United States Government Accountability Office

Report to the Secretary of the Treasury

November 2019

FINANCIAL AUDIT

IRS's FY 2019 and FY 2018 Financial Statements

GAO-20-159

GAO

Highlights

Highlights of GAO-20-159, a report to the Secretary of the Treasury

November 2019

FINANCIAL AUDIT

IRS's FY 2019 and FY 2018 Financial Statements

Why GAO Did This Study

In accordance with the authority conferred by the Chief Financial Officers Act of 1990, as amended, GAO annually audits IRS's financial statements to determine whether (1) the financial statements are fairly presented and (2) IRS management maintained effective internal control over financial reporting. GAO also tests IRS's compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements.

IRS's tax collection activities are significant to overall federal receipts, and the effectiveness of its financial management is of substantial interest to Congress and the nation's taxpayers.

What GAO Recommends

Based on prior financial statement audits, GAO made numerous recommendations to IRS to address internal control deficiencies. GAO will continue to monitor and will report separately on IRS's progress in implementing prior recommendations that remain open. Consistent with past practice, GAO will also be separately reporting on the new internal control deficiencies identified in this year's audit and providing IRS recommendations for corrective actions to address them.

In commenting on a draft of this report, IRS stated that it continues its efforts to improve its financial reporting systems controls and internal controls over unpaid assessments.

View GAO-20-159. For more information, contact Cheryl E. Clark at (202) 512-3406 or clarkce@gao.gov.

What GAO Found

In GAO's opinion, the Internal Revenue Service's (IRS) fiscal years 2019 and 2018 financial statements are fairly presented in all material respects, and although controls could be improved, IRS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2019. GAO's tests of IRS's compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements detected no reportable instances of noncompliance in fiscal year 2019.

Limitations in the financial systems IRS uses to account for federal taxes receivable and other unpaid assessment balances, as well as other control deficiencies that led to errors in taxpayer accounts, continued to exist during fiscal year 2019.These control deficiencies affect IRS's ability to produce reliable financial statements without using significant compensating procedures. In addition, unresolved information system control deficiencies from prior audits, along with application and general control deficiencies that GAO identified in IRS's information systems in fiscal year 2019, placed IRS systems and financial and taxpayer data at risk of inappropriate and undetected use, modification, or disclosure.

IRS continues to take steps to improve internal controls in these areas. However, the remaining deficiencies are significant enough to merit the attention of those charged with governance of IRS and therefore represent continuing significant deficiencies in internal control over financial reporting related to (1) unpaid assessments and (2) financial reporting systems. Continued management attention is essential to fully addressing these significant deficiencies.

Contents

Abbreviations

CFO	chief financial officer
FASAB	Federal Accounting Standards Advisory Board
FFMIA	Federal Financial Management Improvement Act of 1996
FMFIA	Federal Managers' Financial Integrity Act
IRS	Internal Revenue Service
RSI	required supplementary information

U.S. GOVERNMENT ACCOUNTABILITY OFFICE
441 G St. N.W.
Washington, DC 20548

November 8, 2019

The Honorable Steven T. Mnuchin
Secretary of the Treasury

Dear Mr. Secretary:

The accompanying report presents the results of our audits of the fiscal years 2019 and 2018 financial statements of the Internal Revenue Service (IRS). Specifically, we found

- IRS's financial statements as of and for the fiscal years ended September 30, 2019, and 2018, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles;
- although internal controls could be improved, IRS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2019; and
- no reportable noncompliance for fiscal year 2019 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

This report also provides a discussion of continuing significant deficiencies[1] in IRS's internal control over financial reporting related to (1) unpaid assessments[2] and (2) financial reporting systems that we believe merit attention by those charged with governance of IRS. Continued management attention is essential to improving the management and reporting of unpaid assessments and addressing financial reporting

[1]A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

[2]An unpaid assessment is a legally enforceable claim against a taxpayer and consists of taxes, penalties, and interest that have not been collected or abated (i.e., the assessment reduced by IRS). See, e.g., implementing guidance in Internal Revenue Manual § 1.34.4.1.6(1.p), *Terms/Definitions* (Aug. 25, 2015).

system deficiencies. IRS also continues to face significant management challenges that we have reported in previous audits relating to safeguarding taxpayer receipts and associated information and preventing and detecting fraudulent refunds based on identify theft. It is important that IRS continue its efforts to minimize the risks these challenges pose to taxpayers and any associated losses to the federal government.

We performed our audit pursuant to authority conferred by the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994.

We are sending copies of this report to the Chairman and Vice Chairman of the Joint Committee on Taxation, the Chairmen and Ranking Members of the Senate Committee on Finance and the House Committee on Ways and Means, and other interested congressional committees and subcommittees. We are also sending copies of this report to the Commissioner of Internal Revenue, the Director of the Office of Management and Budget, and other interested parties. In addition, the report is available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions concerning this report, please contact me at (202) 512-3406 or clarkce@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report.

Sincerely yours,

Cheryl E. Clark

Cheryl E. Clark
Director
Financial Management and Assurance

U.S. GOVERNMENT ACCOUNTABILITY OFFICE
441 G St. N.W.
Washington, DC 20548

Independent Auditor's Report

To the Commissioner of Internal Revenue

In our audits of the fiscal years 2019 and 2018 financial statements of the Internal Revenue Service (IRS), we found

- IRS's financial statements as of and for the fiscal years ended September 30, 2019, and 2018, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles;
- although internal controls could be improved, IRS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2019; and
- no reportable noncompliance for fiscal year 2019 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

The following sections discuss in more detail (1) our report on the financial statements and on internal control over financial reporting, which includes required supplementary information (RSI)[1] and other information included with the financial statements;[2] (2) our report on compliance with laws, regulations, contracts, and grant agreements; and (3) agency comments.

[1]The RSI consists of Management's Discussion and Analysis and the Required Supplementary Information section, which are included with the financial statements.

[2]Other information consists of information included with the financial statements, other than the RSI and the auditor's report.

Report on the Financial Statements and on Internal Control over Financial Reporting

In accordance with our authority conferred by the Chief Financial Officers (CFO) Act of 1990, as amended by the Government Management Reform Act of 1994, we have audited IRS's financial statements.[3] IRS's financial statements comprise the balance sheets as of September 30, 2019, and 2018; the related statements of net cost, changes in net position, budgetary resources, and custodial activity for the fiscal years then ended; and the related notes to the financial statements. We also have audited IRS's internal control over financial reporting as of September 30, 2019, based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

We conducted our audits in accordance with U.S. generally accepted government auditing standards. We believe that the audit evidence we obtained is sufficient and appropriate to provide a basis for our audit opinions.

Management's Responsibility

IRS management is responsible for (1) the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; (2) preparing, measuring, and presenting the RSI in accordance with U.S. generally accepted accounting principles; (3) preparing and presenting other information included in documents containing the audited financial statements and auditor's report, and ensuring the consistency of that information with the audited financial statements and the RSI; (4) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; (5) evaluating the

[3]See the CFO Act of 1990, Pub. L. No. 101-576, 104 Stat. 2838 (Nov. 15, 1990), codified, in relevant part, as amended, at 31 U.S.C. § 3521(g); see also the Government Management Reform Act of 1994, Pub. L. No. 103-356, 108 Stat. 3410 (Oct. 13, 1994), codified, in relevant part, as amended, at 31 U.S.C. § 3515(c). Pursuant to the authority of 31 U.S.C. § 3515, the Office of Management and Budget requires IRS to issue annual audited financial statements that are separate from those of the Department of the Treasury or that are presented separately in the department's audited, consolidated financial statements. Although the CFO Act designates the agency's inspector general, or where applicable an independent external auditor, as the responsible auditor of an agency's financial statements, the act also gives GAO the authority to perform such audits at its discretion. Based on that authority, we audit IRS's financial statements because of the significance of IRS's tax collections to the consolidated financial statements of the U.S. government, which GAO is required to audit. See 31 U.S.C. § 331(e)(2).

effectiveness of internal control over financial reporting based on the criteria established under FMFIA; and (6) its assessment about the effectiveness of internal control over financial reporting as of September 30, 2019, included in the accompanying Management's Report on Internal Control over Financial Reporting in appendix I.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements and an opinion on IRS's internal control over financial reporting based on our audits. U.S. generally accepted government auditing standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement, and whether effective internal control over financial reporting was maintained in all material respects. We are also responsible for applying certain limited procedures to RSI and other information included with the financial statements.

An audit of financial statements involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the auditor's assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances. An audit of financial statements also involves evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

An audit of internal control over financial reporting involves performing procedures to obtain evidence about whether a material weakness exists.[4] The procedures selected depend on the auditor's judgment,

[4]A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

including the assessment of the risk that a material weakness exists. An audit of internal control over financial reporting also includes obtaining an understanding of internal control over financial reporting, and evaluating and testing the design and operating effectiveness of internal control over financial reporting based on the assessed risk. Our audit of internal control also considered IRS's process for evaluating and reporting on internal control over financial reporting based on criteria established under FMFIA. Our audits also included performing such other procedures as we considered necessary in the circumstances.

We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing performance information and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Our internal control testing was for the purpose of expressing an opinion on whether effective internal control over financial reporting was maintained, in all material respects. Consequently, our audit may not identify all deficiencies in internal control over financial reporting that are less severe than a material weakness.

Definition and Inherent Limitations of Internal Control over Financial Reporting

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition, and (2) transactions are executed in accordance with provisions of applicable laws, including those governing the use of budget authority, regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Opinion on Financial Statements

In our opinion, IRS's financial statements present fairly, in all material respects, IRS's financial position as of September 30, 2019, and 2018, and its net cost of operations, changes in net position, budgetary resources, and custodial activity for the fiscal years then ended in accordance with U.S. generally accepted accounting principles.

In accordance with federal accounting standards, IRS's financial statements do not include an estimate of the dollar amount of taxes that are owed to the federal government but that taxpayers have not reported or that IRS has not identified through its enforcement programs, often referred to as the tax gap,[5] nor do they include information on tax expenditures.[6] Further detail on the tax gap and tax expenditures, as well as the associated dollar amounts, is provided in the other information included with the financial statements.

Opinion on Internal Control over Financial Reporting

In our opinion, although internal controls could be improved, IRS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2019, based on criteria established under FMFIA.

Our fiscal year 2019 audit identified continuing deficiencies concerning IRS's internal control over unpaid assessments and continuing and new deficiencies concerning IRS's internal control over financial reporting systems.[7] While not considered material weaknesses, these deficiencies are collectively important enough to merit attention by those charged with governance of IRS. Therefore, we considered these issues affecting IRS's internal controls over unpaid assessments and financial reporting systems to be significant deficiencies in internal control as of September

[5]The tax gap arises when taxpayers, whether intentionally or inadvertently, fail to (1) accurately report tax liabilities on tax returns (underreporting), (2) pay taxes due from filed returns (underpayment), or (3) file required tax returns altogether or on time (nonfiling). Based on its most recent study, which relied on 2011-2013 data, IRS estimated the average annual tax gap to be about $441 billion.

[6]Tax expenditures are revenue forgone because of preferential provisions of the tax code, such as special exclusions, exemptions, deductions, credits, deferrals, and tax rates.

[7]An unpaid assessment is a legally enforceable claim against a taxpayer and consists of taxes, penalties, and interest that have not been collected or abated. See, e.g., implementing guidance in Internal Revenue Manual § 1.34.4.1.6(1.p), *Terms/Definitions* (Aug. 25, 2015).

30, 2019.[8] These two significant deficiencies are discussed in more detail below.

We considered these significant deficiencies in determining the nature, timing, and extent of our audit procedures on IRS's fiscal year 2019 financial statements. Although the significant deficiencies in internal control did not affect our opinion on IRS's fiscal year 2019 financial statements, misstatements may occur in unaudited financial information reported internally and externally by IRS because of these significant deficiencies.

In addition, because of the significant deficiencies in internal controls over unpaid assessments and financial reporting systems that existed during fiscal year 2019, IRS's financial management systems did not comply substantially with federal financial management systems requirements as required by the Federal Financial Management Improvement Act of 1996.[9]

We will be reporting additional details concerning any new issues relating to these significant deficiencies separately to IRS management, along with recommendations for corrective actions. We also identified other deficiencies in IRS's internal control over financial reporting that we do not consider to be material weaknesses or significant deficiencies.

---

[8]A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

[9]Section 803(a) of the Federal Financial Management Improvement Act of 1996 (FFMIA), which is reprinted in 31 U.S.C. § 3512 note, requires that CFO Act agencies implement and maintain financial management systems that comply substantially with federal financial management systems requirements, applicable federal accounting standards, and the *U.S. Government Standard General Ledger* at the transaction level. IRS's financial management systems did not comply substantially with federal financial management systems requirements because of the financial management system–related internal control deficiencies discussed in this report. However, IRS's financial management systems did comply substantially with federal accounting standards and the *U.S. Government Standard General Ledger* at the transaction level. FFMIA applies directly to the U.S. Department of the Treasury (Treasury), which is a CFO Act agency. As a Treasury component, IRS is not required to be assessed separately; however, it is included in Treasury's agency-wide FFMIA assessment. Since IRS is a significant component of Treasury, we conducted this assessment to support the audit of the Treasury agency-wide financial statements. *See* Appendix D to Office of Management and Budget Circular No. A-123, § 4.A., *Compliance with the Federal Financial Management Improvement Act of 1996* (Sept. 20, 2013).

Nonetheless, these deficiencies warrant IRS management's attention. We have communicated these matters to IRS management and, where appropriate, will report on them separately along with related recommendations for corrective actions.

Further, as we have reported in past audits, IRS continues to face significant ongoing financial management challenges relating to safeguarding taxpayer receipts and associated information, and preventing and detecting fraudulent refunds based on identify theft.[10] Although these challenges do not rise to the level of significant deficiencies in internal control, we believe they are sensitive matters requiring IRS management's attention. We have made several recommendations to IRS to enhance its internal controls to mitigate these challenges.[11] It is important that IRS continue its efforts to minimize the risks these challenges pose to taxpayers and any associated losses to the federal government.

Significant Deficiency in Internal Control over Unpaid Assessments

Limitations in the financial systems IRS uses to account for federal taxes receivable and other unpaid assessment balances, as well as other control deficiencies that led to errors in taxpayer accounts, continued to exist during fiscal year 2019. As a result of these deficiencies, IRS's systems were unable to provide the timely, reliable, and complete

[10]GAO, *Financial Audit: IRS's Fiscal Years 2018 and 2017 Financial Statements*, GAO-19-150 (Washington, D.C.: Nov. 9, 2018).

[11]GAO, *Management Report: Improvements Are Needed to Enhance the Internal Revenue Service's Internal Control over Financial Reporting*, GAO-19-412R (Washington, D.C.: May 9, 2019), and *Identity Theft: IRS Needs to Strengthen Taxpayer Authentication Efforts*, GAO-18-418 (Washington, D.C., June 22, 2018).

transaction-level financial information necessary to enable IRS to appropriately classify and report unpaid assessment balances.[12]

As in prior years,[13] IRS used a complex and labor-intensive statistical estimation process[14] to compensate for the effects of its system limitations and other deficiencies on a material portion of its federal taxes receivable balance to help ensure that this balance was free of material misstatement.[15] During fiscal year 2019, IRS recorded adjustments totaling about $17 billion to correct the effects of continued errors in its underlying data that IRS identified during its manual estimation process.

---

[12]Federal accounting standards classify unpaid assessments into one of the following three categories for reporting purposes: federal taxes receivable, compliance assessments, and write-offs. Federal taxes receivable are taxes due from taxpayers for which IRS can support through the existence of a taxpayer agreement such as filing of a tax return without sufficient payment, or a court ruling in favor of IRS. Compliance assessments are proposed tax assessments where neither the taxpayer (when the right to disagree or object exists) nor a court has affirmed that the amounts are owed. Write-offs represent unpaid assessments for which IRS does not expect further collections because of factors such as the taxpayer's death, bankruptcy, or insolvency. Federal accounting standards require only federal taxes receivable, net of an allowance for uncollectible taxes receivable, to be reported on the financial statements. See Statement of Federal Financial Accounting Standards No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting* (May 10, 1996). See also implementing guidance in Internal Revenue Manual, § 1.34.4, *Unpaid Assessments* (Oct. 3, 2019).

[13]See GAO-19-150.

[14]The estimation process involves IRS manually testing statistical samples of unpaid assessments extracted from its master files (the detailed records of taxpayer accounts) and extrapolating the results to estimate the year-end balances to be reported as (1) federal taxes receivable reported in its financial statements and in the associated RSI and (2) compliance assessments and write-offs reported in the RSI.

[15]Beginning in fiscal year 2019, IRS's federal taxes receivable, net balance includes amounts pertaining to the taxes imposed on foreign earnings pursuant to provisions of the Tax Cuts and Jobs Act of 2017 (Act). In particular, the Act included a provision imposing a transition tax on foreign earnings at reduced tax rates, which the Act permitted affected taxpayers to elect to pay in eight annual installments in increments that the act specified (section 965 installment payment election). See Pub. L. No. 115-97, § 14103(a), 131 Stat. 2054, 2195 (Dec. 22, 2017), which is codified, in part, at 26 U.S.C. § 965(h). IRS manually reviewed all section 965 installment payment election claims amounting to $1 million or more to determine if the balances were accurately recorded in IRS's systems. In reviewing these claims, IRS also corrected errors in taxpayer accounts, and since all of these claims were classified as taxes receivable, they were unaffected by IRS system limitations related to accurately classifying and reporting unpaid tax assessments. In addition, IRS developed an econometric model to estimate the collectability of taxes receivable associated with section 965 installment payment elections.

While using this process to determine a material portion of taxes receivable has enabled IRS to produce reliable related balances for year-end reporting, it does not provide IRS management with readily available, reliable unpaid assessment information on a daily basis throughout the year in order to effectively manage unpaid assessment balances. Further, errors in taxpayer accounts create a burden for those taxpayers whose accounts were affected.

While not collectively considered a material weakness, IRS's ongoing control deficiencies related to unpaid assessments are important enough to merit attention by those charged with governance of IRS. Therefore, these issues represent a significant deficiency in IRS's internal control over financial reporting as of September 30, 2019. During fiscal year 2019, IRS documented the key management decisions in the design and use of the estimation process. This step should reduce the risk that IRS may perform sampling procedures inconsistent with management intent or plans. Continued management commitment and sustained efforts are necessary to build on the progress made to date and to fully address IRS's remaining unresolved issues concerning the management and reporting of unpaid assessments.

Significant Deficiency in Internal Control over Financial Reporting Systems

During our fiscal year 2019 audit, we determined that unresolved information system control deficiencies from prior audits, along with new control deficiencies pertaining to business process application controls[16] and general controls[17] in IRS's information systems, collectively represent a significant deficiency in IRS's internal control over financial reporting systems. Specifically, IRS did not correct control deficiencies we reported

[16]Business process application controls (input, processing, output, interface, and data management system controls) help to provide reasonable assurance about the completeness, accuracy, validity, confidentiality, and availability of transactions and data during application processing.

[17]General controls help to provide reasonable assurance that access to data is appropriately restricted, physical access to sensitive computing resources and facilities is restricted, systems are securely configured to avoid exposure to known vulnerabilities, and incompatible duties are segregated among individuals. In addition, controls should ensure that backup and recovery plans are adequate and tested to ensure the continuity of essential operations and that security is managed entity-wide under a framework that provides a continuing cycle of activity for managing risk, developing security policies, assigning responsibilities, and monitoring the adequacy of the entity's computer-related controls.

as of September 30, 2018,[18] concerning (1) unnecessary access rights granted to accounts, (2) inconsistent monitoring of systems and accounts, (3) out-of-date and unsupported hardware and software, (4) change controls over tax and financial management processing on the mainframe, and (5) developing and implementing effective policies and procedures as part of IRS's security management program.[19] In addition, during this year's audit, we found new control deficiencies in the following areas: (1) implementing automated financial controls of interfaces between key applications, (2) ensuring that authorized personnel reviewed key documents for external systems, (3) enforcing multifactor authentication, (4) enforcing adequate encryption to protect systems and data, or (5) ensuring that patches installed on systems were current to protect against known vulnerabilities.

The potential effect of these continuing and new deficiencies on IRS's financial reporting for fiscal year 2019 was mitigated primarily by IRS's compensating management controls designed to detect potential misstatements on the financial statements. Nevertheless, these application and general control deficiencies increase the risk of unauthorized access to, modification of, or disclosure of sensitive financial and taxpayer data and disruption of critical operations, and are therefore important enough to merit the attention of those charged with governance of IRS. According to IRS management, IRS has developed a plan that focuses on strengthening its information system controls. Continued and consistent management commitment and attention will be essential to addressing existing financial reporting system deficiencies.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles issued by the Federal Accounting Standards Advisory Board (FASAB) require that the RSI be presented to supplement the financial statements. Although the RSI is not a part of the financial statements, FASAB considers this information to be

[18]See GAO-19-150.

[19]We have previously reported deficiencies in certain information system controls, and made recommendations to address them, and reported on IRS's corrective actions in various reports on IRS's information security program. See, for example, GAO, *Management Report: Improvements Are Needed to Enhance the Internal Revenue Service's Information System Security Controls*, GAO-19-474R (Washington, D.C.: July 18, 2019).

an essential part of financial reporting for placing the financial statements in appropriate operational, economic, or historical context. We have applied certain limited procedures to the RSI in accordance with U.S. generally accepted government auditing standards, which consisted of inquiries of management about the methods of preparing the RSI and comparing the information for consistency with management's responses to the auditor's inquiries, the financial statements, and other knowledge we obtained during the audit of the financial statements, in order to report omissions or material departures from FASAB guidelines, if any, identified by these limited procedures. We did not audit and we do not express an opinion or provide any assurance on the RSI because the limited procedures we applied do not provide sufficient evidence to express an opinion or provide any assurance.

Other Information

IRS's other information contains a wide range of information, some of which is not directly related to the financial statements. This information is presented for purposes of additional analysis and is not a required part of the financial statements or the RSI. We read the other information included with the financial statements in order to identify material inconsistencies, if any, with the audited financial statements. Our audit was conducted for the purpose of forming an opinion on IRS's financial statements. We did not audit and do not express an opinion or provide any assurance on the other information.

Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

In connection with our audits of IRS's financial statements, we tested compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements consistent with our auditor's responsibility discussed below. We caution that noncompliance may occur and not be detected by these tests. We performed our tests of compliance in accordance with U.S. generally accepted government auditing standards.

Management's Responsibility

IRS management is responsible for complying with laws, regulations, contracts, and grant agreements applicable to IRS.

Auditor's Responsibility

Our responsibility is to test compliance with selected provisions of laws, regulations, contracts, and grant agreements applicable to IRS that have a direct effect on the determination of material amounts and disclosures in IRS's financial statements, and perform certain other limited procedures. Accordingly, we did not test compliance with all laws, regulations, contracts, and grant agreements applicable to IRS.

Results of Our Tests for Compliance with Laws, Regulations, Contracts, and Grant Agreements

Our tests for compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements disclosed no instances of noncompliance for fiscal year 2019 that would be reportable under U.S. generally accepted government auditing standards. However, the objective of our tests was not to provide an opinion on compliance with laws, regulations, contracts, and grant agreements applicable to IRS. Accordingly, we do not express such an opinion.

Intended Purpose of Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

The purpose of this report is solely to describe the scope of our testing of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements and the results of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering compliance. Accordingly, this report on compliance with laws, regulations, contracts, and grant agreements is not suitable for any other purpose.

Agency Comments

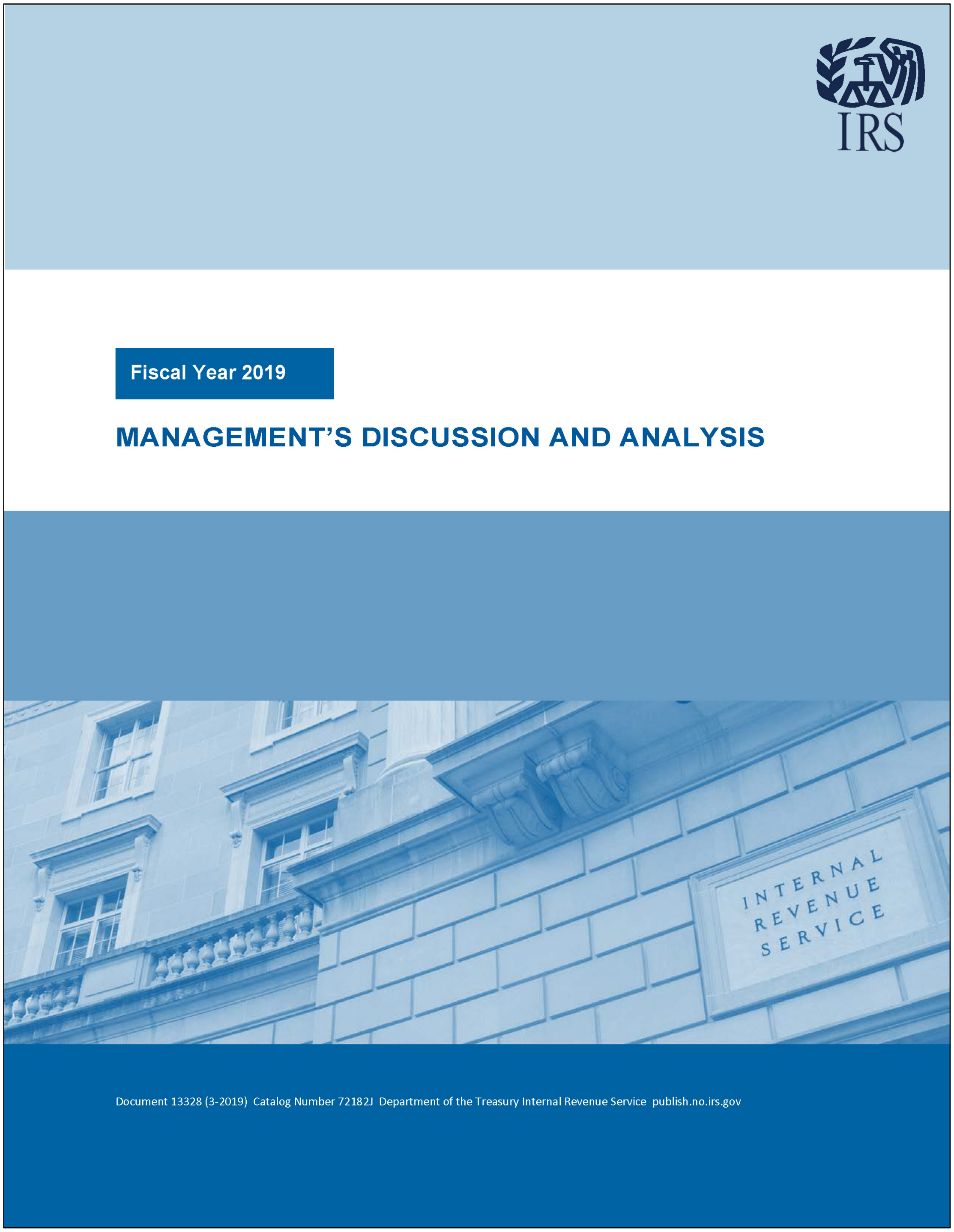
In commenting on a draft of this report, IRS stated that it was pleased to receive an unmodified opinion on its financial statements. IRS also commented on its continued efforts to address its financial reporting systems control deficiencies and improve its internal controls in financial reporting of unpaid assessments. The complete text of IRS's response is reproduced in appendix II.

Cheryl E. Clark

Cheryl E. Clark
Director
Financial Management and Assurance

November 7, 2019

Management’s Discussion and Analysis

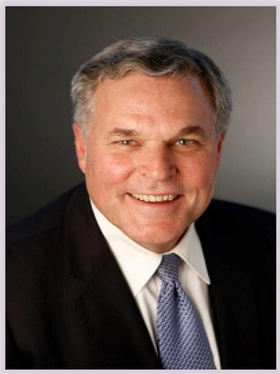


Fiscal Year 2019

MANAGEMENT’S DISCUSSION AND ANALYSIS

Document 13328 (3-2019) Catalog Number 72182J Department of the Treasury Internal Revenue Service publish.no.irs.gov

Table of Contents



"The IRS plays a unique role in the nation. The people of our agency are committed to helping taxpayers, enforcing the laws fairly and serving our great nation. Tax collection plays a critical role funding the country, supporting everything from schools and roads to our military. IRS employees are proud of their public service in support of the nation, and they are committed to making continued improvements to assist taxpayers." – IRS Commissioner Charles Rettig

While the IRS is well-known as the nation's tax collector, what's less well-known is how much the agency helps taxpayers. In everything the IRS does, it strives to put taxpayers first. IRS employees make a difference, they care, and they take pride in serving taxpayers and America.

A fully functioning IRS is vital to the success of our country. Each year, the IRS brings in about 95 percent of the gross revenue of this country – about $3.6 trillion. This revenue, from individual and business taxpayers, helps fund our great nation. The IRS touches more Americans than any other entity, public or private. The IRS makes it possible for the government to perform its vital functions, ranging from roads and schools to the nation's military.

The IRS made great strides during 2019 and is committed to doing more in every area – and we will.

The 2019 filing season presented some unique challenges for the agency. One was the need to implement the Tax Cuts and Jobs Act of 2017, the most sweeping set of changes to the tax laws in 30 years. The other was the 35-day partial government shutdown that began December 22, 2018, just as the IRS was in the final stages of preparing for the 2019 filing season.

Since the new law was passed, the IRS has been encouraging taxpayers to do a "Paycheck Checkup," to make sure they had not over- or under-withheld at tax time, by using the Withholding Calculator on IRS.gov. In 2019, the IRS redesigned and renamed this online tool. Our new Tax Withholding Estimator is even more user friendly and covers a wider range of tax situations that individuals might find themselves in.

The Withholding Estimator is just one of the IRS's many FY 2019 accomplishments described in this document.

About the IRS

History

The IRS is one of the oldest bureaus in the United States Government. Article 1, Section 8 of the Constitution gave the federal government the power to "lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States…" In 1862, President Lincoln and the Congress established the Bureau of Internal Revenue and the nation's first income tax. In 1953, the Bureau of Internal Revenue's name was changed to the Internal Revenue Service (IRS).

In FY 2019, the IRS added a new, interactive feature on IRS.gov to highlight the history of the IRS. Visit the IRS History Timeline at www.irs.gov/irs-history-timeline.

Internal Revenue Service Building, Washington D.C.

Mission

Provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.

Vision

The IRS will uphold the integrity of the nation's tax system and preserve the public trust through the IRS's talented workforce, innovative technology and collaborative partnerships.

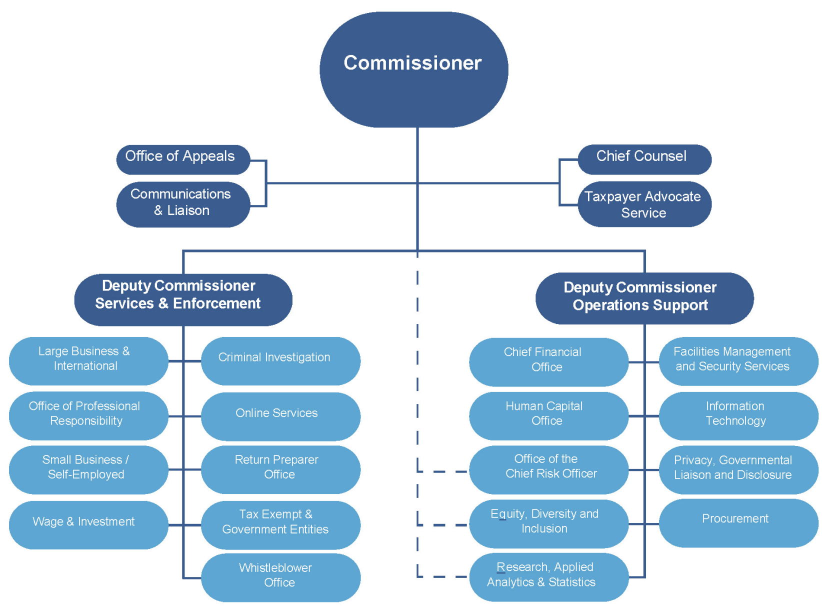
Organization

The IRS's core operations include collection of individual and corporate taxes, filing and processing tax returns, taxpayer assistance, enforcement of the tax laws through examination and collection, as well as criminal investigation of tax crimes. The wide IRS portfolio also includes tax-exempt organizations, tax-exempt bonds, multiple refundable tax credits, and other specialized programs. IRS operations are supported by four business units focused on unique groups of taxpayers: individual taxpayers, small business owners, large corporations and offshore activities, and tax-exempt and government entities.

Business Unit Summary

- **Wage and Investment (W&I)** serves more than 155 million taxpayers, including those who file jointly, with wage and investment income only.
- **Small Business and Self-Employed (SB/SE)** serves about 57 million small businesses and self-employed individuals operating as sole proprietorships, small corporations or flow-through entities. The division is also responsible for estate, gift, fiduciary, excise, and most employment tax returns and is responsible for the collection of all unpaid federal tax accounts.
- **Large Business and International (LB&I)** serves approximately 250,000 corporations, subchapter S corporations, and partnerships with assets greater than $10 million. LB&I also serves U.S. citizens and residents with offshore activities and nonresidents with U.S. activities.
- **Tax Exempt and Government Entities (TE/GE)** serves customers across three distinct taxpayer segments - Employee Plans, Exempt Organizations, and Government Entities.

Criminal Investigation (CI) investigates potential criminal violations and financial crimes in a manner that fosters confidence in the tax system.



How the IRS Serves the Country

The IRS and its employees take pride in collecting more than 95 percent of the revenue that funds key operations in the United States. The IRS is one of the world's most efficient tax administrators. Some key performance achievements in FY 2019:

255M Federal Tax Returns and Forms Processed

$3.6T Collected in Gross Taxes

$2,800 Average Individual Refund

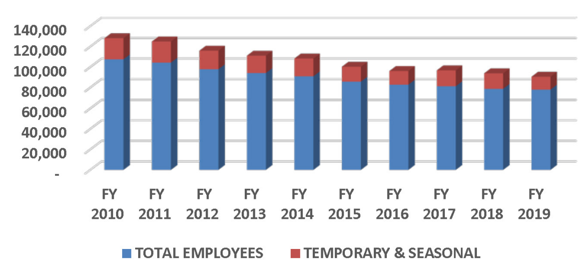
$57.5B Enforcement Revenue Collected

State of the IRS Workforce

In FY 2019, the IRS employed about 78,004 employees, including more than 12,600 temporary and seasonal staff. The IRS gained 1,593 full time positions between FY 2018 and FY 2019, although staffing levels remain well below levels in previous decades.

