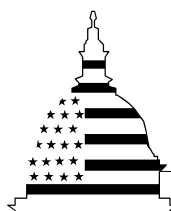


April 2004

INTERNAL REVENUE SERVICE

Status of
Recommendations
from Financial Audits
and Related Financial
Management Reports



G A O

Accountability * Integrity * Reliability



Highlights of [GAO-04-523](#), a report to the Commissioner of Internal Revenue

Why GAO Did This Study

In its role as the nation's tax collector, the Internal Revenue Service (IRS) has a demanding responsibility in collecting taxes, processing tax returns, and enforcing the nation's tax laws. Since GAO's first audit of IRS's financial statements in fiscal year 1992, a number of weaknesses in IRS's financial management operations have been identified. In related reports, GAO has recommended corrective action to address those weaknesses.

Each year as part of the annual audit of IRS's financial statements, GAO not only makes recommendations to address any new weaknesses identified but also follows up on the open weaknesses GAO identified in previous years' audits. The purpose of this report is to assist IRS management in tracking the status of audit recommendations and actions needed to address them.

www.gao.gov/cgi-bin/getrpt?GAO-04-523.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Steven J. Sebastian at (202) 512-3406 or sebastians@gao.gov.

INTERNAL REVENUE SERVICE

Status of Recommendations from Financial Audits and Related Financial Management Reports

What GAO Found

Although IRS has made improvements to address a number of financial management weaknesses, some of the open audit recommendations have been outstanding for an extended period of time. IRS has continued to experience delays in the implementation of the new systems intended to correct some of these long-standing deficiencies. Others, however, could be resolved with additional management attention. The continued existence of these financial management weaknesses exposes IRS to loss due to errors or theft and impairs the availability of current, accurate financial information that management needs to make decisions on a day-to-day basis.

Of 100 recommendations related to financial management (consisting of 78 recommendations open as of May 2003, 7 recommendations included in GAO's July 2003 report on IRS's excise tax certification process, and 15 new recommendations included in GAO's management report for fiscal year 2003), GAO is closing 24 because of actions IRS has taken to address the issues that gave rise to them. These actions were verified by GAO in the course of conducting the audit of IRS's fiscal year 2003 financial statements.

Of the remaining 76 financial management recommendations GAO considers open as of the date of this report, 66 are short term (capable of being addressed within 2 years) and 10 are long term (expected to require more than 2 years to implement). IRS considers 37 (49 percent) of the 76 recommendations to be closed. GAO considers 12 of these 37 still open because it has not yet had an opportunity to verify the actions taken by IRS. The actions cited by IRS for these 12 recommendations are recent and were taken after GAO's financial statement audit work for the year was completed. For 24 of the 37 recommendations that IRS considers closed, GAO found that action taken by IRS has not yet been fully effective in addressing the conditions that gave rise to the recommendations. IRS disagrees with the remaining recommendation.

IRS continues to exhibit a strong commitment to addressing its ongoing financial management problems and has made improvements in recent years that have resulted in the closing of many recommendations. At the same time, the continued existence of the serious financial management weaknesses that gave rise to the remaining open recommendations represents a serious obstacle that IRS needs to overcome to achieve effective financial management.

GAO will continue to monitor IRS's progress in implementing the 76 recommendations that remain open during the fiscal year 2004 audit. IRS said it expects GAO to find in its fiscal year 2004 financial audit that IRS has taken corrective actions to allow closure of another 37 recommendations. In addition, IRS stated that it is actively working to implement corrective actions to address all remaining open recommendations.

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Abbreviations

CADE	Customer Account Data Engine
CAP	Custodial Accounting Project
FA	Field Assistance
FAOP	Field Assistance Operating Procedures
FMS	Financial Management Service
IFS	Integrated Financial System
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
ITAMS	Information Technology Asset Management System
LPG	Lockbox Processing Guidelines
MOU	Memorandum of Understanding
NBIC	National Background Investigation Center
P&E	property and equipment
SETS	Security Entry and Tracking System
SLA	Service Level Agreement
SPC	Submission Processing Center
TAC	Taxpayer Assistance Center
TFRP	Trust Fund Recovery Penalty
W&I	Wage and Investment

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United States General Accounting Office
Washington, D.C. 20548

April 28, 2004

The Honorable Mark W. Everson
Commissioner of Internal Revenue

Dear Mr. Everson:

This report provides the status of the Internal Revenue Service's (IRS) efforts to implement recommendations we have made based on our audits of IRS's financial statements and other efforts related to financial management. In updating the status of these recommendations, we have included the results of our audits of IRS's financial statements for fiscal years 2003 and 2002.¹ This report is being provided to you to (1) assist IRS management in tracking the unresolved issues identified in our prior audits² and (2) report on the current status of open audit recommendations detailed in our previous financial audit and financial management-related reports. In cases where IRS has taken action on open recommendations that did not result in our closing them, we explain why this occurred. No new recommendations are being made in this report.

Since our first audit of IRS's financial statements in fiscal year 1992, our audits have identified a number of weaknesses in IRS's financial management operations. In related reports on IRS's internal controls, we have recommended corrective actions to address those weaknesses. Appendix I lists (1) recommendations we have made based on our financial audits and other financial management-related work that we have not previously reported as closed, (2) the status of each of these recommendations and corrective actions taken or planned as of February 2004 as reported to us by IRS and incorporated in appendix I, and (3) our analysis of whether the issues that gave rise to the recommendations have been effectively and fully addressed based on the work performed during our fiscal year 2003 financial audit. Effectively implementing recommendations is critical for IRS to resolve its financial management challenges.

¹U.S. General Accounting Office, *Financial Audit: IRS's Fiscal Years 2003 and 2002 Financial Statements*, [GAO-04-126](#) (Washington, D.C.: Nov. 13, 2003).

²U.S. General Accounting Office, *Internal Revenue Service: Status of Recommendations from Financial Audits and Related Financial Management Reports*, [GAO-03-665](#) (Washington, D.C.: May 29, 2003).

Status of Recommendations

In May 2003, we issued a report that provided (1) the status of IRS's efforts to implement prior recommendations as of our fiscal year 2002 financial audit³ and (2) new recommendations based on the results of our fiscal year 2002 financial audit.⁴ In the May 2003 report, we included 98 audit recommendations that we had not previously reported as being closed, 1 dating back as far as 1993. Of the 98 recommendations, 20 were closed at the time that report was issued, leaving 78 that were used as a starting point for appendix I of this report. For this year, we added 7 recommendations from our July 2003 report on the excise tax certification process⁵ and 15 new recommendations included in GAO's management report for fiscal year 2003,⁶ for a total of 100 recommendations. Based on the results of our recently completed fiscal year 2003 financial audit, we are closing 24 recommendations made in prior audits due to verified actions IRS has taken to address the issues that gave rise to them. Therefore, as of the date of this report, 76 financial management recommendations remain open, 66 of which are short term and 10 of which are long term.⁷

³U.S. General Accounting Office, *Financial Audit: IRS's Fiscal Year 2002 and 2001 Financial Statements*, [GAO-03-243](#) (Washington, D.C.: Nov. 15, 2002).

⁴[GAO-03-665](#).

⁵U.S. General Accounting Office, *Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process*, [GAO-03-687R](#) (Washington, D.C.: July 23, 2003).

⁶U.S. General Accounting Office, *Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures*, [GAO-04-553R](#) (Washington, D.C.: Apr. 26, 2004).

⁷Short-term recommendations are defined as those that could be addressed within 2 years. Long-term recommendations are defined as those expected to require 2 years or more to implement.

As indicated in appendix I, of the 76 recommendations we consider to be open, IRS considers 37 (49 percent) to be closed. We consider 12 of these recommendations to be open because IRS took corrective action to resolve these recommendations after we completed our testing for the fiscal year 2003 audit and, as a result, we have not yet had time to verify implementation of the corrective actions, which is a prerequisite to our closing a recommendation. We will verify the effectiveness of IRS's actions to address these recommendations during our fiscal year 2004 audit. For 24 of the 37 recommendations that IRS considers closed, we found that action taken by IRS has not been fully effective in addressing the conditions that gave rise to the recommendations. IRS disagrees with the remaining recommendation,⁸ though it had agreed with the recommendation at the time it was made.

Twenty-three of the 24 recommendations that IRS considers closed but that we consider open involved the issuance of formal written policies or directives aimed at addressing the internal control deficiencies that gave rise to the recommendations. However, we found that these policies or directives were not being adhered to or were not fully effective in correcting the deficiencies that led to the recommendations. We also found that the revised policies or directives intended to correct 6 of these 23 recommendations did not adequately address the underlying issues. We believe that all these recommendations could be resolved with additional management follow-up to ensure that the revised policies and directives specifically address the issues and to ensure that corrective actions as envisioned in policy and procedural changes are fully and effectively implemented. In the interim, the underlying weaknesses will likely continue to exist, impairing the quality and timeliness of IRS's financial information and increasing its exposure to losses.

A number of the 76 recommendations in appendix I that we consider to be open have been outstanding for an extended period of time. For example, 24 (32 percent) of the recommendations were made over 2 years ago, including 15 recommendations from more than 3 years ago, 4 recommendations from more than 5 years ago, and 1 recommendation that has remained open for over 10 years. The continued existence of the issues that gave rise to these recommendations exposes IRS to losses due to

⁸Recommendation 03-08 in appendix I was issued to correct a potential conflict in the responsibilities of lockbox coordinators, who assist lockbox banks with processing issues and who also perform the on-site performance review of those banks.

errors or theft, and impairs the availability of the current, accurate financial information management needs to make decisions.

The majority of the 76 recommendations we consider to be open address one of two broad issues:

- Forty-one (54 percent), all of which we consider to be short term, relate to weaknesses in (1) management controls over lockbox banks that process taxpayer receipts and (2) controls intended to safeguard taxpayer receipts and data at IRS sites. These continued weaknesses expose IRS to unnecessary risk of loss and increase taxpayer exposure to losses from financial crimes committed by individuals who inappropriately gain access to confidential personal information. IRS considers 28 of these recommendations closed. However, during our fiscal year 2003 financial audit, we found that IRS's corrective actions had not fully resolved the issues for 22 of these 28 recommendations and, for the remaining 6 recommendations, IRS's actions occurred after we completed our testing for the fiscal year 2003 audit. For example, in November 1998, we recommended that IRS ensure that all returned refund checks be stamped "nonnegotiable" as soon as extracted. In May 2000, IRS updated its policies to add instructions and establish a policy for safeguarding returned refund checks. However, during our audits in fiscal years 2001 through 2003, we found that IRS employees at some sites we visited were not consistently adhering to the policy for handling returned refund checks.
- Fourteen (18 percent) relate to system deficiencies that will not be fully corrected until IRS implements new financial management systems. Prior GAO reviews have disclosed numerous modernization management control deficiencies that have contributed to reported cost overruns and delays in the implementation of the systems intended to resolve these issues.⁹ For example, IRS had planned to implement the first release of its new Integrated Financial System (IFS) in October 2003, but announced shortly before the start of the new fiscal year that it was delaying implementation until at least the middle of fiscal year 2004. As of February 2004, implementation of IFS release 1, which is intended to provide core financial, budget formulation, and cost accounting

⁹U.S. General Accounting Office, *Business Systems Modernization: Internal Revenue Service Needs to Further Strengthen Program Management*, [GAO-04-438T](#) (Washington, D.C.: Feb. 12, 2004).

systems, had been further delayed. In addition, according to IRS, implementation of subsequent releases, which provide property, procurement, and performance management functions, is being reevaluated because of release 1 delays and funding availability. IRS has also encountered delays in the implementation of the Customer Account Data Engine (CADE), the new system designed to modernize IRS's taxpayer files, and the Custodial Accounting Project (CAP), which is intended to provide management information related to tax operations needed for day-to-day decision making, performance management, and reporting. As a result of cost overruns and delays, IRS and a contractor undertook a comprehensive review of CADE and IRS's entire business systems modernization program. Based on the results of the review, IRS launched an action plan to remedy the problems plaguing its systems modernization program. However, the program continues to face significant challenges and risks, and IRS does not expect that its new financial management systems will be fully implemented until at least 2007. Successful implementation of IFS, CAP, and CADE is essential to correcting IRS's long-standing financial management deficiencies and internal control weaknesses that prevent IRS from producing reliable and timely financial information needed for decision making on an ongoing basis.

Although IRS continues to experience delays in implementing the systems intended to address many underlying financial management and operations issues, it has made improvements in recent years that have resulted in the closing of many recommendations. For example, IRS made significant progress in addressing issues related to property and equipment (P&E), which resulted in closing 5 of the 11 P&E-related recommendations. However, delays in implementing IFS would inhibit significant additional progress in addressing P&E issues because IFS is intended to address 5 of the remaining 6 P&E-related recommendations. Delays in implementation of IFS and other systems would also inhibit IRS's ability to correct 14 deficiencies related to financial reporting, unpaid tax assessments, tax revenue, and refunds. Consequently, the continued existence of delays in the implementation of new systems and the other serious financial management weaknesses that gave rise to many of the remaining open recommendations represents a serious obstacle that IRS needs to overcome in order to achieve effective financial management and have available accurate, timely financial reporting and other information that is useful for day-to-day decision making. This was the overriding intent of the Federal Managers' Financial Integrity Act, the Chief Financial Officers Act

of 1990, the Federal Financial Management Improvement Act of 1996, and other federal financial management reform legislation.

