Interest Deduction: Despite Challenges Presented by Complex Tax Rules, IRS Could Enhance Enforcement and Guidance</i> (GAO-09-769)	http://www.gao.gov/products/GAO-09-769	IR
<i>Real Estate Tax Deduction: Taxpayers Face Challenges in Determining What Qualifies; Better Information Could Improve Compliance</i> (GAO-09-521)	http://www.gao.gov/products/GAO-09-521	IR
Improving rental real estate compliance		
<i>Tax Gap: Actions That Could Improve Rental Real Estate Reporting Compliance</i> (GAO-08-956)	http://www.gao.gov/products/GAO-08-956	IR
Improving sole proprietors' compliance		
<i>Tax Gap: Limiting Sole Proprietor Loss Deductions Could Improve</i>	http://www.gao.gov/products/GAO-09-815	IFB

Appendix III: GAO Products with Open Matters for Congressional Consideration and Recommendations to IRS with a Potential Financial Benefit

<i>Compliance but Would Also Limit Some Legitimate Losses (GAO-09-815)</i>		
Improving tax credit administration		
<i>Small Employer Health Tax Credit: Factors Contributing to Low Use and Complexity (GAO-12-549)</i>	http://www.gao.gov/products/GAO-12-549	ISR
Improving third party compliance		
<i>Tax Gap: IRS Could Do More to Promote Compliance by Third Parties with Miscellaneous Income Reporting Requirements (GAO-09-238)</i>	http://www.gao.gov/products/GAO-09-238	IR, IFB
Improving use of whistleblower claims		
<i>Tax Whistleblowers: Incomplete Data Hinders IRS's Ability to Manage Claim Processing Time and Enhance External Communication (GAO-11-683)</i>	http://www.gao.gov/products/GAO-11-683	IR, IFB
Increasing tax debt collection		
<i>Tax Debt Collection: IRS Needs to Better Manage the Collection Notices Sent to Individuals (GAO-09-976)</i>	http://www.gao.gov/products/GAO-09-976	ISR
Promoting effective use of third-party data		
<i>Tax Gap: IRS Has Modernized Its Business Nonfiler Program but Could Benefit from More Evaluation and Use of Third-Party Data (GAO-10-950)</i>	http://www.gao.gov/products/GAO-10-950	IR, IFB
Reducing tax evasion		
<i>Tax Gap: IRS Can Improve Efforts to Address Tax Evasion by Networks of Businesses and Related Entities (GAO-10-968)</i>	http://www.gao.gov/products/GAO-10-968	IFB

Legend: IR – Increase revenue, IS – Increase savings, ISR – Increase savings and revenue, IFB – Indirect financial benefit.

Source: GAO.

Notes: Products with open matters and recommendations identified as of March 11, 2013, with the exception of GAO-13-318 (see table note a). Some products may have matters and/or recommendations that do not have potential financial benefits or could be placed in different categories than provided above.

^aThis product includes open recommendations identified as of March 27, 2013.

Appendix IV: GAO Contact and Staff Acknowledgements

GAO Contact

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Staff Acknowledgements

In addition to the contact named above, Libby Mixon, Assistant Director; Amy Bowser, Chuck Fox, Paul Middleton, Ulyana Panchishin, Sabine Paul, Laurel Plume, Neil Pinney, Mark Ryan, Erinn L. Sauer, Cynthia Saunders, and Robert Yetvin made key contributions to this report.

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