The IRS lost more than 29,618 full time positions between FY 2010 and FY 2019, which included more than14,663 key enforcement personnel. These losses included Revenue Agents and Revenue Officers who audit returns and perform collection activities; and Special Agents in the IRS's Criminal Investigation organization which investigates tax-related crimes and other issues. These losses directly correlate with a steady decline in the number of individual audits during the past nine years.

IRS Employees by Fiscal Year



The IRS anticipates up to 31 percent of its current workforce (about 19,719 full-time employees) will retire within the next five years, creating a significant risk of a large knowledge and experience gap for the nation's tax agency.

In FY 2019, the IRS made progress in addressing its resource limitations by rescinding exception-only hiring policies in place since FY 2011 and adding efforts to hire new staff across all age groups.

The IRS continues to make strategic shifts within its existing workforce to accomplish its current and future goals and meet the needs of taxpayers. However, the recent passage of P.L. 116-25, *Taxpayer First Act*, signed July 1, 2019, created a new request for the IRS. The agency must submit to Congress by the end of FY 2020 a comprehensive proposal to redesign the organization of the IRS to better support America's taxpayers. The IRS has not had a major reorganization of its structure since implementation of the *IRS Restructuring and Reform Act of 1998*.

IRS 2018-2022 Strategic Plan

The IRS FY 2018-2022 Strategic Plan articulates the IRS's vision of becoming a more taxpayer-centric and modern agency and will guide the IRS in moving forward over the coming years.

The core of the IRS vision for the future is to enhance the taxpayer experience. The IRS strives for excellent service to taxpayers and their representatives through their preferred service channel. The IRS also aims to reduce taxpayer burden and preempt noncompliance issues, allowing the IRS to focus enforcement on more complex cases and intentional abuses of tax law.

The IRS's ability to provide high-quality taxpayer service and maintain the integrity of the tax system requires modern, secure, and nimble operations, as well as a sustained and talented workforce. As the IRS strives to provide service to taxpayers and their representatives and ensure successful implementation of changes in tax laws, the IRS is embracing and integrating data into its culture. Using analytics, the IRS strives to continuously improve all facets of its operations — taxpayer service, enforcement efforts and a range of internal operations — maximizing learning from tests and data. The IRS is committed to using this research to guide organizational priorities. Greater collaboration with a variety of partners, such as government agencies, international tax administrations, software providers, and industry groups will enable the IRS to deliver on its mission more effectively and efficiently.

The FY 2018 – 2022 IRS Strategic Plan serves as a roadmap to guide resource decisions, programs and operations to meet the changing needs and expectations of taxpayers and members of the tax community who serve taxpayers. The following six strategic goals reflect the Commissioner's priorities:

Empower and enable all taxpayers to meet their tax obligations - We will empower taxpayers by making it easier for them to understand and meet their filing, reporting and payment obligations. We continue to add and enhance tools and support to improve taxpayers' and tax professionals' interactions with the IRS on whichever channel they prefer.

Protect the integrity of the tax system by encouraging compliance through administering and enforcing the tax code - The American tax system is based on voluntary compliance and supported by appropriate enforcement. As part of the IRS's efforts to close the tax gap, we will pursue innovative approaches to understand, detect and resolve potential noncompliance. We will use behavioral insights on how people process and react to information. This will inform how we design programs to encourage voluntary compliance.

Collaborate with external partners proactively to improve tax administration - Partnerships with IRS stakeholders enrich service to taxpayers. Collaboration will yield innovative solutions to pressing problems, improving the taxpayer experience. We will engage partners to improve service and outreach to taxpayers, enhance global collaboration and share leading practices.

Cultivate a well-equipped, diverse, flexible and engaged workforce - IRS employees are committed to serving the American taxpayer. We strive for a culture that values innovation, welcomes multiple perspectives and celebrates diversity. The IRS's approach to development will be complemented by a forward-looking talent management strategy that considers future business and stakeholder needs.

Advance data access, usability and analytics to inform decision-making and improve operational outcomes - We'll continue to use data to drive decisions and make the most effective use of resources. Advancements across the full data lifecycle — from collection to storage to access to analysis — will allow the IRS to better deploy data and implement insights. Improving data and analytics provides repeatable processes for selecting and assigning work.

Drive increased agility, efficiency, effectiveness and security in IRS operations - We will focus on streamlining and simplifying IRS business processes to serve taxpayers better and improve IRS stewardship of taxpayer resources. Efficient operations and modern infrastructure are the foundation of a stable, reliable organization and are essential elements of sustaining excellent service and enforcement capabilities. Strong data systems are critical to safeguarding taxpayer and employee data from threats.

FY 2019 Performance Highlights

Empower and enable all taxpayers to meet their tax obligations

The IRS is dedicated to improving the taxpayer experience, so that taxpayers and their representatives can understand and meet their tax obligations with as little burden as possible.

The IRS's aim is to increase voluntary compliance through simplifying the processes for tax filing, correction and payment, improving education and outreach on taxpayer rights and obligations, and modernizing and expanding service channels to meet taxpayer needs.

FY 2019 Tax Filing Season: Implementing the Tax Cuts and Jobs Act (TCJA)

The most visible taxpayer service the IRS provides each year is the delivery of a smooth, reliable tax filing season. The 2019 filing season presented some challenges for the IRS that included the implementation of TCJA and the government shutdown just as the IRS was in the final stages of preparation for the filing season.

Implementation of the TCJA required immediate changes to instructions and processing procedures, as well as technical and systemic changes needed within extremely compressed timeframes. The IRS's top priority was to ensure taxpayers and tax professionals had the information they needed and the support of knowledgeable IRS employees to help fulfill tax obligations with the least possible burden.

The IRS's efforts to implement the new tax law extended into many different areas that affected taxpayers in many ways. These efforts included:

- Creating or revising more than 500 IRS forms and publications
- Reprogramming IRS information technology systems with special focus on return processing, payment and fraud detection systems
- Training IRS employees so they could assist the public in understanding how the tax law changes applied to them
- Providing education and outreach to taxpayers and tax professionals to increase their understanding of the various tax changes including a year-round effort encouraging taxpayers to conduct a Paycheck Checkup to review their tax withholding
- Developing the legal guidance that taxpayers and tax professionals need to understand and navigate the new law

New Forms, Instructions, and Publications

The IRS's efforts to create, revise and update various Tax Year (TY) 2018 filing season tax products reached across all types of individual and business returns. For example:

- The IRS developed and heavily promoted new IRS Publication 5307, *Tax Reform Basics for Individuals and Families*, which the IRS had translated into seven languages. Publication 5307 provided an overview of TCJA provisions that affect individual taxpayers and highlighted the changes to deductions, retirement plans, and dependent benefits for the 2018 tax year.
- The IRS published numerous new forms, instructions, and publications on business and tax exempt and government entities provisions including the excise tax on large college endowments, unrelated trade or business reporting, and expanded access to retirement funds in case of disaster.
- The IRS streamlined Form 1040, *U.S. Individual Income Tax Return*, into a shorter, simpler form for the 2019 tax season. Based on feedback from the tax community, additional improvements were made to the TY 2020 Form 1040 to ensure taxpayers have an even better experience, including reducing the number of schedules.
- The IRS also developed Form 1040-SR, *U.S. Tax Return for Seniors*. The new form will be used for the first time in the 2020 filing season and is designed specifically for taxpayers age 65 and older.

Tax Withholding

Since the implementation of TCJA, the IRS has been encouraging taxpayers to do a "Paycheck Checkup," to ensure they are not over- or under-withholding at tax time, by using the Withholding Calculator on IRS.gov. In July 2019, the IRS redesigned and renamed this online tool. The IRS's new Tax Withholding Estimator is even more user friendly and covers a wider range of tax situations.

To account for major changes resulting from tax reform legislation, the IRS developed a new Form W-4, *Employee's Withholding Allowance Certificate*, for TY 2020. This is a tax form completed by an employee in the United States to indicate his or her tax situation to the employer. During this effort, the IRS worked to ensure the new design would provide simplicity, accuracy and privacy to employees. The IRS incorporated feedback from stakeholders, including tax practitioners and the payroll community, to ensure the new form would minimize burden on employers and payroll processors.

Reprogramming IT Systems

To prepare for the 2019 filing season, the IRS identified required computer programming changes needed to process new or revised tax forms. For example, the IRS changed computer programming to account for new lines on certain tax forms and capture the value from those new lines for tax return processing. The IRS updated business rules used to validate information included on e-filed tax returns for acceptance into return processing, as well as error resolution codes used to identify mathematical and clerical errors on a tax return. By the start of the 2019 filing season, these changes were in place and all information technology functional testing was complete with all critical defects resolved.

The TCJA required the IRS to perform computer programming changes and updates for 69 of the 119 provisions. The IRS estimated these changes and updates affected 128 information technology systems. Information technology work requests required the creation of 275 new e-file business rules, updates to 36 existing e-file business rules, and deletion of 248 e-file business rules no longer needed. The IRS also created four new error resolution codes and updated 22 existing error resolution codes.

About 770 of 1,200 total tax products required revisions for the 2019 filing season. More than 500 of those products were affected by the TCJA. Computer programming requirements were issued for about 200 different forms of which roughly 150 were affected by the TCJA. Almost 600 products needed early releases for review by partners in the tax community.

The IRS took a novel approach to tax reform implementation considering the significant tax processing changes and condensed timeline. For example, the IRS collaborated early with internal groups to enhance and innovate the practices used each filing season. The IRS used an approach called "Rapid Requirements Elicitation," which allowed the IRS to identify necessary system changes faster, with greater agility and efficiency. The IRS established new forums that allowed closer coordination, which mitigated the effects of the partial government shutdown.

Despite the compressed schedule, the IRS completed thousands of system updates that stemmed from form changes to comply with the TCJA and improved quality control for calculations and validation of taxpayer submissions, completing development in mid-December before the filing season officially began. In FY 2019, the IRS developed and used the first ever Integrated Master Schedule and Critical Path Summary. This allowed for more real-time and synchronized data across areas, from software development to deployment production. In effect, the IRS had better insights into potential issues and risks due to schedule slippage, which strengthened the overall filing season readiness process.

Delivering the 2019 Tax Filing Season

Despite the challenges the IRS faced, the agency had a very successful filing season, which opened on time on January 28, 2019, the same day the government shutdown ended.

On April 15, 2019, the IRS processed the largest single-day filing volumes ever recorded (about 15.3 million returns) and observed record-breaking use of IRS Online Account and Direct Pay applications.

At the end of 2019, the IRS will have processed more than 155 million individual tax returns from households across the nation and issued more than 109 million federal tax refunds totaling more than $300 billion. Nine out of 10 of those refunds were issued within 21 days. The average refund per household in 2019 was about $2,800

The IRS's worked to provide top-quality service to taxpayers during the tax filing season and beyond. Throughout the year the IRS provided service online; answered taxpayer calls on its toll-free line; offered in-person help at Taxpayer Assistance Centers; and corresponded with taxpayers through the mail. All service channels are designed to provide taxpayers and their representatives with the information and answers they need to fulfill their tax responsibilities.

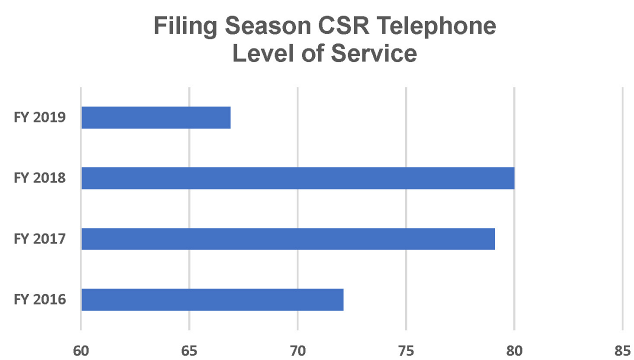
In-Person Assistance: Taxpayer Assistance Centers, Volunteer Income Tax Assistance/Tax Counseling for the Elderly

For the filing season through April 19, 2019, IRS employees answered more than 1.0 million calls to schedule an appointment with almost 536,000 necessitating a visit to a Taxpayer Assistance Center. The IRS was able to assist an additional 483,000 taxpayers who called for an appointment without the taxpayer having to come to the Taxpayer Assistance Center. The IRS assisted more than 87,000 taxpayers who did not have an appointment with issues that should have required an appointment (taxpayers who travel to a Taxpayer Assistance Center without an appointment are assisted if there is availability). Overall, the IRS served nearly 1.3 million taxpayers with more than 798,000 face-to-face assistor contacts and more than 483,000 phone-based resolutions for taxpayers who originally called for an appointment.

In addition, more than 82,000 volunteers prepared more than 3.4 million federal tax returns at approximately 11,000 Volunteer Income Tax Assistance/Tax Counseling for the Elderly locations with 99.2 percent of these returns being electronically filed. The Quality Statistical Sample accuracy rate, which is a review process that validates accuracy of tax returns and compliance with quality site requirements and volunteer standards of conduct, was 98 percent, exceeding the FY 2019 goal of 91 percent.

On the Phone: Toll-Free Help Line

The IRS's toll-free telephone line constitutes one of the world's largest customer service phone operations and is a key part of the IRS's taxpayer service delivery. For the 2019 filing season the IRS planned to deliver an 80 percent Telephone Customer Service Representative (CSR) Level of Service (LOS), which is the relative success rate of taxpayers who call the toll-free number seeking live assistance. The planned CSR LOS for all of FY 2019 was 75 percent. However, the government shutdown delayed training and decreased assistor availability, resulting in the need to revise the LOS targets to 65 percent for filing season and 63 percent for the fiscal year. The IRS exceeded those revised targets and delivered a 66.9 percent telephone level of service for the filing season and 65.4 percent for the fiscal year.



In addition to the telephone LOS, the IRS monitors performance and the taxpayer experience (both for assistors and automation) including wait time (average speed of answer); handle time (average length of call once the taxpayer reaches an assistor); accuracy of CSR responses; and customer satisfaction.

The average wait time during the filing season was nine minutes and the average handle time was 12 minutes. The toll-free tax law and accounts accuracy remains high, and customer satisfaction exceeded 90 percent.

Ensuring Uninterrupted Filing and Payment

Serving taxpayers also involves building and improving IRS systems to ensure that the process of filing returns and making payments is as seamless for taxpayers as possible and can occur without interruption.

During FY 2019, the IRS made enhancements to help automate and improve the recovery time in the event of an information technology system outage. Strategic investments allowed the IRS to build in redundancy and backup measures for the primary filing season storage array, which helps reduce the risk of major outage events due to the unavailability of data. The IRS achieved its goal of being capable of recovering from a filing season system failure in less than two hours. These new resiliency measures allowed taxpayers to file returns and make online payments independent of the IRS mainframe systems. One result of these investments was greater revenue collection. The IRS collected more than $1 billion through IRS Direct Pay during what would in the past have been system downtimes, when the tool was unavailable to accept payments due to maintenance, momentary network communication issues, or other unplanned outages.

Overall, IRS systems maintained a 100 percent uptime throughout the filing season, which allowed the IRS to continue return processing and fraud detection activities and gave taxpayers the ability to make online payments without interruption. This contributed to the IRS's successful delivery of the 2019 filing season.

Online Services: Expanding Digital Options

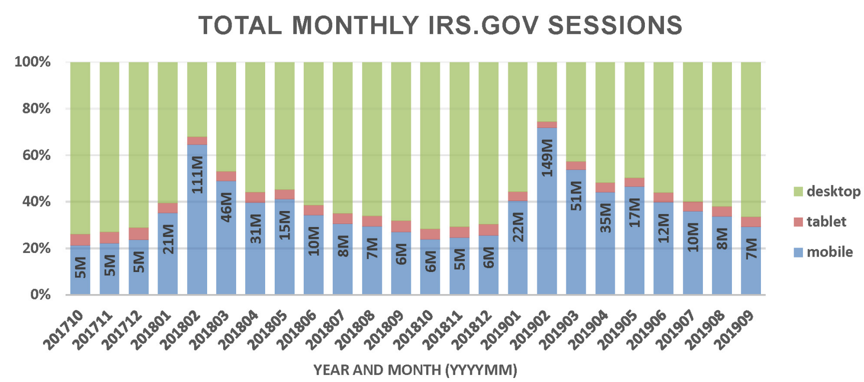
The IRS continually works to improve and expand its online offerings to meet taxpayers' expectations so that they can interact with the IRS as they would with any financial institution. These efforts to improve continued during FY 2019.

The IRS completed a comprehensive Filing Season Readiness review on January 19, 2019 that included the topmost popular 300 IRS.gov webpages (by visitor volume) to ensure that they were ready for filing season. A Certificate of Readiness was completed on February 1, 2019, after the government shutdown. These activities and accomplishments supported a series of major filing season projects which included:

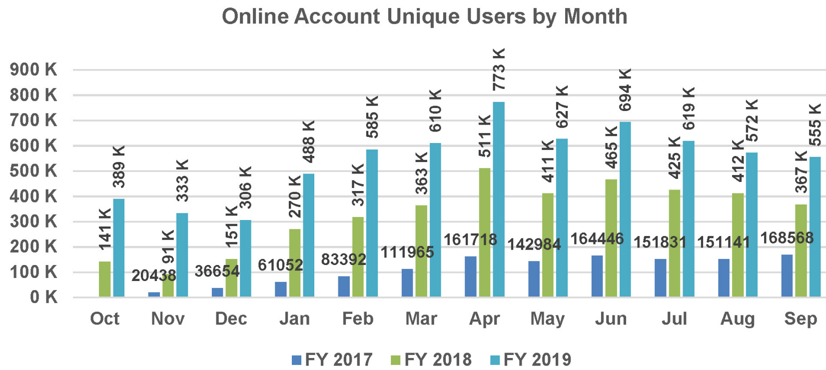
- New Form 1040 Content
- Free File Fillable Form Error code updates
- Withholding Calculator content updated (YouTube)
- Free File Content Consolidation
- Tax Topics update (English and Translations)
- Let Us Help You (English and Translations)
- Earned Income Tax Credit (EITC) Due Diligence Training Module
- EITC Assistance (English and Translations)
- Interactive Tax Assistant

Overall, IRS.gov usage showed slight growth in FY 2019 compared to FY 2018. This growth was driven entirely by mobile device usage, which experienced 22 percent growth. Mobile traffic to the site reached an all-time quarterly high of 62.1 percent, driven primarily by refund-related inquiries. In February 2019, 72 percent of all site visits came from mobile devices. Mobile devices also accounted for 208 million of 264 million total accesses of the Where's My Refund application.

Similarly, usage of the IRS2Go mobile application increased by 17 percent more users in FY 2019; growth was driven by refund inquiries.



The Online Account application continues to grow in reach and usage as well, contributing to growth in digital payments and installment agreements. In FY 2019, there was a 58 percent increase in unique users compared to FY 2018 and 4.8 million unique users of the tool since launch. Growth during filing season was highlighted by an all-time single-day high on April 15th for Direct Pay transactions, Online Payment Agreements, and Online Account visits.



Deployed in advance of the filing season, ID Verify Phase 2 enables taxpayers with returns selected by the Taxpayer Protection Program for additional scrutiny in the tax year to provide identity and return verification information online rather than by calling a live assistance telephone line or visiting a Taxpayer Assistance Center. This reestablishes an online self-service option, after the original ID Verify application was discontinued in August 2016. As of September 30, 2019, 134,200 taxpayers who are eligible to use ID Verify have logged in and verified their identity since the application launched for the 2019 filing season.

In July, the IRS released the Multi-Page View enhancement of the Online Account that allows the user interface to accommodate additional future features more easily. The first of these new features includes integration of installment agreement status, followed by further installment agreement and payment capabilities in the future.

First introduced in November 2017, the IRS gradually expanded web-enabled chat options to customers of the Online Payment Agreement application. New features this year included:

- Proactive chat, offering chat to users spending significant time on steps within the service
- Providing targeted content based on specific error conditions that resolves some issues before live assistance is even required
- Authenticated chat, allowing live assistors to securely provide detailed assistance specific to the taxpayer's unique circumstance

Key Performance Data Highlights

Performance Measure	Target	Actual
Customer Service Representative (CSR) Level of Service	63.0%	65.4%
Customer Accuracy – Tax Law Phones	92.0%	91.6%
Customer Accuracy – Customer Accounts (Phones)	94.0%	94.3%
Timeliness of Critical Individual Filing Season Tax Products to the Public	85.0%	92.6%
Timeliness of Critical TE/GE and Business Tax Products to the Public	85.0%	96.1%
Percent Business Returns Processed Electronically	58.0%	57.8%
Enterprise Self-Assistance Participation Rate	Indicator	85.4%
Taxpayers Satisfied with the IRS[1, *]	Indicator	N/A

1. Based on the American Customer Satisfaction Index (ACSI) survey; the All Individual Tax Filer score is calculated from separate ACSI Individual Paper Filer and Electronic Filer customer satisfaction index scores; available on an annual basis at the end of January and computed on a 100-point scale.

* New measure added for FY 2019 reporting.

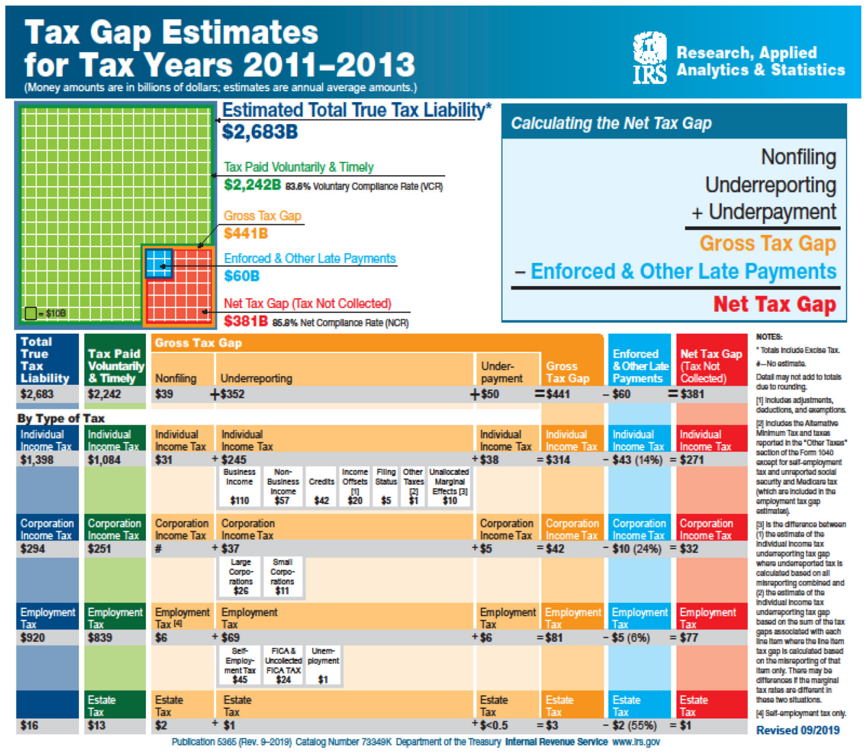
Protect the integrity of the tax system by encouraging compliance through administering and enforcing the tax code

One of the IRS's key responsibilities is to ensure taxpayers comply with the tax law. The IRS continues to develop innovative approaches to understanding, detecting and resolving potential noncompliance to maintain taxpayer confidence in the tax system.

The Tax Gap

The tax gap and associated concepts are a particular way of defining and analyzing compliance and noncompliance and are based on tax year liability. The tax gap provides a rough gauge of the level of overall noncompliance and voluntary compliance given all the events that occurred during the relevant tax periods and the Internal Revenue Code provisions in effect at the time. Tax gap estimates provide the IRS with periodic appraisals about the nature and extent of noncompliance for use in formulating tax administration strategies. The word "tax" in the phrase "tax gap" is used broadly to encompass both tax and refundable and non-refundable tax credits.

In FY 2019, the IRS released a new tax gap estimate of $441 billion, which covers tax years 2011, 2012 and 2013. The gross tax gap is the amount of true tax liability that is not paid voluntarily and timely. The net tax gap is the gross tax gap less tax that subsequently will be paid, either paid voluntarily but late or collected through IRS administrative and enforcement activities; it is the portion of the gross tax gap that will not be paid. It is estimated that $60 billion of the gross tax gap eventually will be paid resulting in a net tax gap of $381 billion. The voluntary compliance rate is a ratio measure of relative compliance and is defined as the amount of "tax paid voluntarily and timely" divided by "total true tax", expressed as a percentage. The voluntary compliance rate corresponds to the gross tax gap. The estimated voluntary compliance rate is 83.6 percent. The net compliance rate is a ratio measure corresponding to the net tax gap. The net compliance rate is defined as the sum of "tax paid voluntarily and timely" and "enforced and other late payments" divided by "total true tax", expressed as a percentage. The estimated net compliance rate is 85.8 percent. The following figure is a schematic representation of the tax gap estimates.



In FY 2019, the IRS continued to be extremely active in the enforcement area, through a variety of activities, including investigations of tax noncompliance and the millions of notices sent each year to taxpayers when issues are discovered on their returns, such as failing to report income from Forms W-2 or 1099.

IRS compliance programs are focused on several major areas, including:

Criminal Investigations

The IRS Criminal Investigation (CI) organization focuses on important national law enforcement priorities such as refund fraud, tax-related identity theft, unscrupulous return preparers and employment taxes, as well as money laundering, currency violations and terrorist financing, all of which adversely affect tax administration. During FY 2019, CI investigators:

- Completed 2,797 criminal investigations;
- Achieved 1,735 convictions with a conviction rate of 91.2 percent and

18

- Achieved a Department of Justice case acceptance rate of 93.0 percent and a U.S. Attorney case acceptance rate of 88.5 percent, which compares favorably with other federal law enforcement agencies.

The IRS's Questionable Refund Program identifies schemes that involve individuals that use genuine identities for the purpose of preparing and filing fictitious tax returns to generate fraudulent claims for refund. Questionable Refund Program figures include identity theft and non-identity theft-related Questionable Refund Program schemes. FY 2019 Questionable Refund Program performance results included:

- Initiated 65 criminal investigations
- Completed 140 criminal investigations
- Achieved 167 convictions with a 91.8 percent conviction rate
- Achieved a 66.7 percent Publicity Rate on adjudicated investigations

In FY 2019, the IRS Scheme Development Centers identified 46 Questionable Refund Program schemes comprised of 10,160 individual tax returns with more than $83 million in potentially fraudulent refund claims.

Through its Return Preparer Program, the IRS encourages compliance in the return preparer community by engaging in enforcement strategies targeting untrustworthy or incompetent return preparers. These strategies include education, outreach, and coordinated cross-functional publicity. FY 2019 Return Preparer Program performance results included:

- Initiated 163 criminal investigations
- Completed 295 criminal investigations
- Achieved 147 convictions with a 94.8 percent conviction rate
- Achieved a 73.4 percent publicity rate
- Identified 212 schemes, comprised of 119,165 individual tax returns with more than $475 million in potentially fraudulent refund claims.

International Tax Compliance

Stopping offshore noncompliance continues to be a very high priority for the IRS. In 2018, the IRS closed its Offshore Voluntary Disclosure Program, under which taxpayers made more than 57,000 disclosures, and the IRS collected more than $11.9 billion. In the post-Offshore Voluntary Disclosure Program environment, taxpayers without criminal exposure still have the option of filing a delinquent or amended return to correct tax and reporting noncompliance. In November 2018, the IRS issued interim guidance on procedures for voluntary disclosures in the post-Offshore Voluntary Disclosure Program world. These procedures provide a path for taxpayers with criminal exposure to come into compliance with the law and potentially avoid criminal prosecution.

Large Businesses: Campaigns

Since 2017, the IRS has used a "compliance campaign" process to identify areas of risk that require a response in the form of one or more treatment streams to achieve compliance objectives. This approach leverages resources and IRS knowledge, deploying the right resources to address the right issues. The IRS continues to refine its issue-based strategy approach, designed to ensure that examination programs are focused on the highest priority compliance areas to promote effective tax administration. During FY 2019, the IRS announced nine additional campaigns, bringing the total number of campaigns to more than 50. The IRS continues to evaluate and implement changes to improve its other workload selection processes to ensure that the highest compliance-risk tax returns and issues are identified and assigned for examination.

Employment Tax

Payroll taxes withheld by employers account for nearly 72 percent of all revenue collected by the IRS, making noncompliance and fraud in this area one of the biggest challenges for the nation's tax system.

In FY 2019, the IRS engaged in a special two-week effort to address this area of noncompliance. During this period, IRS revenue officers visited nearly 100 businesses around the country suspected of having serious issues with employment tax compliance. Business owners were informed about ways to catch up with back payroll taxes, how to stay current, and the potential for civil and criminal penalties. On the criminal enforcement side, the IRS worked with the Department of Justice Tax Division and U.S. attorneys around the nation to focus on about 50 law enforcement actions related to employment tax crimes. During these two weeks, the IRS indicted 12 individuals, executed four search warrants, and saw six individuals or businesses sentenced for crimes associated with payroll taxes. In addition to these numbers, roughly 24 or more enforcement actions were planned in the weeks following the campaign.

Tax-Related Identity Theft

The IRS has a comprehensive and aggressive identity theft strategy to assist taxpayers, protect revenue, and prevent refund fraud. It continues to seek opportunities to realize efficiencies and improve the taxpayer experience.

The IRS's key indicators of identity theft on tax returns have dropped significantly at a time when many in the private sector continue to struggle with this issue. Between 2015 and 2018:

- The number of taxpayers who reported to the IRS that they were victims of identity theft fell 71 percent. In 2018, the IRS received 199,000 identity theft affidavits from taxpayers compared to 677,000 in 2015. This was the third consecutive year this number declined.
- The number of confirmed identity theft returns stopped by the IRS declined by 54 percent, falling from 1.4 million in 2015 to 649,000 in 2018.
- The number of suspicious refunds recovered has declined by 66 percent. In 2018, financial institutions recovered 84,000 federal refunds totaling $112 million for the IRS. By comparison, institutions recovered 249,000 refunds totaling $852 million in 2015.

Even with all this progress, the IRS is continuing its efforts against tax-related identity theft and is concerned that identity thieves continue to become more sophisticated, continuing to look for new ways of obtaining taxpayer data so they can more easily file false tax returns and claim fraudulent refunds. These criminals have the resources, the technology and the tax skills to carry on this fight. And the IRS continues to be concerned that identity thieves are targeting tax professionals, businesses, human resources departments and other places because they have large amounts of sensitive financial information.

Private Debt Collection

During FY 2019, the IRS continued to see increased collections under the Private Debt Collection program, which began in 2017. Under the program, the IRS assigns certain overdue federal tax accounts to one of four private-sector collection agencies.

Since the start of the program, the private collection agencies have assisted almost 200,000 taxpayers who either established a payment arrangement or paid their account in full. The IRS assigned more than 2.4 million cases to private collection agencies totaling more than $22.5 billion of balances due. The program also brought in $301.7 million in revenue. Since June 2018, the total program revenue continues to exceed program costs. Using a percentage of the collected revenue, the IRS hired 100 Special Compliance Personnel employees to work in the Automated Collection System organization.

In June 2019, the IRS began assigning inactive business accounts to private collection agencies. Business accounts include delinquent balances owed by corporations, partnerships, and limited liability companies, as well as employment tax and excise tax delinquencies. The addition of business accounts to the program means that many more taxpayers will be contacted to resolve their tax bills.

Abusive Tax Shelters

To help increase compliance, the IRS is focusing on several special areas in its enforcement activities - one of which involves abusive tax shelters. The IRS is committed to pursuing those who promote and make use of such schemes. Abusive shelters, in fact, made the IRS annual list of "Dirty Dozen" tax scams that taxpayers are urged to avoid, and they will remain a major focal point for enforcement efforts in 2020. The IRS is especially concerned about three major variations:

- **Abusive trust arrangements**, which often use multiple layers of trusts – as well as offshore shell entities that are disregarded for tax purposes – to attempt to hide the true ownership of assets and income, or to disguise the substance of transactions.
- **Micro-captive insurance shelters**, in which promoters of these transactions persuade owners of closely held entities to participate in schemes that take advantage of certain tax benefits available to insurance companies, even though the entities lack many of the attributes of insurance.
- **Syndicated conservation easements**, which purport to give investors the opportunity to obtain charitable deductions, even though the tax benefits the investors receive significantly exceed the amount they have invested.

Emerging Issues

The IRS also has new and emerging compliance areas that require attention, including crypto/virtual currency and the sharing or "gig" economy. Along with enforcement activities, the IRS is providing outreach and education to both areas.

- **Sharing economy**. The rise in online platforms that allow people to provide a wide range of goods and services – everything from renting out a spare bedroom to providing car rides – has also given rise to tax issues. People participating in the sharing economy may be unaware of the taxes they might owe or records they should keep, and they may need the IRS's help to make sure they are tax compliant. IRS efforts to raise public awareness about this emerging area include creating a special Sharing Economy Tax Center on IRS.gov with a wealth of information to help people understand their tax responsibilities, as well as expanded outreach efforts with companies active in the sharing economy.

- **Virtual currency**. The IRS has been working to ensure taxpayers with virtual currency transactions understand and meet their tax obligations. In 2019, the IRS sent educational letters to more than 10,000 taxpayers who may have failed to properly report virtual currency transactions. The letters explained the tax obligations associated with virtual currency and describe how taxpayers can correct past filing and reporting errors. Virtual currency, also called crypto currency, will remain an important focal point for the IRS in 2020.

Key Performance Data Highlights

Performance Measure	Target	Actual
Examination Coverage – Individual (1040)	0.5%	0.45%
Examination Coverage – Business (assets >$10M)	2.2%	1.6%
Examination Efficiency – Individual (1040)	122	109
Automated Underreporter (AUR) Coverage	1.6%	1.3%
Collection Coverage	40.1%	41.3%
Time to Start Compliance Resolution[1]	Indicator	N/A
Time to Resolve Compliance Issue After Filing (days) [1]	Indicator	N/A
Repeat Noncompliance Rate[1]	Indicator	N/A
Cost to Collect $100 (in cents)[1, *]	Indicator	N/A
Criminal Investigations Completed	2,800	2,797
Conviction Rate	92.0%	91.2%

1. New measure added for FY 2019 reporting.

* Results for Cost to Collect $100 are not available until after the beginning of the calendar year

Collaborate with external partners proactively to improve tax administration

To support the nation's tax system, the IRS must work with partners inside and outside the tax community to improve service and outreach to taxpayers, enhance collaboration and share leading practices.

The IRS is committed to strengthening and expanding its partnerships with stakeholders invested in and affected by tax administration. Outreach efforts also work in coordination with IRS communications to share information with taxpayers across the nation.

Expanded Outreach Efforts with Partners

To run and operate the nation's tax system, the IRS must work closely with a variety of partner groups across the tax system. This ranges from private-sector partners in the tax professional and software communities to government partners in state revenue agencies.