Agency Comments

In commenting on a draft of this report, IRS said it believed that we would be able to confirm its implementation of an additional 37 recommendations based on our fiscal year 2004 audit. IRS stated that it is actively working to implement corrective actions to address all remaining open recommendations. We will review the effectiveness of these corrective actions and the status of IRS's progress in addressing all open recommendations as part of our fiscal year 2004 financial audit.

Objective, Scope, and Methodology

The objective of this report is to assist IRS management in tracking the status of financial audit and financial management-related recommendations and the actions needed to address them. To accomplish this objective, we evaluated the effectiveness of IRS's corrective actions implemented in response to open recommendations during fiscal year 2003 as part of our fiscal years 2003 and 2002 financial audits.¹⁰ Further details on the scope and methodology of our IRS financial audit work are included in appendix II. We obtained from IRS its assessment of the status of each recommendation and corrective action taken or planned as of February 2004, which we included in appendix I. We compared IRS's actions to our fiscal year 2003 audit findings and noted any differences between IRS's and our conclusions regarding the status of each recommendation. We conducted our audit in accordance with U.S. generally accepted government auditing standards. We requested comments on a draft of this report from the Commissioner of Internal Revenue or his designee. We received written comments from IRS, which are reprinted in appendix III.

We are sending copies of this report to the Chairmen and Ranking Minority Members of the Senate Committee on Appropriations; Senate Committee on Finance; Senate Committee on Governmental Affairs; Senate Committee on the Budget; Subcommittee on Transportation, Treasury, and General Government, Senate Committee on Appropriations; Subcommittee on Taxation and IRS Oversight, Senate Committee on Finance; Subcommittee on Oversight of Government Management, the Federal Workforce, and the

¹⁰[GAO-04-126](#).

District of Columbia, Senate Committee on Governmental Affairs; House Committee on Appropriations; House Committee on Ways and Means; House Committee on Government Reform; House Committee on the Budget; Subcommittee on Transportation, Treasury, and Independent Agencies, House Committee on Appropriations; Subcommittee on Government Efficiency and Financial Management, House Committee on Government Reform; and Subcommittee on Oversight, House Committee on Ways and Means. In addition, we are sending copies of this report to the Chairman and Vice Chairman of the Joint Committee on Taxation, the Secretary of the Treasury, the Director of the Office of Management and Budget, the Chairman of the IRS Oversight Board, and other interested parties. Copies will be made available to others upon request. In addition, the report will be available at no charge on GAO's Web site at <http://www.gao.gov>.

If you have any questions concerning this report, please contact me at (202) 512-3406 or sebastians@gao.gov. Contributors to this report are listed in appendix IV.

Sincerely yours,



Steven J. Sebastian
Director
Financial Management and Assurance

Status of GAO Recommendations from Prior IRS Financial Audits and Related Management Reports

Count	No.	Recommendation	Source report	Status of recommendations	
				Per IRS	Per GAO
1	94-2	Monitor implementation of actions to reduce the errors in calculating and reporting manual interest on taxpayer accounts, and test the effectiveness of these actions. (short-term)	<i>Financial Management: Important IRS Revenue Information Is Unavailable or Unreliable</i> (GAO/AIMD-94-22, Dec. 21, 1993)	Open. IRS is addressing the issue by increasing automation of restricted interest calculations, developing a quality review process, educating the workforce and measuring accuracy. Specifically, IRS has completed the rollout of the new software, provided training, and implemented a national help desk to support the end users. Additionally, IRS plans to implement quality reviews of the new manual interest procedures during 2004.	Open. We will review the changes IRS has implemented and continue to test the accuracy of IRS's manual interest calculations during our fiscal year 2004 financial audit.
2	99-1	Manually review and eliminate duplicate or other assessments that have already been paid off to assure that all accounts related to a single assessment are appropriately credited for payments received. (short-term)	<i>Internal Revenue Service: Immediate and Long-Term Actions Needed to Improve Financial Management</i> (GAO/AIMD-99-16, Oct. 30, 1998)	Open. IRS is developing an automated system to manage Trust Fund Recovery Penalties (TFRP). Phase I, to automate calculation of the penalties and assessment process to ensure accuracy and assessment timeliness, was implemented in July 2003, and various aspects of the implementation continue. IRS is conducting the pilot for Phase II, which automates the manual steps of the campus process to timely cross-reference payments. Phase II has been delayed until at least April 2004. Software necessary for Phase III, centralization of some TFRP functions, is scheduled for release in 2004. IRS anticipates completing Phase III by March 31, 2005. IRS is developing an action plan to improve timely and accurate manual processing of TFRP transcripts. Additional reviews have been recommended for each campus on TFRP cases. Processing problems have been identified and recommendations for corrective actions have been made. Training was developed to provide clarification of IRM issues.	Open. This recommendation specifically calls for IRS to review and correct its existing taxpayer records. In fiscal year 2003 we found that 24 of the 59 cases with Trust Fund Recovery Penalties (TFRP) had payments that were not properly reflected in each responsible party's account. We recognize automation of the current TFRP program is much needed. Until implemented, TFRP cases will continue to depend on campus personnel manually inputting the cross-reference information needed to link these assessments, but these efforts to date have not been effective. For 17 (71 percent) of the 24 cases with mis-posted payments noted above, all necessary manual cross-indexes had been posted. Even after the new system is implemented, it will require significant manual effort to correct existing taxpayer records and ensure that it functions as needed for future cases. We will continue to test TFRP cases for proper postings to all related accounts.

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Status of GAO Recommendations from Prior
IRS Financial Audits and Related
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(Continued From Previous Page)

Count	No.	Recommendation	Source report	Status of recommendations	
				Per IRS	Per GAO
3	99-3	Ensure that IRS's modernization blueprint includes developing a subsidiary ledger to accurately and promptly identify, classify, track, and report all IRS unpaid assessments by amount and taxpayer. This subsidiary ledger must also have the capability to distinguish unpaid assessments by category in order to identify those assessments that represent taxes receivable versus compliance assessments and write-offs. In cases involving trust fund recovery penalties, the subsidiary ledger should ensure that (1) the trust fund recovery penalty assessment is appropriately tracked for all taxpayers liable but counted only once for reporting purposes and (2) all payments made are properly credited to the accounts of all individuals assessed for the liability. (short-term)	<i>Internal Revenue Service: Immediate and Long-Term Actions Needed to Improve Financial Management</i> (GAO/AIMD-99-16, Oct. 30, 1998)	Open. IRS's Custodial Accounting Project (CAP) includes development of a Taxpayer Account Sub Ledger, which is expected to provide the ability to identify duplicate trust fund recovery assessments, taxes receivable, compliance assessments, and write-offs for financial reporting purposes. CAP Release 1 is behind schedule, and a new strategy is being developed. Cost and schedules will not be known until the new strategy is validated. In addition, IRS is developing an automated system to manage cases with Trust Fund Recovery Penalties (TFRP), as discussed under recommendation 99-1 above. When Phase II of the system is implemented, the Chief Financial Officer (CFO) can establish the links to more accurately report the single balance due from these assessments. Final phase of implementation is anticipated in 2005.	Open. IRS's plan to address our specific recommendation regarding TFRP cases is discussed in recommendation 99-1 above. We will continue to monitor IRS's development of a new strategy for CAP, as well as its implementation of the new TFRP system.

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Count	No.	Recommendation	Source report	Status of recommendations	
				Per IRS	Per GAO
4	99-17	Ensure that all returned refund checks are stamped "nonnegotiable" as soon as they are extracted. (short-term)	<i>Internal Revenue Service: Physical Security over Taxpayer Receipts and Data Needs Improvement</i> (GAO/AIMD-99-15, Nov. 30, 1998)	Closed. IRS updated Internal Revenue Manual (IRM) 3.10.72.6(1) to reflect the policy of stamping all returned refund checks "unless for credit to the U.S. Treasury, this instrument is non-negotiable" as soon as they are extracted. In May 2000, IRS added instructions to the IRM that required extraction personnel to place returned refund checks in a designated bucket/bin for manager review to ensure compliance. This question is on the Submission Processing Checklist and the campuses are reviewed monthly against the checklist to ensure compliance. A memo will be issued to Compliance Field Functions reminding them to properly stamp returned checks as non-negotiable.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. During our fiscal year 2003 site visits, we found checks at a service center campus that had not been stamped. Additionally, in several units of IRS's Small Business/Self Employed division that received payments at a field office, we found that staff were unaware of the procedures for handling returned refund checks. Furthermore, some of these units did not have "non-negotiable" stamps. Additionally, the Compliance unit in another field office did not stamp returned refund checks. Consequently, several employees handled the checks before they were eventually restrictively endorsed, thus increasing their risk of theft.
5	99-19	Ensure that walk-in payment receipts are recorded in a control log prior to depositing the receipts in the locked container and ensure that the control log information is reconciled to receipts prior to submission of the receipts to another unit for payment processing. To ensure proper segregation of duties, an employee not responsible for logging receipts in the control log should perform the reconciliation. (short-term)	<i>Internal Revenue Service: Physical Security over Taxpayer Receipts and Data Needs Improvement</i> (GAO/AIMD-99-15, Nov. 30, 1998)	Open. IRS issued guidance to the field in August 1999 and updated the IRM in January 2000 to include instructions for a control log and reconciliation of receipts. IRS will write new IRM procedures relating specifically to the control and reconciliation of remittances maintained in locked containers/safes. The draft IRM will be completed by June 30, 2004. Operational review of the Taxpayer Assistance Center (TAC) will include steps to ensure adherence to IRM procedures.	Open. During our fiscal year 2003 audit, at both field office units that handle receipts, including TAC, the individual who posted receipts to the log also reconciled the log. We will review IRS's actions during our fiscal year 2004 audit.

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Count	No.	Recommendation	Source report	Status of recommendations	
				Per IRS	Per GAO
6	99-20	Analyze and determine the factors causing delays in processing and posting TFRP assessments. Once these factors have been determined, IRS should develop procedures to reduce the impact of these factors and to ensure timely posting to all applicable accounts and proper offsetting of refunds against unpaid assessments before issuance. (short-term)	<i>Internal Revenue Service: Custodial Financial Management Weaknesses</i> (GAO/AIMD-99-193, Aug. 4, 1999)	Open. Automated Trust Fund Recovery Penalty programming continues. Phase I, to automate calculation of the penalties and assessment process to ensure accuracy and assessment timeliness was implemented July 1, 2003. IRS is conducting the pilot for Phase II, which automates the manual steps of the campus process to timely cross-reference payments. Phase II Pilot solution identified and tested: the system works well in production and productivity doubled when the campus began using the system.	Open. When IRS implements its Automated Trust Fund Recovery Penalty Program, we will review its effectiveness in eliminating processing delays. In the meantime, we will continue to monitor Trust Fund Recovery Penalty processing timeliness.
7	99-22	Expand IRS's current review of campus deterrent controls to include similar analyses of controls at IRS field offices in areas such as courier security, safeguarding of receipts in locked containers, requirements for fingerprinting employees, and requirements for promptly over stamping checks made out to "IRS" with "Internal Revenue Service" or "United States Treasury." Based on the results, IRS should make appropriate changes to strengthen its physical security controls. (short-term)	<i>Internal Revenue Service: Custodial Financial Management Weaknesses</i> (GAO/AIMD-99-193, Aug. 4, 1999)	Closed. Guidelines were included in the fiscal year 2003 Operating Procedures for Taxpayer Assistance Centers (TAC) for safeguarding receipts in locked containers and over-stamping checks made payable to IRS. Operating procedures state, in part, that all remittances and related returns must be recorded on Form 795, Daily Report of Collection Activity, and placed in a locked container until transmitted to the appropriate Submission Processing Center. Payments in the form of personal checks, cashier checks, and money orders should be made payable to "United States Treasury." Checks made out to IRS or U.S. Treasury must be over-stamped with the words "United States Treasury" immediately upon receipt. IRS is also including these issues in its operational reviews of the TACs. Managers in the TACs are also required to complete an annual review that includes these issues. In April 2003, IRM 5.1.2 was revised with new sub-sections, including: Timeliness of Remittances and Physical Security Controls over Remittances.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. We verified that IRS has included guidelines in the fiscal year 2003 Operating Procedures for Taxpayer Assistance Centers (TACs) for safeguarding receipts in locked containers and over-stamping checks made payable to IRS. IRS has also included these issues in its TAC reviews. In addition, IRS provided evidence that it performed reviews of Forms 809 used in field collections. However, similar to prior audits, we continued to find control weaknesses over the safeguarding and accounting for taxpayer receipts and data in TAC as well as in Small Business/Self Employed field office units that handle receipts. During our fiscal year 2003 audit, we did not find any issues with courier security and hiring practices in IRS field offices. We will continue to monitor IRS's efforts.