In 2019, the IRS worked with more than 500 tax practitioner organizations, 85 payroll organizations, more than 1,000 industry partners and about 250 government partners across 50 states. More than 1,000 separate events occurred in all 50 states, with participants receiving the latest in tax law information. The IRS also expanded virtual webinars in 2019 to reach more in the tax community on issues ranging from tax reform, tax scams and disaster relief issues. In all, the IRS presented 30 webinars in FY 2019 with more than 113,000 participants, up from 24 in FY 2018 when about 62,000 attended.

The IRS also works closely with groups outside of the traditional tax community, such as small business groups and others, representing a spectrum of taxpayers, businesses and tax-exempt groups.

During FY 2019, the IRS took additional steps to reach groups outside of the tax community to help share information with key communities. The goal is to provide a direct, interactive line of contact, while sharing real-time relevant tax information of interest to their employees, members or customers and business entities. Some of the topics included filing season readiness, tax scams, TCJA and other topics.

By the end of FY 2019, the IRS had reached out to more than 125 different groups - representing hundreds of millions of taxpayers – covering educational institutions, retail, financial institutions, sharing economy platforms, transportation industry, small businesses, government-related associations and large employers. The IRS formed 36 new relationships with special emphasis placed on reaching out to the underserved, millennials, and those who speak English as a second language.

The IRS also focused on the sharing/gig economy and provided input to the IRS Sharing Economy Strategy Team following interactions with nearly a dozen major companies active in the sharing economy. The IRS also shared information with groups active in the cash economy community to help raise taxpayer awareness about tax responsibilities.

National and Local Partners

To help support the filing season, the IRS fosters and maintains relationships with a variety of partners – including community-based non-profits, schools, churches, corporations, employee organizations – to provide taxpayers with:

- Free federal and state income tax preparation and filing through the Volunteer Income Tax Assistance/Tax Counseling for the Elderly program
- Information and services surrounding Financial Education and Asset Building, such as Individual Development Accounts, credit counseling and repair, information on savings bonds, etc.
- Information on tax filing responsibilities and understanding refundable credits such as the Earned Income Tax Credit

The IRS uses a leveraged approach to accomplish its goals by partnering with national and local partners who deliver most of the programs and services. More than three million taxpayers are served annually through Volunteer Income Tax Assistance/Tax Credit for the Elderly alone.

The IRS's partners were instrumental in ensuring a successful FY 2019 filing season, especially with the implementation of the tax law changes related to the TCJA and the lingering effects of the government shutdown.

Security Summit

The IRS continued its partnership with the Security Summit to implement measures to prevent and detect identity theft-related refund fraud. The IRS held its annual Security Summit meeting in December 2018. The Security Summit continues to demonstrate the strength of the public-private partnership. Representatives from industry, state tax agencies, the IRS, and key stakeholders associated with the tax ecosystem met to get updates on the collective efforts to combat identity theft. Membership in the Security Summit continues to grow and now includes representatives from the payroll industry.

The IRS continues to work with the Security Summit Communications Workgroup to leverage partnerships across the tax community to more efficiently monitor the ecosystem, provide outreach, and educate the tax community. The IRS also continues to work with the Electronic Tax Administration Advisory Committee on their recommendations related to the Security Summit and Information Sharing & Analysis Center, and to implement where appropriate/applicable.

A major highlight of this year's Security Summit's work was Tax Security Awareness Week, which was held in December. This marked the fourth year in a row for the program where the IRS, the states and private-sector partners participated in events across the country to remind taxpayers about the importance of data security in advance of the busy online shopping season and the 2019 filing season. This year's session featured a daily series of national news releases and 36 press conferences and partner events across the country. The efforts led to hundreds of web articles and social media postings.

During the summer, Summit partnering continued education efforts aimed at the tax professional community to encourage them to think more about client data security. The effort started in 2016 with the "Protect Your Clients – Protect Yourself" campaign. To continue this effort, the 2019 campaign focused on the "Taxes-Security-Together Checklist." The checklist is a good starting point that spells out the basic steps every tax practitioner should be aware of to help protect the sensitive tax data they handle. The effort included a six-week series of news releases as well as continuing education sessions for tax professionals at the five major IRS Nationwide Tax Forums.

IRS Nationwide Tax Forums

The IRS Nationwide Tax Forums focused on sharing information and providing continuing education credits to more than 11,000 tax professionals in 2019. Each attendee could earn up to 19 continuing education credits during the session. Tax Reform and Section 199A continued to be popular seminars, as were Security Summit sessions related to data security, including "Cybersecurity for Tax Professionals," sponsored by the American Coalition for Taxpayer Rights. New in 2019, the Forums hosted two special cross-cultural discussions focused on Spanish language issues in the tax community and a session on "Overcoming Language & Cultural Barriers in the Tax Preparation Industry."

Preparer Tax Identification Number (PTIN) Registration

The IRS continued to be active on issues related to Preparer Tax Identification Number (PTIN) issues. Language was added to the PTIN registration and renewal "Welcome" letters encouraging tax return preparers to subscribe to e-News for Tax Professionals to ensure return preparers know where to get the most updated information on data and security issues. In addition, the PTIN application has been modified for the 2020 registration and renewal cycle to include language on preparer obligations to maintain data and system security.

Communicating with Taxpayers: Filing Season and Beyond

Another way the IRS serves taxpayers is through its communication efforts, which partners closely with IRS outreach efforts. The IRS is sharing information with taxpayers in new and evolving ways to keep up with taxpayer preferences and with changes in the communications landscape. The IRS is increasing its presence on social media to share information on tax law changes, alert taxpayers to scams, and to let people know about IRS products and services.

Throughout the 2019 filing season, the IRS communicated and conducted outreach about TCJA, Individual Taxpayer Identification Number renewals, changes to personal casualty losses and individual shared responsibility payments, as well as the Protecting Americans from Tax Hikes (PATH) Act of 2015, which requires the IRS to hold refunds on all returns claiming EITC and/or the Additional Child Tax Credit until February 15 of each year. For 2019, the IRS held 10.7 million returns with $57.8 billion in refunds.

In FY 2019, the IRS again promoted its web-first service delivery strategy that encouraged all taxpayers to get the help they need through IRS.gov, IRS2Go, and other self-service or partner options. This allowed customer service employee resources to focus their attention on helping taxpayers with complex issues that required them to interact with the IRS on the phone or in person.

The IRS launched its 13th annual EITC Awareness Day on January 25, 2019. EITC Awareness Day is a one-day nationwide event designed to promote EITC to eligible taxpayers, including potentially-eligible taxpayers who did not claim the credit and newly eligible workers. Due to the government shutdown, Awareness Day communications were limited to social media activity and sharing social media posts.

In addition, the IRS updated content on the IRS.gov EITC Central web page and updated the Due Diligence Online Training Module. The Due Diligence Online Training Module, which is part of the Tax Preparer Toolkit, educates preparers on their due diligence requirements. To assist taxpayers selected for examination for EITC-related issues, the IRS launched the Form 886-H-EIC, *Documents You Need to Send to Claim the Earned Income Credit on the Basis of a Qualifying Child or Children*, Toolkit on IRS.gov. The Toolkit is an online tool that helps the taxpayer identify the documentation needed to verify their EITC eligibility.

Social Media Growth Continues

As part of the IRS commitment to communicate information broadly, efforts continued to share more information via social media channels in FY 2019. In addition to supporting filing season efforts for individual taxpayers, the IRS continued using social media to share details focused on tax scams, small businesses, natural disaster preparedness and many other topics.

As part of this effort, the IRS launched its first Instagram account called IRSnews in November 2018. The creative graphics used by the IRS on the platform earned praise from partners and taxpayers for offering a fresh look at tax issues. In FY 2019, more than 10,000 people started following the IRS Instagram account.

The IRS also saw growth in other social media platforms. Twitter's @IRSnews topped 108,000 followers, almost a 10 percent increase from a year before. Facebook followers grew to 125,000 The IRS channels on YouTube received 1.8M combined views followers, a 45 percent increase. And LinkedIn grew to 86,000 followers, a 49 percent increase. The IRS channels on YouTube received 1.8 million combined views.

The IRS also took steps to enhance its e-news list-serve products following a recommendation from the Internal Revenue Service Advisory Committee. In 2019, the e-News subscription service was revamped and streamlined to offer several benefits including an easier subscription process and improved content for users tailored by topic. The redesign effort removed 11 subscriptions, leaving 20 core subscriptions focused on issues such as tax tips and e-news for tax professionals. In all, 183,102 new subscribers were added in FY 2019, bringing the total number of subscribers to 2.47 million.

Partnering with Foreign Government to Improve Tax Administration

One of the IRS's strategic goals is to expand partnerships with foreign governments and international organizations to address global tax administration concerns. The IRS is achieving this goal through its many interactions with two international organizations, the Inter-American Center of Tax Administrations (in Spanish, Centro Interamericano de Administraciones Tributarias) and the Organization for Economic Cooperation and Development.

The IRS supports the Centro Interamericano de Administraciones Tributarias's efforts to promote international cooperation and the exchange of experiences and know-how, thus contributing to the strengthening of the tax administrations of all Centro Interamericano de Administraciones Tributarias' member countries. Centro Interamericano de Administraciones Tributarias is a regional tax organization focusing primarily, but not exclusively, on countries in North, Central, and South America and the Caribbean. The IRS supports this organization through its active participation in two annual conferences where countries share their experiences and best practices on designated topics. The IRS participation in Centro Interamericano de Administraciones Tributarias raises international standards for all aspects of tax administration, including compliance, taxpayer service, and ethical conduct.

At the Organization for Economic Cooperation and Development, the IRS is an active member of the Forum on Tax Administration. The Forum on Tax Administration's key aim is to improve taxpayer service and tax compliance by helping tax administrations increase the efficiency, effectiveness and fairness of tax administration and reduce the costs of compliance. While the IRS participates in most Forum on Tax Administration projects, efforts have been particularly significant in the following areas:

- The IRS chairs the Mutual Agreement Procedure Forum, which provides a venue for tax administrations to collaborate to improve the processes for preventing and resolving treaty disputes.
- The International Compliance Assurance Program is a voluntary pilot, recently expanded to 17 countries, operating as a co-operative risk assessment and assurance process through which taxpayers may achieve greater tax certainty in less time through simultaneous interaction with multiple tax administrations.
- The IRS co-leads the Comparative Risk Assessment Initiative, a project that focuses on analyzing how countries approach the task of assessing compliance risks, developing a common vocabulary for discussing such risks, working toward the longer-term goal of mapping areas of convergence and divergence of perspectives and, ultimately, seeking to reach common understandings of which tax issues present relatively lower and higher risk across jurisdictions.
- The Joint International Tax Shelter Information Collaboration program offers a platform to enable the IRS and other participating tax administrations to collaborate to address tax avoidance and other tax administration issues through exchanges of information within the established legal framework of bilateral and multilateral tax conventions and tax information exchange agreements.

Cultivate a well-equipped, diverse, flexible and engaged workforce

With IRS employees committed to serving the American taxpayer, the future of the IRS depends on a workplace culture that empowers employees to improve the taxpayer experience and uphold the tax code fairly. Enhanced skills development, succession planning, and knowledge transfer coupled with a forward-looking talent management strategy and modernized training are critical to passing on the leadership skills and institutional knowledge necessary for continued effective tax administration.

The IRS recognizes that its taxpayer service, enforcement and business modernization efforts require a strong workforce.

In FY 2019, the IRS hired 4,702 Enforcement positions including Revenue Agents, Customer Service Representatives, Tax Compliance Officers, and Revenue Officers. In support of TCJA the IRS also hired 6,873 positions to help with tax reform. TCJA hiring exceeded that of FY 2018 by 488 positions, with the greatest staff onboarding occurring in the pay periods prior to and immediately following the 2018-2019 partial government shutdown.

Employee Development/Training

The IRS continues to ensure its employees are provided training and developmental opportunities to meet their job obligations and career aspirations.

FY 2019 highlights include:

- The IRS continued to ensure its employees were provided training and developmental opportunities to meet their job obligations and career aspirations.
- The IRS conducted knowledge transfer sessions across key professions for ongoing development and knowledge capture prior to employee exits.
- The IRS continues to utilize the Leadership Succession Review for succession planning and knowledge transfer and revised Internal Revenue Manuals and other procedural guidance to provide the staff with updated work processes.

Knowledge Management

The IRS actively participates in the Federal Knowledge Management Community, which encourages engagement among agencies to improve KM practices across the federal government.

The IRS achieved continued success in expanding the program including:

- Established more than 36 active Knowledge Bases in the Virtual Library, created by 12 participating business units, with an additional 23 Knowledge Bases in development. The Virtual Library sites received more than 1.7 million views in the last two years.

- Established and supported 42 cross-functional Communities of Practice, which encourage members to share ideas and resources. Ten business units and six cross-functional teams facilitate Communities of Practice organized around tax administration, information technology, content development, budget, and project management topics.
- Developed and tested Knowledge Management executive metrics dashboard and benchmarked potential use of Artificial Intelligence/Robotics Process Automation for automated Knowledge Management use case reporting.
- Enhanced Knowledge Management initiatives and processes through the Virtual Library Content Contributor Tool upgrade, which streamlined the process and reduced article publication timeframes.

The IRS enterprise-wide Knowledge Management program received multiple awards and recognitions as well as partnerships with industry leaders and peer federal agencies:

- The Self-Help Online Tutorial library, which houses more than 300 videos, received more than 132,000 views internally and was awarded the "Five-Star Award" by the Federal Government Distance Learning Association. Two Self-Help Online Tutorial videos were featured on the IRS YouTube Channel for global access.
- In April 2019, the IRS received the "Excellence in KM Award" for achieving an "Enterprise 3 Level" at the American Productivity and Quality Center's Knowledge Management Conference for overall program maturity.

Talent Management

Mission Critical Occupations losses have exceeded hiring for several years and the new Authorized Staffing Plan allowed additional hiring in FY 2019. Until this year, the IRS operated under an exception-only hiring policy since December 2010 to address annual declining IRS appropriations. Restrictions on hiring, travel, contractor support, administrative costs, and training allowed the IRS to operate within its appropriated budget.

In March 2019, the IRS issued a streamlined hiring and recruiting process that allowed internal organizations flexibility to manage their staffing levels within approved limits. Since then, businesses have been announcing positions and recruiting and hiring multi-generational individuals, as well as conducting necessary enforcement and program travel and delivering training. Guidance for FY 2020 will depend on what appropriated levels can support, especially considering unplanned pay raises and the recent increase in the government's contribution to the Federal Employees Retirement System.

Advance data access, usability and analytics to inform decision-making and improve operational outcomes

The IRS strives to operate more efficiently to provide superior service to taxpayers and their representatives and ensure successful implementation of changes in tax laws. Using analytics, the IRS works continuously to improve all facets of its operations - taxpayer service, enforcement efforts and a range of internal operations.

This fiscal year, the IRS:

- Delivered an updated Enterprise Research Plan. The second version of the Enterprise Research Plan provided the most significant research initiatives supporting the 2018-2022 IRS Strategic Plan. The document identified critically important projects, programs, and infrastructure advances from the IRS research community in terms of potential effect, resources and costs, and stakeholder awareness. Each selected project was aligned to one of the six goals of the IRS Strategic Plan.

- Expanded the new data and analytics steering group created to improve coordination, decision-making, and alignment of data and analytics initiatives across business units. Charters were established for the Data & Analytics Strategic Integration Board and the Data & Analytics Advisory Group. Two sub-councils were also launched in FY 2019 from this initiative, including the Data Council and Analytics & Tools Council.

- Created an IRS Learning Agenda working group.
    - By establishing a Learning Agenda, the IRS will be able to incorporate new "evidence" needed to make better decisions to meet the changing needs and expectations of taxpayers and members of the tax community who serve taxpayers.
    - The Learning Agenda working group will be initiating conversations and discussions with relevant stakeholders over the next few months to identify the key policy-relevant questions for which the agency intends to develop evidence to support policymaking. The group will also determine what data the agency intends to collect, use, or acquire to facilitate the use of evidence in policymaking and define which methods and analytical approaches will be used to develop evidence to support policymaking.

Taxpayer Service

Improving Performance Objectives in Taxpayer Assistance Centers

The IRS has taken steps to establish and implement clear program performance objectives and metrics aligned with organizational goals. This achieves desired results by using analytical tools and reporting mechanisms to communicate the goal of improving the efficiency in Taxpayer Assistance Centers. Without considering the lapse in appropriations, this has resulted in a 1.1 percentage point performance improvement. The Taxpayer Assistance Centers produced more direct time (face-to-face time with taxpayers) when compared to the same time last fiscal year.

The improvement equates to an additional 28,000 hours of time devoted to serving taxpayers in the Taxpayer Assistance Centers.

Field Assistance Scheduling Tool

Just in time for the filing season, the Field Assistance Scheduling Tool was enhanced with new features that increase performance and offer an optional feature that provides the taxpayer with an appointment confirmation/reminder email. Since implementation, through FY 2019, the IRS sent nearly 1.2 million confirmation and reminder emails to taxpayers who scheduled appointments at Taxpayer Assistance Centers.

The Field Assistance Scheduling Tool team members are winners of several awards and recognitions. The most recent honor received was the 2018 Gears of Government Award, which showcases federal employees' pivotal roles in achieving a modern and effective government. This award also recognizes outstanding individuals and teams whose performance and dedication support exceptional delivery of key outcomes for the American people.

Partner Satisfaction Survey

Partner Burden and Volunteer Recruitment Teams were created to address feedback from the Partner Satisfaction Survey. Each year, the IRS and the Partner Burden and Volunteer Recruitment teams review the survey results to determine if the feedback warrants any changes to processes and procedures. In addition to the formalized actions recommended by these teams, the survey results are shared with employees. In FY 2019, changes implemented based on this feedback directly resulted in improvements in the Volunteer Income Tax Assistance program.

Integrated Automation Technologies

Integrated Automation Technologies recently celebrated its 10-year anniversary, surpassing one billion tool uses by IRS employees. The Integrated Automation Technologies tool simplifies taxpayer data processing by automating research and taxpayer account management within the Integrated Data Retrieval System. These tools save time, improve accuracy, and enhance employee satisfaction.

Employer Identification Number (EIN) Application Process

As part of ongoing security reviews, the IRS strengthened the requirements around the Employer Identification Number (EIN) application process. Form SS-4, *Application for Employer Identification Number*, and instructions were updated in December 2017 to only allow a natural person to be the responsible party when obtaining an EIN. However, due to programing constraints with the Online EIN Assistant, implementation was delayed until May 13, 2019. The change ensured domestic taxpayers would no longer have the option to use an EIN as the responsible party for obtaining an EIN. This change applies to EINs assigned via the Online EIN Assistant and mailed/faxed Forms SS-4. Governmental entities (federal, state, local, and tribal) are exempt from the responsible party requirement as well as the military, including state national guards. Since the update to the responsible party, the IRS has continued to successfully assign EINs via both the Online EIN Assistant and mail/faxed applications with no effect to the overall assignment of EINs.

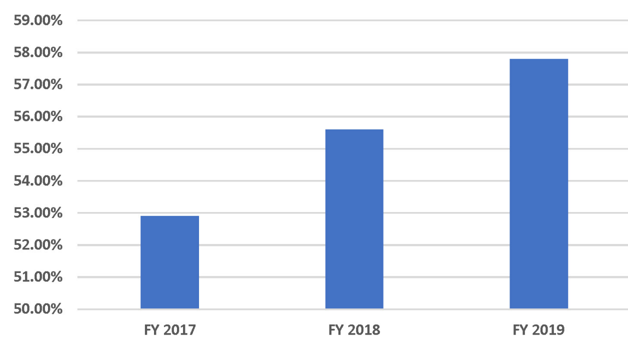
In addition, the IRS focused on developing a process to authenticate foreign individuals applying for an EIN without a social security number/Individual Taxpayer Identification Number.

The IRS also issued a news release on March 27, 2019 advising external stakeholders of the upcoming changes to the EIN application process. These changes also were explained in e-News for Tax Professionals, e-News for Small Business, and e-News for Large Taxpayers (businesses). Also, messaging was shared in a briefing provided to Senate Finance Committee staff on April 17.

E-File Employment Tax Returns

Employment tax returns are the second largest population of returns, and therefore provide the best opportunity for growth in electronic filing. The IRS redesigned the 94X e-file landing page on IRS.gov and held a forum with payroll industry partners. In FY 2019, the IRS processed 29.0 million business returns electronically, which includes roughly 14.7 million e-filed employment tax returns, an increase of 8.6 percent from 2018.

E-File Rate – Business



Enrollment Toll-Free Telephone Line

The IRS analyzed the volume and timing of calls made to the Office of Enrollment toll-free telephone line in FY 2018 and determined that staffing to cover the telephones needed to be increased and realigned. These changes resulted in improved phone coverage and increased the LOS from 74 percent at the end of FY 2018 to 82 percent at the end of FY 2019. The IRS Office of Enrollment administers the enrolled practitioner program; specifically, the office oversees enrolled agents and enrolled retirement plan agents, who are authorized to represent taxpayers before the IRS.

Enforcement

Large Business Returns

The IRS's efforts to improve its selection processes for complex and large business returns is ongoing. As a result of those continued efforts, the IRS decided to replace the Coordinated Industry Case Program with the Large Corporate Compliance Program. The Large Corporate Compliance Program uses advanced analytics, employing an array of value and transactional characteristics to define the population, replacing the labor-intensive, burdensome manual pointing process of the Coordinated Industry Case Program. The Large Corporate Compliance Program then applies analytics and algorithms against that population to stratify the returns into risk tiers, with high-risk returns assigned to the field for potential examination. The IRS will continually monitor and update the process based on feedback and operational results.

Taxpayer Noncompliance Indicators

Graph data environments provide powerful tools for exploring and understanding relationships between entities in the tax ecosystem, including taxpayers, businesses, return preparers and personal devices. The IRS developed and deployed a graph database environment that currently supports nearly 3,300 users across the IRS, including field revenue agents and officers. Through a user-friendly interface, investigators and analysts can quickly access information to identify indicators of taxpayer noncompliance thereby leading to more efficient and actionable investigations. The graph data environment also supports identity theft detection and efforts are underway to develop a graph data set to identify changes in the tax structures of large corporations more easily.

Examination Planning Scenario Tool

The IRS developed the Examination Planning Scenario Tool to improve its use of data and analytics in the examination work planning arena. The tool employs a data-driven approach to generate and evaluate optimal, executable audit plans that improve business outcomes through incorporation of predictive analytical models. These models, balanced with policies and prioritization rules, help IRS managers make data-driven decisions to identify the next best case to assign.

Customer Accuracy Rate

The IRS conducts regular quality reviews of call center operations for three of its contractors who are contractually required to maintain a Customer Accuracy rate of at least 90 percent. Two of the contractors' rates fell below the 90 percent target near the beginning of FY 2019. To prevent future errors and increase quality rates, the IRS identified the most common errors and error trends and provided suggestions for improvement. The IRS also provided a desk guide to one of the contractors, describing how calls are evaluated and included examples of errors that affect accuracy rates. As of September 30, 2019, both contractors' Customer Accuracy rates had reached 90 percent.

Work Selection

The IRS continually seeks to advance data and analytics to drive decisions in identifying and addressing existing and emerging high-risk areas of noncompliance. This strategy allows the IRS to optimize the resources of these problem areas. The IRS partnered on data-driven approaches using historical examination results and return data in queries to select work based on quantitative criteria. Managers and analysts are being given broader access to different types of software, and ecosystem maps and service design blueprints for use as visual tools to make it easier to identify opportunities to enhance IRS operations.

Examination Workstreams

The IRS analyzed data (e.g. partnership filings, return preparers, non-filers) associated with various examination workstreams to refine return selection models. The IRS successfully imported Financial Crimes Enforcement Network (a bureau of the Department of the Treasury) data into the IRS's Compliance Data Warehouse to improve analytical capabilities. The Financial Crimes Enforcement Network's new search engine provides a modernized IT foundation to better collect, store, safeguard, analyze and share data with the IRS as well as other federal, state and local law enforcement authorities.

The IRS continues to test and advance the Exam Planning Scenario Tool to select the most productive work to maximize limited resources. The IRS also developed simulation models to identify process improvements as well as conduct virtual experiments of process changes without affecting current case processing. The first simulation focused on Automated Underreporting to reduce processing bottlenecks and establish work plans for tax return examination to enable optimal performance levels.

Taxpayer Behavior Models

The IRS uses statistical models to help predict future taxpayer behavior, including how much of a balance due owed by a taxpayer will be collected over time, whether a case is likely to be resolved by full payment or via an installment agreement, or if a currently uncollectible determination is likely.

Building upon existing research, the IRS is using behavioral insights to redesign notices and develop new forms of outreach to help taxpayers satisfy their tax obligations. Being able to predict taxpayer behavior using statistical models helps improve the likelihood of a desired outcome by matching the outreach to a given taxpayer's characteristics.

The IRS is better able to efficiently use limited resources to accomplish tax administration goals such as fairness, reducing taxpayer burden, revenue collection, and ensuring compliance through the judicious use of these data analytic techniques.

Program Assessment Optimization Model

The Program Assessment Optimization Model assesses the business effects of potential staffing placement decisions. The current model parameters are set to maximize collected revenue; however, further model development will enable additional parameters. This model was used to provide hiring placement guidance to IRS Executives for the FY 2019 Compliance hiring initiative and will be used for FY 2020 hiring.

Internal Operations

Information Technology

The IRS continues to harness advanced analytical approaches to make data-driven decisions. In FY 2019, new approaches were used not only to improve visibility into the health of information technology operations but also create a centralized repository for key reporting measures applicable to information technology. The IRS built a set of interactive new dashboards to improve its ability to monitor and visualize key information technology metrics, such as the percentage of aged hardware, the status and composition of the information technology workforce, and the status of any critical service disruptions. Using these tools, the IRS is better able to address strategic issues using key measures and indicators that allow for more informed decision-making.

The IRS also made strides in another analytical effort to better inform information technology decision-making - Technology Business Management. Through the Technology Business Management initiative, the IRS now has a better perspective on the types of services and support needed throughout the Service, which permits a more efficient allocation of its more than $2.7 billion information technology budget. Technology Business Management lets the IRS better evaluate cost and spending data, as well as helps the IRS to provide greater transparency into its financial activity with year-over-year trending analysis and other benchmarking.

Together, these data analytic initiatives help to articulate the purpose and results of spending across the information technology portfolio.

Customer Online Experience

New legislation and government requirements call for improvements to government Customer Experience and specifically, digital services. Collectively they require consistent experiences informed by customer feedback and research. Pursuant to these goals, the IRS updated its IRS.gov site survey and OLA site survey. These updates offer greater insight into customer perceptions of satisfaction, ease of task completion, service quality, service efficiency, and confidence in the IRS. Both survey updates were introduced during annual tax filing season; responses to satisfaction surveys tend to follow strong seasonal patterns and baseline data is still being established.

Human Capital

The IRS continues to research and identify automation tools to promote effective and efficient program management and service delivery. From creating a data warehouse for human resources data collection and reporting systems to Enterprise Case Management, the IRS continues its commitment to modernization and operational efficiency.

The Integrated Talent Management system is a single, integrated information system made up of modules that support multiple human capital business processes. This Treasury system integrates competency-based human resource processes by providing a common interface, workflow, and cross-process reporting and analytics. The IRS implemented a performance management module for executives in 2019 and will implement an IRS learning module in early FY 2020, followed by employee performance management, workforce planning and succession planning capabilities.

Drive increased agility, efficiency, effectiveness and security in IRS operations

The IRS is continuing to find ways to streamline and simplify processes and manage expenses to make operations more cost effective, a task necessary for sound financial stewardship – all the while remaining dedicated to maintaining the physical and digital security of its systems and taxpayer information, enhancing internal controls, managing risks, and upholding accountability.

Modernizing the IRS

The IRS believes the key to achieving increased agility, efficiency, effectiveness and security is to modernize the IRS. Modernization is vital to all core functions: serving taxpayers, delivering the filing season, and enforcing tax laws. The IRS has already made major progress to improve systems and upgrade service to taxpayers in recent years. For example, efforts to phase out old equipment, have reduced the percent of aged computer hardware from 52.3 percent in FY 2017 to 45.5 percent in FY 2018 and 31 percent in FY 2019. But to ensure the IRS can fulfill the mission over the long term, more needs to be done, including updates to legacy computing infrastructure and business operations.

To put the IRS on the right path, during FY 2019 the agency released its Integrated Modernization Business Plan for the agency. It provides a six-year roadmap for modernizing IRS systems and taxpayer services. The plan outlines a bold strategy to enable business transformation that is focused on improving services for taxpayers and the tax community, while protecting taxpayer data.

This plan envisions real, visible results for the taxpayer and the tax system. Modernizing the IRS will greatly improve the experience that taxpayers, businesses, exempt organizations, tax professionals and others have with the agency.

The IRS believes modernization will improve how taxpayers interact with the IRS, whether filing a return, receiving a refund or paying a tax bill. It will change the interaction between IRS employees and taxpayers or their representatives, and all for the better. With better technology, the IRS will be able to accomplish much more, in less time, and provide better across-the-board service. The IRS is working toward the best-in-class service that is equivalent to what people receive when they contact an online retailer or place a single call to a financial institution and obtain a wide range of services. A few examples of what the IRS modernization plan calls for:

- Longer term, taxpayers will have shorter waits on the phone and see their cases resolved sooner.
- An expanded customer callback feature, so taxpayers will have the option of receiving a call back to avoid waiting on hold.
- For victims of identity theft or instances where there are questions about who is filing the tax return, the IRS will simplify identity verification to expand access to online services while safeguarding data.

- More online account options to make it easier for taxpayers to share documents and information when there is an issue with a tax return that needs to be resolved, bringing the IRS in step with the best practices found in the financial sector.
- A more efficient process for implementing required technology changes due to new tax provisions, which requires a lot of lead time and behind the scenes work by IRS employees.

Another benefit of modernization is that, if the IRS were to more effectively serve taxpayers who prefer to interact with the IRS online, the agency would be able to free up resources to improve service on other channels, including over the phone and in person.

Ultimately, these efforts add up to an improved IRS that will help taxpayers, the tax community and the nation.

Cybersecurity

During FY 2019, the IRS continued working diligently to safeguard the security of its systems and taxpayer data, battling increasingly sophisticated and frequent efforts by cybercriminals to steal data, file fraudulent refunds, and infiltrate IRS systems. These attacks include 1.6 billion annually, which consist of denial-of-service attacks, unsuccessful intrusion attempts, probes or scans, and other unauthorized connectivity attempts. The IRS has increased monitoring, detection, and analytical capabilities to identify suspicious activity within its systems. These improvements have helped the IRS slow down identity thieves, but more is needed as reflected in the IRS Integrated Modernization Business Plan.

In FY 2019, the IRS detected and mitigated 2,534 phishing and malware sites and identified and responded to 147 cyber incidents, 104 of which involved common threats such as removable media, email, and web-based activity. The IRS also implemented 12,527 content filtering restrictions to mitigate internet content deemed a security risk to IRS information systems.

Additionally, IRS Cybersecurity penetration testing and the Department of Homeland Security's Security Architecture Reviews identified unrestricted network access as an IRS network vulnerability. To mitigate this vulnerability, the IRS is implementing a network access control solution that immediately blocks network access for all unauthorized devices and users. To date, the IRS is 100 percent complete for wireless and remote network access and 96 percent complete for wired in-office network access.

Space Consolidation

Another component of the IRS's efforts to streamline operations involves space consolidation. During FY 2019, the IRS continued to use data to select the best opportunities to release excess facility space by looking at the timing of expiring leases and planned General Services Administration renovation projects, and by analyzing IRS housing needs to plan building closures and consolidations. The IRS analyzed where limited funds should be spent, to minimize costs and capture the greatest returns on investment. As a result, in FY 2019, nine buildings and 450,000 square feet of space were released from the IRS portfolio.

Additionally, the IRS used telework and mobile work data to expand the number of offices that incorporate hoteling and shared workspace for employees and contractors who do not require full time space. During FY 2019, the IRS completed facility planning for the ramp down of the

Submission Processing operation in Covington, KY, and continued planning the future Fresno, CA submission processing ramp down in 2021.

Key Performance Data Highlights

Performance Measure	Target	Actual
Rentable Square Feet per Person	Indicator	298
Percent of Aged Hardware[1, *]	43.8%	31.0%
Percent of Major IT Investments within +/- 10 Percent Cost Variance at the Investment Level[2]	90.0%	88.9%
Percent of Major IT Investments within +/- 10 Percent Schedule Variance at the Investment Level[2]	90.0%	88.9%

1. The measure definition changed in FY 2018; removing certain asset categories (fax machines, low-end printers and scanners) that are no longer being actively refreshed from the calculation to more accurately define the inventory that's reflective of risk to the IT environment.
2. Starting in FY 2015, this measure includes all major IT investments (Business Systems Modernization (BSM) and non-BSM). In previous years, it included BSM only.

* New measure added for FY 2019 reporting.

Looking into the Future – Fiscal Year 2020

The core of the IRS's vision for the future is to enhance the taxpayer experience. In 2019, Congress passed the Taxpayer First Act, an act that is designed to improve taxpayer service and ensure that the IRS continues to enforce the tax laws in a fair, impartial manner.

Changes made by this new law will help the IRS and the nation's tax system move forward. During the next year and beyond, the IRS will be working diligently to implement this important new law, to improve the agency and the taxpayer experience.

Modernization is vital to IRS core functions: serving taxpayers, delivering the filing season and enforcing the tax laws. To ensure the IRS fulfills its mission over the long term, the IRS will need to update legacy computing infrastructure and business operations.

Modernization will improve interaction with the IRS, whether filing a return, receiving a refund or paying a tax bill. It will change the interaction between IRS employees and taxpayers or their representatives, and all for the better. With better technology, the IRS will be able to accomplish more, in less time, and provide better across-the-board service. Ultimately, working toward the sort of best-in-class service that is equivalent to what people get when they contact an online retailer or place one call to a financial institution and get a whole host of services taken care of.

These efforts add up to an improved IRS that will help taxpayers, the tax community and the nation.

Performance Results

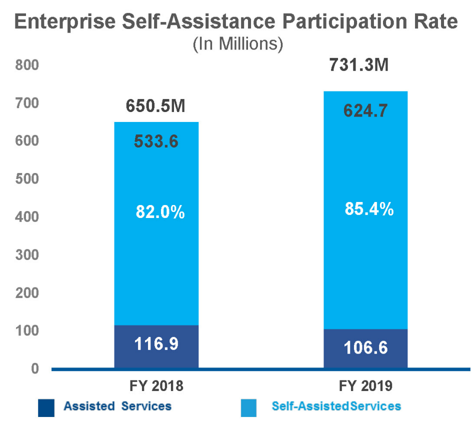
The IRS collects, analyzes and reports performance measures from business operations across the organization. The performance measures serve as metrics for organizational improvement and accountability and align to IRS strategic goals and objectives. The IRS reports its budget-level performance measures annually, providing transparency to internal and external stakeholders.

As part of the development of the FY 2018 – 2022 Strategic Plan, the IRS assessed its budget level measures and added six new measures, modified five existing measures, and discontinued 12 measures.

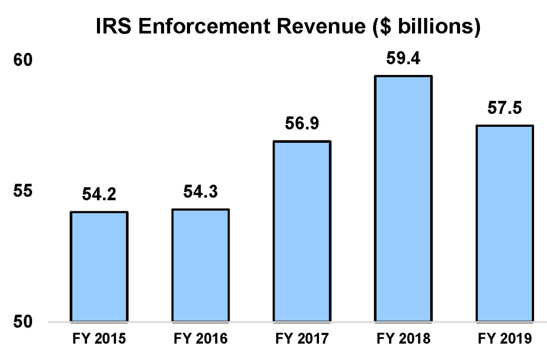
In FY 2019, the IRS tracked 23 budget-level measures, of which seven were indicators that had no targets. The IRS met or exceeded only 6 of 16 measures that had targets for a 38 percent success rate due, in part, to the 35-day government shutdown. Taxpayer Service ended the year achieving 67 percent of its targets (4 of 6), while Enforcement reached 14 percent (1 of 7) of its targets. For this fiscal year, the IRS met or exceeded the Cost and Schedule Variance on 89 percent (16 of 18) of the major IT investments and exceeded the Percent of Aged Hardware target by 29 percent to reach a final level of 31 percent.

The IRS continues to improve taxpayer services by developing and improving self-assistance tools and traditional services. In response to taxpayer preferences, the IRS also continued expanding secure digital communication options. The IRS measures progress toward improvement to taxpayer service by its Enterprise Self-Assistance Participation Rate metric.

The FY 2019 Enterprise Self-Assistance Participation Rate was 85.4 percent, exceeding the FY 2018 result by 4.1 percent. This is due in part to increases in Get Transcripts Online by 30 percent, "Where's My Refund?" by more than 19 percent, and Transcript Delivery Service by almost 31 percent. Compared to FY 2018, total services increased by 12.4 percent, self-assisted services increased by 17.1 percent and assisted services fell 6.5 percent. As the IRS provides new self-assistance applications to the public, the IRS will add them to the calculation.



Enhancing voluntary compliance is integral to the IRS strategic goal of Protecting the Integrity of the Tax System. Despite many challenges during the fiscal year, the IRS collected more than $57.5 billion in enforcement revenue in FY 2019, a 3.1 percent decrease compared to FY 2018.



Detailed information on performance measures is in Appendix A, Performance Measures Descriptions; Appendix B, Performance Measurement Data; Appendix C, Explanations of Shortfalls; and Appendix D, Strategic Plan Measures.

Financial Management Highlights

Financial Resources

The IRS's FY 2019 base appropriated level was $11.2 billion, an increase of about $115 million over FY 2018 enacted, excluding administrative provision Section 112 (an administrative provision of the IRS's appropriations bill supporting implementation of the Tax Cuts and Jobs Act).

Appropriation	FY 2018 Enacted	FY 2018 Operating Plan	FY 2019 Enacted	FY 2019 Operating Plan
Taxpayer Services	$ 2,506,554	$ 2,456,554	$ 2,491,554	$ 2,491,554
Enforcement	4,860,000	4,617,000	4,860,000	4,665,600
Operations Support	3,634,000	3,927,000	3,724,000	3,918,400
Business Systems Modernization	110,000	110,000	150,000	150,000
Subtotal	$ 11,110,554	$ 11,110,554	$ 11,225,554	$ 11,225,554
Tax Cuts and Jobs Act Implementation (Section 113/112)	320,000	320,000	77,000	77,000
Total Appropriated Resources	**$ 11,430,554**	**$ 11,430,554**	**$ 11,302,554**	**$ 11,302,554**

Note: The FY 2018 Operating Plan included transfer of up to $50 million from Taxpayer Services to Operations Support. The actual transfer was $13 million, resulting in final appropriation levels of $2.494 billion in Taxpayer Services and $3.898 billion in Operations Support.

In addition to the annually appropriated budget, IRS funding also included $1.4 billion from user fees, offsetting collections and unobligated balances from prior years. This raised the IRS's budget authority to $12.7 billion.

Unfortunately, the IRS continues to face resource challenges. The enacted level did not fully cover the cost of labor and non-labor inflationary increases of about $172 million. The IRS required about $86 million more for other mandatory labor increases, including career ladder promotions and step increases. The IRS absorbed these unfunded requirements by continuing to defer critical IT infrastructure refreshment, modernization and enhancement of IT systems, facilities projects, and with the annualized savings realized from executing an exception-only hiring policy over the last several years.

The IRS expects more than 35 percent of its workforce will be able to retire by FY 2021 and only 2 percent of the workforce is under 30 years old, creating a significant risk of a large knowledge and experience gap. Resource constraints coupled with an interruption in hiring efforts in late December due to the extended government shutdown have inhibited the IRS's ability to address this risk. Without the sustained ability to hire a workforce with a greater projected longevity, the IRS will have great difficulty developing the leaders it will need in five to ten years.

The IRS has shouldered these losses across the agency with effects to all program areas. Key enforcement personnel have declined by around 40 percent since FY 2010 to fewer than 14,000 employees. These employees include Revenue Agents and Revenue Officers who audit returns and perform collection activities; Special Agents in the IRS's Criminal Investigation organization who investigate stolen identity refund fraud and other tax-related crimes; and other staff who engage in critical compliance activities. Performance has declined in tandem with staffing losses, including the individual examination coverage rate, which has fallen from 0.9 percent in FY 2010 to 0.45 percent in FY 2019.

Support organizations including the HCO, CFO, and Procurement have seen declines of more than 20 percent since FY 2010. Decreased staffing levels in these critical support organizations intensify the risk of a large knowledge and experience gap by further limiting the ability to hire and train the workforce necessary to carry out the IRS's mission.

The IRS remains one of the most cost-effective investments in the federal government. Annually, on average the IRS enforcement programs collect more than $56 billion while annual spending on these programs including operations support costs is only about $5.5 billion, for an average return on investment (ROI) of about $10 for every $1 invested in IRS enforcement programs. This ROI estimate is likely understated because it does not include the revenue effect of the deterrence value of IRS enforcement programs or the effect of education and outreach on voluntary tax compliance.

The lack of Operations Support funding weakens the IRS's ability to address the increased information technology workload associated with identity theft, refund fraud, and improper payments. For the past few years, the IRS has experienced an increased demand for information technology projects and services, with significant resources going toward implementing unfunded legislative mandates passed since 2010. Examples of these mandates include the Foreign Account Tax Compliance Act, Affordable Care Act, Achieving a Better Life Experience Act, retroactive extension of the Health Care Tax Credit, Private Debt Collection, and to improve the identification and prevention of refund fraud and identity theft. This has severely limited the IRS's capacity to address other operational areas, including maintenance for newly-deployed information technology infrastructure. Continued underfunding of the IRS in the Operations Support and Modernization accounts threatens to erode its effectiveness and ability to be efficient.

Funding by Appropriation ($ thousands)

Taxpayer Services [$2,556,554, includes §112 allocation of $65,000] funds staffing for the processing of tax returns and related documents, and assistance for taxpayers in filing returns and paying taxes due.

Enforcement [$4,677,600, includes §112 allocation of $12,000 and an inter-appropriation transfer to Operations Support of $194,400] funds staffing for the examination of tax returns, collection of balances due, the administrative and judicial settlement of taxpayer appeals of examination findings, and provides resources for strengthening enforcement to reduce invalid claims and erroneous filings associated with the EITC program as well as other refundable tax credits.

Operations Support [$3,918,400, includes an inter-appropriation transfer of $194,400 from Enforcement] funds overall planning, direction, operations management and control, and critical infrastructure activities for the IRS. These activities include information technology and cybersecurity that keep tax systems running and protect taxpayer data, the financial management activities that ensure effective stewardship of the nation's revenues, and the physical infrastructure and security that helps keep IRS employees and customers safe and well served in office, campus, and TAC sites. Human resource, telecommunications, and communications infrastructure are also critical components of this appropriation and are vital to maintaining adequate levels of customer service and the post-filing processes that ensure the tax system's fairness and equity.

Business Systems Modernization [$150,000] funds capital asset acquisitions of information technology to modernize key tax administration systems.

In addition to the core appropriations, the IRS has the following appropriations (special funds): **Other Resources: User Fees** [$392,759] from payment for services provided and [$513,433] from prior year balances brought forward October 1, **Offsetting Collections Resources** [$134,308], **Unobligated Balance Transferred In** (50 percent Carryover) [$10,389], and **Unobligated Balances** [$358,638] brought forward October 1.

In FY 2019, the IRS transferred to the Operations Support account, with Congressional approval, $194.4 million from the Enforcement account. This late-in-the-year funds transfer reflects an imbalance of appropriated resources between these appropriations that has been growing since FY 2013. Thus, yearly transfers have been critical to providing the necessary information technology infrastructure for IRS personnel to carry out their duties and to support customer service programs.

Use of Resources

The IRS uses a cost allocation methodology to assign support and overhead costs to each program described below. The Statement of Net Cost reflects the use of IRS resources in conducting its major programs and reports the full cost of these programs in accordance with the Statement of Federal Financial Accounting Standards No. 4, *Managerial Cost Accounting*.

Use of Resources ($ thousands)		
Program	**FY 2018**	**FY 2019**
Taxpayer Assistance and Education	$530,757	$536,196
Filing and Account Services	$4,684,737	$4,997,737
Compliance	$7,855,928	$7,919,906
Administration of Tax Credit Programs	$137,412	$138,058
Total Costs	**$13,208,834**	**$13,591,897**

Taxpayer Assistance and Education activities [4 percent] include taxpayer education and outreach, tax publication issuance and distribution.

Filing and Account Services activities *[37 percent]* include filing tax returns, maintaining customer accounts, processing taxpayer information, providing service to taxpayers, and resolving issues.

Compliance activities *[58 percent]* include pre-filing agreements, document matching, examination, collection, and criminal investigation activities.

Administration of Tax Credit Programs *[1 percent]* primarily includes costs for EITC program activities.

In addition to the EITC, which is the single largest refundable tax credit program, the IRS also administers several other refundable and non-refundable tax credit programs. The IRS Financial Statements reflect those tax credits and the associated costs.

Overview of Revenue and Administrative Accounts

Financial Statements Analysis

The IRS's financial statements and footnotes received an unmodified audit opinion for 20 consecutive years.

The principal financial statements are prepared to report the financial position and results of operations of the reporting entity, pursuant to the requirements of 31 U.S.C. Section 3515(b). The statements are prepared from the books and records of federal entities in accordance with federal Generally Accepted Accounting Principles and the formats prescribed by OMB. Reports used to monitor, and control budgetary resources are prepared from the same books and records. The financial statements should be read with the realization that they are for a component of the U.S. Government.

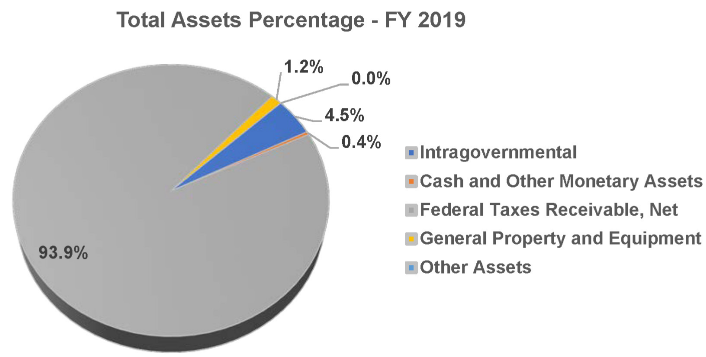
Administrative accounts reflect resources used and expenses incurred in administering the tax laws. Custodial accounts reflect net taxes receivable and taxes collected to support the federal government.

An overview of the IRS's change in financial position from FY 2018 to FY 2019 is presented in the analysis sections of the Balance Sheet, Statement of Net Cost, Status of Budgetary Resources and Statement of Custodial Activity.

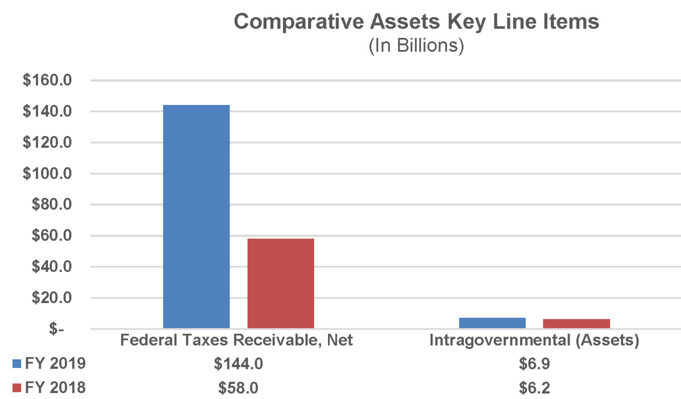
Analysis of the Balance Sheet

The total assets of $153.3 billion and total liabilities of $150.1 billion yielded a net position of $3.3 billion. This represents a six percent decrease compared to FY 2018, which was attributed to a decrease in FY 2019 appropriations.

Assets consist of total intragovernmental transactions; cash and other monetary assets; federal taxes receivable, net; general property and equipment; and other assets:



Federal taxes receivable, net and intragovernmental transactions represented the largest portion of total assets. The changes in these two key asset line items as of September 30, 2019 compared to September 30, 2018 are presented in the graph below:

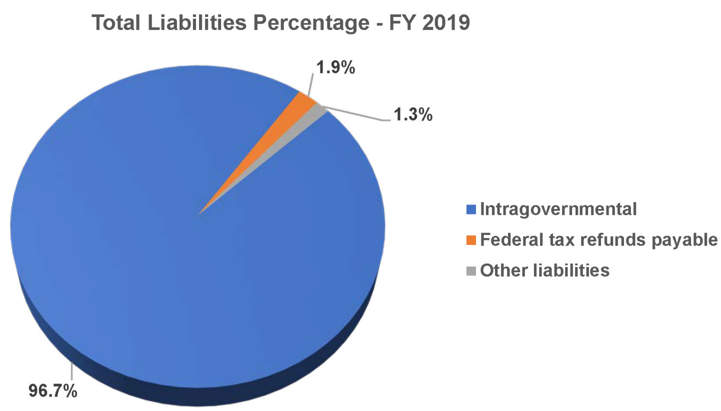


Federal taxes receivable, net consists primarily of tax assessments, penalties, and interest not paid. Federal taxes receivable represented 93.9 percent of total assets. This represented an increase in federal taxes receivable largely due to the revision of Internal Revenue Code §965(h) regarding the inclusion of non-delinquent amounts. See the Analysis of Unpaid Assessments section for additional information.

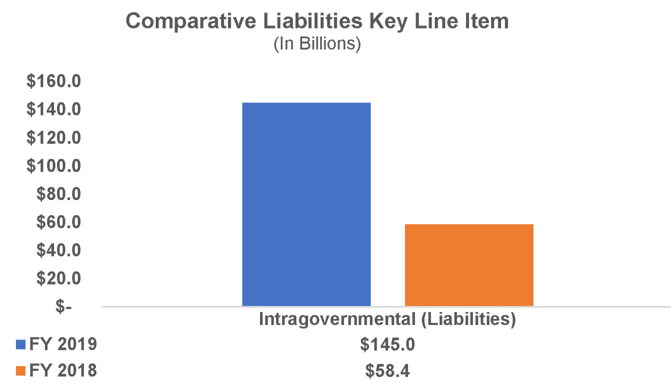
Intragovernmental transactions (assets) represented 4.5 percent of total assets and consisted of 1) Fund Balance with U.S. Treasury, where appropriated funds and other funds are maintained until final disposition, 2) Due from General Fund of the U.S.

Government consisting of refunds of individual tax collections and interest, and 3) Other Assets, which include services provided from other federal agencies through advances or interagency agreements. The Fund Balance with U.S. Treasury was the largest asset in this key line item representing 57 percent and Due from General Fund of the U.S. Government represented 43 percent of intragovernmental transactions as of September 30, 2019. Overall there was a 10 percent increase in intragovernmental transactions attributed to the increase of funding based on the percentage of tax revenue collected from the taxpayers. These funds are dedicated for services provided by the Private Debt Collection program.

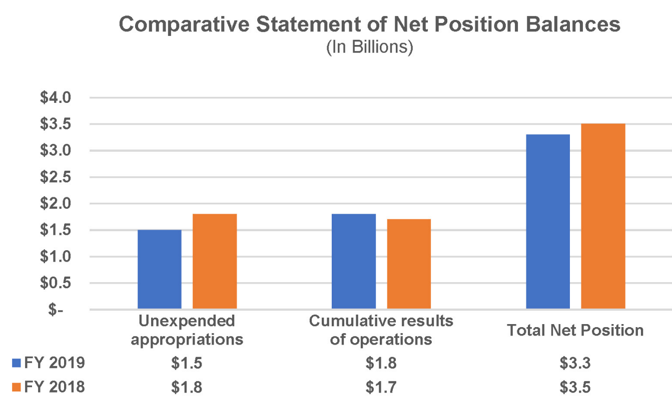
Liabilities consist of intragovernmental, federal tax refunds payable and other liabilities.



Intragovernmental (liabilities) Due to General Fund of the U.S. Government was the largest increase in liabilities. This key line item predominantly includes taxes collected on behalf of the U.S. Government to be transferred to the general fund. The large increase in comparison to FY 2018, presented in the graph below, was a result of the revision to Internal Revenue Code §965(h) regarding the inclusion of non-delinquent amounts. See the Analysis of Unpaid Assessments section for additional information.



Net Position consist of two components: Unexpended Appropriations and Cumulative Results of Operations. Funds made available by Congress are recorded in Unexpended Appropriations. Cumulative Results of Operations is the net difference between 1) expenses, losses, and transfers out from the inception of an agency or activity, and 2) financing sources such as appropriations and revenues, and gains from the inception of an agency or activity (whether financed from appropriations, transfers in, revenues, reimbursements, or any combination of the four) to the reporting date of the financial statements. The comparison of net position for the fiscal years ended September 30, 2019 and September 30, 2018 is shown in the graph below:

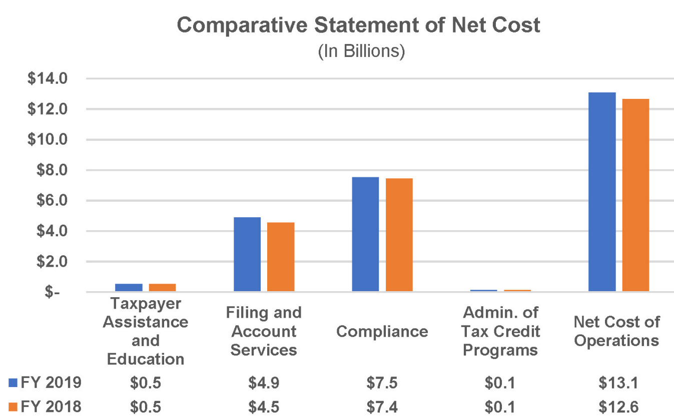


Total net position decreased by six percent primarily due to a slight decline in appropriations received and an increase in appropriations used, compared to FY 2018. In addition, there was a steady decline in the IRS Ruling and Determination user fee collections and less funding received for the U.S. Treasury Forfeiture fund.

Internal Revenue Service – FY 2019 Management's Discussion and Analysis

Analysis of the Statement of Net Cost

The Statement of Net Cost consisted of four major programs with a net cost of $13.1 billion. Total net cost of operations included $13.6 billion in gross cost and $515 million in revenue earned. The gross cost increased by $383 million and decreased by $51 million in revenue earned. Costs increased mostly in information technology, submission processing, accounts management, and criminal investigation activities. The decrease in exchange revenue was due to the loss of revenue from FEMA after the completion of the inter-agency agreement in FY 2018 during which the IRS answered calls from taxpayers affected by Hurricane Harvey. Cost increases occurred mainly for labor and benefit related expenses, consulting services, and ADP operations. The comparison of net cost of operations for fiscal year ended September 30, 2019 and September 30, 2018 is presented by program in the graph below:



Analysis of the Statement of Budgetary Resources

IRS operations are financed through appropriations, spending authority from offsetting collections, and unobligated balances carried forward. Budgetary resources were approximately $13.1 billion, which included $1.2 billion from authority carried forward from FY 2018, $11.8 billion in appropriations, and $135 million in collections. The total of budgetary resources increase was insignificant; however, there was a 14 percent increase in un-obligated balances from FY 2018 primarily due to an increase in recoveries of prior year unpaid obligations. In addition, there was a 31 percent decrease in offsetting collections resulting from the decline in use of the FEMA natural disaster assistance interagency agreement.

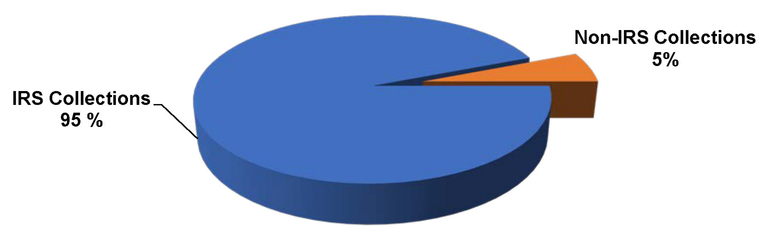
50

Sources of Funds (in millions)	FY 2019	FY 2018	$ Change	% Change
Unobligated balance from prior year budget authority, net	$ 1,210	$ 1,059	$ 151	14%
Appropriation (discretionary and mandatory)	11,789	11,854	(65)	-1%
Spending authority from offsetting collections (discretionary and mandatory)	135	196	(61)	-31%
Total Budgetary Resources	$ 13,134	$ 13,109	$ 25	0%

Analysis of the Statement of Custodial Activity

The Statement of Custodial Activity reports collection of taxes resulting in $3.6 trillion of gross federal receipts before tax refunds. IRS collections totaled 95 percent of the Federal Government receipts, as shown in the following chart.

Total Federal Receipts (Percent)



Revenue and Refund Trend Information

FY 2019 revenue receipts collected by the IRS totaled $3.6 trillion, which was an increase from $3.5 trillion in FY 2018. Federal tax revenues are collected through six major classifications: individual income and FICA/SECA, corporate income, excise taxes, estate and gift taxes, railroad retirement, and federal unemployment taxes.

FY 2019 tax refund and outlay activity totaled $452 billion, which was a decrease from $464 billion in FY 2018. Federal tax refunds include refunds of tax overpayments, payments for interest, and disbursements for refundable tax credits such as EITC and the Additional Child Tax Credit.

Analysis of Unpaid Assessments

Unpaid Assessments Include Non-Delinquent 965(h) Amounts

The unpaid assessment balance consists of non-delinquent 965(h) amounts[1] owed by taxpayers who can elect by law to pay over eight years without being subject to penalties or interest, and delinquent balances owed by taxpayers who file returns without sufficient payment as well as amounts assessed through the IRS's enforcement programs.

Under federal accounting standards, unpaid assessments require taxpayer or court agreement to be considered federal taxes receivable. Assessments not agreed to by taxpayers or the courts are considered compliance assessments and are not considered federal taxes receivable. Assessments considered to have no future collection potential are called write-offs.

As reflected in the supplemental information to the IRS's FY 2019 Financial Statements, the unpaid assessment balance as of September 30, 2019, was $550 billion, which includes interest and penalties of $244 billion (44 percent). Of the total, $75 billion have not been agreed to by taxpayers or the court and therefore are not considered to be federal taxes receivable (compliance assessment), and $106 billion are considered to have no further collection potential (write-off).

Of the total unpaid assessments, $369 billion (67 percent) have been agreed to by taxpayers or determined by the court and are therefore classified as federal taxes receivable.

Growth in Unpaid Assessments is Largely due to Non-Delinquent 965(h) Amounts in Taxes Receivable

Growth in UA is largely due to the inclusion of non-delinquent 965(h) amounts within UA. The FY 2019 federal taxes receivable balance $369 billion includes $160 billion (43 percent) of nondelinquent 965(h). A $160 billion (94,891 percent) increase over the less than $0.2 billion amount in FY 2018 is due to new 965(h) taxpayer filings in FY 2019.

Most of Unpaid Assessments Is Not Considered a Collectable Receivable

Overall collectability combines separate collectability calculations for 965(h) amounts, restitution-based assessments, un-booked fees, and audited taxes receivable. Generally, $225 billion (61 percent) of federal taxes receivable are uncollectible. Examples of uncollectible taxes include taxpayers who agree they owe the tax but are unlikely to pay, taxpayers with extreme financial hardships, and taxpayers who are in litigation.

[1] Section 14103 of the Tax Cuts and Jobs Act (TCJA) of 2017, P.L. 115-97, required changes to IRC section 965. IRC 965 requires U.S. shareholders to pay a transition tax on untaxed foreign earnings of corporations as if those earnings had been repatriated to the United States. Specifically, these repatriated profits are subject to a one-time reduced tax rate, with the option to pay on an eight-year installment schedule, referred to as subpart (h) elections.

Taxes Receivable in 2019	
(Dollars in Billions)	
Taxes Receivable (including non-delinquent IRC 965(h) amounts)	$369
Allowance for Uncollectible Taxes Receivable	*$225*
Federal Taxes Receivable, Net	*$ 144*

As of September 30, 2019, $144 billion in taxes receivable was considered collectible, a $86 billion (148 percent) increase over FY 2018. The increase is largely due to the inclusion of large non-delinquent 965(h) balances, with an overall high collectability. Other factors affecting the reported gross and net taxes receivable include changes in inventory, un-booked fees, and collectability rates (for the net balances).

Excise Tax Trust Fund

Trust Fund	Fiscal Year	
	2017	2018
Airport & Airway Trust Fund	$14,879,254,564	15,549,351,718
Black Lung Disability Trust Fund	$431,724,692	382,129,317
Highway Trust Fund	$41,372,198,466	43,045,618,505
Total	**$56,683,177,722**	**58,977,099,540**

Form 720, The Quarterly Federal Excise Tax Return, reports taxpayer liability for excise taxes. Taxpayers make periodic deposits in advance of filing the return. These deposits are classified as Federal Excise Tax. After the IRS receives and processes the returns, the IRS certifies amounts for several trust funds. Amounts reported on the Statement of Custodial Activity are for fiscal year collections (October 1 through September 30). Because Form 720 reporting requirements are completed after receipt of most of the deposits, the certification amounts will not match the amounts collected during the fiscal year. The table shows revised receipts certified to the Airport and Airway Trust Fund, Black Lung Disability Trust Fund, and the Highway Trust Fund for the eight liability quarters from December 2016 through September 2018. The Department of the Treasury prepares the warrants and allocations to the trust funds.

Internal Controls and Compliance with Other Laws

The IRS continued to enhance financial management and appropriate controls that are an integral component of all IRS programs.

As required by Office of Management and Budget (OMB) Circular No. A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, the IRS evaluated its internal controls and financial management systems to ensure the IRS was operating in accordance with the procedures and standards prescribed by the Comptroller General and OMB guidelines. Results of these evaluations are below.

Federal Managers' Financial Integrity Act (FMFIA)

During FY 2019, the IRS continued to make important progress in addressing its deficiencies in internal controls. Specifically, based on success in addressing internal controls over its estimation process for the total amount of tax receivable, IRS considers unpaid assessments reported in earlier fiscal years as a longstanding material weakness, to be a significant deficiency. The IRS uses a well-documented estimation process to mitigate the risk of material misstatement. The IRS will continue to improve data quality and enhance financial systems through projects such as Pending Payments II, Financial Status Notice History, and Revenue DataMart in order to maintain and improve the significant deficiency.

OMB Circular A-123, Management's Responsibility for Enterprise Risk Management and Internal Control

Management is responsible for managing risks and maintaining effective internal control and financial management systems that meet the objectives of the FMFIA. Risk management practices that identify, assess, respond to, and report on risks are considered when designing internal controls and assessing their effectiveness. The IRS assessed risk and internal controls in accordance with OMB Circular A-123, *Appendix A, Management of Reporting and Data Integrity Risk*. Based on the results of this assessment, the IRS provides reasonable assurance that the internal controls over strategic, operational, reporting, and compliance objectives were operating effectively as of September 30, 2019, with no identified material weaknesses.

The FY 2019 OMB Circular A-123 testing included the following activities:

- Tested internal control sets for 27 transaction processes identified by the Department of the Treasury that are material to its Consolidated Financial Statements. The tests included 14 administrative processes covering material portions of the $11.3 billion in annual administrative transactions, five information system processes, and eight custodial processes covering material portions of the $3.6 trillion in tax revenue receipts through September 30, 2019
- Reviewed controls over IRS financial reporting relative to unpaid assessments, and verified controls remained effective throughout the year
- Reviewed and documented Affordable Care Act related controls over the procedures and processes for recording beginning of year funding in the general ledger, the monthly

journaling and reconciliation of Centers for Medicare and Medicaid Services payments of Advance Premium Tax Credit, the Premium Tax Credit to Advance Premium Tax Credit reconciliation based on tax returns, and beginning of year funding and oversight of the State Waiver Innovation Program
- Reviewed the DATA Act process, including the IRS's Corrective Action Plan responses to Treasury, the quarterly quality assurance statement. and the controls related to financial and award data
- Conducted a self-assessment of the internal control environment using the Government Accountability Office's (GAO) Internal Control Evaluation Checklist and GAO's Green Book that included brief written statements in support of the assessments
- Reviewed IRS compliance with applicable laws and regulatory requirements regarding financial reporting and internal control
- Reviewed GAO and Treasury Inspector General for Tax Administration (TIGTA) audit reports and findings during the test plan development stage and at the end of the A-123 reporting period

Integration of Enterprise Risk Management and Internal Controls

The IRS is responsible for managing risks and maintaining effective internal control and financial management systems that meet the objectives of the FMFIA. Risk management practices that identify, assess, respond to, and report on risks are considered when designing internal controls and assessing their effectiveness. The IRS assessed risks and internal controls in accordance with OMB Circular A-123 and OMB Circular A-123, Appendix A, *Management of Reporting and Data Integrity Risk*. Based on the results of this assessment, the IRS provides reasonable assurance that the internal controls over strategic, operational, reporting, and compliance objectives were operating effectively as of September 30, 2019, with no identified material weaknesses.

Internal Control over Operations and Compliance

The IRS conducted its assessment of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123. Based on the results of this assessment, the IRS provides reasonable assurance that internal control over operations and compliance with applicable laws and regulations were operating effectively as of September 30, 2019 and found no material weaknesses in the design or execution of the internal control over operations and compliance.

The Quality Assurance (QA) Program conducted review testing in FY 2019. The reviews tested consisted of a random sample of quality assurance activities conducted by the IRS's operating and functional divisions to meet their performance and internal control goals and objectives. The QA program assessment activities included:

- Testing internal controls for 66 randomly selected reviews obtained from the 787 reviews on the FY 2019 Quality Assurance Review Listing. This testing evaluated reviews with high risk ratings and frequencies ranging from daily to annual performance from 17 operating and functional divisions. Specific test objectives included:
    - Assessing adherence to references, standard operating procedures, and/or authoritative directives
    - Evaluating control activities

 - Identifying risk factors. including audit recommendations from external auditors and internal testers
 - Examining associated prior year Internal Control Managerial Assessments for each selected review
 - Determining the review outcomes on accounting information recorded in the financial systems and/or the annual audited financial statements
- Identifying 44 FY 2019 findings with recommendations for process improvements in FY 2020 around control activities including physical security, password protection, internal use only and personally identifiable information, and elements of the control environment including adherence to and updating guidance
- Examining the status of one open FY 2016 finding, which was closed in FY 2019
- Examining the status of 11 open FY 2017 findings, which were all closed in FY 2019
- Examining the status of 43 open FY 2018 findings, of which 40 were closed in FY 2019 and the remaining three are scheduled to close in FY 2020

Federal Financial Management Improvement Act (FFMIA)

The IRS assessed its financial management systems in accordance with OMB Circular A-123, *Appendix D, Compliance with the FFMIA*. The IRS's financial management systems did substantially comply with the federal accounting standards and the USSGL at the transaction level. However, the IRS's financial management systems did not substantially comply with federal financial management systems requirements as of September 30, 2019.

As part of its evaluation process, the IRS considered the results of extensive testing and assessment across the organization and independent audits. As required by OMB Circular A-123, the IRS evaluated its internal controls and financial management systems to determine whether these objectives are compliant. The IRS provides an unmodified statement of assurance that its internal controls and financial management systems meet the objectives relative to FMFIA Sections 2 and 4, except that the financial management systems did not substantially comply with the systems requirements under the Federal Financial Management Improvement Act of 1986. In addition, the IRS complies with all improper payment reporting requirements contained in the Improper Payments Information Act (IPIA), as amended by the Improper Payments Elimination and Recovery Act (IPERA) of 2010, and the Improper Payments Elimination and Recovery Improvement Act (IPERIA) of 2012, except reducing the overall EITC improper payment rate to less than 10 percent.

Information Security Significant Deficiency

The IRS worked diligently during FY 2019 to continue to enhance its Information Technology (IT) security, currently identified as a significant deficiency. The IRS implemented a strategy and assessment process to verify the effectiveness of internal controls for the financial systems that affect the financial statements. This process supports the IRS's overall internal control framework and provides assurance that the likelihood of a material weakness reoccurring in the IT environment is low. In FY 2019, the IRS completed the following activities:

- Complied with Federal Information Security Management Act (FISMA) [amended by the Federal Information Security Modernization Act of 2014]; FMFIA Sections 2 and 4; and OMB, National Institute of Standards and Technology (NIST), Department of the Treasury, and IRS security requirements.