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(Continued From Previous Page)

Count	No.	Recommendation	Source report	Status of recommendations	
				Per IRS	Per GAO
8	99-25	Ensure that additional staff are employed or existing staff appropriately cross-trained to be able to perform the master file extractions and other ad hoc procedures needed for IRS to continually develop reliable balances for financial reporting purposes. (short-term)	<i>Internal Revenue Service: Custodial Financial Management Weaknesses</i> (GAO/AIMD-99-193, Aug. 4, 1999)	Open. The need to build an appropriate depth of experience is both immediate and ongoing; resources are examined to see if work can be realigned, and if existing employees can be retrained. Contractor support is used to provide the support and backup necessary for preparation of the compensating procedures, pending implementation of the Custodial Accounting Project (CAP) and the Customer Account Data Engine (CADE). IRS is committed to supporting the funding of contractor resources that are used for the Custodial Financial Statement Audit. This corrective action will be continually monitored and developed as new solutions to the problem are identified. This recommendation will remain open until the full implementation of CAP for the entire custodial financial audit (IMF, BMF, INMF, and IRAF) with an anticipated date of October 1, 2007, pending the CAP Release 1 replan and rescheduling of Release 2.	Open. In fiscal year 2003, IRS continued to utilize compensating procedures to enable it to generate reliable information for financial reporting purposes. Additional resources were not added in FY 2003 to perform current compensating procedures pending implementation of CAP/CADE. IRS has noted that the depth of IRS experience of staff is inadequate. IRS's current position is to support the financial statement audit process with available resources and contractors, without hiring until the full implementation of CAP. We will continue to assess IRS's actions during our fiscal year 2004 audit.

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Count	No.	Recommendation	Source report	Status of recommendations	
				Per IRS	Per GAO
9	99-29	Develop the data to support meaningful cost information categories and cost-based performance measures. (long-term)	<i>Internal Revenue Service: Serious Weaknesses Impact Ability to Report on and Manage Operations</i> (GAO/AIMD-99-196, Aug. 9, 1999)	Open. Integrated Financial System (IFS) Release 1 includes requirements for a cost module that is interfaced with program area management information systems. Once implemented, both direct and indirect resource cost data will be linked to the budget process and the strategic planning goals of all business units. This will help move the Service forward in transitioning to a Performance-Based Organization. Full cost accounting will not be realized until future releases such as Asset Management and Work Management are implemented. At present these releases are being evaluated based on IFS Release 1 delays and funding availability. All future releases have been delayed or placed on indefinite hold.	Open. We will follow up during future audits to assess the effectiveness of the implementation of IFS's cost accounting features.
10	99-30	Develop and implement procedures and controls to ensure that detailed P&E records are accurately maintained. These procedures and controls would include ensuring that physical inventories at field locations are effectively performed, including prompt resolution of discrepancies found in the inventories and appropriate adjustment of detailed records. (short-term)	<i>Internal Revenue Service: Serious Weaknesses Impact Ability to Report on and Manage Operations</i> (GAO/AIMD-99-196, Aug. 9, 1999)	Closed. IRM 2.14.1, Information Technology Asset Management, was first published in June 2002. It was updated and republished in July 2003. Increased automation, including the expansion of the Electronic Packing Slip initiative, helped IRS establish accurate skeletal records in ITAMS. IRS's Asset Management office publishes exception reports for the field Single Point Inventory Function (SPIF) employees to reconcile on a biweekly basis. Errors and exceptions are tracked on these exception reports for SPIF employees to use in order to perfect incorrect P&E records. IRS also now has one authoritative IRM that consolidates all the procedures and policies for SPIF employees in one location.	Closed. During fiscal year 2003, IRS (1) developed and implemented procedures to use electronic data from vendors to create inventory records, which helped ensure that assets were promptly and accurately recorded upon receipt of the assets, (2) focused additional effort on ensuring that assets disposals were recorded timely, (3) expanded use of network monitoring software to track assets, and (4) enhanced monitoring and quality control over the annual inventory process. As a result, our testing during fiscal year 2003 indicated significant improvement in the accuracy and reliability of IRS's P&E inventory records.

**Appendix I
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Count	No.	Recommendation	Source report	Status of recommendations	
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11	99-36	Make enhancements to IRS financial systems to include recording P&E and capital leases as assets when purchased and to generate detailed records for P&E that reconcile to the financial records. (long-term)	<i>Internal Revenue Service: Serious Weaknesses Impact Ability to Report on and Manage Operations</i> (GAO/AIMD-99-196, Aug. 9, 1999)	Open. In IFS Release 1, P&E and leasehold improvements will be recorded as assets when purchased. However, amortization will remain a manual process. The ability to tie to the detailed physical asset information and a fully integrated system with subsidiary records will not be available until the Asset Management module is implemented during Release 2. All future releases are being evaluated based on IFS Release 1 delays and funding availability and have been delayed or placed on indefinite hold.	Open. We will evaluate IFS Release 1 after it is implemented and we will continue to monitor IRS's progress with Release 2.
12	01-01	Better monitor IRS's procedures requiring that a freeze code be entered on all accounts of a taxpayer who IRS has determined is potentially liable for unpaid payroll taxes. This should be done on all such accounts to prevent the inadvertent release of refunds to the taxpayer until IRS determines the validity of the tax liability. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Closed. In September 2001 IRS issued a memorandum to the field emphasizing the timely input of the freeze code and revised Internal Revenue Manual (IRM) procedures to allow 30 days for the assessment of the trust fund penalty after input of the freeze code. IRS group managers are responsible for ensuring that the IRM procedures are followed and that adherence is tested when they review cases.	Closed. After IRS took action, our financial audit procedures in 2002 and 2003 have not identified the inadvertent release of refunds due to lack of freeze codes. Therefore, we are closing this specific recommendation regarding timely input of freeze codes to prevent erroneous refunds.

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13	01-02	Revise policies and procedures governing the processing of abatement transactions to establish (1) appropriate time frames for processing abatements, (2) a methodology for monitoring the timeliness of abatement processing, and (3) procedures to identify the causes for delays and formulate corrective actions. Also, examine abatement transactions arising from IRS errors to determine the causes for the errors and, based on this examination, formulate and implement appropriate procedures to reduce the level of errors made when entering data into taxpayer accounts. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Closed. IRS has not established specific time frames for processing abatements because large dollar claims often require additional documentation to verify a claim's validity. Often these cases go through examination, or have other taxpayer compliance issues. Allowing interest on refunds for these cases taking longer than 45 days to process is part of IRS's cost of doing business. The Office of Unpaid Assessments reviewed abatement cases identified for the 2002 audit and found that there were compliance activities in each case that required interest. In addition, IRS continues to enhance its policies and procedures to monitor the processing of abatement transactions.	Open. Although we agree that many cases may take longer than 45 days, we believe IRS should establish general targets for timeliness as well as a method for measuring and evaluating the processing times for abatements. In fiscal year 2003 we continued to find delays. Additionally, our recommendation calls for a review of abatements caused by IRS input errors to determine causes and corrections. We will continue to monitor timeliness of abatement processing and evaluate the effectiveness of IRS procedures for monitoring abatement transactions during our fiscal year 2004 financial audit.
14	01-03	Implement procedures to monitor the age of all pending offers and to require supervisors to follow up with staff to determine within 6 months whether to accept or reject the offer. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. IRS continues to make progress in the "closed within six months" measure. IRS is re-examining the six-month processing time goal. (<i>IRS Should Evaluate the Changes to Its Offer in Compromise Program</i> , GAO-02-311).	Open. IRS has improved its closure rate for offers in compromise, partly because it centralized processing at two campuses. In fiscal year 2003, the percentage of offers closed within six months increased to 56 percent, up from 38 percent the prior year. We will continue to monitor the timeliness of offer in compromise processing as part of our 2004 financial audit.

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15	01-04	As an alternative to prematurely suspending active collection efforts, and using the best available information, develop reliable cost-benefit data relating to collection efforts for cases with some collection potential. These cost-benefit data would include the full cost associated with the increased collection activity (i.e., salaries, benefits, and administrative support), as well as the expected additional tax collections generated. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. IRS presented to the GAO a comprehensive action plan with short and long-term actions to address the material weakness on collection of unpaid taxes. In addition, the IRS is developing a cost accounting module. However, due to IFS Release 1 delays and funding availability, all future releases have been delayed or placed on indefinite hold. Therefore, IRS will explore currently available information and determine the feasibility of developing a type of interim cost-benefit data or take other steps to enhance resource allocation decisions with regard to collection activities.	Open. We will continue to monitor IRS's development of new systems and its efforts to use currently available information to develop interim cost-benefit data.
16	01-06	Implement procedures to closely monitor the release of tax liens to ensure that they are released within 30 days of the date the related tax liability is fully satisfied. As part of these procedures, IRS should carefully analyze the causes of the delays in releasing tax liens identified by our work and prior work by IRS's former internal audit function and ensure that such procedures effectively address these issues. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. IRS has taken steps to improve the timeliness of lien releases involving settlement by Offer-in-Compromise. Offer-in-Compromise tax examiners were given access to the lien system to initiate lien releases once an offer has been settled. IRS staff will review lien processing units during scheduled reviews during the second and third quarters of fiscal year 2004. They will visit Offer-in-Compromise sites during the fourth quarter of fiscal year 2004. Additionally, they have developed an action plan to address the root causes of untimely lien releases from the fiscal year 2003 audit.	Open. During our fiscal year 2003 audit, we continued to find delays in release of liens. We found 12 instances out of 59 cases tested in which IRS did not release the applicable federal tax lien within the 30-day statutory period. The time between the satisfaction of the liability and release of the lien ranged from 35 days to 249 days. We will review the impact of IRS's actions to date and will continue to review IRS's release of tax liens.

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17	01-12	For (1) IRS's Automated Underreporter and Combined Annual Wage Reporting programs, (2) screening and examination of Earned Income Tax Credit claims, and (3) identifying and collecting previously disbursed improper refunds, use the best available information to develop reliable cost-benefit data to estimate the tax revenue collected by, and the amount of improper refunds returned to, IRS for each dollar spent pursuing these outstanding amounts. These data would include (1) an estimate of the full cost incurred by IRS in performing each of these efforts, including the salaries and benefits of all staff involved, as well as any related nonpersonnel costs, such as supplies and utilities, and (2) the actual amount (a) collected on tax amounts assessed and (b) recovered on improper refunds disbursed. (long-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. The key objective of IRS's efforts in developing cost data is to use data to make informed resource allocation decisions. IRS intends to consider cost data associated with its major programs, when developed, in all facets of the strategic planning process. Once implemented, the cost module of IFS, Release 1, will provide both direct and indirect resource cost data and will be linked to the budget process and the strategic planning goals of all business units. Full cost accounting will not be realized until future IFS releases, including Asset Management and Work Management, are implemented. At present these releases are being evaluated based on IFS Release 1 delays and funding availability. All future releases have currently been delayed or placed on indefinite hold.	Open. We will review the IFS plans to verify that it includes requirements that meet the objectives of the recommendation. We will continue to monitor IRS's development and use of cost data.
18	01-15	Ensure that all IRS units receiving collections have consistent policies and procedures to safeguard and account for cash receipts. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Closed. Completed September 1, 2002. Multi-disciplinary teams composed of management from Security Services, Information Services, and Agency-Wide Shared Services will continue to work with local staff to ensure consistent, on-going implementation of policies and procedures. In April 2003, IRM 5.1.2 was revised with new subsections, including: Timeliness of Remittances and Physical Security Controls over Remittances.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. During our FY 2003 audit, we found that both field office TACs we visited accepted walk-in payments in an unsecured area. In addition, at one of the sites, receipts were not stored in locked containers.

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19	01-17	Develop a subsidiary ledger for leasehold improvements and implement procedures to record leasehold improvement costs as they occur. (long-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. In IFS Release 1, property and equipment (P&E) and leasehold improvements will be recorded as assets when purchased. However, amortization will remain a manual process. The ability to tie to the detailed physical asset information and a fully integrated system with subsidiary records will not be available until the Asset Management module is implemented during Release 2. All future releases are being evaluated based on IFS Release 1 delays and funding availability and have been delayed or placed on indefinite hold.	Open. We will evaluate IFS Release 1 after it is implemented and we will continue to monitor IRS's progress with Release 2.
20	01-18	Implement procedures and controls to ensure that expenditures for P&E are charged to the correct accounting codes to provide reliable records for expenditures as a basis of extracting the costs for major systems and leasehold improvements. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. In IFS Release 1, P&E and leasehold improvements will be posted to the correct accounting string and Release 1 ties corresponding Federal Supply Classification codes to P&E material groups. The ability to tie to the detailed physical asset information and a fully integrated system with subsidiary records will not be available until the Asset Management module is implemented during Release 2. In the interim, IRS has implemented processes to identify, extract, and reclassify capitalized P&E transactions into the proper general ledger accounts.	Open. During our fiscal year 2003 audit, we found that IRS, with contractor assistance, implemented interim procedures to identify, extract, and reclassify P&E costs. However, IRS continued to lack current, reliable P&E information on an ongoing basis because P&E transactions were not properly recorded as transactions occurred. In addition, we continued to find that charges to accounting codes were not always correct. We will evaluate IFS Release 1 after it is implemented and we will continue to monitor IRS's progress with Release 2.

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21	01-21	Consolidate and update the P&E policies and procedures currently documented in various handbooks and policy memorandums into a comprehensive document that personnel responsible for maintaining inventory records can use as a reference. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. IRS updated IRM 2.14.1, Information Technology Asset Management, to include all policies and procedures pertaining to information technology assets. IRS is in the process of revising IRM 1.14.2.49, Property Management Handbook, which will provide policies and procedures for non-information technology assets. Target date for the new consolidated handbook is April 2004. Once published, these revised IRMs will provide authoritative guidance for both information technology and non-information technology assets.	Open. We will continue to monitor IRS's progress in revising and updating its IRMs during our fiscal year 2004 audit.
22	01-27	Perform sufficient supervisory reviews to help ensure that transactions recorded on P&E inventory records are accurately entered into subsidiary records and appropriately supported by documentation. (short-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Closed. IRS established an Electronic Packing Slip initiative, which helped establish accurate inventory records. IRS also implemented procedures to identify potential errors and discrepancies on inventory records and produce exception reports that are reviewed by SPIF personnel on a biweekly basis.	Closed. In fiscal year 2003, IRS developed procedures to obtain and use electronic data from vendors to create inventory records, which helped ensure that assets were promptly and accurately recorded upon receipt of the assets. In addition, IRS enhanced monitoring and quality control over the annual inventory process. As a result, our testing during fiscal year 2003 indicated significant improvement in the accuracy and reliability of IRS's P&E inventory records.

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23	01-33	Establish policies and procedures to ensure that all administrative and, to the extent possible, custodial transactions are promptly recorded in the general ledger, preferably within 30 days of the transaction. (long-term)	<i>Internal Revenue Service: Recommendations to Improve Financial and Operational Management</i> (GAO-01-42, Nov. 17, 2000)	Open. As of June 1, 2002, Revenue Systems/Interim Revenue Accounting Control System (IRACS) is using a spreadsheet to ensure that all documents are received and recordable transactions are input into the Interim Revenue Accounting Control System prior to month-end activities. The capability for recording custodial transactions for taxes receivable and refunds payable at the detail level will not be available until full implementation of CAP with integration to IFS. Additionally, for administrative transactions, the IRS is in the midst of an initiative to identify all major non-payroll expense transactions that can be accrued and/or recorded on an interim basis. During fiscal year 2003, IRS implemented interim accruals to monthly record material non-payroll administrative activities, such as rent, postage, and telephone expenses.	Open. We verified that during fiscal year 2003, IRS implemented interim accruals to more timely record material administrative activities, such as rent, postage and telephone expenses. This has significantly improved the reliability of related balances during the year. However, for taxes receivable and the related balances due to Treasury, the balances reported are not based on the routine recording of transactions. We will continue to monitor IRS's progress during our fiscal year 2004 financial audit.

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24	01-39	Develop a mechanism to track and report the actual costs associated with reimbursable activities. (long-term)	<i>Management Letter: Improvements Needed in IRS' Accounting Procedures and Internal Controls</i> (GAO-01-880R , July 30, 2001)	Open. IRS has developed guidance for costing reimbursable agreements. This guidance includes instructions on tracking labor and was completed February 1, 2002. IFS Release 1 includes requirements for a cost module that is interfaced with program area management information systems. Once implemented, both direct and indirect resource cost data will be linked to the budget process and the strategic planning goals of all business units. This will help move the Service forward in transitioning to a Performance-Based Organization. Full cost accounting will not be realized until future releases, such as Asset Management and Work Management, are implemented. At present these releases are being evaluated based on IFS Release 1 delays and funding availability. All future releases have been delayed or placed on indefinite hold.	Open. We confirmed that IRS completed procedures for costing reimbursable agreements that provides the basic framework for the accumulation of both direct and indirect costs at the necessary level of detail. IRS plans to implement these procedures over several years as it phases in various program area management information systems that will provide critical information to its new cost accounting system. However, as indicated by IRS, these systems have been placed on indefinite hold. We will continue to monitor IRS's efforts to fully implement its cost accounting system and, once it has been fully implemented, evaluate the effectiveness of IRS procedures for developing cost information for its reimbursable agreements.

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25	02-01	Implement policies and procedures to record capitalizable acquisition costs for P&E, capital leases, leasehold improvements, and major systems in the appropriate P&E general ledger accounts as transactions occur. (long-term)	<i>Internal Revenue Service: Progress Made, but Further Actions Needed to Improve Financial Management</i> (GAO-02-35, Oct. 19, 2001)	Open. IRS P&E capitalization policies and procedures provide for use of the pooling concept to capitalize costs associated with ADP equipment with a useful life of greater than 1 year. The pooling method is used, as opposed to the preferred process of capturing costs on a transactional basis, due to system limitations. In IFS Release 1, P&E and leasehold improvements will be recorded as assets when purchased. P&E will also be posted to the correct accounting string and Release 1 ties corresponding Federal Supply Classification codes to P&E material groups. However, a fully integrated system with subsidiary records will not be available until the Asset Management module is implemented during Release 2. All future releases are being evaluated based on IFS Release 1 delays and funding availability and have been delayed or placed on indefinite hold.	Open. We will continue to evaluate the effectiveness of IRS's interim procedures for capitalizing P&E costs under the pooling concept during our fiscal year 2004 financial audit. We will evaluate IFS Release 1 after it is implemented and we will continue to monitor IRS's progress with Release 2.
26	02-03	Perform periodic reviews to monitor and ensure that obligations are promptly established in the accounting system. Such reviews would assist IRS in maintaining accurate and complete records of its obligations and in reducing the risk of obligations exceeding available funding. (short-term)	<i>Internal Revenue Service: Progress Made, but Further Actions Needed to Improve Financial Management</i> (GAO-02-35, Oct. 19, 2001)	Closed. IRS issued guidance to all business units requesting a complete review of obligations to be completed monthly and certified quarterly and a complete review of commitments to be certified quarterly. Obligation guidance was completed June 26, 2001. Commitment guidance was completed December 31, 2002.	Closed. During our fiscal year 2003 audit work, we verified that IRS implemented its commitment guidance, which requires business units to certify that unliquidated commitments were reviewed to determine whether the commitments should be converted into obligations. In addition, we found that IRS promptly established obligations in its accounting system.

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27	02-05	Develop, document, and implement policies and procedures to require that reconciliations between proprietary and budgetary accounts be performed monthly so that differences can be identified in a timely manner, and, if necessary, adjusted. (short-term)	<i>Internal Revenue Service: Progress Made, but Further Actions Needed to Improve Financial Management</i> (GAO-02-35, Oct. 19, 2001)	Closed. Policies and procedures addressing monthly reconciliations were documented on June 1, 2002. Monthly reconciliations are currently being prepared between proprietary and budgetary accounts and differences are adjusted when identified. During fiscal year 2003, IRS implemented interim accruals to monthly record material administrative activities, such as rent, postage, and telephone expenses. These accruals have resulted in significantly reduced suspense amounts at all reporting periods.	Closed. We confirmed that quarterly reconciliations between budgetary and proprietary accounts are performed and documented. Informal reconciliations are prepared monthly. During fiscal year 2003, IRS implemented interim accruals to monthly record material administrative activities, such as rent, postage, and telephone expenses. In addition, IRS implemented procedures to accrue user fees on a quarterly basis. This has significantly improved the reliability of the related balance during the year and has reduced the balance of the suspense account at June 30, 2003, to \$22 million and as of year-end \$6 million.

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28	02-08	Implement policies and procedures to require that all employees itemize on their time cards the time spent on specific projects. (long-term)	<i>Internal Revenue Service: Progress Made, but Further Actions Needed to Improve Financial Management</i> (GAO-02-35, Oct. 19, 2001)	Open. IRS agreed with the objective of this recommendation, which is to allow it to collect and report the full payroll costs associated with its activities. While IRS indicated that most of its employees already itemize their time charges in functional tracking systems, it has acknowledged that full implementation of the IFS cost accounting module is required to close this recommendation. IFS Release 1 includes requirements for a cost module that is interfaced with program area management information systems. Once implemented, both direct and indirect resource cost data can be linked to the budget process and the strategic planning goals of all business units. This will help move the Service forward in transitioning to a Performance-Based Organization. Full cost accounting will not be realized until future releases, such as Asset Management and Work Management, are implemented. At present these releases are being evaluated based on IFS Release 1 delays and funding availability. All future releases have been delayed or placed on indefinite hold.	Open. We confirmed that IRS employees use functional tracking (workload management) systems to itemize and track their time charges. However, this recommendation remains open because its objective is to allow IRS to collect and report the full payroll costs associated with its activities. During our fiscal year 2003 audit, we continued to find that the functional tracking systems are insufficient for this purpose because they do not interface with each other or the general ledger to allow management to use them to readily accumulate the time charged to specific projects. The new cost accounting module of IFS is expected to track IRS's costs at the activity level and, thus, may address the recommendation. However, IRS plans to fully implement cost accounting, which are expected to require several years to execute, are currently on hold. We will continue to monitor IRS's progress in implementing the IFS cost accounting module.

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29	02-09	Implement policies and procedures to allocate nonpersonnel costs to programs and activities on a routine basis throughout the year. (long-term)	<i>Internal Revenue Service: Progress Made, but Further Actions Needed to Improve Financial Management</i> (GAO-02-35, Oct. 19, 2001)	Open. IRS agreed with this recommendation and indicated plans to address this issue with the cost accounting module that will be part of IFS. IFS Release 1 includes requirements for a cost module that is interfaced with program area management information systems. Once implemented, both direct and indirect resource cost data can be linked to the budget process and the strategic planning goals of all business units. This will help move IRS forward in transitioning to a performance-based organization. Full cost accounting will not be realized until future releases, such as Asset Management and Work Management, are implemented. At present, these releases are being evaluated based on IFS Release 1 delays and funding availability. All future releases have been delayed or placed on indefinite hold.	Open. We confirmed that the IFS plans include requirements that meet the objectives of this recommendation; however, in fiscal year 2003 IRS delayed, or placed on hold, the implementation of these requirements for an indefinite period. IRS plans to implement these requirements are expected to be executed over several years as IRS phases in various program area management information systems that will provide critical information to the cost accounting system. We will continue to monitor IRS's efforts and, once IFS is completed, follow up on IRS's implementation of these plans.
30	02-11	Develop policies and procedures to require that field office employees provide taxpayers receipts for all walk-in payments. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. IRS issued the Field Assistance (FA) IRM in June 2003, which instructs TAC employees to issue Form 809, Receipt for Payment of Taxes, when taxpayers request a receipt as proof of payment even if cash was not received. (IRM 21.3.4.7.1.1(4). The IRM also states Document 10161-Payments May Be Made By- will be posted in all TACs. IRS monitored adherence to these requirements during operational reviews conducted in the TACs during fiscal year 2003.	Closed. We verified that IRS has incorporated guidelines in its FY 2002 & 2003 Field Assistance Operations Procedures (FAOP) to instruct employees to issue receipts to taxpayers upon request.

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31	02-12	Develop policies and procedures to require that field offices post signs in the most visible locations to remind taxpayers to obtain receipts for payments. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R , July 18, 2002)	Closed. IRS issued the FA IRM in June 2003, which lists the required signs for each TAC. Sign #10161 is the Payment Upon Request sign and each TAC is required to display the sign where it can be seen (IRM 21.3.4.3(4)). IRS monitored adherence to these procedures during operational reviews of the TACs conducted in fiscal year 2003. Signs were posted in TACs as required and additional employees have been assigned 809 books in various TACs. Periodic reviews and verification of the requirement are required at a minimum during the annual filing season readiness operational review.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. We verified that IRS included instructions in its FY 2003 FAOP but the instructions did not specify that the signs be posted in the most visible location. During our FY 2003 audit we found that no signs were posted in one of the two field offices we visited.

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32	02-14	Develop policies and procedures to require that IRS and lockbox employees performing final candling record receipts in a control log at the time of discovery, recording at a minimum the total number of payments found, the amount of each payment, and the taxpayer who submitted the payment. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. The 2003 Lockbox Processing Guidelines (LPG), 3.2.8.1(1), directs "Lockbox employees to complete Form 9535, Record of Lockbox Discovered Remittance and Correspondence" when receipts are discovered during candling. The employee must record the type of document and remittance found, dollar amount, taxpayer's name and address, Social Security Number/Taxpayer Identification Number, and discoverer's name on Form 9535. Each remittance must be listed as a separate entry. The 2003 Extracting, Sorting & Numbering IRM, 3.10.72.6.2, requires "management to maintain a log identifying the employees responsible for overlooking the items and items discovered." The 2003 LPG was updated January 31, 2003.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. During our FY 2003 audit we verified that IRS revised the LPG to direct employees to complete Form 9535, Record of Lockbox Discovered Remittance and Correspondence when receipts are discovered during candling and specified information to be recorded. We also verified that the IRM, updated May 28, 2003, requires management to maintain a log identifying the employees responsible for overlooking the items and information on the items discovered (check amount/form number). However, at 2 service centers and at one lockbox bank we found that staff did not immediately record items found during final candling in a control log. Furthermore, 1 service center's candling log did not capture the minimum information in this recommendation. Since IRS's action relating to the IRM occurred after our site visits, we will continue to monitor IRS's efforts.