- Performed security assessments in compliance with OMB Circular A-123, Appendix A, to provide an integrated view of the security controls affecting confidence in and integrity of the financial statements, enabling the IRS to assess the effect of control deficiencies on the financial statements, prioritize mitigation efforts, and demonstrate progress as the IRS resolves deficiencies. It is important to note that controls require time to mature and show evidence of their effectiveness.
- Facilitated GAO's review of the IRS's IT Security Controls including Boundary Protection, Identification and Authentication, Authorization, Cryptography, Audit and Monitoring, Physical Security, Configuration Management. Segregation of Duties, Contingency Planning, Risk Assessments, Policies and Procedures, Security Plans, Training, Testing and Evaluation, and Remedial Actions.
- Analyzed and prioritized 2019 activities based on the greatest effect on the financial statements, developed corrective actions to mitigate the risk and apply compensating controls, and communicated the strategy to key stakeholders.
- Closed 44 confirmed Planned Corrective Actions (PCAs) from the GAO FY 2018 Financial Statement Audit following GAO's review and validation.
- Received GAO's FY 2019 Financial Statement Audit final report resulting in 14 new findings with 20 associated recommendations, compared to 18 new findings with 37 associated recommendations in FY 2018.
- Reviewed the 127 open recommendations from the GAO FY 2019 Financial Statement Audit. The 127 recommendations were comprised of the following areas: Access Controls (93), Configuration Management (26), Contingency Planning (1), Segregation of Duties (1), Information Security Program (6).
- Submitted 14 PCAs to GAO for review, validation, and potential closure during the GAO FY 2019 Financial Statement Audit. The IRS is still awaiting GAO's concurrence.
- Performed continuous monitoring of internal controls for systems that affect the financial statements to demonstrate that management, technical, and operational controls are in place and are effective.
- Reviewed the security monitoring controls for IT systems owned or operated by external entities to provide assurance that their systems' security management programs have adequate documentation. During FY 2019, there were 68 Contractor Security Assessments completed: 15 associated with the Mission Essential Functions aligned with Critical Business Processes (CBPs) 1-2-3 that support Processing of Remittances, Processing of Returns, and Processing of Refunds; 34 associated with contractor site assessments for environments and facilities supporting tax examination, customer surveys, identity theft initiatives, and other non-CBPs; 10 associated with security assessments to support the IRS's Private Debt Collection programs, which are aligned with CBP-1; and nine associated with contractor sites conducting printing activities.

Federal Information Security Management Act (FISMA)

In accordance with FISMA requirements and OMB Circular A-130, the IRS maintained an agency-wide information security program and provided a comprehensive framework for validating the effectiveness of information security controls over resources that support IRS business operations and goals. Specifically, the IRS inventory of FISMA reportable systems is compliant with the security requirements from OMB, NIST, the Department of the Treasury, and IRS internal policies. The IRS completed annual security control testing on these systems, participated in required security authorization and assessment activities, and addressed required Plans of Actions and Milestones (POA&Ms) for identified weaknesses.

Continuity of Operations (COOP)

Under the IRS Information System Contingency Plan (ISCP), the IRS tests application and system contingency plans annually to ensure that recovery of the IRS's technical infrastructure and resumption of processes can be accomplished in the event of an incident or disaster. During FISMA 2019, the IRS validated that ISCPs for all FISMA reportable applications and systems were updated and tested, and that they adhered to standards, guidelines, government regulations and industry best practices specific for information system recovery and data restoration. The IRS conducted more than 294 exercises and tests to validate that contingency plans were current and executable, backed-up data was available and readable, and Critical Infrastructure Protection assets performed disaster recovery or alternate site processing tests to ensure they could recover within their defined Recovery Time Objective. If vulnerabilities were identified during ISCP testing, POA&Ms were assigned for resolution.

Improper Payments Elimination and Recovery Act (IPERA) of 2010

The IRS conducted quantitative risk assessments for these programs in FY 2019 and determined that while each program had strong internal controls in place, the dollar value of potential improper payments for each of the programs indicate they should be reported as susceptible to risk of significant improper payments. Both ACTC and AOTC will be reported along with EITC in the FY 2019 Treasury Agency Financial Report (AFR). The sample size of PTC returns is not yet sufficient to yield an estimate within the statistical confidence interval and margin of error required by OMB guidance and, as a result, will not be reported in the AFR this fiscal year.

The IRS continues to face challenges to reducing the EITC error rate and plans to report on the actions taken in the FY 2019 AFR. The AFR discussion will include a report on the root causes of EITC, ACTC, and AOTC improper payments, and future planned corrective actions intended to reduce the programs' payment error rates. In December 2015, Congress enacted the Protecting Americans From Tax Hikes (PATH) Act. which contains significant legislative changes intended to help reduce improper EITC, ACTC, and AOTC claims. Employers were to file Forms W-2 with the Social Security Administration by January 31, 2019, and the IRS could not issue a refund on returns claiming EITC or ACTC until February 15, 2019. The earlier filing date and later issuance date gave the IRS more time to verify EITC and ACTC claims before issuing refunds; however, it did not expand the IRS's authority to systematically correct erroneous claims identified for processed tax returns.

The IRS included several legislative change proposals in its FY 2019 and FY 2020 budget requests to improve refundable tax credit compliance. These proposals include providing greater flexibility to address correctable errors to help the IRS deny certain erroneous claims before refunds are paid and increasing oversight of paid tax return preparers to promote high quality services and improve voluntary compliance. If enacted, these legislative changes would provide the IRS with additional tools to combat waste and fraud and expanded authority to take actions to prevent payment errors and improve taxpayer compliance. The IRS and Treasury also have reengaged OMB to discuss whether it is appropriate to evaluate refundable tax credit programs within the context of improper payments reporting requirements. The refundable tax credits are deeply integrated into the tax administration system and evaluating them as one would evaluate a distinct payment program carries certain risks and challenges. Treasury, the IRS, and OMB will continue to discuss alternative reporting opportunities in FY 2020, such as analyzing and reporting refundable tax credits in the context of the tax gap. Meanwhile, the IRS continues to implement tax administration tools and techniques available to reduce erroneous payments.

Government Charge Card Abuse Prevention Act of 2012

In accordance with the requirements of the Government Charge Card Abuse Prevention Act of 2012, the IRS provides assurance that its internal control over the use of government charge cards was effective. Specifically, the IRS complied with the Department of the Treasury Charge Card Management Plan and provided agency-wide purchase card guidance for the proper use of government charge cards. The IRS conducted monthly and quarterly reviews of charge card activity to verify proper card use and to address potential inappropriate use. TIGTA reviewed the IRS's purchase card program and found that controls are generally effective, and the number of purchase card violations identified by the IRS Credit Card Services Branch were minimal and generally for nominal amounts. (See TIGTA report #2019-10-053, dated July 24, 2019.)

Reports Consolidation Act of 2000

In accordance with the Reports Consolidation Act of 2000, the IRS provides assurance that the IRS Critical Performance Measures are reliable. Internal Revenue Manual 1.5.1, *Managing Statistics in* a *Balanced Measurement System, The IRS Balanced Performance Measurement System,* provides a detailed template that documents each measure's definition, formula, reliability, and reporting frequency. These controls verify that performance data is consistent and accurately collected over time.

Anti-deficiency Act

The IRS is not aware of any violations of the Anti-deficiency Act. The IRS is in receipt of GAO Decision B-331093 (October 22, 2019) related to the IRS's processing of tax remittances and claims for refunds during the most recent lapse in appropriations. The IRS is currently reviewing the decision. As of September 30, 2019, and through the date of this document, the IRS has not made a report to the Congress and the President.

Management Challenges

GAO High-Risk Areas and Other Financial Management Challenges

GAO reports on federal programs and operations that are vulnerable to waste, fraud, abuse, and mismanagement or that need broad reform at the start of each new Congress in its biennial High-Risk Report. The IRS's high-risk area and its two components below appear in GAO's High-Risk Series report, *Substantial Efforts Needed to Achieve Greater Progress on High-Risk Areas* (GAO-19-392T), published March 6, 2019.

GAO High-Risk Area

Enforcing Tax Laws
- Addressing the tax gap
- Combatting identity theft refund fraud

In addition, GAO identified three other financial management challenges in its report, *Financial Audit: IRS's Fiscal Years 2018 and 2017 Financial Statements* (GAO-19-150), published on November 9, 2018.

Other Financial Management Challenges

1. Safeguarding Taxpayer Receipts and Associated Information
2. Preventing and Detecting Fraudulent Refunds Based on Identity Theft
3. Implementing Patient Protection and Affordable Care Act Tax-Related Provisions

The IRS remains dedicated to improving taxpayer compliance, identity theft refund fraud, and safeguarding taxpayer receipts and associated information and has identified specific steps and actions to address these issues through new and existing program activities as presented throughout this document and in the following actions taken and actions planned.

Safeguarding Taxpayer Receipts and Associated Information

The IRS continued its efforts to strengthen its internal controls devised to safeguard taxpayer information. In FY 2019, the IRS conducted a survey to determine the reasons for noncompliance with the required Emergency Contact List tasks as outlined in the existing Internal Revenue Manual and Standard Operating Procedure. Based on the results of the Emergency Contact List assessment, the IRS will establish a process to improve compliance with the requirement for maintaining an Emergency Contact List at all IRS facilities. The IRS also plans to create a strategy document to provide reasonable assurance concerning its nationwide coordination, consistency, and accountability for internal control over key areas of physical security. This strategy will include nationwide improvements for:

- Coordinating physical security programs among all IRS facilities

- Implementing internal controls and monitoring the effectiveness of physical security policies and procedures at all IRS facilities, such as alarm testing and maintenance and video surveillance systems
- Ongoing communication about identifying, documenting and taking corrective action to resolve underlying control issues that affect the IRS's facilities.

Preventing and Detecting Fraudulent Refunds Based on Identity Theft

The IRS continued its efforts to identify, design, and implement the most effective systems, processes, and internal controls for preventing and detecting identity theft tax refund fraud. In FY 2019, the IRS began improvements to IRS systems for prevention and detection of automated attacks and to become compliant with the National Institute of Standards and Technology (NIST) guidance. The IRS developed a plan with milestone dates and resources needed to implement changes to the online authentication capability. The schedule outlines a solution path through a series of three tests and a pilot. The IRS and GAO reviewed the work conducted throughout the past eight months that culminated into the development of the schedule. The plan is heavily dependent upon resources, adequate funding, timely procurements, ensuring the appropriate decision-making framework, and favorable outcomes of the tests and pilot. Due to the complexity of the initiative, the IRS will periodically meet with GAO to provide updates on its progress.

Also, in FY 2019 the IRS took several steps to strengthen taxpayer authentication, such as:

- Developing a status update that assesses the IRS's progress in implementing Foundational Initiatives and capturing resource estimates for projects supporting each FI
- Mapping each Foundational Initiative to existing IRS strategies and plans, ranging from high-level enterprise strategies to organization-specific implementation plans
- Developing an omni-channel risk assessment process for non-electronic authentications that culminated in the development of a draft policy document. The policy will be the cornerstone of the plan for instituting reviews that monitor the risk associated with paper, face-to-face, and telephone authentication
- Developing a repeatable process for authentication improvement and Information Technology Identity and Access Management with accompanying tools and governance for an Innovation Working Group

During FY 2020, the IRS plans to take further steps to strengthen taxpayer authentication. These include:

- Mapping the IRS's identity assurance capabilities and supporting projects to enterprise strategies and relevant organization-specific implementation plans through the annual strategy refresh process
- Leveraging the newly created policy for reviewing non-electronic authentications and finalizing an implementation plan that will establish the frequency and content of risk assessment reviews
- Incorporating new authentication options identified by the Innovation Working Group and IRS business units into the Identity Assurance Strategy

The IRS also initiated a pilot to assess the potential for early notification to taxpayers that may have underreported wages on a tax return based on receipt of earlier Forms W-2 to determine if a soft notice informing them of income underreporting will change taxpayer behavior. For the pilot, a soft notice was issued to taxpayers alerting them of the possible oversight. The IRS will use the results and recommendations from this pilot to make additional adjustments to the implementation, as needed. Reviews of 2016 tax returns showed that late filed Forms W-2 do not affect timely filing of tax returns. As of November 2018, about 13 percent of taxpayers filed 2016 taxes after the April tax deadline compared to 12 percent of the late W-2 population. Less than one percent of the late W-2 population returns were identified as theft-related or fraudulent. The IRS will continue to use existing authority to prevent the payment of fraudulent or noncompliant refunds. The assessment of costs and benefits associated with modifications to the PATH Act's February 15 refund hold date requirement will include a discussion of actions that the IRS could implement with existing authorities. The IRS will identify potential actions that could improve the prevention of fraudulent or noncompliant refunds but would require additional or modified authority.

Implementing Patient Protection and Affordable Care Act Tax-Related Provisions

The IRS continues to implement the complex tax-related provisions of the Patient Protection and Affordable Care Act (ACA) as additional provisions become effective. Doing so requires extensive coordination not only within the IRS but also with multiple agencies and external partners tasked with responsibilities under the Act. The IRS continued to work closely with agencies and entities to improve the timeliness and accuracy of the information they provide to the IRS. The IRS also continued efforts to design and implement systems and processes as new ACA provisions become effective to assure the processing of valid and accurate payment amounts. In doing so, the IRS conducted a detailed review of the feasibility of incorporating information from marketplaces about individuals who failed to meet citizenship or lawful presence eligibility requirements in the tax compliance process. The review resulted in the IRS proposing a new reporting method to prevent improper payments of Advance Premium Tax Credit. However, it will require significant changes internally, i.e. programming, forms and instructions as well as process changes in the way that Marketplaces verify and report information to the IRS for individuals who have failed to meet the citizenship or lawful presence requirements.

The IRS discussed legal requirements with the Department of the Treasury and programming and resources with the Department of Health and Human Services Centers for Medicare and Medicaid Services, which reports data to the IRS for 39 states. The IRS will report the outcome of this study and determine the feasibility of the new reporting method and obtain management approval.

TIGTA Management and Performance Challenges

The Reports Consolidation Act of 2000 requires that TIGTA summarize for inclusion in the annual Department of the Treasury Agency Financial Report its perspective on the most serious management and performance challenges confronting the IRS.

Each year, TIGTA evaluates IRS programs, operations, and management functions to identify the areas of highest vulnerability to the Nation's tax system and presents them to the IRS in a memorandum titled *Management and Performance Challenges Facing the Internal Revenue Service*. The IRS addresses these challenges through new and existing program activities. For FY 2019, the IRS's top management and performance challenges, in order of significance, were:

1. Security Over Taxpayer Data and Protection of IRS Resources
2. Implementing the Tax Cuts and Jobs Act and Other Tax Law Changes
3. Identity Theft and Impersonation Fraud
4. Providing Quality Taxpayer Service
5. Upgrading Tax Systems and Expanding Online Services
6. Improving Tax Reporting and Payment Compliance
7. Reducing Fraudulent Claims and Improper Payments
8. Impact of Global Economy on Tax Administration
9. Protecting Taxpayer Rights
10. Achieving Program Efficiencies and Cost Savings

Below the IRS addresses each challenge with actions taken in FY 2019 and any future actions planned to correct the issue.

Security Over Taxpayer Data and Protection of IRS Resources

The IRS continues to focus on identity theft tax refund fraud. Taxpayer authentication has become more difficult for the IRS with the wide availability of personally identifiable information and perpetrators' ability to develop more complex and sophisticated methods to commit fraud undetected. In FY 2019, the IRS made progress in improving its electronic authentication controls, such as modifying eAuthentication to accommodate the inclusion of a universally unique identifier for all Security Audit and Analysis System events and deployed the changes to production on June 23, 2019.

The IRS also met policy requirements for monitoring the generation of suspicious activity audit log reports by assisting the eAuthentication application owner in reviewing their audit logs and following review and analysis methods outlined in several standard operating procedures.

In addition to protecting taxpayer data against outside attacks, the IRS ensured that contractors or other third parties protected taxpayer data to prevent unauthorized disclosure. The IRS updated the policy for vulnerability remediation, which will change the remediation timeframe for high-risk vulnerabilities. The IRS posted Publication 4812, *Contractor Security Controls*, to IRS.gov and is working on updates to reflect the remediation timeline.

In addition, the IRS reconfirmed the encryption of taxpayer data while in-transit and has worked with external partners to strengthen their security practices including implementing file-based encryption for Private Debt Collection data.

The IRS also updated its Private Debt Collection Operations Guide to ensure annual physical security assessments of mailrooms and mail processing sites, with follow-up assessments of any identified deficiencies within the same year. Additionally, the updated guide ensures monthly communication of private collection agencies' system vulnerabilities and timely remediation. IRS Publication 4812 requires that contractors mirror the requirements in the IRS Lockbox Security Guidelines for mailroom security. The private collection agencies have adopted all required changes within their facilities and the IRS began using the updated security requirements during its annual assessments of private collection agencies.

Also, to protect taxpayers against unauthorized release of their tax information, the IRS required all existing Income Verification Express Service participants to certify compliance to two sets of requirements. The IRS disabled the accounts of Income Verification Express Service participants not submitting timely certifications as well as all new Income Verification Express Service participant accounts until receipt of certifications. New procedures require all e-Services users to register to access their account through Secure Access, an identity proofing and two-factor authentication process. The IRS has three remaining applications to fully protect using network security monitoring tools, which is on schedule for implementation in February 2020.

In addition to external threats, the IRS continued to ensure protection of its systems and data against internal threats. The IRS continued to reduce the number of rehires with performance/conduct issues through implementation of new rehire policies and procedures implemented in 2017 and amended in 2018, which include sharing the prior performance and conduct issues with selecting officials, requiring written justifications for rehire, and the Business Unit Commissioner and IRS Human Capital Officer's approvals. Preliminary research of hires from October 2017 through June 2018 shows procedures are effective and resulted in a decline, from 11 percent to three percent, in the total population of rehires with performance/conduct issues. The IRS is continuing to advocate for legislation that would prohibit the rehiring of former IRS employees with prior egregious misconduct violations.

Implementing the Tax Cuts and Jobs Act and Other Tax Law Changes

The TCJA contains 119 domestic and international tax provisions administered by the IRS. Once enacted, the IRS immediately began the difficult and large-scale task of implementing the various provisions. Even with the high volume of changes needed to implement the new legislation, the IRS began the 2019 filing season on time on January 28, 2019.

In addition to the TCJA, the IRS continued to administer other tax law provisions, such as those in the PATH Act intended to reduce fraudulent refundable tax credit claims and modifications to the Individual Taxpayer Identification Number (ITIN) program. The IRS issued a quality assurance alert to tax examiners to remind them of the requirement that ITIN applications require original or certified copies of supporting documents. The IRS also completed a review of the nine ITIN applications identified as being erroneously issued and determined that due to the PATH Act requirements, seven of the nine applicants' ITINs were systematically deactivated due to non-use, with no further actions warranted. The two remaining applicants were in active status and would have to renew their ITIN within the next year based on the PATH Act. The IRS continues to identify incomplete and fraudulent ITIN applications to take appropriate actions and determine systemic changes and resources needed to more efficiently identify ITIN applications that are questionable based on potentially false or fraudulent supporting documentation.

In addition, the IRS addressed the PATH Act integrity provisions intended to reduce improper tax credit claims by reviewing tax returns with a discrepancy in wages reported on the tax return compared to wages reported on third-party Forms W-2.

Identity Theft and Impersonation Fraud

One of the IRS's primary focuses is to detect and prevent the filing of fraudulent individual and business tax returns by identity thieves. In FY 2019, the IRS continued to adapt its detection and prevention processes to reject fraudulent electronically filed tax returns and prevent fraudulent paper tax returns from posting, thus preventing the issuance of millions in fraudulent tax refunds.

In addition, the IRS created business identity theft filters and selection lists to identify potential business identity theft returns. The IRS increased the number of business identity theft detection filters from seven in Processing Year (PY) 2015 to 25 in PY 2017 and is developing employment tax form identity theft filters for other 940 series returns for implementation in June 2020.

The IRS also performed an analysis of the EINs on the Suspicious EIN Listing and developed a methodology incorporating a monthly review process to ensure monitoring of the EINs on the Suspicious EIN Listing. The IRS removes EINs that no longer meet the criteria for monitoring and locks any EIN remaining on the Suspicious EIN Listing for more than 18 months with no legitimacy characteristics or if they appear to be bogus or fictitious businesses. The IRS also added cross-referencing TINs and questionable addresses to the monthly Suspicious EIN Listing review. Monitoring will continue for other EINs on the listing unless otherwise deemed legitimate. Additional research of accounts will be determined on a case-by-case basis. The IRS updated policies and procedures to reflect the methodology and procedures for EIN and business identity theft tax accounts reviews.

Providing Quality Taxpayer Service

Providing taxpayers with quality customer service is a key component in the IRS's mission. This includes providing quality service to taxpayers affected by identity theft.

Taxpayers learn they are victims of employment-related identity theft when they receive a notification from the IRS of an income discrepancy between the amounts reported on their tax returns and the amounts employers reported to the IRS. A computer programming error limited the IRS notifications to only those employment identity theft victims not identified as a victim in previous years. As a result, the IRS did not notify repeat victims of employment identity theft that it identified in both PY 2017 and on tax returns processed in prior years. In addition, the IRS sent many of the employment theft notices to taxpayers who were not employment identity theft victims, such as spouses of taxpayers who filed legitimate tax returns reporting the spouses' wages and social security number. The IRS erroneously placed an employment identity theft marker on the spouses' tax accounts, which generated the notices. The IRS corrected the programming error that caused this issue and verified that the programming is working as intended. In FY 2019, the IRS also notified all identified repeat victims of employment identity theft informing them of the use of their social security number by another person to obtain employment. In addition, the IRS acted to reverse the erroneous identity theft markers applied to the spousal accounts identified and sent a letter to each taxpayer affected to apologize for the error.

In addition, the ITIN/social security number mismatch process erroneously placed employment identity theft markers on the tax accounts of social security number owners who are spouses of ITIN holders. The IRS has verified that the programming is working as intended and is identifying the number of spouses who erroneously received a marker on their account. After identifying the number of spouses affected, the IRS will conduct additional research to verify that another ITIN holder is not also using their social security number for employment purposes prior to reversing any indicators that may have been correctly added to taxpayers' accounts.

Upgrading Tax Systems and Expanding Online Services

Successful modernization of systems and the development and implementation of new information technology applications are critical to meeting the IRS's evolving business needs and enhancing services provided to taxpayers.

The IRS established the Enterprise Case Management program to streamline case management processes across the business units and to consolidate the case management systems into one common solution. The IRS is using an innovative product assessment approach with challenge-based evaluation to identify a viable Enterprise Case Management solution that can consolidate most legacy case management systems. The challenge-based evaluation will confirm that mission-critical Enterprise Case Management program requirements are determined, and all initial planning and completion of initial activities are at the program level prior to procurement of the solution and the start of Enterprise Case Management projects. The current product acquisition plan is based on two requests for quotations and information from industry information exchanges with other government agencies. The IRS published a robust request for quotations, which contains 18 minimum mandatory requirements and more than 300 technical and business requirements to evaluate and select a product. The IRS will confirm the completion of all initial planning and program-level activities prior to the final product acquisition in late 2019.

In addition, the IRS continued efforts to replace aged and obsolete hardware and software and provide a stable foundation for delivering technology services required for day-to-day operations - transforming the tax experience and modernizing operations. The IRS released the Integrated Modernization Business Plan, which addresses aging infrastructure and improves operational efficiencies by reducing system complexities, increasing standardization, and consolidating infrastructure and application components across the IRS. This includes rapidly and efficiently leveraging new, next generation infrastructure and cloud computing technologies to provide a more robust, scalable and resilient infrastructure. The IRS continues phasing out old equipment and the percent of aged infrastructure has declined from 52 percent in FY 2017 to 39 percent in FY 2019 due to a significant push to refresh workstations and the replacement of additional aged Windows servers this fiscal year. The IRS is refreshing employees' equipment every four years, upgrading operating software on employee workstations and replacing more than half of the agency's workstations over the next year. The IRS will continue executing the IRS Integrated Modernization Business Plan and further the use of agile delivery methods to further progress towards reducing aged infrastructure, and then sustaining it at 25 percent. The IRS is also standing up a technology planning office that will ensure a comprehensive program oversight structure for hardware and software to strategically drive refresh priorities, funding decisions, integration, and delivery while ensuring stakeholder accountability.

The IRS also continues to demonstrate its commitment to broaden access to secure digital services to the general public, Federal agencies, and tax professionals. The IRS established a policy for the contractor who determines remediation time frames for all identified configuration weaknesses to ensure protection against system vulnerabilities and misconfigurations. The IRS corrected the Plan of Action and Milestones remediation timeframes within the Integrated Enterprise Portal Continuous Monitoring Plan. In addition, the IRS ensures thorough review of monthly status reports and conducts monthly stakeholder meetings prior to approval of the reports. Also, the IRS reviews the monthly inventory reports for accuracy and has made the Inventory Report a formal deliverable for the Integrated Enterprise Security team. The Inventory Reports now require formal approval each month. The IRS will continue to thoroughly review monthly status reports and conduct monthly stakeholder meetings prior to approval of the reports.

Improving Tax Reporting and Payment Compliance

The IRS consistently works to improve tax reporting and payment compliance by ensuring taxpayers understand their filing requirements and obligations to comply with the tax law. In FY 2019, the IRS took several actions to improve tax compliance.

As of September 30, 2019, the Private Debt Collection program, established by the Fixing America's Surface Transportation Act, generated $301.7 million in revenue compared to $131.7 million in costs. The private collection agencies have assisted almost 200,000 taxpayers with either paying their tax debt in full or establishing a payment arrangement. In FY 2019, the IRS updated the Private Debt Collection Communications Plan to include revising the Private Debt Collection webpage on IRS.gov. The newly designed Private Debt Collection webpage will help taxpayers easily find answers to commonly-asked questions, know what to expect from a private collector, how to validate their assignment, and allow them to access a link to the Taxpayer Bill of Rights. In March 2018, the IRS began providing taxpayer telephone numbers to the private collection agencies. The IRS continues to analyze program data for both individual and business cases distributed to the private collection agencies. The IRS will determine if an established set of criteria would be more effective than applying an artificial time period for a private collection agency to retain a case so that taxpayers are not effectively assigned to a private collection agency on a permanent basis for their compliance-related issues.

In addition, the IRS wrote and issued State Audit Report Program (SARP) participation guidance to address filing noncompliance and underreporting issues. This guidance assisted in developing the SARP Expansion Plan. The IRS held SARP meetings with six new states to discuss SARP program criteria, the state's ability to share audit files, and the next steps for

SARP participation. The IRS made follow-up contact with five states that indicated interest in the SARP program and those included in the SARP Expansion Plan. The IRS coordinated a disclosure review of the Control File Template, which filters and summarizes information received in each SARP submission and shared it with states to ensure consistency in SARP submissions. Four new states have started sharing audit reports with the IRS. The IRS will continue to work with business leads on the SARP Expansion Plan to contact and engage new state participation.

The IRS evaluated high-income and repeat non-filers prior to dropping them from SARP inventory. The IRS also worked to build a database to properly document the examination non-select reason, and in 2018 began manually tracking non-selects until the database was fully operational. In FY 2019, 10 additional states participated in the SARP resulting in 10,767 reports subject to selection criteria within the program; these may or may not have resulted in an audit.

The IRS also restarted the issuance of systemic levies in July 2018, initially focusing on high priority case categories, such as delinquent employment tax balances and high-risk individual income tax balances. From that point until September 30, 2018, the IRS issued 190,690 systemic levies. In FY 2019, the IRS issued 413,354 systemic levies. The IRS recognizes the compliance effect of issuing notices of levy; therefore, it regularly assesses its capacity to handle levy responses and will adjust levy volumes as appropriate on an ongoing basis.

The IRS established a servicewide team to develop a return preparer strategy. This team evaluated the current activities around return preparer compliance, identified gaps and associated risks with current initiatives, and developed recommendations for a comprehensive and coordinated Servicewide Return Preparer Strategy. Once approved, the IRS will establish the supporting goals. In the meantime, the IRS added new language to letters sent to return preparers who are not in tax compliance to clarify that the IRS had previously provided details to the recipient about alleged tax noncompliance. Also, the IRS worked with TIGTA's Office of Investigations to update the referral criteria for return preparers who misrepresent their professional credentials. The IRS currently prepares a quarterly report to track and analyze progress on Compliance Initiative Projects utilizing the Preparer Risk Identification Scoring Model feature of the Return Preparer Database.

The IRS created Schedule UTP, *Uncertain Tax Position Statement*, to assist the examination process by establishing certainty regarding a taxpayer's tax obligations for U.S. Corporation Income Tax Returns. It provides important benefits in promoting voluntary compliance through due diligence. However, to strengthen its usefulness and enhance compliance benefits, the IRS determined that it would modify the instructions to Schedule UTP to provide clearer guidance and provide examples to show the required level of detail. The IRS is moving forward with the necessary policy, budget, and procedural steps required to modify the instructions to Schedule UTP.

Reducing Fraudulent Claims and Improper Payments

Refund fraud caused by identity theft is one of the biggest challenges facing the IRS today and the harm it inflicts on innocent taxpayers is a problem the IRS takes very seriously. The IRS has a comprehensive and aggressive identity theft strategy to assist taxpayers, protect revenue, and prevent refund fraud. It continues to seek opportunities to realize efficiencies and improve customer experiences.

Identity theft detection and results continue to improve:

- Identity theft and fraud detection systems contain complex models and filters developed from historical and newly emerging known fraud characteristics that identify questionable income, withholding and refundable credits.
- The IRS continually reviews and enhances its identity theft screening filters to improve proficiency in detecting false returns before processing and issuing refunds.

The TCJA contained two provisions affecting Refundable Credits: Advance Child Tax Credit /Credit for Other Dependents and Tax Preparer Due Diligence. The new legislation requires a valid social security number for employment at the time of return filing. The law was silent on Math Error Authority for taxpayers claiming the Child Tax Credit; therefore, the IRS established rules to select potential ineligible taxpayers for examination to prevent improper payments.

Impact of Global Economy on Tax Administration

In FY 2019, the IRS initiated action to enforce withholding agent compliance with the Foreign Account Tax Compliance Act (FATCA). In November 2018, the IRS issued soft letters to Model 2 Intergovernmental Agreement (IGA) Foreign Financial Institutions (FFIs) regarding the accuracy of their filed Forms 8966, *FATCA Report*, to ensure that the FFI correctly provide data for mandatory fields. On June 6, 2019, the IRS issued notices of default (or Event of Default/EOD notices) for financial institutions that should have submitted their FATCA certifications but didn't. This initiative will ensure that non-IGA FFIs and Model 2 IGA FFIs submit FATCA reports. The IRS also initiated compliance efforts to address and correct the invalid Taxpayer Identification Numbers on all Form 1042-S, *Foreign Person's U.S. Source Income Subject to Withholding*, filings by non-IGA FFIs and Model 2 IGA FFIs.

The IRS also established Campaign 975 to address financial Institutions that have filed Form 8938, *Statement of Foreign Financial Assets*, but not the corresponding Form 8966 and to identify Form 8957, *Foreign Account Tax Compliance Act (FATCA) Registration*, filed with no corresponding Form 8966. Currently, the campaign is in the filter development stage with completion of the first filter expected in 2019 and soft letters issued. As part of the private banking campaign, the IRS is working on a filter to compare Forms 8938 to Forms 8966 to locate taxpayers who underreported income from offshore assets. The IRS updated Form 8938 instructions on November 29, 2018, to include guidance directing taxpayers to the FFI list search and download tool.

In FY 2020, the IRS expects to complete the development of all filters and issue additional soft letters addressing the compliance issues. The results will affect how the IRS will conduct further compliance efforts concerning non-filings of Form 8938. The IRS will consider feedback from the taxpayers involved in the campaign and compliance staff working the selected treatment streams when deciding future compliance efforts.

The IRS also made necessary updates to clarify and expand the language in the Form 1040NR/EZ, *Income Tax Return for Certain Nonresident Aliens With No Dependents*, instructions and Publication 519, *U.S. Tax Guide for Aliens*, for the 2019 tax year. The changes will help Nonresident Alien (NRA) taxpayers understand entitlements to claim treaty benefits when filing their income tax returns despite failing to file a Form 8233, *Exemption From Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual*, with the withholding agent/payor. The IRS is updating the *"Taxation by Immigration Status"* landing page on IRS.gov and various work visa status web pages as part of its outreach efforts. Also, the IRS is increasing outreach efforts to external communities which have direct interaction with most foreign visitors. On November 7, 2018, the United States Business Advisor Practice Network participated in a webinar for the National Association of College and Business Officers, discussing various tax topics related to universities and their foreign students. The IRS will continue its efforts to complete the work needed to update web pages on IRS.gov and its outreach efforts to include other important organizations dealing with foreign students and scholars.

Protecting Taxpayer Rights

The IRS continues to dedicate significant resources and attention to complying with the taxpayer rights provisions of the *IRS Restructuring and Reform Act of 1998*. The IRS revised IRM 5.12.6.3.10 in January 2018 to clarify that, ordinarily, the IRS would send a copy of the Collection Due Process lien notice to a representative only if the taxpayer checked the box on Form 2848, *Power of Attorney and Declaration of Representative*, indicating to systemically send copies of notices to the representative.

In addition, IRS management issued a communication to staff that highlighted IRM guidance on the topics of fair market value of assets and expenses of seizure and sale, as well as on the requirement for the revenue officer to discuss these issues with the property appraisal and liquidation specialists (PALS) prior to seizure. The communication also highlighted the guidance on documenting these discussions. The IRS updated the PALS and General Services Administration (GSA) Outsourcing Initiative Project Plan, and IRM 5.10.4.6.1 to include the selection criteria.

The IRS also deployed additional programming for the Collection account case processing system, that recognizes and alerts Compliance Representatives to the possibility of additional assessments not covered by the initial final notice. Additionally, when levies are prepared on cases with additional assessments, those levy notices now go through an additional screening process to ensure the IRS sent a final notice on each assessment associated with the levy. The IRS reviewed 200 manually issued final notice cases in FY 2019 to test the programming and the new process. In FY 2020, the IRS will expand its review to further validate the effectiveness of the new system.

Achieving Program Efficiencies and Cost Savings

After payroll, rent is the IRS's largest operating expense; therefore, the IRS continues to take steps to reduce its total office space. To achieve more effective space utilization, the IRS enhanced the space reduction project planning process to incorporate a more detailed account of employees' out-of-office status to increase workspace sharing and reduce quantity of leased space required. The IRS developed two new Standard Operating Procedures to outline an enhanced process for reviewing and improving Graphic Database Interface data in posts of duty by conducting a Space Occupancy Survey and if necessary, conduct an on-site survey to assess and resolve any building data findings. The IRS uses official timekeeping and telework data to determine employees' hours out of the office by IRS building to calculate the quantity of unassigned and assigned workstations required in an office, typically reducing the square feet required and requested for acquisition by GSA. A report is available to track the progress on the reduction of workspaces in each project as a result of employees' out-of-office status and use of unassigned workspaces. Requests for deviations from the unassigned ratios require written justifications and executive-level approval. The IRS Strategic Plan 2018-2022 established an IRS-wide measure of Efficient Space Utilization.

The IRS's priority is to right-size the portfolio as leases expire and to propose building closures or consolidations wherever feasible. Telework, mobile work, and other work/life initiatives will continue to reduce actual office space needs. Therefore, the IRS evaluates each opportunity for the possibility of workspace and square footage reductions. By optimizing funding of space reduction projects, the use of hoteling offices and workstations as well as lease expirations, the IRS anticipates a significant overall workspace reduction, notwithstanding hiring and business needs.