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33	02-15	Develop policies and procedures to require that IRS and lockbox managers or designated officials reconcile logs of payments found during final candling to the related receipts and documents. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. The 2003 LPG, 3.2.8.1(1), directs the responsible manager to validate that the information was correctly entered on Form 9535 for every shift worked. The 2003 Extracting, Sorting & Numbering IRM, 3.1072.6.2(1)e, states, "management shall immediately reconcile the discovered remittances with the final candling log." The 2003 LPG was updated January 31, 2003.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. We verified that the LPG directs lockbox managers to daily validate Form 9535 and the IRM, which was updated on May 28, 2003, to coordinate with the LPG, requires that management initial the log to validate that all available information is correctly entered and ensure that all remittances listed in the log are brought to the deposit function on a daily basis. However, at 1 service center we found that items discovered during candling were not reconciled.
34	02-16	Ensure that field office management complies with existing receipt control policies that require a segregation of duties between employees who prepare control logs for walk-in payments and employees who reconcile the control logs to the actual payments. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. IRS had issued guidance to TAC managers requiring the separation of duties. Further, this item is included in the self-assessment, which is to be conducted periodically. IRS monitored adherence to the existing procedures during operational reviews of the TACs conducted in fiscal year 2003.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. In addition, the applicable IRM no longer requires segregation of duties. During our fiscal year 2003 audit, at both field office units that handle receipts, including TAC, the individual who posted receipts to the log also reconciled the log.

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				Per IRS	Per GAO
35	02-17	Clarify that the intent of the requirement for background investigations is meant to apply to personnel being entrusted with taxpayer receipts and information rather than just personnel being granted access to an IRS facility. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R , July 18, 2002)	Closed. On October 3, 2002, IRS issued a memorandum, "Clarification of Background Investigation Requirements for Contractors" to clarify that the intent of the requirement for background investigations is meant to apply to personnel being entrusted with taxpayer receipts and information rather than just personnel being granted access to an IRS facility. Additionally, banks have been required to ensure that courier services employees working with the lockbox facility are getting Federal Bureau of Investigation fingerprint checks (LPG, January 2003).	Closed. During our fiscal year 2003 audit we verified that the October 3, 2002, memorandum reiterated the IRS requirement that all contractor employees who have access to taxpayer receipts and information must have an approved background investigation conducted by the IRS National Background Investigations Center (NBIC). In addition, we found that IRS was pursuing courier background investigations at all ten of its campuses.
36	02-18	Work with the National Finance Center (NFC) to resolve the technical limitations that exist within the Security Entry and Tracking System (SETS) database and continue to periodically review SETS data to detect and correct errors. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R , July 18, 2002)	Open. NFC is in the process of upgrading the SETS application to a web version, which they anticipate deploying in six to nine months. Treasury has requested that NFC include IRS as a participant in the design and development sessions. In the interim, NFC will continue to address any problems reported by IRS.	Open. We will continue to monitor IRS's actions.

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37	02-20	Establish procedures to track the release of liens up to the point of delivery to the local jurisdiction to ensure liens are released timely to avoid unduly burdening taxpayers once they have satisfied their tax liability. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. IRS issued a memorandum dated January 28, 2003, with instructions for tracking when the certificates of lien release leave our immediate control. Certificates must be generated at least weekly. Based on the results of the 2003 audit, IRS has drafted a detailed action plan for lien release issues, which includes operational reviews. The new procedures are for Automated Lien System Units to date stamp a duplicate copy of the line release-billing voucher so that the Service has actual knowledge of when line releases are no longer under our direct control. This was issued in the Internal Revenue Manual on October 1, 2003. Certificates must be generated weekly. A memo was issued January 28, 2003, on Payment Compliance, which was reinforced via email on April 1, 2004, to Territory Managers in Case Processing, emphasizing that the requirements and the procedures have been incorporated into IRM 5.12.6.4.1. Reviews will be conducted at all management levels to ensure that these procedures are being followed.	Open. Although IRS established procedures for tracking liens, none of the 7 lien units that we visited in 2003 had properly implemented the date-stamping procedures. We will continue to review the implementation of IRS's corrective actions during our 2004 financial audit.
38	02-21	Ensure that complete skeletal records are created and available for the SPIF units to update upon receipt of P&E. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. IRS successfully implemented an Electronic Packing Slip initiative with its primary hardware vendor. Using an automated transfer method, the vendor provides an electronic feed of all equipment that was shipped. IRS updates the Information Technology Asset Management System with that information and has skeletal records established before the equipment reaches a Single Point Inventory Function's loading dock.	Closed. IRS implemented a process for suppliers to provide "electronic packing slip" information when equipment is purchased and shipped. This information is used to establish skeletal records on ITAMS before property is received at the loading dock. During our fiscal year 2003 audit, we found that skeletal records were almost always available for Single Point Inventory Function units to update upon receipt of P&E.

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39	02-23	Develop and implement procedures to ensure that procurement award and requisition numbers recorded on property records are complete, accurate, and linked to the accounting records. (long-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Open. IRS's Information Technology Services is working with Procurement and vendors to establish a reliable vehicle for transmitting packing slip information. IRS will continue to work with Procurement to see that these fields are made a part of every procurement and that the necessary procurement award and requisition numbers are established on ITAMS at the time of purchase via an electronic feed from Procurement and matched via the electronic packing slip IRS will receive from vendors. A fully integrated system that provides the ability to tie to the detailed physical asset information will not be available until the Asset Management module is implemented during IFS Release 2. All future releases are being evaluated based on IFS Release 1 delays and funding availability and have been delayed or placed on indefinite hold.	Open. During our fiscal year 2003 audit, we continued to find that accounting transactions could not always be linked to P&E inventory records. We will continue to review IRS's corrective actions during our fiscal year 2004 financial audit.
40	02-24	Record software licenses in IRS's property management system. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. All software valued at more than \$25,000 was recorded into ITAMS by June 2003. IRS also developed and implemented procedures to update software information on an on-going basis.	Closed. In fiscal year 2003, IRS developed and implemented policy and procedures to identify and record software licenses.
41	02-25	Develop an approach to assess IRS's compliance with the terms of these software licenses. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. IRS developed and implemented procedures to reconcile the number of software users with the number of licenses purchased. This allows IRS to determine compliance with the terms of software licenses and to know when to purchase more or less software based on usage.	Closed. In fiscal year 2003, IRS implemented a process to inventory software licenses and assess compliance with the terms of the licenses.

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42	02-26	Ensure that, in the absence of an integrated general ledger system for IRS's custodial and administrative activities, IRS strengthens monitoring and analysis of receivables to ensure that receivables are not being erroneously recorded as a result of the lack of integration between these two activities. (short-term)	<i>Management Report: Improvements Needed in IRS's Accounting Procedures and Internal Controls</i> (GAO-02-746R, July 18, 2002)	Closed. IRS agrees with this recommendation and has taken steps to better manage reimbursable activity. IRS is now reconciling all reimbursable receivable accounts with the appropriate general ledger accounts monthly and is monitoring activities between custodial and administrative accounts as part of this process. Additionally, IRS has implemented a process to routinely review open receivables and take action to write off amounts, as appropriate.	Closed. During our fiscal year 2003 audit, we verified that IRS initiated corrective actions, that involved monitoring and detailed analysis of its reimbursable receivables that effectively addressed this recommendation. We found that, at fiscal yearend, IRS had identified and written off most of its old reimbursable receivable accounts and maintained no receivable balances that were due from its custodial activities.
43	03-01	Document IRS's oversight roles and responsibilities in agency policy and procedure manuals and determine appropriate level of IRS oversight of lockbox sites throughout the year, particularly during peak processing periods. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The MOU between FMS and IRS, detailing the roles and responsibilities of each organization in administering the IRS Lockbox Program, was signed April 30, 2003. In addition, IRM 3.0.230, Lockbox Processing Procedures, and the Lockbox Processing Guidelines (2003) and (2004) outline the duties and responsibilities of FMS and IRS.	Open. During our fiscal year 2003 audit, we reviewed the MOU in draft form and have since confirmed its ratification. We will evaluate IRS's documentation of its oversight roles and responsibilities in agency policy and procedure manuals as part of our fiscal year 2004 financial audit.
44	03-02	Establish and document guidelines and procedures in policy and procedure manuals for implementing the new penalty provision for lockbox banks to reimburse the government for direct costs incurred in correcting errors made by lockbox banks. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Open. Rescheduled to November 15, 2004. IRS/FMS has drafted a high-level reimbursement process. The plan includes the use of a special Lockbox Program code to delineate IRS rework costs as a result of errors made by the lock box sites. Currently the IRS/FMS is working on further detailing the plan for approval by FMS/IRS management. Once the plan is approved, IRS will incorporate the procedures in both the Lockbox Processing Guidelines and the Lockbox Processing IRM.	Open. We will evaluate IRS's corrective actions in future financial audits.

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45	03-03	Finalize and document the recently developed waiver process in IRS policy and procedure manuals and ensure that decisions on requests for waivers are formally and promptly communicated to lockbox management. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. Both the new waiver process, which is described in section 2.1.3.1 of the 2003 and 2004 Lockbox Processing Guidelines (LPG), revised April 8, 2003, and issued December 1, 2003, respectively, and the Security Memorandum of Understanding (MOU), which was used to document the internal process between the IRS and the FMS, and completed on April 1, 2003, address this recommendation.	Closed. During our fiscal year 2003 IRS financial audit, we verified that the new waiver process is described in the LPG and that the internal process between IRS and FMS is documented in the MOU.
46	03-04	Establish and document a process in IRS policy and procedure manuals to ensure that lockbox bank management formally responds to IRS oversight findings and recommendations promptly and that corrective actions taken by lockbox bank management are appropriate. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The Security MOU, completed on 04/01/03, documents the roles and responsibilities of the Security Review Team, which is comprised of FMS and IRS security experts. IRS documents our findings, which are sent to FMS to be included in a final report to the banks. This report covers findings, recommendations, and due dates for all corrective actions. IRS receives a copy of the final report.	Open. During our fiscal year 2003 IRS financial audit, we verified that a process to ensure that lockbox bank management formally responds to IRS and FMS was documented in the Security MOU. The MOU does not however document IRS's oversight roles and responsibilities in IRS policy and procedure manuals.
47	03-05	Establish and document a process in IRS policy and procedure manuals to ensure that IRS officials with the appropriate levels of expertise continue to participate in announced and unannounced security reviews of lockbox banks. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The Security MOU, which was completed on April 1, 2003, documents the roles and responsibilities of the Security Review Team, which is comprised of FMS and IRS security experts.	Closed. During our fiscal year 2003 IRS financial audit, we verified that the roles and responsibilities of the security review team were documented in the Security MOU.

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48	03-06	Ensure that the results of on-site compliance reviews are completed and promptly submitted to IRS's National Office. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. Lockbox banks underwent security reviews in 2003. The banks were required to respond officially to the items identified in the security report. Security reviews were based on the lockbox sites' compliance with the LPG. IRS is represented on the security review team, provides input related to the review to FMS, and then receives a copy of the final response sent by FMS to the lockbox bank.	Open. Based on our review during our fiscal year 2003 IRS financial audit, the lockbox coordinators completed a compliance review checklist during January and April 2003 peak for the 4 lockbox banks we visited. However, we noted that in some instances the coordinator did not complete all the steps noted on the checklist. We were unable to determine whether or not the reviews were submitted promptly to IRS's National Office. We will continue to monitor IRS's efforts in our fiscal year 2004 financial audit.
49	03-07	Revise the guidance used for compliance reviews so it requires reviewers to (1) determine whether lockbox contractors, such as couriers, have completed and obtained favorable results on IRS fingerprint checks and (2) obtain and review all relevant logs for cash payments and candled items to ensure that all payments are accounted for. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. IRS updated the security checksheet to instruct reviewers to determine whether contractors have completed and obtained favorable fingerprint results and to review all relevant logs for cash payments and candling logs. In addition, IRS and FMS personnel review all contractor (including courier) documentation during peak. Lockbox Coordinators are responsible for reviewing the candling log and cash log.	Open. During our fiscal year 2003 financial audit, we verified that IRS updated FMS's check sheet and found it contained all of the recommended requirements. In addition, we verified that the LPG was updated to revise guidance for candling. However, we also reviewed the lockbox coordinators' on-site review checksheet and found that it did not contain the courier or the candling log requirements. We will continue to monitor IRS's efforts in our fiscal year 2004 financial audit.