The IRS increased conduct and tax compliance issues screening procedures prior to issuing performance awards. The IRS updated processing procedures to require management to document consideration of willful factors and the determination of whether reasonable cause exists. The IRS also developed and released resources and training to assist managers with making the determination of willfulness and reasonable cause, as appropriate. In FY 2019, all IRS labor relations specialists and managers have completed refresher process training on Section 1203, which provides for the termination of IRS employees from Federal employment if they violate certain rules in connection with the performance of their official duties.

Appendices

Appendix A

Performance Measures Descriptions

Customer Service Representative (CSR) Level of Service[1]	The number of toll-free callers that either speak to a Customer Service Representative or receive informational messages divided by the total number of attempted calls.
Customer Accuracy – Tax Law Phones	The percentage of correct answers given by a live assistor on Toll-free tax law inquiries.
Customer Accuracy – Accounts (Phones)	The percentage of correct answers given by a live assistor on Toll-free account inquiries.
Timeliness of Critical Individual Filing Season Tax Products to the Public[2]	The percentage of critical individual filing season tax products (tax forms, schedules, instructions, and publications required by many filers to prepare a complete and accurate tax return) available to the public in a timely fashion.
Timeliness of Critical TE/GE & Business Tax Products to the Public[2]	Percentage of critical business tax products (tax forms, schedules, instructions, and publications used by many TE/GE and Business filers to prepare a complete and accurate return or form) available to the public in a timely fashion.
Percent Business Returns Processed Electronically	The percentage of electronically filed business tax returns divided by the total business returns filed.
Enterprise Self-Assistance Participation Rate[3]	The percentage of taxpayer assistance requests resolved using self-assisted automated services.
Taxpayers Satisfied with the IRS (based on 100-point scale)[4, *]	The percentage of taxpayers satisfied with the IRS according to the American Customer Satisfaction Index (ACSI) survey. The All Individual Tax Filer score is calculated from separate ACSI Individual Paper Filer and Electronic Filer Customer Satisfaction Index Scores. Based on a 100-point scale.
Examination Coverage – Individual (1040)	The sum of all individual 1040 returns closed by Small Business/Self Employed (SB/SE), Wage & Investment (W&I), Tax Exempt and Government Entities (TE/GE) and Large Business and International (LB&I) divided by the total individual return filings for the prior calendar year.
Examination Coverage – Business (Assets >$10M)	The number of LB&I returns (C and S Corporations with assets more than $10 million and all partnerships) examined and closed by LB&I during the current fiscal year divided by the number of filings for the preceding calendar year.
Examination Efficiency – Individual (1040)	The sum of all individual 1040 returns closed by SB/SE, W&I, TE/GE and LB&I (Field Exam and Correspondence Exam programs) divided by the total Full Time Equivalent (FTE) expended in relation to those individual returns.
Automated Underreporter (AUR) Coverage	A percentage representing the total number of W&I and SB/SE contact closures (a closure resulting from a case where SB/SE and W&I made contact) divided by the total return filings for the prior year.
Collection Coverage	The volume of collection work disposed divided by the volume of collection work available.
Time to Start Compliance Resolution[*]	The percentage of all individual income tax enforcement cases started within six months of the return posting date.
Time to Resolve Compliance Issue After Filing[*]	The average time it takes to close all individual income tax enforcement cases in days. This is an annual measure based on all cases closed in a fiscal year.
Repeat Noncompliance Rate[*]	The percentage of individual taxpayers in a fiscal year with additional non-compliance two years after the initial tax year that contains a filing, payment, or reporting compliance issue, compared to total taxpayers
Cost to Collect $100 (in cents) [*]	The cost of collecting $100 is computed as total operating costs divided by gross collection divided by 100.

Criminal Investigations Completed	The total number of subject criminal investigations completed during the fiscal year, including those that resulted in prosecution recommendations to the Department of Justice as well as those discontinued due to a lack of prosecution potential.
Conviction Rate	The percent of adjudicated criminal cases that result in convictions.
Rentable Square Feet per Person	The amount of rentable square feet the IRS maintains per personnel requiring space. The IRS will use this as an indicator for FY 2019.
Percent of Aged Hardware[5, *]	This measure shows the quantity of IT hardware in operation past its useful life as a percentage of total hardware in use.
Percent of Major IT Investments within +/- 10 Percent Cost Variance at the Investment Level[6]	Number of major IT investments within +/-10 percent variance between planned total cost and projected/actual cost within a fiscal year divided by the total number of major IT investments in that fiscal year.
Percent of Major IT Investments within +/- 10 Percent Schedule Variance at the Investment Level[6]	Number of major IT investments within +/-10 percent variance between planned days and projected/actual days within a fiscal year divided by the total number of major IT investments in that fiscal year.

1. The FY 2019 level of service target was calculated at the FY 2019 Enacted level.
2. Modified in FY 2019.
3. Starting in FY 2017, the IRS modified the Taxpayer Self Assistance Rate measure (renamed to Enterprise Self Assistance Participation Rate) to include additional self-service channels including Get Transcript and payment applications such as Direct Pay and Online Payment Agreements.
4. Based on the American Customer Satisfaction Index (ACSI) survey; the All Individual Tax Filer score is calculated from separate ACSI Individual Paper Filer and Electronic Filer customer satisfaction index scores; available on an annual basis at the end of January and computed on a 100-point scale.
5. The measure definition changed in FY 2018; removing certain asset categories (fax machines, low-end printers and scanners) that are no longer being actively refreshed from the calculation to more accurately define the inventory that's reflective of risk to the IT environment.
6. Starting in FY 2015, this measure includes all major IT investments (Business Systems Modernization (BSM) and non-BSM). In previous years, it included BSM only.

* New measure added for FY 2019 reporting.

Internal Revenue Service – FY 2019 Management's Discussion and Analysis

Appendix B

Performance Measurement Data

	2016	2017	2018	2019	
				Plan	Actual
Drive increased agility, efficiency, effectiveness and security in IRS operations					
Rentable Square Feet per Person	N/A	297	301	Indicator	298
Percent of Aged Hardware	N/A	N/A	45.5%	43.8%	31%
Percent of Major IT Investments within +/- 10 Percent Cost Variance at the Investment Level	76.2%	50.0%	72.2%	90.0%	88.9%
Percent of Major IT Investments within +/- 10 Percent Schedule Variance at the Investment Level	85.7%	88.9%	83.3%	90.0%	88.9%
Empower and enable all taxpayers to meet their tax obligations					
Customer Service Representative (CSR) Level of Service	53.4%	77.1%	75.9%	63.0%	65.4%
Customer Accuracy – Tax Law Phones	96.4%	96.7%	95.5%	92.0%	91.6%
Customer Accuracy – Customer Accounts (Phones)	96.1%	96.0%	96.1%	94.0%	94.3%
Timeliness of Critical Individual Filing Season Tax Products to the Public	92.5%	93.1%	59.6%	85.0%	92.6%
Timeliness of Critical TE/GE and Business Tax Products to the Public	98.0%	96.7%	100.0%	85.0%	96.1%
Percent Business Returns Processed Electronically	50.0%	52.9%	55.6%	58.0%	57.8%
Enterprise Self-Assistance Participation Rate	89.0%	79.0%	82.0%	Indicator	85.4%
Taxpayers Satisfied with the IRS[1]	74	74	74	Indicator	N/A
Protect the integrity of the tax system by encouraging compliance through administering and enforcing the tax code					
Examination Coverage – Individual (1040)	0.7%	0.6%	0.6%	0.5%	0.45%
Examination Coverage – Business (assets >$10M)	3.0%	2.5%	2.2%	2.2%	1.6%
Examination Efficiency – Individual (1040)	143	121	131	122	109
Automated Underreporter (AUR) Coverage	2.3%	2.2%	2.0%	1.6%	1.3%
Collection Coverage	43.4%	42.2%	41.6%	40.1%	41.3%
Time to Start Compliance Resolution[2]	-	-	-	Indicator	Under Development
Time to Resolve Compliance Issue After Filing (days)[2]	-	-	-	Indicator	Under Development
Repeat Non-Compliance Rate[2]	-	-	-	Indicator	Under Development
Cost to Collect $100 (in cents)[3]	-	-	-	Indicator	N/A
Criminal Investigations Completed	3,721	3,089	3,051	2,800	2,797
Conviction Rate	92.1%	91.5%	91.7%	92.0%	91.2%

74

1. Based on the American Customer Satisfaction Index (ACSI) survey; the All Individual Tax Filer score is calculated from separate ACSI Individual Paper Filer and Electronic Filer customer satisfaction index scores; available on an annual basis at the end of January and computed on a 100-point scale.
2. These new measures are currently under development.
3. Results for Cost to Collect $100 are not available until after the beginning of the calendar year.

Appendix C

Explanation of Shortfalls

Percent of Major IT Investments within +/- 10 percent Cost Variance at the Investment Level: Sixteen of 18 major investments (88.89 percent) were within the cost variance threshold at the close of the 4th quarter.

1. Account Management Services - The cost underrun was caused by the Account Management Services project redirecting funds from October 2018 to January 2019 to support tax reform and subsequently, required less labor than what was allocated for the July Mid-Year Release project.
2. Foreign Account Tax Compliance Act - The cost underrun was due to an accelerated schedule instigated by the lapse in appropriations which reduced the amount of contract labor hours.

IRS IT will continue to closely monitor cost reporting for investments in FY 2019 to improve current performance levels for this measure.

Percent of Major IT Investments within +/- 10 percent Schedule Variance at the Investment Level: Sixteen of 18 major investments (88.89 percent) were within the schedule variance threshold at the close of the 4th quarter.

1. Foreign Account Tax Compliance Act - The schedule variance is showing ahead of schedule due to no P1 or P2 defects being found during Milestone (MS) 5 window which would have required additional time and resources to resolve. Improvements in the quality of Enterprise Life Cycle documentation pre-work activities, and the improved MS4b process to finalize the Cybersecurity Concurrence Memo also aided in the early completion.
2. IRS End User Systems and Services - The ahead of schedule variance is due to the Scanners and Workstations Refresh projects combining resources from multiple organizations to achieve a faster than projected deployment.

IRS IT will continue to closely monitor schedule reporting for investments in FY 2019 to improve current performance levels for this measure.

Customer Accuracy – Tax Law Phones: Performance of 91.6 percent is 0.4 percent below the plan of 92 percent. The delay in training prior to Filing Season impacted the accuracy results. W&I will continue to monitor results through data-driven analysis of reports obtained from the Embedded Quality Review System to ensure achievement of future goals. Ongoing efforts have and will continue to focus on production meetings with field sites, promoting coding consistency of product reviews, and providing training to managers and employees to ensure quality service to customers.

Exam Coverage – Individual: Closures were short of plan due to the impact of the government shutdown and resumption activities, including delays in enforcement hiring. Significant staffing losses, including unplanned hiring across business units, also adversely affected closures. IRS Operating Divisions will monitor resources, starts, and work-in-process to ensure FY 2020 targets are met.

Examination Coverage – Business (assets >$10M): Coverage is 1.6 percent and below the FY 2019 target of 2.2 percent. Actual attrition has exceeded the attrition rate factored into the closure plan for FY 2019. LB&I is currently embarking upon a significant hiring initiative that will expand IRS resources available to examine large business returns going forward. Closures of corporate returns in the highest asset classes are well below plan in anticipation of the transition from the traditional coordinated industry case program to the new large corporate compliance program.

Examination Efficiency – Individual: Efficiency is below plan due to the five-week lapse in appropriations. In addition, the amount of overtime worked with no additional closures added to the workplan, negatively affected exam efficiency.

Percent Business Returns Processed Electronically: Business returns processed was 0.3 percent below the FY 2019 target of 58.0 percent. Business paper returns processed of 21.1 million was 4.7 percent above plan (20.2 million). Business returns processed electronically (29.0 million) was 2.5 percent above plan (28.3 million).

Automated Underreporter Coverage: Manpower was short of the plan due to the impact of the shutdown and resumption activities, including delays in the enforcement hiring timeline. SB/SE will monitor resources, work in process, and planned starts to ensure FY 2020 targets are met.

Criminal Investigations Completed: FY 2019 year-end results were three cases short (2,797) of the FY 2019 target and reflects an 8.3 percent decrease compared to FY 2018. Overall performance in FY 2019 continued to be impacted by a steady decrease in the number of special agents available to work cases (due to attrition and limited hiring) as well as Criminal Investigation's focus on traditional tax case programs, which tend to have a higher cycle time. Cases of Legal, Illegal and Narcotics nature completed through 4th quarter decreased (1.2 percent, 13.2 percent and 12.6 percent, respectively) compared to the same period in FY 2018. Criminal Investigation will continue to utilize proven case development strategies, expand case development efforts, and leverage interagency partnerships to identify, initiate and complete significant criminal investigations in all program areas.

Conviction Rate: The FY 2019 conviction rate is slightly below the year-end target of 92 percent. The average number of Acquittals and Dismissals remained comparable to previous years while the overall number of Convictions decreased 7.7 percent from FY 2018, contributing to the slight drop in the Conviction Rate. Appropriate case selection and effective field performance continue to positively affect the quality of cases. Consequently, Criminal Investigation's rate of conviction continues to be a strong indicator of investigative quality given that it is one of the highest in federal law enforcement. Since Criminal Investigation does not prosecute its own cases, it must depend on the ability of the Department of Justice to accept its cases for prosecution and to move such cases through the courts. Criminal Investigation's management will continue its current efforts of appropriate and consistent contact with the Department of Justice Tax Division and U.S. Attorney Offices regarding prosecutorial priorities and the appropriate movement of pipeline investigations to ensure a high rate of conviction.

Appendix D

Strategic Plan Measures

Strategic Goal	***Performance Measure***
Empower and enable all taxpayers to meet their tax obligations	**Enterprise Self-Assistance Participation Rate –** Measures the percent of instances where a taxpayer uses one of the IRS's self-assistance service channels (i.e., automated calls, web services) versus needing support from an IRS employee (i.e., face-to-face, over the phone, via paper correspondence). **Progress towards Goal: The** FY 2019 Enterprise Self-Assistance Participation Rate of 85.4 percent was 4.1 percent higher from the prior year of 82.0 percent. Compared to FY 2018, total services increased by 12.4 percent, self-assisted services increased by 17.1 percent and assisted services fell 6.5 percent.
Protect the integrity of the tax system by encouraging compliance through administering and enforcing the tax code	**Time to Start –** Measures the percentage of total instances where IRS compliance enforcement divisions contact a noncompliant taxpayer within six months of receiving a taxpayer's return (or when a taxpayer should have filed their return but may not have). **Progress towards Goal:** This measure is currently under development and expected to be reported in FY 2020.
Collaborate with external partners proactively to improve tax administration	**Enhanced Partnership Strategy –** Meeting key milestones in the IRS's ability to maintain and create new partnerships with external stakeholders (e.g., tax preparer community, international compliance/cyber security experts, other government agencies). **Progress towards Goal**: In FY 2019, the IRS worked to expand relationships outside the traditional outreach and communication channels to deliver messages about filing season readiness, tax scams, TCJA and other topics. During FY 2019, the IRS formed new relationships with special emphasis placed on reaching out to the underserved, millennials, and those who speak English as a second language. The IRS continued to partner with national and local partners to deliver free tax filing to millions of taxpayers through the VITA/ICE program. The IRS initiated new and innovative social media efforts that drew praise inside and outside government on Twitter, Facebook, LinkedIn, and for the first time, on Instagram. Other FY 2019 key accomplishments included holding EITC Awareness Day, holding Procurement Industry and Reverse Industry Day events, conducting Security Summits, and holding IRS Nationwide Tax Forums.
Cultivate a well-equipped, diverse, flexible and engaged workforce	**Employee Engagement –** Percentage of employees that say they feel engaged in their work as measured by Office of Personnel Management's index of relevant questions from the Federal Employee Viewpoint Survey. **Progress towards Goal:** In FY 2019, the IRS implemented the Leadership Engagement Action Plan for FY 2019-2021. This plan incorporated all IRS business units planning targeted efforts to enhance the workplace morale and retention service wide. In addition, the IRS complied with the President's Management Agenda, 20/20/20 engagement initiative. This enhanced employee feedback frequency and created tailored action plans for work units with the largest opportunities for improvement.

Advance data access, usability and analytics to inform decision-making and improve operational outcomes	**Data Strategy –** Meeting key milestones related to the creation and deployment of a data strategy. **Progress towards Goal:** In FY 2019 the IRS delivered an updated Enterprise Research Plan. The plan identified critically important projects, programs, and infrastructure advances from the IRS research community. Each selected project was organized into at least one of the six goals of the IRS Strategic Plan. The IRS expanded the new data and analytics steering group to improve coordination, decision-making, and alignment of data and analytics initiatives across business units. A learning agenda was also established that will facilitate better decision-making to meet the changing needs and expectations of taxpayers and members of the tax community. Formal charters were established for the Data & Analytics Strategic Integration Board and the Data & Analytics Advisory Group
Drive increased agility, efficiency, effectiveness and security in IRS operations	**Aged Hardware Percentage –** Quantity of hardware in operation past its useful life as a share of total hardware in use. **Progress towards Goal**: The IRS has made considerable progress reducing the percentage of aged hardware within the IT environment from 45.5 percent at the end of FY 2018 to 31 percent at the end of FY 2019. This represents a reduction of nearly 36,000 aged assets during the fiscal year through efforts such as refreshing employee workstations, upgrading aged server operating systems and related aged hardware, and phasing out old equipment. **Efficient Space Utilization –** Ratio that measures overall rentable square footage per person (includes contractors). **Progress towards Goal:** The IRS has continued to release excess office space through building closures and consolidations. In FY 2019, the Rentable Sq. Ft. per Person was 298, a one percent improvement over the same period in FY 2018. The IRS released more than 400,000 sq. ft. of space since FY 2018. This was used as an indicator for FY 2019.

Principal Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the Internal Revenue Service, pursuant to the requirements of the *Chief Financial Officers Act of 1990* (Public Law 101-576), the *Government Management Reform Act of 1994,* and the Office of Management and Budget Circular No. A-136, *Financial Reporting Requirements*. The responsibility for the integrity of the financial information included in these statements rests with the management of the IRS. The audit of the IRS principal financial statements was performed by the Government Accountability Office.

The IRS principal financial statements for fiscal years 2019 and 2018 are as follows:

- The **Balance Sheets** present the assets, liabilities, and net position.
- The **Statements of Net Cost** present the net cost of operations by program. It includes the gross costs less any exchange revenue earned from activities.
- The **Statements of Changes in Net Position** present the change in net position resulting from the net cost of operations, budgetary financing sources other than exchange revenues, and other financing sources.
- The **Statements of Budgetary Resources** present the budgetary resources; the status of those resources; and the agency outlays, net. Additional detail by major budget accounts is available in the Required Supplementary Information section.
- The **Statements of Custodial Activity** present the sources and disposition of non-exchange federal tax revenues collected and refunds disbursed.

Internal Revenue Service
Balance Sheets
As of September 30, 2019 and 2018

(In Millions)

	2019	2018
Assets		
Intragovernmental		
Fund balance with Treasury (Note 2)	$ 3,919	$ 3,206
Due from General Fund of the U.S. Government (Note 6)	2,922	2,974
Other assets (Note 3)	12	42
Total intragovernmental	**6,853**	**6,222**
Cash and other monetary assets (Notes 4, 6)	548	536
Federal taxes receivable, net (Notes 5, 6, 8)	144,000	58,000
General property and equipment, net (Note 7)	1,896	1,976
Other assets (Note 3)	15	13
Total assets	**$ 153,312**	**$ 66,747**
Liabilities		
Intragovernmental		
Due to General Fund of the U.S. Government (Note 8)	$ 144,954	$ 58,219
Other liabilities (Note 9)	164	166
Total intragovernmental	**145,118**	**58,385**
Federal tax refunds payable	2,922	2,974
Other liabilities (Note 9)	2,011	1,931
Total liabilities	**150,051**	**63,290**
Net position		
Unexpended appropriations	1,506	1,765
Cumulative results of operations	1,755	1,692
Total net position	**3,261**	**3,457**
Total liabilities and net position	**$ 153,312**	**$ 66,747**

The accompanying notes are an integral part of these statements.

2

Internal Revenue Service
Statements of Net Cost
For the Years Ended September 30, 2019 and 2018

(In Millions)

	2019	2018
Program		
Taxpayer Assistance and Education		
Gross cost	$ 536	$ 531
Earned revenue	(2)	(3)
Net cost of program	**534**	**528**
Filing and Account Services		
Gross cost	4,998	4,685
Earned revenue	(109)	(148)
Net cost of program	**4,889**	**4,537**
Compliance		
Gross cost	7,920	7,856
Earned revenue	(404)	(416)
Net cost of program	**7,516**	**7,440**
Administration of Tax Credit Programs		
Gross cost	138	137
Earned revenue	-	-
Net cost of program	**138**	**137**
Net cost of operations	**$ 13,077**	**$ 12,642**

The accompanying notes are an integral part of these statements.

3

Internal Revenue Service
Statements of Changes in Net Position
For the Years Ended September 30, 2019 and 2018

(In Millions)

	2019		2018	
	Unexpended Appropriations	**Cumulative Results of Operations**	**Unexpended Appropriations**	**Cumulative Results of Operations**
Beginning balances	**$ 1,765**	**$ 1,692**	**$ 1,513**	**$ 1,618**
Budgetary financing sources				
Appropriations received	11,303		11,431	
Other adjustments	(107)		(94)	
Appropriations used	(11,455)	11,455	(11,085)	11,085
Non-exchange revenues	-	97	-	38
Transfers in/out without reimbursement	-	9	-	25
Other financing sources				
Imputed financing (Note 12)		1,583		1,577
Transfers in/out without reimbursement		-		-
Transfers to General Fund of the U.S. Government		(4)		(9)
Total financing sources	**(259)**	**13,140**	**252**	**12,716**
Net cost of operations		**(13,077)**		**(12,642)**
Net change	**(259)**	**63**	**252**	**74**
Ending balances	**$ 1,506**	**$ 1,755**	**$ 1,765**	**$ 1,692**

The accompanying notes are an integral part of these statements.

4

Internal Revenue Service
Statements of Budgetary Resources
For the Years Ended September 30, 2019 and 2018

(In Millions)

	2019	2018
Budgetary resources		
Unobligated balance brought forward, October 1	$ 1,133	$ 1,058
Recoveries of prior year unpaid obligations	101	58
Other changes in unobligated balance	(24)	(57)
Unobligated balance from prior year budget authority, net	1,210	1,059
Appropriations (discretionary and mandatory)	11,789	11,854
Spending authority from offsetting collections (discretionary and mandatory)	135	196
Total budgetary resources	**$ 13,134**	**$ 13,109**
Status of budgetary resources		
New obligations and upward adjustments (total)	$ 12,108	$ 11,976
Unobligated balance, end of year		
Apportioned, unexpired accounts	565	730
Exempt from apportionment, unexpired accounts	8	7
Unapportioned, unexpired accounts	257	167
Unexpired unobligated balance, end of year	830	904
Expired unobligated balance, end of year	196	229
Unobligated balance, end of year (total)	1,026	1,133
Total budgetary resources	**$ 13,134**	**$ 13,109**
Outlays, net		
Outlays, net (total) (discretionary and mandatory)	$ 11,707	$ 11,379
Distributed offsetting receipts	(386)	(382)
Agency outlays, net (discretionary and mandatory)	**$ 11,321**	**$ 10,997**

The accompanying notes are an integral part of these statements.

5

Internal Revenue Service
Statements of Custodial Activity
For the Years Ended September 30, 2019 and 2018

(In Billions)

	2019	2018
Revenue activity		
Collections of federal tax revenue (Note 15)		
Individual income, FICA/SECA, and other	$ 3,177	$ 3,090
Corporate income	277	263
Excise	81	73
Estate and gift	18	24
Railroad retirement	6	6
Federal unemployment	6	9
Total collections of federal tax revenue	**3,565**	**3,465**
Increase in federal taxes receivable, net	86	6
Total federal tax revenue	**$ 3,651**	**$ 3,471**
Distribution of federal tax revenue due to General Fund of the U.S. Government	$ 3,565	$ 3,465
Increase in amount due	86	6
Total disposition of federal tax revenue	**3,651**	**3,471**
Net federal revenue activity	**$ -**	**$ -**
Federal tax refund and outlay activities		
Total refunds of federal taxes and outlays (Note 16)	$ 452	$ 464
Appropriations used for refund of federal taxes and outlays	(452)	(464)
Net federal tax refund and outlay activities	**$ -**	**$ -**

The accompanying notes are an integral part of these statements.

6

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

The Internal Revenue Service (IRS) is a bureau of the United States (U.S.) Department of the Treasury (Treasury). The IRS originated in 1862, when Congress established the Office of the Commissioner of the Internal Revenue. The IRS administers the nation's tax laws and annually collects 95 percent of the revenues funding the Federal Government. Numerous organizational divisions and major programs within the IRS contribute to this achievement.

Operating Divisions
The IRS has four operating divisions:

- Wage and Investment provides customer support, submission processing, and compliance activities with respect to individuals with wage and investment income;
- Small Business and Self-Employed administers compliance activities for small businesses, self-employed individuals, and others with income from sources other than wages;
- Tax Exempt and Government Entities oversees and assists employee plans, tax exempt organizations, and government entities in complying with tax laws and regulations; and
- Large Business and International serves corporations, subchapter S corporations and partnerships with assets greater than $10 million; which deal with complicated issues involving tax law and accounting principles, and conduct business in an expanding global environment.

Functional Divisions
Five functional divisions within the IRS provide enforcement services supporting both internal and external operations:

- Appeals
- Criminal Investigation
- Communications & Liaison
- Taxpayer Advocate Service
- Office of Chief Counsel

The National Taxpayer Advocate reports directly to Congress and the IRS Chief Counsel reports to the Secretary of the Treasury.

Support Divisions
Nine support divisions provide shared services support to all of the IRS organizations:

- Information Technology
- Agency-Wide Shared Services
- Stewardship
- Wage & Investment - Stewardship
- Executive Leadership and Direction
- Privacy, Governmental Liaison and Disclosure
- Human Capital Office
- Human Capital Office Corporate Programs
- Chief Financial Officer

Major Programs
The IRS has four major programs (further discussed in Note 1.K., Program Costs):

- Taxpayer Assistance and Education
- Filing and Account Services
- Compliance
- Administration of Tax Credit Programs

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

B. Basis of Accounting and Presentation

The financial statements have been prepared from the accounting records of the IRS in conformity with accounting principles generally accepted in the U.S. and in accordance with the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*. Accounting principles generally accepted for federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board, which is the official body for setting accounting standards of the Federal Government.

These comparative financial statements and related notes consist of the Balance Sheet, the Statement of Net Cost, the Statement of Changes in Net Position, the Statement of Budgetary Resources (SBR), and the Statement of Custodial Activity (SCA).

The accounting structure of federal agencies is designed to reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds. The SCA is presented on the modified cash basis of accounting. Under this method, cash collections and transfers to the General Fund of the U.S. Government are reported on a cash basis. The collections and transfers are adjusted on the face of the statement for the net change in taxes receivable, producing modified cash basis balances.

Certain assets, liabilities, earned revenues, and costs have been classified as intragovernmental throughout the financial statements and notes. Intragovernmental is defined as transactions made between two reporting entities within the Federal Government.

C. Fund Balance with Treasury

The fund balance with Treasury is the aggregate of funds in the accounts of the IRS, primarily appropriated funds, from which the IRS is authorized to make expenditures and pay liabilities.

The status of fund balance with Treasury represents amounts obligated and unobligated. The obligated balances not yet disbursed represent the unpaid funds with budgetary obligations. Unobligated balances, available represent amounts in unexpired appropriations as of the end of the current fiscal year. Unobligated balances become available when apportioned by the OMB. Unobligated balances, unavailable represent amounts in expired appropriations and amounts not apportioned for obligation as of the end of the current fiscal year.

D. Other Assets

Accounts receivable consist of amounts due to the IRS from the public and from federal agencies. Accounts receivable are recorded, and reimbursable revenues are recognized as the services are performed and costs are incurred. The allowance for uncollectible accounts is based on an annual review of groups of accounts by age for accounts receivable balances older than one year. Receivables include an expenditure transfer receivable from the Treasury Forfeiture Fund for the repayment of costs incurred in criminal investigations related to seizure and forfeitures.

Advances to the public represent cash outlays for criminal investigations and employee travel.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Forfeited property held for sale is acquired as a result of forfeiture proceedings or foreclosure sales to satisfy a tax liability. The Federal Tax Lien Revolving Fund, established in accordance with Title 26 United States Code (USC), Section 7810, is used to redeem real property foreclosed upon by a holder of a lien. The IRS may sell the property, reimburse the revolving fund in an amount equal to the redemption, and apply the net proceeds to the outstanding tax obligation.

E. Cash and Other Monetary Assets

Imprest funds are maintained by headquarters and field offices in commercial bank accounts. Other monetary assets consist primarily of offers-in-compromise, voluntary deposits received from taxpayers pending application of the funds to unpaid tax assessments, and seized monies pending the results of criminal investigations.

F. Federal Taxes Receivable, Net

Federal taxes receivable, net, are not accrued until related tax returns are filed or assessments are made by the IRS and agreed to by either the taxpayer or the court. Accruals are made to reflect penalties and interest on taxes receivable through the balance sheet date. The majority of the Due to General Fund of the U.S. Government balance is the offsetting liability of Federal taxes receivable, net.

Taxes receivable consist of unpaid assessments (taxes and associated penalties and interest) due from taxpayers. The existence of a receivable is supported by a taxpayer agreement, such as filing of a tax return without sufficient payment, or a court ruling in favor of the IRS. The Internal Revenue Code (IRC) §965 requires United States shareholders to pay a transition tax on the untaxed foreign earnings of certain specified foreign corporations as if those earnings had been repatriated to the United States. IRC §965(h) which allows taxpayers to elect to pay their 965(h) tax on an eight-year installment schedule and restitution-based assessments are included in the taxes receivable balance. The allowance reflects an estimate of the portion of total taxes receivable deemed to be uncollectible.

Compliance assessments are unpaid assessments which neither the taxpayer nor a court has affirmed is owed to the Federal Government. Examples include assessments resulting from an IRS audit or examination in which the taxpayer does not agree with the results. Write-offs consist of unpaid assessments for which the IRS does not expect further collections due to factors such as taxpayers' bankruptcy, insolvency, or death. Compliance assessments and write-offs are not reported on the balance sheet. Statutory provisions authorize the IRS to collect on unpaid assessments for a specific statutory timeframe. In order to pursue collections and account for collection efforts, the IRS maintains unpaid assessment accounts in the financial records until the statute for collection expires.

Tax Assessments

Under the Internal Revenue Code (IRC) §6201, the Secretary of the Treasury is authorized and required to make inquiries, determinations, and assessments of all taxes imposed and accrued under any internal revenue law, which have not been duly paid, including interest, additions to the tax, and assessable penalties. The Secretary has delegated this authority to the Commissioner of the IRS. Unpaid assessments result from taxpayers filing returns without sufficient payments and from the enforcement programs of the IRS, such as examination, under-reporter, substitute for return, and combined annual wage reporting.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Abatements

IRC §6404 authorizes the Commissioner of the IRS to abate certain paid or unpaid portions of assessed taxes, interest, and penalties. Abatements occur for a number of reasons and are a standard part of the tax administration process. Abatements may be allowed for qualifying corporations claiming net operating losses that create a credit when carried back and applied against a prior year's tax liability. Additionally, abatements can correct previous assessments from enforcement programs, eliminate taxes discharged in bankruptcy, reduce or eliminate taxes encompassed in offers-in-compromise, eliminate penalty assessments for reasonable cause, eliminate contested assessments caused by mathematical or clerical errors, and eliminate assessments contested after the liability has been satisfied. Abatements may result in claims for refunds or reductions of the unpaid assessed amounts.

G. General Property and Equipment

General property and equipment is recorded at historical cost. It consists of tangible assets and software. The IRS depreciates property and equipment on a straight line basis over its estimated useful life. Except for leases meeting the 75 percent useful life and/or 90 percent of net present value (NPV) criteria, the IRS records a half-year of depreciation in the first year and the final year for all property and equipment. The IRS depreciates leases meeting the 75 percent useful life and/or 90 percent of NPV criteria over the life of the leases, with no use of a half-year convention. Disposals are recorded when deemed material.

In fiscal year (FY) 2018, the IRS changed its capitalization threshold for telecommunications Information Technology (IT) equipment by implementing a threshold of $50 thousand or greater. Prior to FY 2018, this category was capitalized regardless of cost. Additionally, in FY 2018, the IRS changed its process of capitalizing leasehold improvements to construction in progress when projects have not yet been completed. Prior to FY 2018, leasehold improvements were capitalized and amortized when the services were received and accepted.

The IRS capitalization policy for property and equipment by asset class and threshold:

Asset Class	Capitalization Threshold
IT equipment	Bulk cost of $50 thousand or greater.
Non-IT equipment	Assets with bulk cost of $50 thousand or greater and the individual cost is $5 thousand or greater.
Furniture and fixtures	Assets with bulk cost of $50 thousand or greater and the individual cost is $5 thousand or greater.
Investigative equipment	Bulk cost of $50 thousand or greater.
Vehicles	No threshold.
Major systems	Projects with costs of $20 million or greater.
Internal use software	Projects with an estimated cost of greater than or equal to $10 million per year or greater than or equal to $50 million over the life cycle.
Leasehold improvements (LHI)	Improvements with bulk cost of $50 thousand or greater.
Assets under capital lease	Assets with bulk cost of $50 thousand or greater.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Prior to the implementation of Statement of Federal Financial Accounting Standards (SFFAS) No. 10, *Accounting for Internal Use Software*, Major systems was an asset class established to account for large-scale computer systems. These assets are fully depreciated, but still used in the IRS's daily operations and are reported on the financial statements.

Internal use software captures the costs of major Business Systems Modernization (BSM) projects in accordance with SFFAS No. 10. It encompasses software design, development, and testing of projects adding significant new functionality and long-term benefits. Costs for developing internal use software are accumulated in work in process until final acceptance and testing are successfully completed. When the software is completed and placed into service, the costs are transferred to amortizable property.

H. Due to General Fund of the U.S. Government

Due to General Fund of the U.S. Government is the liability for Federal taxes receivable, net and State Innovation Waiver Program (SIWP). It primarily represents amounts to be collected on behalf of the General Fund of the U.S. Government. The IRS provides funding for the SIWP to the Centers for Medicare and Medicaid Services (CMS) through two allocation accounts. SIWP are the issued awards by CMS, under Section 1332 of the Affordable Care Act, where the grantees participating in the program have not drawn down the funds per the term of the grant. The program is also referred to as a State Relief and Empowerment Waiver.