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50	03-08	Assign individuals, other than the lockbox coordinators, responsibility for completing on-site performance reviews. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. IRS disagrees with this recommendation. The Lockbox Coordinators were specifically hired to conduct the performance reviews and to represent the IRS interests at the banks during peak processing. IRS has increased the monitoring of the Lockbox Coordinator's performance by establishing direct report of these positions to a newly established organization in the Revenue and Deposit Branch. Reports prepared by the Lockbox Coordinators are analyzed and reviewed by the manager of the Lockbox Coordinators, also the Lockbox Policy and Procedure Section and FMS. This review will identify any inconsistencies with other on-site observations and findings by other staff. In addition, each Submission Processing Center conducts a review of the documents and remittances returned by the Lockbox Bank. The role of the Lockbox Coordinators is not only to ensure the proper reviews are completed for each site but also to be the Liaison for the Bank and related Submission Processing Center. They will respond to questions and provide direction based on established guidelines in the Lockbox Processing Guidelines. To ensure Lockbox Coordinators are able to perform all of the prescribed reviews the Revenue and Deposit Branch will ensure additional staff is available as needed. GAO's concern regarding the objectivity and integrity of each individual Lockbox Coordinator becoming questionable will be addressed through monitoring of individual performance by the newly assigned manager. IRS is also working towards standardization of the review process that should decrease this concern as well.	Open. We continue to believe the current lockbox coordinator structure, where lockbox coordinators are responsible for performing performance reviews as well as assisting lockbox banks with processing issues, does not alleviate the potential conflict of competing responsibilities in completing on-site performance reviews. However, we will review IRS's actions during our fiscal year 2004 audit to determine their effect on this issue. IRS previously agreed with this recommendation in its comments on the lockbox report dated December 20, 2002.

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51	03-09	Require lockbox management to ensure that perimeter doors are locked and alarms on perimeter doors are functioning and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. Security reviews have been completed to address this requirement.	Closed. During our fiscal year 2003 IRS financial audit, we verified that IRS had taken steps to monitor compliance with this requirement. Additionally, this item is included in FMS's monitoring/oversight checklist used to monitor compliance with this requirement.
52	03-10	Require lockbox management to ensure that guards are responsive to alarms and that IRS takes steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The requirement to ensure that door alarms are responded to by the guards was previously established in the 2002 LPG issued January 1, 2002. During on-site reviews, IRS and FMS security teams observe the guards responding to door alarms, etc., by performing tests during on-site security review. Documented in Section 2.4 of 2003 (revised April 8, 2003) and 2004 LPG (issued December 1, 2003).	Open. During our fiscal year 2003 IRS financial audit, we noted that IRS had taken steps to monitor compliance with this requirement. Additionally, this item is included in FMS's monitoring/oversight checklist used to monitor compliance with this requirement. However, in our fiscal year 2003 audit, we observed that guards did not respond to alarms at one of the four lockbox banks we visited.
53	03-11	Require lockbox management to ensure that employees' identity and employment status are verified prior to granting access to the processing floor and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The requirement to ensure that employee identity and employment status are verified prior to granting access to the processing floor was previously listed in the 2002 LPG issued January 1, 2002. During the on-site security reviews, the security review teams ensure the banks meet this requirement by reviewing personnel folders for temporary employees, bank officials, couriers, and guards. Documented in Section 2.5 of the 2003 (revised April 8, 2003) and 2004 LPG (issued December 1, 2003).	Closed. During our fiscal year 2003 IRS financial audit, we noted that IRS had taken steps to monitor compliance with this requirement. Additionally, this item is included in FMS's monitoring/oversight checklist used to monitor compliance with this requirement as well as in the LPG. Furthermore, we noted no exceptions during our observations.

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54	03-12	Require lockbox management to ensure that visitor access to and activity in the processing area are adequately controlled and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The requirement to control visitor access was previously listed in the 2002 LPG issued January 1, 2002. During the on-site security reviews, IRS/FMS security teams observe the sites' handling of visitors to ensure that the banks meet this requirement. Additionally, during peak visits a lockbox coordinator observes adherence to this requirement. Documented in Section 2.6.2 of the 2003 (revised April 8, 2003) and 2004 LPG (issued December 1, 2003).	Closed. During our fiscal year 2003 IRS financial audit, we verified that IRS had taken steps to monitor compliance with this requirement. Additionally, this item is included in FMS's monitoring/oversight checklist used to monitor compliance with this requirement.
55	03-13	Require lockbox management to ensure that employee access and items brought into and out of the processing area are closely monitored by guards and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The requirement to ensure that employee access and items brought into and out of the processing area are closely monitored by guards was previously listed in the 2002 LPG issued January 1, 2002. Additionally, Post Orders are required to be developed and reviewed with security guards prior to each peak to reinforce this requirement. On-site security review, as well as Lockbox Coordinator visits, monitors the adherence to this requirement. During the on-site security reviews, IRS and FMS security teams observe the sites handling of visitors to ensure the banks meet this requirement. Documented in Section 2.7 of the 2003 (revised April 8, 2003) and 2004 LPG (issued December 1, 2003).	Closed. During our fiscal year 2003 IRS financial audit, we verified that IRS had taken steps to monitor compliance with this requirement. Additionally, this item is included in FMS's monitoring/oversight checklist used to monitor compliance with this requirement as well as in the LPG. Furthermore, we noted no exceptions during our observations.

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56	03-14	Require lockbox management to ensure that surveillance cameras and monitors are installed in ways that allow for effective, real-time monitoring of lockbox operations and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. Surveillance cameras have been installed at all lockbox sites. Security review teams continually monitor compliance. These procedures were updated in Section 2.4.1 of the 2003 (revised April 8, 2003) and the 2004 LPG, issued December 1, 2003.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. During our fiscal year 2003 financial audit we found that at one of four lockbox banks we visited, guards did not use the cameras to monitor external activity when the door alarm was activated. At another site, we found that guards did little to no monitoring of the cameras while at the guard console.
57	03-15	Require lockbox management to ensure that envelopes are properly candled and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. These procedures were updated in Section 3.5.1.1 of the 2003 (revised April 8, 2003) and the 2004 LPG, issued December 1, 2003. Candling procedures are clarified to ensure envelopes are properly candled. Adherence to the requirements was added to the Lockbox Security Check Sheet. Adherence will be monitored by the lockbox FMS and IRS security team announced and unannounced visits.	Open. IRS needs to ensure that all requirements are consistently and routinely adhered to by lockbox management at all of the lockbox sites. During our review of lockbox banks in 2003, we found one lockbox bank where envelopes that were not opened on 3 sides were not candled twice and at another bank employees were unable to determine whether 2 candlings had been performed.
58	03-16	Require lockbox management to perform and adequately document candling reviews and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The requirement to perform and adequately document candling reviews was added in Section 3.5.1.1 of the 2003 (revised 04/08/03) and 2004 LPG, issued 12/01/03. Adherence to the requirements was added to the Lockbox Security Check Sheet. Adherence will be monitored by the lockbox FMS and IRS security team during announced and unannounced visits. Additionally Lockbox Coordinators review candling as part of their quality review checks during each peak.	Open. While IRS has added candling reviews requirement to LPG 3.5.1.1 and has taken steps to monitor adherence to this requirement by including this requirement in FMS's oversight/monitoring checklist, its actions have not been sufficient to ensure compliance. During our fiscal year 2003 IRS financial audit, we found that at three of the four sites we visited, reviews of final candled envelopes were not performed as required and/or was not documented.

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59	03-17	Require that returned refund checks are restrictively endorsed immediately upon extraction and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The requirement to ensure that returned refund checks are restrictively endorsed immediately upon extraction was previously listed in Section 3.2.1 of the 2002 LPG issued January 1, 2002, as well as the 2003 (revised April 8, 2003) and 2004 LPG, issued December 1, 2003. During the on-site security reviews, IRS and FMS security teams review adherence to this requirement. Additionally, adherence to this requirement is evaluated during the daily SPC ^a quality reviews.	Open. During our fiscal year 2003 IRS financial audit, we verified that IRS had taken steps to monitor compliance with this requirement. Additionally, this item is included in FMS's monitoring/oversight checklist used to monitor compliance with this requirement. However, we found that at three of the four sites we visited, returned refund checks were not consistently restrictively endorsed immediately upon extraction.
60	03-18	Require that lockbox couriers are properly identified prior to granting them access to taxpayer data and receipts and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The 2003 LPG, Section 2.8.7, effective January 1, 2003, specifies that guards identify couriers before granting access. Adherence to the requirements was added to the Lockbox Security Check Sheet. Adherence is monitored by the Lockbox FMS and IRS security team during their announced and unannounced security visits.	Closed. During our fiscal year 2003 audit, we verified that IRS had taken steps to monitor compliance with this requirement.
61	03-19	Require that employees have received favorable results on fingerprint checks before they are granted access to taxpayer data and receipts and that IRS take steps to monitor adherence to this requirement. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The requirement for lockbox sites to obtain favorable results on employees' fingerprint checks before allowing them access to the processing floor was previously listed in the 2002 LPG. The 2003 LPG, Section 2.6.1, effective January 1, 2003, was updated to reflect the new requirements. The FMS and IRS security team review personnel files to ensure employees currently working with taxpayer remittances have fingerprint clearance.	Closed. In our fiscal year 2003 financial audit, we found that IRS had made significant improvements in ensuring that lockbox bank employees received favorable fingerprint checks before being granted access to taxpayer data and receipts and no exceptions were noted in this area.

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62	03-20	Revise the LPG to require that before lockbox bank couriers receive access to taxpayer data and receipts they undergo and receive favorable results on background investigations that are deemed appropriate by IRS and are consistent across lockbox banks. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. On September 23, 2003, at the annual Lockbox Conference, NBIC ^b presented the new background investigation requirements for permanent Lockbox bank employees, couriers and guards. The new procedures require a moderate risk National Agency Check with Law and Credit investigation on all permanent bank employees, couriers and guards. The banks were given an implementation schedule beginning October 1, 2003 with full implementation by April 1, 2004. On December 15, 2003, the Lockbox Project Office sent out a Lockbox Electronic Bulletin with the 2004 Lockbox Processing Guidelines (LPG) containing the revised background investigation requirements under L.P.G.4.2, Personnel Security and L.P.G.5.1.2(5).	Open. During our fiscal year 2003 financial audit, we continued to find that lockbox couriers were not undergoing background investigations. In our fiscal year 2004 financial audit, we will evaluate the recent actions taken by IRS.
63	03-21	Revise the LPG to require that before permanent lockbox bank employees receive access to taxpayer data and receipts they undergo and receive favorable results on background investigations that are deemed appropriate by IRS and are consistent across lockbox banks. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. On September 23, 2003, at the annual Lockbox Conference, NBIC presented the new background investigation requirements for permanent Lockbox bank employees, couriers and guards. The new procedures require a moderate risk National Agency Check with Law and Credit investigation on all permanent bank employees, couriers and guards. The banks were given an implementation schedule beginning October 1, 2003 with full implementation by April 1, 2004. On December 15, 2003, the Lockbox Project Office sent out a Lockbox Electronic Bulletin with the 2004 Lockbox Processing Guidelines (LPG) containing the revised background investigation requirements under L.P.G.4.2, Personnel Security and L.P.G.5.1.2(5).	Open. In our fiscal year 2004 financial audit, we will evaluate the recent actions taken by IRS.

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				Per IRS	Per GAO
64	03-22	Revise the LPG to require that guards inspect courier vehicles for unauthorized passengers and unlocked doors. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed (GAO-03-299, Jan. 15, 2003)</i>	Closed. The 2003 LPG, Section 2.7.4, which was effective January 1, 2003, was updated to include this requirement.	Closed. During fiscal year 2003 we reviewed a Lockbox Electronic Bulletin (LEB) alert that revised the LPG to require that guards inspect courier vehicles for unauthorized passengers and unlocked doors. During our audit, we did not identify any instances where guards did not inspect courier vehicles for unauthorized passengers and unlocked doors.
65	03-23	Revise the LPG to require that candling procedures for the various types of extraction methods be clarified. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed (GAO-03-299, Jan. 15, 2003)</i>	Closed. In the 2003 LPG, Section 3.2.8, effective January 1, 2003, candling procedures for the various types of extraction methods were clarified. Splitting the envelope on three sides and flattening the envelope is sufficient to meet candling requirements. This process is sufficient to meet the candling requirements without further light source viewing. All other methods of extraction require viewing the envelope twice, through a light source, to meet the candling requirement.	Closed. During our fiscal year 2003 financial audit, we verified that the LPG revision clarified the candling procedures for the various types of extraction methods.
66	03-24	Revise the LPG to require that during candling, lockbox bank employees record which machines and which extraction clerks missed items. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed (GAO-03-299, Jan. 15, 2003)</i>	Closed. On April 2, 2003, IRS instructed the banks to change the quality review process for candling. The new procedures require that banks track which machines and which employees missed items. The procedures were effective April 14, 2003 and included in the 2004 LPG, issued December 1, 2003.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. During our fiscal year 2003 audit, we verified that IRS included this requirement in the April 2003 LPG. However, we found at two of the four sites we visited that neither the machines nor the clerks responsible for overlooking discovered items were recorded on the candling logs.