I. Federal Tax Refunds Payable and Due from General Fund of the U.S. Government

Federal tax refunds payable is comprised of measurable and legally payable amounts due to taxpayers under established refund processes of the IRS. It is a fully funded liability offset by a corresponding asset, Due from General Fund of the U.S. Government. The IRS records an amount Due from General Fund of the U.S. Government to designate approved funding to pay year-end tax refund liabilities to taxpayers.

J. Financing Sources and Revenues

Appropriations Received

The IRS receives the majority of its funding through annual, multi-year, and no-year appropriations available for use within statutory limits for operating and capital expenditures. Appropriations are recognized as budgetary financing sources when the related expenses are incurred.

Appropriations

The major budget accounts are:

- Taxpayer Services
- Enforcement
- Operations Support
- Other

Taxpayer Services provides funds for the direct costs of the Taxpayer Assistance and Education and the Filing and Account Services Programs discussed in Note 1.K., Program Costs.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Enforcement provides resources for the direct costs of the Compliance Program discussed in Note 1.K., Program Costs. Additionally, it funds the direct costs of administering the Earned Income Tax Credit Program (EITC).

Operations Support funds the indirect costs of all programs. Activities include executive planning and direction; shared service support for facilities, rent, utilities, and security; procurement; printing; postage; headquarters' activities such as strategic planning, finance, and human resources; research and statistics of income; and information systems, data processing, and telecommunication.

The IRS administers various tax provisions in the *Patient Protection and Affordable Care Act of 2010* (PPACA). The administrative costs are funded in the three major budget accounts: Taxpayer Services, Enforcement, and Operations Support.

Other primarily consists of the BSM appropriation, which provides resources for the planning and capital asset acquisition of information technology to modernize the business systems. Additionally, BSM is obligated pursuant to an expenditure plan submitted to Congress.

Exchange Revenues
Exchange revenues recognized by the IRS represent reimbursements and user fees. Reimbursements are recognized as the result of costs incurred for services performed for federal agencies or the public under reimbursable agreements. User fees are derived from transactions with the public and are generally recognized when collected.

Non-exchange Revenues
Budgetary financing sources includes non-exchange revenue collected for outstanding inactive Federal tax receivables through the IRS private debt collection program. The IRS is required by law to enter into qualified tax collection contracts to retain private collection agencies. The collection agents assist in the collection of certain outstanding tax receivables, on behalf of the Federal Government, to provide needed support to close the nation's tax gap.

Imputed Financing Sources
Other financing sources include imputed financing sources to offset the imputed costs recognized for goods or services received from other federal agencies without reimbursement from the IRS. The imputed costs are pension and other benefit costs administered by the Office of Personnel Management (OPM), costs of processing payments and collections by the Bureau of the Fiscal Service, and legal judgments paid by the Treasury Judgment Fund.

K. Program Costs

Taxpayer Assistance and Education provides services to assist taxpayers with tax return preparation. Primary activities include tax law interpretations, developing and disseminating tax forms and publications, researching customer needs and establishing partnerships with stakeholder groups, and taxpayer advocacy. In addition, these programs continue to emphasize taxpayer education, outreach, and enhancing pre-filing taxpayer support through electronic media. Earned revenues include reimbursable revenues from services provided.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Filing and Account Services provides resources and support services to taxpayers with filing returns or paying taxes, and for the issuance of refunds and maintenance of taxpayer accounts. Program activities include providing assistance, education, and compliance services to taxpayers through telephone, correspondence, and electronic means to resolve account and notice inquiries. Earned revenues include user fees from photocopies, U.S. Residency Certification and Income Verification Express Service, and reimbursable revenues from services provided.

Compliance administers compliance activities after a return is filed to identify and correct possible errors or underpayments. This program includes examination and collection programs, which ensure proper payment and tax reporting; criminal investigation programs to uncover violations of internal revenue tax laws and other financial crimes; the development and printing of published IRS guidance materials; and support of taxpayers for pre-filing agreements, determination letters, and advance pricing agreements. It also includes specialty program examinations, international collections, and international examinations. Earned revenues are primarily from user fees for installment agreements, letter rulings and determinations, offers-in-compromise and enrollment programs, Advance Pricing and Mutual Agreement, and reimbursable revenues from services provided.

Administration of Tax Credit Programs primarily administers the EITC program, which works closely with internal and external stakeholders through expanded customer service and public outreach, enforcement, and research efforts to increase the number of eligible taxpayers who claim the EITC and to reduce the number of EITC claims paid in error. The EITC payments actually refunded to individuals or credited against tax liabilities are not included in program costs.

L. Custodial Activity

Non-exchange Revenues
The IRS collects custodial non-exchange revenues for taxes levied against taxpayers for: individual and corporate income, Federal Insurance Contributions Act (FICA) and Self-Employment Contributions Act (SECA), excise, estate, gift, railroad retirement, and federal unemployment taxes. These collections are not available to the IRS for obligation or expenditure and are recognized as custodial revenues when collected. The sources of federal tax revenue and their distribution to the General Fund of the U.S. Government are reported on the SCA.

Permanent Indefinite Appropriations
The IRS was granted permanent and indefinite budgetary authority through legislation to disburse tax refund principal and related interest as they become due. The permanent and indefinite appropriations are not subject to budgetary ceilings set by Congress during the annual appropriation process.

Refunds due to taxpayers are reported as Federal tax refunds payable on the Balance Sheet. The IRS records an offsetting asset, Due from General Fund of the U.S. Government, to reflect the year-end budget authority to pay this liability.

Disbursements for tax refunds, refundable tax credits and related interest, reported on the SCA, are offset by appropriations used for refunds. Disbursements for refunds are not a cost to the IRS, but rather a cost to the Federal Government as a whole.

13

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

M. Funds from Dedicated Collections

In accordance with SFFAS No. 43, *Funds from Dedicated Collections: Amending Statement of Federal Financial Accounting Standards 27, Identifying and Reporting Earmarked Funds*, Funds from Dedicated Collections are financed by specifically identified revenues, which remain available over time. These specifically identified revenues are required by statute to be used for designated activities, benefits or purposes, and must be accounted for separately from the Federal Government's general revenues.

The Federal Tax Lien Revolving Fund (20X4413) was established pursuant to section 112(a) of the *Federal Tax Lien Act of 1966*, to serve as the source of financing for the redemption of real property by the United States.

Established under the *American Jobs Creation Act of 2004,* the Private Collection Agent Program (20X5510) ended in March 2009. The remaining unobligated funds were retained by the IRS. The *Fixing America's Surface Transportation Act*, Public Law 114-94, enacted in December 2015, amended Title 26 United States Code, Section 6306, requiring the IRS to contract with private collection agencies for the collection of delinquent taxes. The delinquent taxes have (1) been removed from the IRS's active inventory due to a lack of resources or inability to find the taxpayer; (2) passed more than one-third of the applicable limitation period and no IRS employee has been assigned to the debt; or (3) been assigned for collection, but more than a year has passed without interaction with the taxpayer for the purpose of increasing the probability of collection. The Private Collection Agent Program (20X5510) is allowed to expend retained funds for qualified tax collection contracts and collection enforcement activities. The Special Compliance Personnel Program Account (20X5622) requires the hiring, training, and employment of personnel in compliance with Section 6307.

N. Allocation Transfers

The IRS is a party to allocation transfers with other federal agencies as both a transferring (parent) entity and a receiving (child) entity. Allocation transfers are legal delegations by one department of its authority to obligate budget authority and outlay funds to another department. A separate fund account (allocation account) is created in the U.S. Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of balances are credited to this account, and subsequent obligations and outlays incurred by the child entity are charged to this allocation account as they execute the delegated activity on behalf of the parent. Financial activity related to these allocation transfers is reported in the financial statements of the parent entity, from which the underlying legislative authority, appropriations, and budget apportionments are derived. The IRS allocates funds, as the parent, to the U.S. Department of Health and Human Services (HHS). Additionally, the IRS receives allocation transfers, as the child, from the U.S. Department of Transportation's Federal Highway Administration and HHS.

O. Fiduciary Activities

Fiduciary activities are the collection or receipt, and the management, protection, accounting, investment, and disposition by the Federal Government of cash or other assets in which non-federal individuals or entities have an ownership interest the Federal Government must uphold.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

The IRS fiduciary activities include the net collections for a taxable year from U.S. military and federal employees working in the U.S. territories of the Northern Mariana Islands, the U.S. Virgin Islands, Guam, and American Samoa. These fiduciary assets are not assets of the IRS.

P. Employee Compensation and Benefits

Accrued Annual, Sick, and Other Leave
Annual and compensatory leave is expensed with an offsetting liability as it is earned, and the liability is reduced as leave is taken. Each year, the IRS adjusts the balance in the accrued annual leave liability account to reflect current pay rates. To the extent current or prior year appropriations are not available to fund annual and compensatory leave earned but not taken, funding is obtained from future financing sources. Sick leave and other types of non-vested leave are expensed as taken.

Federal Employees' Compensation Act
The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases, and to beneficiaries of employees whose deaths were attributed to job-related injuries or occupational diseases. The FECA program is administered by the U.S. Department of Labor (DOL), which pays valid claims and subsequently seeks reimbursement for claims paid. Accrued FECA liability represents amounts due to the DOL for claims paid on behalf of the IRS. Actuarial FECA liability represents the liability for future workers' compensation benefits, which includes the expected liability for death, disability, medical, and miscellaneous costs for approved cases. The DOL estimates the liability for future payments as a result of past events.

Employee Pension Benefits
The IRS recognizes the full costs of its employees' pension benefits. The liabilities associated with these costs are reported by the OPM, who administers the plans. Eligibility of employees to participate in the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS) is based on their hire date with the Federal Government, and the IRS contributes a percentage of an employee's basic pay toward the employee's retirement plan.

EMPLOYEE PENSION BENEFIT CONTRIBUTION RATES

	Category	Employee	Agency
CSRS Rates	Regular	7.0%	7.0%
	Law Enforcement Officers	7.5%	7.5%
FERS Rates	Regular	0.8%	13.7%
Hired prior to January 1, 2013	Law Enforcement Officers	1.3%	30.1%
FERS – Revised Annuity Rate	Regular	3.1%	11.9%
Hired January 1, 2013 - December 31, 2013	Law Enforcement Officers	3.6%	28.4%
FERS – Further Revised Annuity Rate	Regular	4.4%	11.9%
Hired January 1, 2014 or later	Law Enforcement Officers	4.9%	28.4%

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Employees covered by either CSRS or FERS are also eligible to contribute to the Thrift Savings Plan (TSP), a defined contribution plan. A TSP account is automatically established for employees participating in FERS, and the IRS makes a mandatory contribution to this plan equal to one percent of an employee's compensation. Additionally, the IRS matches up to four percent of the compensation for FERS-eligible employees contributing to their TSP accounts. No TSP matching contributions are made for employees participating in the CSRS.

Employee Health and Life Insurance Benefits
Employees are eligible to participate in the Federal Employees Health Benefit Program (FEHB) and Federal Employees' Group Life Insurance Program (FEGLI). The FEHB offers a wide variety of group plans and coverage. The coverage is available to employees, retirees, and their eligible family members. The cost for each plan varies and is shared between the IRS and the employee. An employee participating in the FEGLI program can obtain basic term life insurance, with the employee paying two-thirds of the cost and the IRS paying one-third. Additional coverage is optional, to be paid fully by the employee. The basic life coverage may continue into retirement if certain requirements are met. The IRS recognizes the full cost of providing these benefits.

Q. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions related to the reporting of assets, liabilities, revenues, expenses, and the disclosure of contingent liabilities. Actual results could differ from those estimates.

R. Classified Activities

Accounting standards require reporting entities to disclose the accounting standards allow certain presentations and disclosures to be modified, if needed, to prevent the disclosure of classified information.

S. Statement of Changes in Net Position

In accordance with the FY2019 Treasury United States Standard General Ledger crosswalk for the Statement of Changes in Net Position (SCNP), a change was made to reclassify non-exchange revenues as a separate presentation. Previously, non-exchange revenues were reported as transfers in/out without reimbursement. The fiscal year 2018 balance reported for transfers in/out without reimbursement on the SCNP has been reclassified to conform to the presentation in the current year.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 2. Fund Balance with Treasury

(In Millions)	2019	2018
Fund balance with Treasury	**$ 3,919**	**$ 3,206**

(In Millions)	2019	2018
Unobligated balances		
Available	$ 573	$ 737
Unavailable	453	396
Obligated balance not yet disbursed	1,935	1,853
Non-budgetary and other FBWT	958	220
Status of fund balance with Treasury	**$ 3,919**	**$ 3,206**

Non-budgetary and other FBWT includes Section 1332 SIWP funds. As of September 30, 2019, the grantee has not drawn down the funds per the terms of the grant. In FY 2019 and FY 2018, the SIWP funds were $954 million and $219 million, respectively.

Note 3. Other Assets

	2019		2018	
(In Millions)	Intra-governmental	With the Public	Intra-governmental	With the Public
Accounts receivable, net	$ 12	$ 6	$ 42	$ 5
Advances	-	9	-	8
Other assets	**$ 12**	**$ 15**	**$ 42**	**$ 13**

Note 4. Cash and Other Monetary Assets

(In Millions)	2019	2018
Imprest fund	$ 3	$ 3
Other monetary assets	545	533
Cash and other monetary assets	**$ 548**	**$ 536**

17

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 5. Federal Taxes Receivable, Net

(In Billions)	2019	2018
Federal taxes receivable	$ 369	$ 218
Allowance for uncollectible taxes receivable	(225)	(160)
Federal taxes receivable, net	**$ 144**	**$ 58**

Federal taxes receivable are taxes due from taxpayers for which IRS can support the existence of a receivable through either a taxpayer agreement or a court ruling determining an assessment. Federal taxes receivable, net is the portion of Federal taxes receivable estimated to be collectible and the corresponding liability is Due to General Fund of the U.S. Government which is to be transferred when collected. The taxes receivable consists primarily of two categories:

- Internal Revenue Code (IRC) §965(h) which allowed taxpayers to elect to pay their 965(h) tax on an eight-year installment schedule. Growth in taxes receivable is largely due to the inclusion of non-delinquent §965(h) amounts, and
- Delinquent tax assessments, penalties, and interest not paid or abated, which were agreed to by the taxpayer and the IRS or upheld by the courts.

The Allowance for uncollectible taxes receivable represents the difference between the gross Federal taxes receivable and the portion estimated to be collectible based on collectability projections for the same categories. The $144 billion in Federal taxes receivable, net represents the total amount of taxes receivable estimated to be collectible as of September 30, 2019. The net collectible §965(h) is $98 billion and net collectible delinquent tax assessments are $46 billion.

For each of the taxes receivable categories, specific collectability methods were applied:

- **IRC §965(h) elections**. In FY 2019, the IRS used an econometric model to derive its estimates of collectability. This model considers the average collectability histories of unpaid assessments as well as indicators of the degree to which 965(h) taxpayers are considered to be at-risk of nonpayment based on their assessment and payment history.
- **Delinquent tax assessments**. To derive the estimated collectability rate applied to delinquent gross Federal taxes receivable, the IRS utilized the 2019 sample collectible point estimate of $51 billion (+/- $9.3 billion). The IRS averaged three years of collectability rates (2017-2019) to normalize the effect of significant year-to-year fluctuations. In FY 2018, the $58 billion in taxes receivable, net was derived from a three-year average including the 2018 collectible point estimate of $37 billion (+/-$6.5 billion). In FY 2018, unrecorded Insurance Provider Fees and Branded Prescription Drug fees were included in net taxes receivables. There were no Insurance Provider Fees collected in FY 2019.

18

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 6. Non-entity Assets

(In Millions)	2019 Intra-governmental	2019 With the Public	2018 Intra-governmental	2018 With the Public
Due from General Fund of the U.S. Government	$ 2,922	$ -	$ 2,974	$ -
Federal taxes receivable, net	-	144,000	-	58,000
Other monetary assets	-	545	-	533
Non-entity assets	**$ 2,922**	**$ 144,545**	**$ 2,974**	**$ 58,533**

Non-entity assets are not available for use by the IRS. Federal taxes receivable, net is collected for the U.S. Government, but the IRS does not have the authority to spend them.

Note 7. General Property and Equipment, Net

(In Millions)	Useful Life (Years)	Cost	Accumulated Depreciation	2019 Net Book Value	2018 Net Book Value
IT equipment	3 to 7	$ 1,280	$ (833)	$ 447	$ 393
Internal use software (IUS)	2 to 15	2,976	(1,926)	1,050	1,228
Leasehold improvements (LHI)	2 to 10	230	(159)	71	86
Major systems	7	221	(221)	-	-
IUS - software in development		255	-	255	193
Vehicles	5	3	(3)	-	-
Furniture and non-IT equipment	8 and 10	184	(142)	42	50
Assets under capital lease	4.5 to 8	28	(13)	15	17
Investigative equipment	10	4	(3)	1	1
LHI construction in progress		15	-	15	8
Property and equipment		**$ 5,196**	**$ (3,300)**	**$ 1,896**	**$ 1,976**

The Cost column represents the historical cost of property and equipment, net of disposals. The cost basis for FY 2019 and FY 2018 is $5,196 million and $5,034 million, respectively. Accumulated depreciation for FY 2019 and FY 2018 is $3,300 million and $3,058 million, respectively.

Internal use software projects (deployed and software in development) include:

- Account Management Services (AMS) provides the applications to monitor and interface with taxpayers, issue enhanced notices, and deliver improved customer support and functionality.
- Customer Account Data Engine 2 (CADE 2) is leveraging existing systems and new development to implement a single data-centric solution, which provides daily processing of individual taxpayer accounts.
- Enterprise Case Management (ECM) will provide an enterprise solution for performing case management functions using a common infrastructure platform and common services.
- Foreign Account Tax Compliance Act (FATCA) is a system to enable foreign financial institutions to report information to the IRS about financial accounts held by U.S. taxpayers or foreign entities in which U.S. taxpayers hold a substantial ownership interest.
- Information Reporting and Document Matching (IRDM) is a business document matching program designed to increase voluntary compliance and accurate reporting of income through the use of third-party information reporting data.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Internal use software projects (deployed and software and development) include (continued):

- Integrated Financial System (IFS) is the administrative financial system.
- Knowledge Incident/Problem Service Asset Management (KISAM) is the asset and problem management system.
- Modernized e-file (MeF) is an electronic filing system for tax returns.
- PPACA are the systems to support tax administration responsibilities.
- Return Review Program (RRP) is an automated system designed to maximize fraud detection at the time tax returns are filed.
- Web Applications (Web Apps) is a program to improve the taxpayer's online experience, provide secure digital communications, and add more interactive capabilities to existing web self-service products.

Work in Process Internal Use Software

(In Millions)	2019	2018
CADE 2	$ 214	$ 160
RRP	27	14
Web Apps	4	2
ECM	10	17
Work in process internal use software	**$ 255**	**$ 193**

Deployed Internal Use Software

(In Millions)	Cost	Accumulated Depreciation	2019 Net Book Value	2018 Net Book Value
AMS	$ 78	$ (54)	$ 24	$ 29
CADE 2	347	(290)	57	88
FATCA	316	(164)	152	197
IRDM	59	(56)	3	9
IFS	167	(166)	1	4
KISAM	6	(6)	-	-
MeF	405	(380)	25	41
PPACA	995	(410)	585	685
RRP	200	(84)	116	118
Web Apps	110	(23)	87	57
Other	293	(293)	-	-
Deployed internal use software	**$ 2,976**	**$ (1,926)**	**$ 1,050**	**$ 1,228**

Other deployed internal use software projects fully depreciated, include:

- Customer Communications is a customer service telephone system.
- Custodial Detail Database (CDDB), the subsidiary ledger for Redesigned Revenue Accounting Control System (RRACS), provides the functionality needed for custodial financial management and reporting.
- E-Services is a system of web-based products and services for tax practitioners and the public.
- Enterprise Systems Management (ESM) is an infrastructure system allowing remote monitoring and network management.
- Internet Refund Fact of Filing allows taxpayers to review the status of their refund.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Other deployed internal use software projects fully depreciated, include (continued):

- RRACS adds enhancements to financial reporting of taxpayer receipts and adds traceability between summary records and the detailed subsidiary ledger (CDDB).
- Security and Technology Infrastructure Release (STIR) is the infrastructure for information technology security.

Note 8. Due to General Fund of the U.S. Government

(In Millions)	2019	2018
Federal taxes receivable, net	$ 144,000	$ 58,000
Fund balance with Treasury	954	219
Due to General Fund of the U.S. Government	**$ 144,954**	**$ 58,219**

Due to General Fund of the U. S. Government reports General Fund assets we hold and manage on behalf of the U.S. Government. These General Fund assets constitute resources available to meet the operating needs of the U.S. Government. The Federal taxes receivable, net is the portion of gross Federal taxes receivable estimated to be collectible and will be transferred to the General Fund when collected. The fund balance with Treasury represents funds to administer the SIWP. These funds are not available for use by the IRS.

Note 9. Liabilities

Other Liabilities

	2019		
(In Millions)	Current	Non-Current	Total
Intragovernmental			
Accrued payroll and benefits	$ 78	$ -	$ 78
Accrued FECA liability	37	46	83
Accrued expenses	1	-	1
Capital lease liabilities	1	1	2
Other liabilities	**$ 117**	**$ 47**	**$ 164**
With the Public			
Accrued annual leave	$ 517	$ -	$ 517
Actuarial FECA liability	-	444	444
Accrued payroll and benefits	273	-	273
Accrued expenses	213	-	213
Liability for deposit funds and clearing accounts	546	-	546
Accounts payable	16	-	16
Energy savings performance liability	1	1	2
Other liabilities	**$ 1,566**	**$ 445**	**$ 2,011**

21

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Other Liabilities

(In Millions)	2018 Current	2018 Non-Current	2018 Total
Intragovernmental			
Accrued payroll and benefits	$ 72	$ -	$ 72
Accrued FECA liability	39	48	87
Accrued expenses	6	-	6
Capital lease liabilities	-	1	1
Other liabilities	**$ 117**	**$ 49**	**$ 166**
With the Public			
Accrued annual leave	$ 472	$ -	$ 472
Actuarial FECA liability	-	456	456
Accrued payroll and benefits	240	-	240
Accrued expenses	199	-	199
Liability for deposit funds and clearing accounts	533	-	533
Accounts payable	14	-	14
Capital lease liabilities	3	10	13
Energy savings performance liability	1	3	4
Other liabilities	**$ 1,462**	**$ 469**	**$ 1,931**

Liabilities Not Covered by Budgetary Resources

(In Millions)	2019	2018
Intragovernmental		
Accrued FECA liability	$ 83	$ 87
Capital lease liabilities	2	1
Intragovernmental	**85**	**88**
With the public		
Accrued annual leave	517	472
Actuarial FECA liability	444	456
Energy savings performance liability	2	4
With the public	**963**	**932**
Liabilities not covered by budgetary resources	1,048	1,020
Liabilities covered by budgetary resources	148,457	61,737
Liabilities not requiring budgetary resources	546	533
Liabilities	**$ 150,051**	**$ 63,290**

Liabilities not covered by budgetary resources result from the receipt of goods and services, or occurrence of eligible events in the current or prior periods, for which revenue to pay the liabilities has not been made available through appropriations of the IRS.

22

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 10. Leases

Capital Leases

The IRS leases IT telecommunications equipment for toll free call centers, and currently has a two-year lease and two seven-year leases. There are no future payments due for the equipment under these active leases. The liability for the two-year lease was paid in FY 2012, and title for the equipment remains with the vendor. The liability for the two seven-year leases was paid in FY2011 at the beginning of the leases.

In FY 2018 the IRS entered into a software license agreement for five years with perpetual use rights to the licenses. The liability for the software license agreement was paid in FY 2019.

The IRS has a lease with the General Services Administration (GSA) for vehicles used for enforcement and leases for furniture. The vehicles are being leased over a period of three to five years; the lease payments were completed in FY 2019. The furniture is being leased over a period of five years.

Summary of Assets Under Capital Lease:

(In Millions)

Capital Lease Category	2019	2018
Telecom equipment	$ 8	$ 8
Non-IT equipment	-	-
Software license agreement	17	17
Vehicles	1	1
Furniture	2	2
Accumulated depreciation	(13)	(11)
Assets under capital lease, net	**$ 15**	**$ 17**

Future minimum payments due are as follows:

(In Millions)	2019		
Fiscal Year	Intra-governmental	With the Public	Total
2020	$ 1	$ -	$ 1
2021	1	-	1
After 2021	-	-	-
Capital lease liabilities	**$ 2**	**$ -**	**$ 2**

Capital lease liabilities not covered by budgetary resources	**$ 2**
Capital lease liabilities covered by budgetary resources	**$ -**

23

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Operating Leases

The IRS leases office space from GSA and commercial entities under non-cancelable operating leases with lease terms from 1 to 30 years. This includes all GSA occupancy agreements the IRS determined to be non-cancelable. Future lease payments under non-cancelable leases of office spaces are presented below.

(In Millions) Fiscal Year	2019 Intra-governmental	2019 With the Public	2019 Total
2020	$ 161	$ 6	$ 167
2021	144	1	145
2022	78	-	78
2023	64	-	64
2024	60	-	60
After 2024	285	-	285
Future lease payments	**$ 792**	**$ 7**	**$ 799**

Additionally, the IRS has annual operating leases with the GSA for office space and vehicles, and with commercial entities for equipment and software licenses. These leases may be canceled or renewed on an annual basis at the option of the IRS. They do not impose binding commitments on the IRS for future rental payments on leases with terms longer than one year.

Note 11. Commitments and Contingencies

The IRS is a party to legal actions whose outcome, if unfavorable, could materially affect the financial statements. As of September 30, 2019, and 2018, there were no estimated contingent liabilities arising from these actions.

For some of the legal actions to which the IRS is a party, management and legal counsel cannot determine the likelihood of an unfavorable outcome nor can any related loss be reasonably estimated. The IRS does not accrue for possible losses related to cases where the potential loss cannot be estimated or the likelihood of an unfavorable outcome is less than probable. As of September 30, 2019 and 2018, there are respectively two cases each for which management and legal counsel are unable to determine the likelihood of an unfavorable outcome or establish a range of potential losses. Additionally, for some of the legal actions, management and legal counsel have determined the likelihood of an unfavorable outcome is remote.

As of September 30, 2019, and 2018, the IRS does not have contractual commitments for payments on obligations related to canceled appropriations or contractual arrangements for which the IRS has not recognized liabilities for goods and services provided.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 12. Inter-Entity Costs

(In Millions)	2019	2018
Fiscal Service cost for tax collections and refunds	$ 911	$ 914
Federal Employees Benefit Programs	671	646
Treasury Judgement Fund	1	17
Inter-Entity Costs	**$ 1,583**	**$ 1,577**

Goods and services are received from other federal entities at no cost or at a cost less than the full cost to the providing federal entity. Consistent with the accounting standards, certain costs of the providing entity that are not fully reimbursed are recognized as imputed cost in the statement of net cost and are offset by imputed revenue in the statement of changes in net position. Such imputed costs and revenues relate to business-type activities, employee benefits and claims to be settled by the Treasury Judgement Fund. However, unreimbursed costs of goods and services other than those identified above are not included in the IRS financial statements.

Note 13. Undelivered Orders at the End of the Period

	2019		
(In Millions)	Intra-governmental	With the Public	Total
Unpaid	$ 164	$ 1,216	$ 1,380
Paid	-	9	9
Undelivered orders at the end of the period	**$ 164**	**$ 1,225**	**$ 1,389**

	2018		
(In Millions)	Intra-governmental	With the Public	Total
Unpaid	$ 122	$ 1,241	$ 1,363
Paid	-	9	9
Undelivered orders at the end of the period	**$ 122**	**$ 1,250**	**$ 1,372**

Undelivered orders are the value of goods and services ordered and obligated, but not yet received. This amount includes any prepaid or advanced orders for which delivery or performance has not yet occurred.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 14. Statement of Budgetary Resources

Explanation of Differences Between the FY 2018 Statement of Budgetary Resources and the *FY 2020 Budget of the United States Government*

(In Millions)	Budgetary Resources	New Obligations and Upward Adjustments	Distributed Offsetting Receipts	Outlays, Net
Statement of Budgetary Resources	$ 13,109	$ 11,976	$ 382	$ 11,379
Not included on the *Budget of the United States Government*				
Expired funds	(268)	-	-	-
Offsetting receipts	-	-	(382)	-
Not included on the Statement of Budgetary Resources				
Refundable tax credits, interest refunds to taxpayers, and other outlays	142,002	142,002	-	133,614
Informant payments	215	215	-	215
Other	(1)	6	-	3
Budget of the United States Government	**$ 155,057**	**$ 154,199**	**$ -**	**$ 145,211**

The *FY 2021 Budget of the United States Government* presenting the actual amounts for the year ended September 30, 2019 has not been published as of the issue date of these financial statements and will be available at a future date. A reconciliation of the FY 2018 SBR and the FY 2018 actual amounts in the *FY 2020 Appendix, Budget of the United States Government* for budgetary resources, new obligations and upward adjustments, distributed offsetting receipts, and outlays, net is presented above.

Refundable tax credits, interest refunds, other outlays and Informant payments total $142.2 billion in appropriations. These appropriations primarily consist of EITC, Premium Tax Credit, and Child Tax Credit and are reported with refunds on the SCA and are not reported on the SBR.

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 15. Collections of Federal Tax Revenue

(In Billions)	Tax Year 2019		Tax Year 2018	Tax Year 2017	Tax Year Prior Years	Collections Received FY 2019	Collections Received FY 2018
Individual income, FICA/SECA, and other	$ 2,023	*	$ 1,088	$ 38	$ 28	$ 3,177	$ 3,090
Corporate income	182	**	85	4	6	277	263
Excise	51		30	-	-	81	73
Estate and gift	1		14	1	2	18	24
Railroad retirement	5		1	-	-	6	6
Federal unemployment	4		2	-	-	6	9
Collections of federal tax revenue	**$ 2,266**		**$ 1,220**	**$ 43**	**$ 36**	**$ 3,565**	**$ 3,465**

* Includes other collections of $141 million.
** Includes tax year 2020 corporate income tax receipts of $6 billion.

Note 16. Federal Tax Refund and Outlay Activities

(In Billions)	Tax Year 2019	Tax Year 2018	Tax Year 2017	Tax Year Prior Years	Refunds and Outlays FY 2019	Refunds and Outlays FY 2018
Individual income, FICA/SECA, and other	$ 58	$ 301	$ 30	$ 9	$ 398	$ 402
Corporate income	4	15	11	22	52	60
Excise	1	1	-	-	2	1
Estate and gift	-	-	-	-	-	1
Federal tax refund and outlay activities	**$ 63**	**$ 317**	**$ 41**	**$ 31**	**$ 452**	**$ 464**

Federal tax refunds and outlays include overpayments from taxpayers; payments for the various refundable credits, including EITC and the Premium Tax Credit; and other payments, including the Cost Sharing Reduction (CSR), Basic Health Program, and the SIWP under the PPACA. In FY 2018, an executive order was issued to discontinue CSR payments and the SIWP was added as an outlay.

27

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 17. Fiduciary Activities

(In Millions)	2019 20X6737	20X6738	20X6740	20X6741	Total
Fiduciary net assets, beginning of year	$ -	$ 8	$ -	$ -	$ 8
Contributions	11	22	238	12	283
Disbursements to and on behalf of beneficiaries	(11)	(11)	(238)	(11)	(271)
Increase in fiduciary net assets	-	11	-	1	12
Fiduciary net assets, end of year	**$ -**	**$ 19**	**$ -**	**$ 1**	**$ 20**

(In Millions)	2018 20X6737	20X6738	20X6740	20X6741	Total
Fiduciary net assets, beginning of year	$ -	$ 9	$ -	$ -	$ 9
Contributions	9	19	260	10	298
Disbursements to and on behalf of beneficiaries	(9)	(20)	(260)	(10)	(299)
Decrease in fiduciary net assets	-	(1)	-	-	(1)
Fiduciary net assets, end of year	**$ -**	**$ 8**	**$ -**	**$ -**	**$ 8**

In fiduciary fund 20X6738, the fiduciary net assets, end of year balances are pending a tax matter resolution.

In accordance with the SFFAS No. 31, *Accounting for Fiduciary Activities*, fiduciary cash and other assets are not assets of the Federal Government. The IRS has four fiduciary funds not reported on the balance sheet:

- Internal Revenue Collections for Northern Mariana Islands 20X6737
- Coverover Withholdings – U.S. Virgin Islands 20X6738
- Coverover Withholdings – Guam 20X6740
- Coverover Withholdings – American Samoa 20X6741

IRC §7654 governs the tax coordination between the governments of the United States and the U.S. territories of the Northern Mariana Islands, the U.S. Virgin Islands, Guam, and American Samoa.

The collections of federal income taxes withheld from U.S. military and federal employees working in these U.S. territories are maintained in fiduciary funds of the IRS. The disbursements of these collections to these U.S. territory governments represent the transfer of the individual tax liability for a taxable year.

28

INTERNAL REVENUE SERVICE

Notes to the Financial Statements

For the Years Ended September 30, 2019 and 2018

Note 18. Budget and Accrual Reconciliation

(In Millions)	2019 Intra-governmental	2019 With the Public	2019 Total
Net Cost of Operations	**$ 4,596**	**$ 8,481**	**$ 13,077**
Components of net cost that are not part of net outlays:			
Property, plant, and equipment depreciation	-	(407)	(407)
Property, plant, and equipment disposal and reevaluation	-	(42)	(42)
Other	-	187	187
Increase/decrease in assets:			
Accounts receivable	(30)	1	(29)
Increase/decrease in liabilities			
Accounts payable	-	(2)	(2)
Salaries and benefits	(6)	(33)	(39)
Other liabilities	8	(33)	(25)
Other financing sources			
Federal costs imputed to the agency	(1,583)	-	(1,583)
Transfers out(in) without reimbursement	(9)	-	(9)
Total components of net cost not part of the net outlays	**(1,620)**	**(329)**	**(1,949)**
Components of the net outlays that are not part of net cost			
Acquisition of capital assets	1	192	193
Total components of the net outlays that are not part of net cost	**1**	**192**	**193**
Net outlays	**$ 2,977**	**$ 8,344**	**$ 11,321**

In accordance with the SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting, amended* and SFFAS No. 53, *Budget and Accrual Reconciliation,* the IRS' relationship between the net cost of the programs and operations presented on an accrual basis must be reconciled to the net outlays presented on the budgetary basis during the reporting period. The accrual basis of accounting reports the net cost of resources used. Budgetary accounting reports the outlays of financial resources to acquire or provide goods and services.