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67	03-25	Revise the LPG to require that lockbox bank management reconcile items found during candling to the candling records. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. Instructions for candling have been revised to require management to reconcile items to the Form 9535. The 2003 LPG was updated on January 31, 2003, via Lockbox Electronic Bulletin alert, to include this requirement in the LPG. LPG reference 3.2.8.2.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. During our fiscal year 2003 IRS financial audit we verified that the LPG had been revised to incorporate this requirement. However, we found at one of four sites we visited that management did not initial the candling log for each shift, whether or not items were found to validate that information was entered correctly and items found had been reconciled to the Form 9535.
68	03-26	Revise the LPG to require that lockbox bank management reconcile cash payments to internal cash logs and the cash logs they provide to IRS. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. All cash receipts are documented on Form 9535. LPG 2003 was updated on January 31, 2003, via Lockbox Electronic Bulletin, to include the requirement to document immediately and for management to reconcile payments. LPG reference 3.3.2.14.	Open. IRS's action of establishing a policy does not provide assurance that this policy is consistently adhered to. During our fiscal year 2003 financial audit, we verified that the LPG had been revised to incorporate this requirement. However, we found that at one of four sites we visited cash was not always recorded immediately upon discovery. In addition, there was no documentation that management had reconciled the log.
69	03-27	Revise the LPG to require that lockbox employees immediately seek processing guidance from the lockbox coordinator if envelopes with timely postmark dates are received after the postmark review period has ended. (short-term)	<i>IRS Lockbox Banks: More Effective Oversight, Stronger Controls, and Further Study of Costs and Benefits Are Needed</i> (GAO-03-299, Jan. 15, 2003)	Closed. The January 1, 2003, LPG included a requirement for a lockbox site to notify the SPC Lockbox Coordinator if it receives timely postmarked mail after the grace period. The Lockbox Coordinator will provide instructions for processing and assess the need for further postmark review. See LPG reference 3.2.2.1(2).	Closed. During our fiscal year 2003 financial audit, we verified that the LPG had been revised to incorporate this requirement.

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70	03-28	Enforce 180-day expiration period for fingerprint check results required when an individual enters on duty. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R, May 20, 2003)	Closed. IRS re-emphasized this policy by e-mail to Background Investigations Coordinators and Personnel Officers on September 30, 2002, and during a conference call on October 9, 2002. In addition, the Personnel Security and Investigations staff created and distributed an Excel file that calculates the date when fingerprint results expire. IRS staffs have received instructions on how to use the spreadsheet and to annotate Case Closing documentation. As a result, Personnel Offices are enforcing the 180-day policy for fingerprint results.	Closed. During our fiscal year 2003 financial audit we noted only 5 instances in over 12,000 hires where individuals were hired with fingerprint results over 180 days old.
71	03-29	Confirm with FMS that IRS's requirements for background and fingerprint checks for courier services are met regardless of whether IRS or FMS negotiates the service agreement. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R, May 20, 2003)	Closed. On October 7, 2002, FMS issued an amendment to the Courier MOU, which included the requirement that all courier employees satisfy the basic investigation including an Federal Bureau of Investigation fingerprint and name check. All 10 IRS campuses now have a contact responsible for submitting paperwork to the National Background Investigation Center (NBIC) and ensuring courier employees are granted clearance. On April 10, 2003, IRS requested that NBIC provide a monthly status report of the campus compliance to the Wage and Investment (W&I) Division. The 2004 LPG (issued December 1, 2003) includes Guidelines for Background Investigations under Personnel Security in Section 4.2.	Open. During our fiscal year 2003 audit, we found that the five service centers with Financial Management Service (FMS) negotiated service agreements were not compliant with the revised courier standards requiring couriers to undergo NBIC background investigations.

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72	03-30	Establish procedures to verify that courier services are adhering to the standards established for them by IRS, including the requirement that the courier service have insurance coverage. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R , May 20, 2003)	Closed. The Security Review Team of Receipt and Control reviews monthly compliance with the courier requirements. For the five campuses where IRS holds the courier contract, the Security Review Team was required to verify the campus has a valid insurance certificate valued at \$1 million. For the five campuses with FMS negotiated agreements, FMS drafted a memorandum to the financial institutes advising them to regularly provide a copy of the insurance certificates to IRS. The 2003 LPG included this procedure in Section 2.8.4.1.	Open. During our fiscal year 2003 audit, we reviewed the Campus Security Checklist and found it included a question on whether the Contracting Officer Technical Representative for campuses with IRS-negotiated courier agreements had a copy of the bonding/insurance certificate valued at \$1 million. However, it did not request this information for campuses with FMS-negotiated courier agreements. For four of the five campuses with FMS-negotiated courier agreements, we reviewed an amendment to the agreements and found that three amendments required that the courier service provide its bonding or insurance certification on an annual basis to FMS and one required the service to provide insurance certification to the IRS campus. However, we found during our audit that the IRS campuses had not received the insurance statement as required by the agreement.

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73	03-31	Enforce consistent implementation of policy limiting personal belongings in receipt processing areas at service center campuses. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R, May 20, 2003)	Closed. On February 6, 2004, IRS issued information alert W&I-IA-2002-63-2004 specifying the items that are prohibited from the secure receipt processing areas and requiring that employees use clear plastic bags to transport small items not carried on their person in and out of the secure areas. First line managers or a designated representative conduct, at minimum, monthly random reviews of employee compliance with all security policies as they relate to personal belongings in the secure receipt processing areas. In addition, Campus Security Review Teams conduct monthly reviews to ensure compliance with these procedures. These procedures were added via Information Alerts to IRMs pertaining to the secure receipt processing areas.	Open. During our fiscal year 2003 financial audit, we found that one of four campuses we visited allowed prohibited items such as newspapers, books, and purses into receipt processing areas. Additionally, at the same campus, items transported in and out of the processing area in clear plastic bags were not clearly visible and not all temporary employees had lockers to store personal belonging. Since IRS's actions occurred after our site visits, we will continue to evaluate IRS's corrective actions.
74	03-32	Prohibit the storage of employees' personal belongings with cash payments and receipts at IRS's TACs. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R, May 20, 2003)	Closed. On June 3, 2003, FA ^c included a requirement in IRM 21.3.4.7.3.1(2), which states that cash payments and Form 809 (Receipt for Payment of Taxes) must be stored separately from personal belongings. This issue was also included in operational reviews of the TACs conducted during fiscal year 2003.	Open. During our fiscal year 2003 financial audit, we verified that IRS included this requirement in the IRM guidelines dated June 27, 2003. However, this IRM was completed at the end of our site visits. We found that at one of the two field offices we visited, personal belongings such as purses and briefcases were allowed in areas where taxpayer receipts were received. Since IRS's action occurred near the end of our audit, we will continue to evaluate the effectiveness of IRS's corrective actions during our fiscal year 2004 financial audit.

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75	03-33	Revise candling procedures to specify the precise candling methods to be used based on the dimensions of the mail processed and the extraction method used for both the first and the final candling. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R, May 20, 2003)	Closed. On May 28, 2003, the IRM candling procedures were updated with an Information Alert (W&I-IA-2002-730) to specify precise first and final candling methods based on dimensions of the mail and first and final candling.	Open. We verified that IRS included this requirement in the IRM guidelines. However, during our fiscal year 2003 financial audit, we found that at two of four campuses we visited, not all envelopes were illuminated at least once. Since IRS's action occurred after our site visits, we will continue to evaluate IRS's corrective actions during our fiscal year 2004 financial audit.
76	03-34	Establish and implement procedures prohibiting a single employee from performing the final candling in a remote location. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R, May 20, 2003)	Closed. On May 28, 2003, the IRM candling procedures were updated with an Information Alert (W&I-IA-2002-730) implementing procedures prohibiting a single employee from performing the final candling in a remote location. This requirement was also added to the 2004 revision of IRM 3.10.72.	Open. During our fiscal year 2003 IRS financial audit we verified that IRS included this requirement in the IRM guidelines. However, we found at one campus that while two employees performed candling in a separate room together, there were so many crates and boxes in the area that the two employees could not see one another. Since IRS's action occurred after our site visits, we will continue to evaluate IRS's corrective actions during our fiscal year 2004 financial audit.
77	03-35	Determine which TACs do not presently accept payment of taxes in cash and issue a memorandum reminding them of the requirement that cash be accepted. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R, May 20, 2003)	Closed. Completed June 5, 2003. IRS included guidelines in its Fiscal Year 2003 Field Assistance Operating Procedures (FAOP) stating that all TACs will accept all standard forms of payments from customers, including checks, money orders, and cash.	Closed. We verified that IRS incorporated guidelines in its fiscal year 2003 FAOP stating that all TACs will accept all standard forms of payments from customers including checks, money orders, and cash.

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78	03-36	Establish a mechanism to periodically review adherence to IRS's policy that payment of taxes in cash be accepted. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls</i> (GAO-03-562R , May 20, 2003)	Closed. IRS monitored adherence to these guidelines during operational reviews of the TACs conducted in fiscal year 2003. The FA IRM, issued in June 2003, states "There will be at least one employee in each TAC that is issued a Form 809 Receipt Book". This gives each TAC the ability to issue the official receipt to taxpayers when paying by cash or when a receipt is requested. (IRM 21.3.4.7.3(3)). Managers in the TACs are also required to complete an annual review to address this issue.	Open. Actions taken thus far have not been effective. During our fiscal year 2003 financial audit, we found at one field office TAC that taxpayers wishing to pay in cash were encouraged to obtain a money order from a nearby bank. At the other TAC in that same field office we found that the Compliance unit manager was unaware of the procedures for receiving cash payments.
79	03-37	Develop and implement post-input review procedures to verify the accuracy of excise tax credit information in the master file. (short-term)	<i>Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process</i> (GAO-03-687R , July 23, 2003)	Closed. In July 2003, the Cincinnati Compliance Campus implemented Program Analysis System reviews on Gasoline Wholesale Distributor/End User/Diesel claims submitted on Forms 8849. In August 2003 they implemented and increased the responsibility for managers to review all work including fuel claims as part of their performance review for employees. In December 2003, Excise is included in the Embedded Quality Review System expansion rollout and fuel claims are also included in this review. The Embedded Quality Review System is performed by the employer's manager and is part of the employee's performance rating.	Open. IRS's corrective actions were completed after the cut-off period of transactions included in our fiscal year 2003 testing. We will review the effectiveness of these actions during our fiscal year 2004 audit.
80	03-38	Investigate why certification errors continue to go undetected through IRS's review procedures. (short-term)	<i>Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process</i> (GAO-03-687R , July 23, 2003)	Closed. In October 2003, IRS reiterated to management the importance of reviewing and understanding the Certification process.	Open. IRS's corrective action was completed after we reviewed its final excise tax receipt certification affecting fiscal year 2003 distributions. We will review the effectiveness of this action during our fiscal year 2004 audit.

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81	03-39	Develop and implement an action plan to improve the certification review process. (short-term)	<i>Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process (GAO-03-687R, July 23, 2003)</i>	Closed. In October 2003, IRS reiterated to management the importance of reviewing and understanding the Certification process.	Open. IRS's corrective action was completed after we reviewed its final excise tax receipt certification affecting fiscal year 2003 distributions. We will review the effectiveness of this action during our fiscal year 2004 audit.
82	03-40	Communicate in writing any potential changes in IRS's certification process to other Treasury entities that use the certification information, and obtain concurrence from these entities prior to implementing such changes. (short-term)	<i>Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process (GAO-03-687R, July 23, 2003)</i>	Open. IRS has implemented the taking of minutes at all Treasury Excise Tax Working meetings, and will also have a Memorandum of Understanding (MOU) signed by the Treasury Excise Tax Working Group.	Open. We will review the status of IRS's corrective actions during our fiscal year 2004 financial audit.
83	03-41	Implement procedures to annually identify excise taxpayers with the largest excise tax liabilities affecting the Highway Trust Fund and the Airport and Airway Trust Fund. (short-term)	<i>Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process (GAO-03-687R, July 23, 2003)</i>	Closed. IRS has identified Employer Identification Numbers of the largest excise tax liabilities beginning with tax period 200209. IRS identified the largest excise tax filers to both Cincinnati Submission Processing and Compliance Campuses in August 2003. The Employer Identification Numbers will be updated annually using the September tax periods.	Open. We verified that IRS had identified the excise taxpayers with the largest excise tax liabilities when we reviewed its pre-certification of excise tax receipts for the quarter ended June 30, 2003. We will continue to monitor IRS's actions during our 2004 audit to verify that IRS has implemented this as a recurring annual procedure.
84	03-42	Implement procedures to track the status of tax return filings for the largest payers of excise taxes and contact these taxpayers if the submission processing campus has not received their tax returns by 2 weeks after the due date. (short-term)	<i>Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process (GAO-03-687R, July 23, 2003)</i>	Open. IRS is conducting a pilot to analyze the receipt pattern of the largest excise taxpayers. The Cincinnati Submission Processing and Compliance Campuses have entered into a Service Level Agreement (SLA) to jointly monitor receipts and processing of excise tax returns. IRS implemented a 6-day cycle for expedited processing of all Form 720s. This pilot is on schedule to be completed by November 2004. The SLA was signed in October 2003 and revised in November 2003.	Open. We will review the progress of IRS's pilot during our fiscal year 2004 audit.