29

INTERNAL REVENUE SERVICE

Required Supplementary Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Schedule of Budgetary Resources by Major Budget Accounts

(In Millions)	2019 Taxpayer Services	2019 Enforcement	2019 Operations Support	2019 Other	2019 Total
Budgetary resources					
Unobligated balance brought forward, October 1	$ 64	$ 64	$ 325	$ 680	$ 1,133
Recoveries of prior year unpaid obligations	12	19	65	5	101
Other changes in unobligated balance	24	5	173	(226)	(24)
Unobligated balance from prior year budget authority, net	100	88	563	459	1,210
Appropriations (discretionary & mandatory)	2,557	4,678	3,918	636	11,789
Spending authority from offsetting collections (discretionary & mandatory)	35	37	56	7	135
Total budgetary resources	**$ 2,692**	**$ 4,803**	**$ 4,537**	**$ 1,102**	**$ 13,134**
Status of budgetary resources					
New obligations and upward adjustments (total)	$ 2,650	$ 4,678	$ 4,361	$ 419	$ 12,108
Unobligated balance, end of year					
Apportioned, unexpired accounts	3	92	60	410	565
Exempt from apportionment, unexpired accounts	-	-	-	8	8
Unapportioned, unexpired accounts	-	-	-	257	257
Unexpired unobligated balance, end of year	3	92	60	675	830
Expired unobligated balance, end of year	39	33	116	8	196
Unobligated balance, end of year (total)	42	125	176	683	1,026
Total budgetary resources	**$ 2,692**	**$ 4,803**	**$ 4,537**	**$ 1,102**	**$ 13,134**
Outlays, net					
Outlays, net (total) (discretionary & mandatory)	$ 2,556	$ 4,537	$ 4,287	$ 327	$ 11,707
Distributed offsetting receipts	-	-	-	(386)	(386)
Agency outlays, net (discretionary & mandatory)	**$ 2,556**	**$ 4,537**	**$ 4,287**	**$ (59)**	**$ 11,321**

INTERNAL REVENUE SERVICE

Required Supplementary Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Schedule of Budgetary Resources by Major Budget Accounts (continued)

	2018				
(In Millions)	Taxpayer Services	Enforcement	Operations Support	Other	Total
Budgetary resources					
Unobligated balance brought forward, October 1	$ 90	$ 95	$ 258	$ 615	$ 1,058
Recoveries of prior year unpaid obligations	6	11	37	4	58
Other changes in unobligated balance	(33)	(9)	171	(186)	(57)
Unobligated balance from prior year budget authority, net	63	97	466	433	1,059
Appropriations (discretionary & mandatory)	2,513	4,627	4,198	516	11,854
Spending authority from offsetting collections (discretionary & mandatory)	70	57	69	-	196
Total budgetary resources	**$ 2,646**	**$ 4,781**	**$ 4,733**	**$ 949**	**$ 13,109**
Status of budgetary resources					
New obligations and upward adjustments (total)	$ 2,582	$ 4,717	$ 4,408	$ 269	$ 11,976
Unobligated balance, end of year					
Apportioned, unexpired accounts	24	15	193	498	730
Exempt from apportionment, unexpired accounts	-	-	-	7	7
Unapportioned, unexpired accounts	-	-	-	167	167
Unexpired unobligated balance, end of year	24	15	193	672	904
Expired unobligated balance, end of year	40	49	132	8	229
Unobligated balance, end of year (total)	64	64	325	680	1,133
Total budgetary resources	**$ 2,646**	**$ 4,781**	**$ 4,733**	**$ 949**	**$ 13,109**
Outlays, net					
Outlays, net (total) (discretionary & mandatory)	$ 2,469	$ 4,582	$ 4,061	$ 267	$ 11,379
Distributed offsetting receipts	-	-	-	(382)	(382)
Agency outlays, net (discretionary & mandatory)	**$ 2,469**	**$ 4,582**	**$ 4,061**	**$ (115)**	**$ 10,997**

Other Claims for Refunds

Management has estimated amounts that may be paid out as other claims for tax refunds. This estimate represents an amount (principal and interest), which may be paid for claims pending judicial review by the federal courts or, internally, by Appeals. In fiscal year (FY) 2019, the total estimated payout (including principal and interest) for claims pending judicial review by the federal courts is $7.8 billion and by Appeals is $2.3 billion. In FY 2018, the total estimated payout (including principal and interest) for claims pending judicial review by the federal courts was $11.1 billion and by Appeals was $1.8 billion. To the extent judgments against the government in these cases prompt other similarly situated taxpayers to file similar refund claims; these amounts could become significantly greater.

31

INTERNAL REVENUE SERVICE

Required Supplementary Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Federal Taxes Receivable, Net

In accordance with the Statements of Federal Financial Accounting Standards No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, some unpaid assessments do not meet the criteria for financial statement recognition as discussed in Note 1.F., Federal Taxes Receivable, Net and Note 1.H., Due to General Fund of the U.S. Government. Although compliance assessments and write-offs are not considered receivables under federal accounting standards, they represent legally enforceable claims of the IRS acting on behalf of the Federal Government. There is, however, a significant difference in the collection potential of these categories.

The components of the total unpaid assessments and derivation of net Federal taxes receivable were as follows:

(In Billions)	2019	2018
Total unpaid assessments	$ 550	$ 398
Compliance assessments	(75)	(65)
Write-offs	(106)	(115)
Gross federal taxes receivables	369	218
Allowance for uncollectible taxes receivable	(225)	(160)
Federal taxes receivable, net	**$ 144**	**$ 58**

Total unpaid assessments include $160 billion of non-delinquent IRC §965(h) tax of which $97.5 billion is collectible based on the collection history and the type of taxpayer. The non-delinquent IRC §965(h) component refers to taxpayers who elected to pay their 965 tax on an eight-year installment schedule. (see Note 5) Due to a legislative moratorium within the *Consolidated Appropriations Act 2016*, no Insurance Provider Fees were collected in FY 2019.

To eliminate double-counting, the compliance assessments reported above exclude duplicated trust fund recovery penalties assessed against officers and directors of businesses involved in the non-remittance of federal taxes withheld from their employees. These penalties totaled approximately $1.5 billion as of September 30, 2019 and $1.4 billion as of September 30, 2018. The related unpaid assessments of those businesses are reported as taxes receivable or write-offs, but the IRS may also recover portions of those businesses' unpaid assessments from any and all individual officers and directors against whom a trust fund recovery penalty is assessed.

The IRS cannot reasonably estimate the allowance for uncollectible amounts pertaining to its compliance assessments, and thus cannot determine their net realizable value or the value of the pre-assessment work in process.

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Refundable Tax Credits and Other Outlays

Refundable Tax Credits

To offer tax relief to targeted individuals and businesses, Congress has provided assistance in the form of tax credits. For the majority of tax credits, the economic benefit is limited to the taxpayer's tax liability. Credits limited in this manner are termed non-refundable credits. Refundable credits, in contrast, are fully payable to the taxpayer, even if the credit exceeds the tax liability. These types of credits provide greater economic benefits because the taxpayer realizes the full amount of the credit, regardless of the underlying tax liability.

The following overview summarizes the refundable credits the IRS administers and pays. This overview describes refundable credits in existence for many years, and those created more recently by Congress, including those enacted as part of the *American Recovery and Reinvestment Act of 2009* (ARRA) and the *Patient Protection and Affordable Care Act of 2010* (PPACA).

Earned Income Tax Credit

The Earned Income Tax Credit (EITC) is a refundable tax credit for low to moderate income working individuals and families. Congress originally approved the tax credit legislation in 1975, in part, to offset the burden of social security taxes and to provide an incentive to work. To qualify, taxpayers must meet certain requirements and file a tax return, even if they did not have sufficient income to meet regular tax return filing requirements.

Premium Tax Credit

Starting January 1, 2014, persons who purchase health insurance coverage through the Health Insurance Marketplace may be eligible for the premium tax credit. In general, a person is eligible for the credit if they (a) buy health insurance through the Marketplace, (b) are ineligible for coverage through an employer or government plan, (c) are within certain income limits, (d) do not file a Married Filing Separately tax return (unless they meet specific criteria that allow certain victims of domestic abuse to claim the premium tax credit using the Married Filing Separately filing status for the 2014 calendar year), and (e) cannot be claimed as a dependent by another person. Eligible individuals may elect to have some or all of their estimated credit paid in advance directly to their insurance company to lower the amount they must pay out-of-pocket for their monthly premiums or they may elect to receive all of the credit when they file their tax return. Each person who receives the benefit of a credit advance or who wishes to claim the credit must file an income tax return.

Additional Child Tax Credit

The Additional Child Tax Credit is a special credit for taxpayers who work, have earnings below an established ceiling, and have a qualifying child. The Child Tax Credit is limited to the taxpayer's tax liability and is a nonrefundable tax credit. However, certain individuals who receive less than the full amount of the Child Tax Credit may qualify for the "Additional" Child Tax Credit. Under this credit, subject to additional criteria, the taxpayer may receive the full credit amount even if such amount exceeds the taxpayer's tax liability. Consequently, the Additional Child Tax Credit is categorized as a refundable tax credit. This refundable credit, set to expire at the end of 2012, was extended through December 2017, by the *American Taxpayer Relief Act of 2012*.

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Build America and Recovery Zone Bonds

Build America Bonds (BABs) are a financing tool for state and local governments. The bonds, which allow a new direct federal payment subsidy, are taxable bonds issued by state and local governments to give them access to the conventional corporate debt markets. At the election of the state and local governments, the U.S. Department of Treasury (Treasury) will make a direct payment to the state or local governmental issuer in an amount equal to 35 percent of the interest payment on the BABs. This federal subsidy payment provides state and local governments lower net borrowing costs and allows them to reach more sources of borrowing than they can with more traditional tax-exempt or tax credit bonds.

Created by the ARRA, Recovery Zone Bonds are targeted to areas particularly affected by job losses and help local governments obtain financing for much needed economic development projects, such as public infrastructure development.

Qualified Zone Academy Bonds and Qualified School Construction Bonds

Congress created Qualified Zone Academy Bonds and Qualified School Construction Bonds to help schools raise funds to renovate and repair buildings, invest in equipment and current technology, develop more challenging curricula, and train teachers. The tax credit portion of these bonds depends on the issuance date of the bonds, the number of bonds outstanding, and the time remaining until their redemption.

Qualified Energy Conservation Bonds and New Clean Renewable Energy Bonds

Qualified Energy Conservation Bonds (QECB) may be issued by state, local, and tribal governments to finance qualified energy conservation projects. A minimum of 70 percent of a state's allocation must be used for governmental purposes, and the remainder may be used to finance private activity projects. QECBs were originally structured as tax credit bonds. However, the March 2010 *Hiring Incentives to Restore Employment* (HIRE) *Act* (H.R. 2847 (Sec. 301)) changed QECB from tax credit bonds to direct subsidy bonds similar to BABs. The QECB issuer pays the investor a taxable coupon and receives a rebate from Treasury.

New Clean Renewable Energy Bonds (CREBs) may be issued by public power utilities, electric cooperatives, government entities (states, cities, counties, territories, Indian tribal governments), and certain lenders to finance renewable energy projects. CREBs were originally structured as tax credit bonds. However, the March 2010 HIRE Act (H.R. 2847 (Sec. 301)) changed CREBs from tax credit bonds to direct subsidy bonds similar to BABs. The issuer pays the investor a taxable coupon and receives a rebate from Treasury.

American Opportunity Tax Credit

The American Opportunity Tax Credit modifies the existing Hope Credit. The credit was extended to apply for tax years through 2017 by the *American Taxpayer Relief Act of 2012*. This tax credit makes the Hope Credit available to a broader range of taxpayers, including many with higher incomes and those who owe no tax. Additionally, it adds required course materials to the list of qualifying expenses and allows the credit to be claimed for four post-secondary education years instead of two. Many of those eligible will qualify for the maximum annual credit of $2,500 per student.

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Corporate Alternative Minimum Tax Credit

Internal Revenue Coe (IRC) §168(k)(4) allows a taxpayer to elect to claim a refundable credit for certain unused research credits in lieu of the special depreciation allowance for eligible property.

Health Coverage Tax Credit

The federal Health Coverage Tax Credit (HCTC) was created by the *Trade Act of 2002* to help certain displaced workers and certain retirees pay for health insurance. Generally, those eligible to claim the credit fall into one of two categories: 1) trade-impacted workers who have lost their jobs because of increased imports or a shift in production to another country and are classified as Trade Adjustment Assistance (TAA) or Alternative Trade Adjustment Assistance (ATAA) and, 2) individuals whose pensions are being paid by the Pension Benefit Guaranty Corporation (PBGC), are at least 55 years of age and not entitled to Medicare.

The *Trade Preferences Extension Act of 2015* (Public Law 114-27) extended and modified the expired HCTC. Previously, those eligible for the HCTC could claim the credit against the premiums they paid for certain health insurance coverage through 2013. The HCTC can now be claimed for coverage through 2019. Eligible participants are responsible for paying 27.5 percent of their insurance premium while the IRS is responsible for paying the remaining 72.5 percent.

In general, eligible taxpayers will claim the HCTC for 2016 when they file their federal income tax returns in 2017. However, the IRS implemented a limited interim process for making advance monthly payments in the summer of 2016. This process was only available to individuals for months they were enrolled in qualified health coverage and working with their Health Plan Administrator or a Third-Party Administrator that was willing to meet certain IRS requirements and enter into a Memorandum of Understanding (MOU) with the IRS.

Payments for Disaster Related Tax Relief

On September 29, 2017, the President of the United States of America signed into law H.R. 3823, known as the *Disaster Tax Relief and Airport and Airway Extension Act of 2017* (the Act), which provides a series of relief measures for zones and areas affected by hurricanes Harvey, Irma and Maria, among other matters. Pursuant to Section 504(d)(1)(B) of the Act, the Secretary of the Treasury shall pay to Puerto Rico amounts estimated by the Secretary of the Treasury as being equal to the aggregate benefits that would have been provided to residents of Puerto Rico by reason of the provisions of Title V of the Act if a mirror code tax system had been in effect in Puerto Rico.

Small Business Health Insurance Tax Credit

Certain small employers are eligible for a tax credit, provided they contribute a uniform percentage of at least 50 percent toward their employees' health insurance. For nonprofit (tax-exempt) organizations, the credit cannot exceed the total amount of income and Medicare tax (i.e., hospital insurance) withholdings the employer must make and the related employer share of Medicare tax on employees' wages.

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Other Outlays

Cost Sharing Reduction

In addition to the premium tax credit, individuals who purchased a qualified health care plan through the Marketplace could qualify for Cost Sharing Reductions (CSR) based on their family income. This lowered the amount they had to pay for out-of-pocket costs such as deductibles, coinsurance, and copayments. Unlike the premium tax credit, these subsidies were not tax credits and were not reported on the recipient's income tax return. The CSR program was administered jointly by the U.S. Department of Health and Human Services and the IRS. These CSR payments were outlays of the Federal Government.

On October 10, 2017, the Attorney General issued a formal legal opinion on the permanent, indefinite appropriation for refunding internal revenue collections, 31 U.S.C. §1324, indicating the appropriation is not available to fund the CSR payments authorized by section 1302 of the Affordable Care Act, 42 U.S.C. §18071. Considering the Attorney General's opinion, the Acting Secretary of HHS issued a directive on October 11th prohibiting CSR payments, and on October 12th an executive order was issued to discontinue CSR payments effective October 1, 2017.

Basic Health Program

Section 1331 of the PPACA gives states the option of creating a health benefits coverage program for low-income residents who would otherwise be eligible to purchase coverage through the Health Insurance Marketplace. The Basic Health Program (BHP) gives states the ability to provide more affordable coverage for these low-income residents and improve continuity of care for people whose income fluctuates above and below Medicaid and Children's Health Insurance Program levels. These subsidies, which are Federal Government outlays, are not tax credits and are not reported on the recipient's income tax return. In addition, the CSR portion of the BHP was terminated and no further quarterly payments were disbursed in FY 2018.

State Innovation Waiver Program

Starting January 1, 2017, the states can apply for a waiver under Section 1332 of the Affordable Care Act. The waivers will enable the states to implement innovative ways for providing access to quality health care to their residents. The coverage must be at least as comprehensive and affordable as would be provided absent the waiver. In addition, the states must extend coverage to a comparable number of residents as would be provided coverage absent a waiver and must not increase the federal deficit. Pass through funding is the foundation of the waivers, which will grant the states the equivalent of the forgone financial assistance they otherwise would receive absent the waiver, such as the Premium Tax Credit (IRC §36B), and the Small Business Health Tax Credit (IRC §45R).

Interest on Tax Refunds

The IRS pays interest on refunds sent later than 45 days from the filing deadline of the return. Additionally, interest is generally paid on amended returns that result in a refund. Returns that have been examined and show an overpayment also result in the payment of interest. The interest rate on overpayments is adjusted quarterly.

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Payments of refundable tax credits in excess of tax liabilities and other outlays in FY 2019 and FY 2018 are shown below.

(In Millions)	2019	2018
Earned Income Tax Credit	$ 59,209	$ 58,640
Premium Tax Credit*	43,619	41,694
Additional Child Tax Credit	28,898	18,597
Build America and Recovery Zone Bonds	3,357	3,539
Qualified Zone Academy Bonds	43	57
Qualified School Construction Bonds	650	680
Qualified Energy Conservation Bonds	40	40
New Clean Renewable Energy Bonds	48	46
American Opportunity Tax Credit	2,881	3,102
Corporate Alternative Minimum Tax Credit	8,233	1,120
Health Coverage Tax Credit	24	27
Payments for Disaster Related Tax Relief	200	250
Small Business Health Insurance Tax Credit	-	1
Cost Sharing Reduction**	(335)	(507)
Basic Health Program	5,095	4,750
State Innovation Waiver Program	204	26
Interest on Tax Refunds	2,042	1,551
Refundable tax credits and other outlays	**$ 154,208**	**$ 133,613**

*Includes advanced amounts for the Premium Tax Credit. Beginning in FY 2015, preliminary outlay amounts are adjusted upward or downward based on information from tax returns. In FY 2019 and FY 2018, total Premium Tax Credit advances disbursed by the Center for Medicare and Medicaid Services totaled $52,608 and $49,340, respectively. The FY 2019 and FY 2018 advanced amounts were adjusted downward based on tax return information.

**Negative amount represents funds CMS recovered from insurance companies.

37

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Social Security and Medicare Taxes

The Federal Insurance Contributions Act (FICA) provides for a federal system of old-age, survivors, disability, and hospital insurance benefits. Payments to trust funds established for these programs are financed by payroll taxes on employee wages and tips, employers' matching payments, and a tax on self-employment income.

A portion of FICA benefits involves old-age, survivors, and disability payments. These benefits are funded by the social security tax, which is currently 6.2 percent of wages and tips up to $132,900, and an employer matching amount of 6.2 percent, bringing the total rate to 12.4 percent for calendar year 2019. In calendar year 2018, the rate was 6.2 percent of wages and tips up to $128,400 and an employer matching amount of 6.2 percent, bringing the total rate to 12.4 percent. These benefits are also funded by a self-employment tax of 12.4 percent on self-employment income up to $132,900 and $128,400 for calendar years 2019 and 2018, respectively. Remaining benefits under FICA pertain to hospital benefits (referred to as Medicare) and are funded by a separate 1.45 percent tax on all wages and tips (there is no wage limit) and the employer matching contribution of 1.45 percent, for a total of 2.9 percent. Self-employed individuals pay a Medicare tax of 2.9 percent on all self-employment income. Beginning in 2013, an additional Medicare tax of 0.9 percent was collected on earned individual income of more than $200,000 and $250,000 for married couples filing jointly. Social security taxes collected by the IRS were approximately $923 billion and $863 billion in FY 2019 and FY 2018, respectively. Medicare taxes collected by the IRS were approximately $279 billion and $262 billion in FY 2019 and FY 2018, respectively. Social security taxes and Medicare taxes are included in the Individual income, FICA/SECA, and other financial statement line on the Statement of Custodial Activity.

Tax Expenditures

The *Congressional Budget and Impoundment Control Act of 1974* (Public Law 93-344) defines tax expenditures as "revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability." Tax expenditures are the foregone federal revenue resulting from deductions and credits provided in the Internal Revenue Code. Since tax expenditures directly affect funds available for government operations, decisions to forego federal revenue are as important as decisions to spend federal revenue.

While the term "revenue losses" is used in the statutory definition, tax expenditures have traditionally been measured as reductions in federal tax revenues relative to normal baseline provisions of an individual and corporate income tax system, which were properly approved and authorized by the Congress to accomplish identified policy objectives, recognizing that federal tax revenues would be reduced.

In accordance with Statement of Federal Financial Accounting Standards 52, *Tax Expenditures*, narrative disclosures and information regarding tax expenditures are reported in the consolidated *Financial Report of the U.S. Government*. Such disclosures do not apply to the financial statements of component reporting entities such as the IRS. Tax expenditures also do not affect the reporting in the *Budget of the U.S. Government* or any other special purpose report.

38

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018

Tax Gap and Tax Burden

Tax Gap

The gross tax gap is the amount of true tax liability for a given tax year not paid voluntarily and/or timely. The IRS develops tax gap estimates on a periodic basis. In September 2019, the IRS issued tax gap estimates for the tax year (TY) 2011-2013 timeframe. Like the TY 2008-2010 tax gap estimates, these estimates reflect an average compliance rate and average annual tax gap for a timeframe of three years. This approach was selected as it provides more reliable tax gap estimates by category and source of noncompliance. The estimated average annual gross tax gap for the TY 2011-2013 timeframe is $441 billion.

There are three primary sources of noncompliance:
(1) nonfiling tax gap (the tax not paid on time by those who do not file required returns on time);
(2) underreporting tax gap (the net understatement of tax on timely filed returns); and
(3) underpayment tax gap (the amount of tax reported on timely filed returns not paid on time).

The estimated gross tax gap of each of these components is $39 billion for nonfiling, $352 billion for underreporting, and $50 billion for underpayments. Additionally, the gross tax gap can be grouped by type of tax, as follows:

- $314 billion for individual income tax,
- $ 42 billion for corporation income tax,
- $ 81 billion for employment tax, and
- $ 3 billion for combined estate and excise tax.

(The estimates of the component breakouts may not add to the $441 billion total due to rounding.)

The net tax gap is the gross tax gap less tax subsequently paid either voluntarily paid late or collected through IRS administrative and enforcement activities. As a result, the net tax gap is the portion of the gross tax gap that will not be paid. The portion of gross tax gap that is estimated to be eventually collected is $60 billion, resulting in a net tax gap of $381 billion. The estimated net tax gap by type of tax is:

- $271 billion for individual income tax,
- $ 32 billion for corporation income tax,
- $ 77 billion for employment tax, and
- $ 1 billion for combined estate and excise tax.

Tax Burden

The IRC provides for progressive rates of tax, whereby higher incomes are generally subject to higher rates of tax. The following pages present in both graph and table format various income levels and tax liability levels reported by individuals and corporations (that is, these amounts do not account for tax burdens that taxpayers do not report on their returns). This information is the most recent available for individuals (tax year 2017) and corporations (tax year 2016). The graphs and charts are representative of more detailed data and analyses available from the IRS Statistics of Income Office.

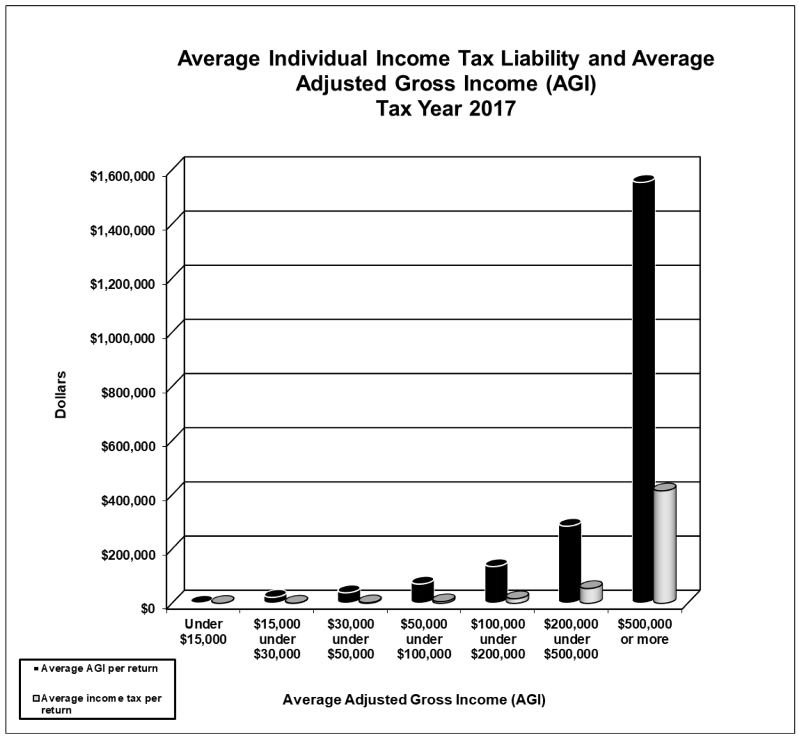
For individuals, the information illustrates, in both percentage and dollar terms, the tax burden that taxpayers bear by varying levels of Adjusted Gross Income (AGI). The corporate information illustrates, for varying corporate asset categories, the tax burden borne by these entities as a percentage of taxable income.

39

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018



Adjusted gross income (AGI).	Number of taxable returns (in thousands)	AGI (in millions)	Total income tax (in millions)	Average AGI per return (in whole dollars)	Average income tax per return (in whole dollars)	Income tax as a percentage of AGI
Under $15,000	34,167	$ 19,440	$ 1,990	$ 569	$ 58	10.2%
$15,000 under $30,000	29,474	652,767	18,925	$ 22,147	$ 642	2.9%
$30,000 under $50,000	27,125	1,062,968	59,757	$ 39,188	$ 2,203	5.6%
$50,000 under $100,000	34,467	2,457,203	218,619	$ 71,291	$ 6,343	8.9%
$100,000 under $200,000	19,951	2,707,841	340,993	$ 135,725	$ 17,092	12.6%
$200,000 under $500,000	6,215	1,770,816	339,963	$ 284,926	$ 54,700	19.2%
$500,000 or more	1,505	2,338,866	625,034	$ 1,554,064	$ 415,305	26.7%
Totals	152,904	$ 11,009,901	$ 1,605,281			

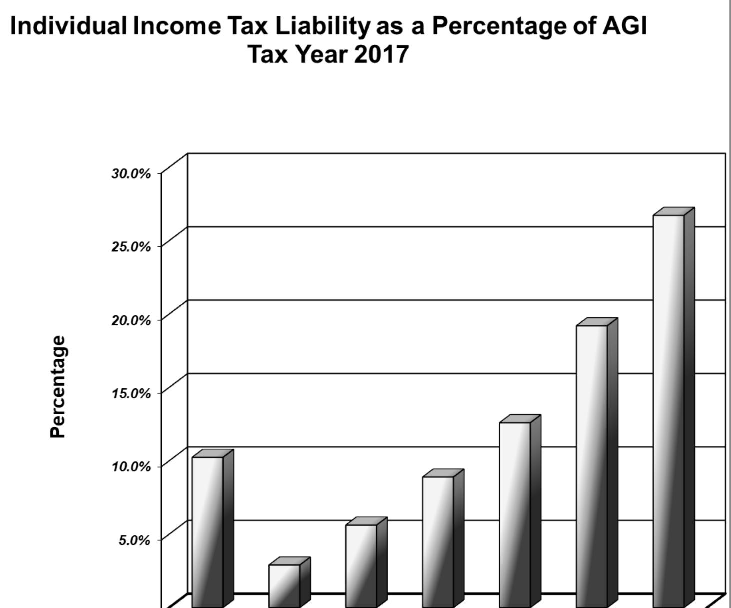
(All figures are estimates and based on samples provided by the Statistics of Income Office.)

40

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018



	Under $15,000	$15,000 under $30,000	$30,000 under $50,000	$50,000 under $100,000	$100,000 under $200,000	$200,000 under $500,000	$500,000 or more
Income tax as a percentage of AGI	10.2%	2.9%	5.6%	8.9%	12.6%	19.2%	26.7%

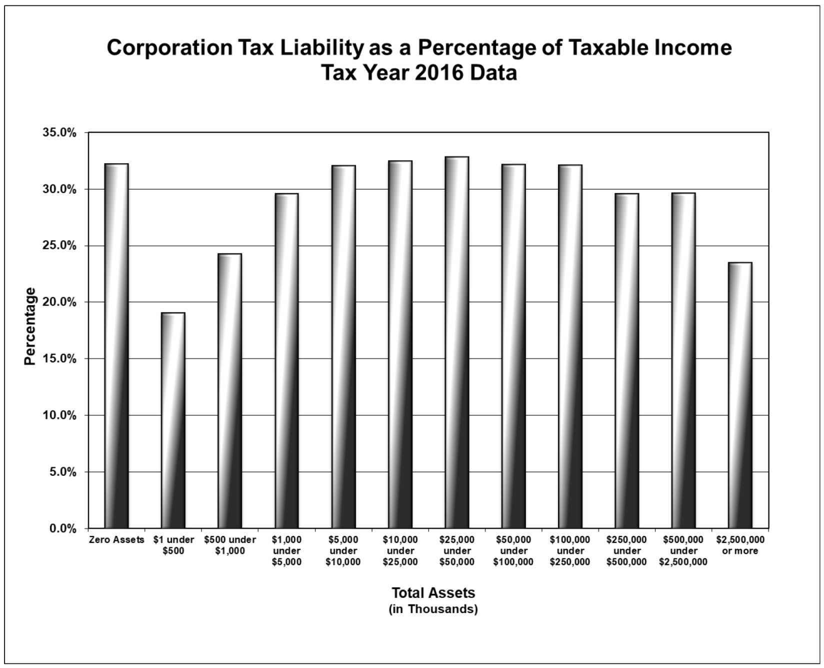
(All figures are estimates and based on samples provided by the Statistics of Income Office.)

41

INTERNAL REVENUE SERVICE

Other Information - Unaudited

For the Years Ended September 30, 2019 and 2018



Total Assets (in thousands)	Income subject to tax (in millions)	Total income tax after credits (in millions)	Percentage of income tax after credits to taxable income
Zero Assets	$ 32,008	$ 10,314	32.2%
$1 under $500	7,032	1,337	19.0%
$500 under $1,000	3,716	901	24.2%
$1,000 under $5,000	13,109	3,879	29.6%
$5,000 under $10,000	8,362	2,678	32.0%
$10,000 under $25,000	13,270	4,309	32.5%
$25,000 under $50,000	12,686	4,163	32.8%
$50,000 under $100,000	14,401	4,630	32.2%
$100,000 under $250,000	24,546	7,883	32.1%
$250,000 under $500,000	26,100	7,715	29.6%
$500,000 under $2,500,000	105,577	31,259	29.6%
$2,500,000 or more	1,010,414	237,291	23.5%
Totals	**$ 1,271,221**	**$ 316,359**	

(All figures are estimates and based on samples provided by the Statistics of Income Office.)

42

Appendix I: Management's Report on Internal Control over Financial Reporting

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

COMMISSIONER

November 7, 2019

Ms. Cheryl E. Clark
Director, Financial Management and Assurance
U.S. Government Accountability Office
441 G Street, NW, Room 5474
Washington, DC 20548

Dear Ms. Clark:

The Internal Revenue Service's (IRS's) internal control over financial reporting is a process effected by those charged with governance and management, as well as other personnel with related responsibilities. The objectives of this process are to provide reasonable assurance that: (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. Generally Accepted Accounting Principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and (2) transactions are executed in accordance with provisions of applicable laws, including those governing the use of budget authority, regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the financial statements.

IRS management is responsible for maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error. IRS management evaluated the effectiveness of the IRS's internal control over financial reporting as of September 30, 2019, based on the criteria established under 31 U.S.C. 3512(c), (d) (commonly known as the Federal Managers' Financial Integrity Act).

Based on that evaluation, we conclude that as of September 30, 2019, the IRS has two significant deficiencies in its internal control over financial reporting, for unpaid assessments and financial reporting systems. On this basis, management provides unmodified assurance that as of September 30, 2019, the IRS's internal control over financial reporting was effective.

Charles P. Rettig
Commissioner of Internal Revenue

November 7, 2019
Date

Jeffrey J. Tribiano
Deputy Commissioner, Operations Support

November 7, 2019
Date

Ursula S. Gillis
Chief Financial Officer

November 7, 2019
Date

Appendix II: Comments from the Internal Revenue Service

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

COMMISSIONER

November 1, 2019

Ms. Cheryl E. Clark
Director
Financial Management and Assurance
U.S. Government Accountability Office
441 G Street, NW, Room 5474
Washington, DC 20548

Dear Ms. Clark:

Thank you for the opportunity to comment on the draft report titled, Financial Audit: IRS's Fiscal Years 2019 and 2018 Financial Statements. We are pleased that the Internal Revenue Service (IRS) received an unmodified opinion on its combined financial statements. The unmodified opinion demonstrates that the IRS accurately accounts for approximately $3.6 trillion in tax revenue receipts, $452 billion in tax refunds and $11 billion in IRS appropriated funds.

We appreciate the Government Accountability Office (GAO) recognizing our continued efforts to address the financial reporting systems significant deficiency and our improvement in internal controls over the management and reporting of more than $208 billion in unpaid assessments (taxes receivable). The IRS also successfully accounted for the foreign earnings repatriation tax resulting from the Tax Cuts and Jobs Act of 2017, which increased gross taxes receivable by more than $160 billion.

The IRS's ability to produce accurate and reliable financial statements each year is due to the efforts of our solid management team and staff. We are dedicated to promoting the highest standard of financial management, and we look forward to working with GAO to continue providing high-quality reporting and improving our internal controls.

Sincerely,

Charles P. Rettig

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through our website. Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. You can also subscribe to GAO's email updates to receive notification of newly posted products.

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, https://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on Facebook, Flickr, Twitter, and YouTube.
Subscribe to our RSS Feeds or Email Updates. Listen to our Podcasts.
Visit GAO on the web at https://www.gao.gov.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact FraudNet:

Website: https://www.gao.gov/fraudnet/fraudnet.htm

Automated answering system: (800) 424-5454 or (202) 512-7700

Congressional Relations

Orice Williams Brown, Managing Director, WilliamsO@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Strategic Planning and External Liaison

James-Christian Blockwood, Managing Director, spel@gao.gov, (202) 512-4707
U.S. Government Accountability Office, 441 G Street NW, Room 7814, Washington, DC 20548

Please Print on Recycled Paper.