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85	03-43	Implement procedures to monitor the receipt and processing status of large excise tax returns to ensure that they are promptly recorded in IRS's master file prior to certifying excise tax distributions. (short-term)	<i>Management Report: Improvements Needed in Controls over IRS's Excise Tax Certification Process</i> (GAO-03-687R, July 23, 2003)	Closed. The Campus' Program Analyst staff and Reports Excise Analysts are monitoring to ensure timely posting of the largest taxpayers. The SLA between the Cincinnati Submission Processing and Compliance Campuses ensures monitoring and processing of all Form 720 returns on a 6-day cycle. Compliance has verified that Form 720 returns are being processed on a six-day cycle, procedures are in place, and IRS is monitoring to ensure timely posting of the largest taxpayers.	Open. IRS's corrective action was completed after we reviewed its final excise tax receipt certification affecting fiscal year 2003 distributions. We will review the effectiveness of this action during our fiscal year 2004 audit.
86	04-01	We recommend that IRS require lockbox bank managers to maintain appropriate documentation on-site demonstrating that satisfactory fingerprint results have been received before contractors are granted access to taxpayer receipts and data. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. The current LPG requires appropriate documentation for couriers and guards before contractors are granted access to taxpayer receipts. To ensure compliance with the LPG, IRS and FMS include this as a review item when performing security and administrative reviews.	Open. This is a new recommendation. We will review IRS's corrective action during our fiscal year 2004 audit.
87	04-02	We recommend that IRS revise its policy on two-person courier teams to prohibit the use of courier teams consisting of closely related individuals to further minimize the risk of collusion in the theft of taxpayer receipts and data. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. Additional background investigation requirements for all couriers have been implemented. However, Wage and Investment will confer with Mission Assurance to assess their current guidelines.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.

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88	04-03	We recommend that IRS develop procedures to require lockbox managers to provide satisfactory evidence that managerial reviews are performed in accordance with established guidelines. At a minimum, reviewers should sign and date the reviewed documents and provide any comments that may be appropriate in the event that their reviews identified problems or raised questions. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. The LPG instructs the banks to perform numerous managerial reviews. IRS will consider the risk level of each of the documented logs, and assess each one to determine the appropriate level of review and if more guidelines are necessary.	Open. This is a new recommendation. We will continue to review IRS's efforts during our fiscal year 2004 audit.
89	04-04	We recommend that IRS revise its candling procedures at lockbox banks to require testing of automated candling machines at appropriate intervals, taking into account such factors as use time, volume processed, machine requirements, and shift cycles. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. IRS requires an additional candling of all envelopes processed by extractors using machines that have automated candling equipment. This requirement mitigates the risk identified by GAO. However, IRS agrees to assess their current guidelines for possible inclusion of testing standards for equipment with automated candling equipment.	Open. This is a new recommendation. We will monitor IRS's actions during our fiscal year 2004 audit.
90	04-05	We recommend that IRS require lockbox managers to maintain logs of these tests and to periodically review their logs. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. IRS will include this recommendation as part of the assessment of testing standards for machines (04-04) with automated candling equipment.	Open. This is a new recommendation. We will monitor IRS's actions during our fiscal year 2004 audit.

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91	04-06	We recommend that IRS discontinue its practice of storing taxpayer receipts and data outside TAC secured areas without storing the receipts in a secured locked container. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. Written procedures have been provided to TAC employees for safeguarding taxpayer receipts when received. IRM 21.3.4.7(6), issued in June 2003, provides guidance stating that payments received from taxpayers will be immediately placed in a locked container. The receipts are also stored away from employees' personal belongings. IRS will continue to conduct operational reviews at TAC offices to ensure IRM procedures are being followed. The TAC location that was noted for securing payments from taxpayers outside the secure area of the TAC was contacted and the location of the desk has been moved inside the secured area of the TAC. The TAC manager was informed to ensure all TAC operations are conducted inside the secured area of the TAC.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.
92	04-07	We recommend that IRS develop procedures to enhance adherence to existing instructions on safeguarding discovered remittances at service center campuses. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. In 2003, IRM 3.8.46 was produced and distributed to all campuses. Form 4287 (Record of Discovered Remittances) has been revised to include a box for managers to indicate that reconciliation has been performed. Also, IRS added to the monthly security checklist to review the discovered remittance procedures.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.

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93	04-08	We recommend that IRS enforce its policies and procedures to ensure that service center campus security guards respond to alarms. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. The IRS Physical Security Programs within Mission Assurance will modify IRM 16.12, Facility and Property Protection, to require the following: development of self assessments, which may be used to test the response capabilities for guards, as these relate to alarms; integrate self assessments into IRM 1.16; conduct initial and then periodic security exercises, which are realistic, to ensure security guards respond to alarms, required by Operational Assurance personnel; Operational Assurance will provide written reports to the Physical Security Program Office to support the conducting of security exercises; review self assessment reports for alarm response and coordinate corrective action of outstanding issues; and, conduct annual security exercise at each of their assigned facilities to test alarm responses by October 31, 2005.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.
94	04-09	We recommend that IRS establish compensating controls in the event that automated security systems malfunction, such as notifying guards and managers of the malfunction, and immediately deploying guards to better protect the processing center's perimeter. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. The IRS Physical Security Programs within Mission Assurance will develop procedures by August 30, 2004, to be used in conjunction with the policies developed in Recommendation 04-08 to ensure that local management is notified whenever there is a malfunction of alarms and that guards are deployed or doors are secured, as necessary, either during tests or when otherwise identified. Procedures will include management notification of alarm failure when reported to the Situational Awareness Management Center/Computer Security Incident Response Center (SAM/CSIRC).	Open. This is a new recommendation. We will continue to review IRS's corrective actions.

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95	04-10	We recommend that IRS modify AUO reports to ensure that they report the last activity date for each outstanding obligation line amount. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Closed. The Beckley Finance Center has revised the Aging Unliquidated Obligations report to accurately capture the last activity date for each obligation line amount.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.
96	04-11	We recommend that IRS require procurement office staff to review and sign off on whether obligations are valid or require deobligation before business units complete their quarterly certifications. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. IRS is evaluating its current approach toward reviewing open obligations and approving those that require deobligation. This includes studying the relative responsibilities of the procurement office, business units, and the Beckley Finance Center with respect to validating and certifying deobligations. New guidelines will be issued at the conclusion of this internal review.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.
97	04-12	We recommend that IRS enhance its compensating internal controls by including tests or recalculations of payroll computations performed by NFC for the IRS employees selected for review each pay period. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. The IRS Transactional Processing Operations division will expand its current random sample payroll review/validation process to include the recalculation of agency Thrift Saving Plan contributions. A detailed Standard Operating Procedure outlining the complete review process is being developed, with implementation expected by June 2004.	Open. This is a new recommendation. We will monitor IRS's corrective actions during our fiscal year 2004 audit.
98	04-13	We recommend that IRS timely investigate and resolve any identified errors. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. The IRS Transactional Processing Operations division is responsible for following up immediately on any discrepancies with NFC and ensuring that NFC takes corrective action within a timely basis.	Open. This is a new recommendation. We will review IRS's actions during our fiscal year 2004 audit.

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				Per IRS	Per GAO
99	04-14	We recommend that IRS establish review procedures for amounts being reported in Supplemental Information to the financial statements for Other Claims for Refund. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. The IRS's Appeals and Chief Counsel provide estimated amounts on Other Claims for Refund to the Office of Revenue Reports. For information received from Appeals, IRS management will perform a second level of review to ensure the accuracy of the amounts to be included in the financial statements. In addition, IRS management will work closely with Chief Counsel to find ways to accelerate getting information on claims pending review by federal courts.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.
100	04-15	Until BPMS is fully operational, we recommend that IRS implement procedures to ensure that all performance data reported in the MPS report are subject to effective, documented reviews to provide reasonable assurance that the data are current at interim periods. (short-term)	<i>Management Report: Improvements Needed in IRS's Internal Controls and Accounting Procedures</i> (GAO-04-553R, April 26, 2004)	Open. IRS has taken steps to ensure that the performance measures data reported in the monthly report is properly reviewed before being published. IRS is increasing the control over data by increasing the number of measures reported through the automated Business Performance Management Systems, requiring the submitting divisions to certify that their data is accurate, and reducing the number of measures manually reported in the monthly report. In addition, Corporate Planning and Performance Unit staff continues to complete the manual review process as described by GAO, which requires the staff to review the draft document, to compare it to the data provided to the divisions, and to compare it to the previous month's report for consistency, thereby validating the accuracy of the manual input of data to the report.	Open. This is a new recommendation. We will review IRS's corrective actions during our fiscal year 2004 audit.

Source: GAO.

^aIn reporting on the status of this recommendation, IRS refers to SPC, which is an acronym for Submission Processing Center.

^bIn reporting on the status of this recommendation, IRS refers to NBIC, which is an acronym for National Background Investigation Center.

^cIn reporting on the status of this recommendation, IRS refers to FA, which is an acronym for Field Assistance.

Details on Audit Methodology

To fulfill our responsibilities as the auditor of the Internal Revenue Service's (IRS) financial statements, we did the following:

- Examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements. This included testing selected statistical samples of unpaid assessment, revenue, refund, accrued expenses, payroll, nonpayroll, property and equipment, and undelivered order transactions. These statistical samples were selected primarily to substantiate balances and activities reported in IRS's financial statements. Consequently, dollar errors or amounts can and have been statistically projected to the population of transactions from which they were selected. In testing these samples, certain attributes were identified that indicated either significant deficiencies in the design or operation of internal control or compliance with provisions of laws and regulations. These attributes, where applicable, can be and have been statistically projected to the appropriate populations.
- Assessed the accounting principles used and significant estimates made by management.
- Evaluated the overall presentation of the financial statements.
- Obtained an understanding of internal controls related to financial reporting (including safeguarding assets), compliance with laws and regulations (including the execution of transactions in accordance with budget authority), and performance measures reported in the Management's Discussion and Analysis.
- Tested relevant internal controls over financial reporting (including safeguarding assets) and compliance, and evaluated the design and operating effectiveness of internal controls.
- Considered the process for evaluating and reporting on internal controls and financial management systems under the Federal Managers' Financial Integrity Act.
- Tested compliance with selected provisions of the following laws and regulations: Anti-Deficiency Act, as amended (31 U.S.C. § 1341(a)(1) and 31 U.S.C. § 1517(a)); agreements for payment of tax liability in installments (26 U.S.C. § 6159); Purpose Statute (31 U.S.C. § 1301); release of lien or discharge of property (26 U.S.C. § 6325); interest on underpayment, nonpayment, or extensions of time for payment of tax

(26 U.S.C. § 6601); interest on overpayments (26 U.S.C. § 6611); determination of rate of interest (26 U.S.C. § 6621); failure to file tax return or to pay tax (26 U.S.C. § 6651); failure by individual to pay estimated income tax (26 U.S.C. § 6654); failure by corporation to pay estimated income tax (26 U.S.C. § 6655); Prompt Payment Act (31 U.S.C. § 3902 (a), (b), and (f), and 31 U.S.C. § 3904); Pay and Allowance System for Civilian Employees (5 U.S.C. §§ 5332 and 5343, and 29 U.S.C. § 206); Federal Employees' Retirement System Act of 1986, as amended (5 U.S.C. §§ 8422, 8423 and 8432); Social Security Act, as amended (26 U.S.C. § 3101 and 3121, and 42 U.S.C. § 430); Federal Employees Health Benefits Act of 1959, as amended (5 U.S.C. §§ 8905, 8906, and 8909); and Consolidated Appropriations Resolution, 2003 (Pub. L. No. 108-7).

- Tested whether IRS's financial management systems substantially comply with the three requirements of the Federal Financial Management Improvement Act of 1996.

Comments from the Internal Revenue Service



COMMISSIONER

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

April 16, 2004

Mr. Steven J. Sebastian
Director
Financial Management and Assurance
U. S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Sebastian:

I am responding to your draft report titled, Internal Revenue Service: Status of Recommendations from Financial Audits and Related Financial Management Reports. We recently provided you with an update on the current status of the recommendations, and you accurately incorporated this information into Appendix I of the draft report.

Of the 100 recommendations cited in your report, we are pleased that GAO agrees that 24 are now closed. In addition, we believe an additional 37 recommendations will be closed based on your fiscal year 2004 financial audit. As stated in your report, some of your recommendations, such as those related to our modernization efforts, will require a longer period of time to resolve and will require our sustained commitment. We are actively working to implement corrective actions to effectively address all remaining open recommendations.

I appreciate the GAO's acknowledgment of our continued strong commitment to addressing financial management issues. I also recognize we must remain committed to achieving effective financial management.

Sincerely,

A handwritten signature in black ink, appearing to read "Mark W. Everson".

Mark W. Everson

GAO Contact and Staff Acknowledgments

GAO Contact

Steven Sebastian, (202) 512-3406

Acknowledgments

In addition to the person named above, Paul Foderaro, Chuck Fox, Larry Malenich, Charles Payton, Ted Hu, Yola Lewis, John Davis, William Cordrey, Valerie Freeman, Alain Dubois, George Jones, Gloria Cano, and Nina Crocker made key contributions to this report.

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