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# IRS Management

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The President of the Senate
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In 1990, the General Accounting Office began a special effort to review and report on the federal program areas its work identified as high risk because of their vulnerability to waste, fraud, abuse, and mismanagement. This effort, which was supported by the Senate Committee on Governmental Affairs and the House Committee on Government Reform and Oversight, brought a much-needed focus on problems that were costing the government billions of dollars.

In December 1992, GAO issued a series of reports on the fundamental causes of problems in high-risk areas, and in a second series in February 1995, it reported on the status of efforts to improve those areas. This, GAO's third series of reports, provides the current status of designated high-risk areas.

This report discusses four high-risk areas at the Internal Revenue Service involving (1) the multibillion dollar Tax Systems Modernization initiative, (2) substantial financial management weaknesses which diminish IRS' ability to assess the results of operations or measure performance, (3) problems in the management and collection of billions of dollars in tax accounts receivable, and (4) significant levels of tax filing fraud. Congress has signaled its concern over these problems through its oversight and funding decisions, and Treasury and IRS have made some progress in addressing problems in each of these four high-risk areas since our last high-risk report series. However, IRS faces a number of significant challenges to continuing this progress, particularly in its efforts to modernize its operations. A sustained, agency-wide commitment will be critical to resolving these serious problems.

Copies of this report series are being sent to the President, the congressional leadership, all other Members of Congress, the Director of the Office of Management and Budget, and the heads of major departments and agencies.

James F. Hinchman
Acting Comptroller General
of the United States

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# Overview

The Internal Revenue Service's (IRS) mission is to collect the proper amount of tax revenue in a fair and efficient manner at the least cost to the public. For fiscal year 1995, IRS reported collecting $1.4 trillion from taxpayers, processing over a billion tax returns and related documents, disbursing $122 billion in tax refunds, and managing an estimated accounts receivable inventory of $113 billion. In addition, IRS administered a reported $400 billion in tax expenditures. To ensure its ability to efficiently and fairly administer the nation's tax system, IRS has articulated a business vision for 2001. This vision calls for reducing the volume of paper returns, providing better customer service, and improving compliance by modernizing IRS' operations.

Since developing its business vision in 1992, IRS has made some progress in modernizing its operations; however, the gap between IRS' current level of performance and that proposed in its vision is great. Specifically, the efficient administration of the nation's tax system is undermined by problems in four areas of IRS' operations: tax systems modernization (TSM), financial management, accounts receivable, and filing fraud. These four areas were identified in our 1995 High-Risk Series as being especially vulnerable to waste, fraud, abuse, and mismanagement.[1] Improvements have been made, but these areas continue to have problems that warrant their inclusion in our 1997 High-Risk Series.

## The Problem

IRS is an agency trying to respond to the demands of the 1990s with 1950s processes and 1970s technology. For years we have chronicled IRS' struggle to modernize and manage its operations, especially in the four high-risk areas, and have made scores of recommendations to improve IRS' systems, processes, and procedures. Without successfully modernizing operations in the high-risk areas, IRS is unlikely to achieve the goals in its business vision.

A key factor for explaining IRS' difficulties in the high-risk areas is its lack of a comprehensive implementation strategy or detailed business plan for modernization. Such a strategy would guide IRS in setting priorities, changing internal management and administrative processes, developing necessary in-house technical skills, and acquiring relevant technology. To be successful, this strategy should include performance measures that could be used by

[1] GAO/HR-95-20SET.

Congress, the Department of the Treasury (Treasury), and IRS to track IRS' progress in accomplishing its vision.

The problems IRS confronts in attempting to eliminate its high-risk vulnerabilities are compounded by their interdependencies. Specifically, IRS' success in addressing its financial management, accounts receivable, and filing fraud vulnerabilities is linked to its success in modernizing its information systems. IRS' processes and systems were not designed to address the critical needs and vulnerabilities that IRS confronts today. These processes and systems must be modernized to support IRS' business vision and to address its high-risk areas. However, until clearly defined business requirements drive IRS' modernization efforts, there is no assurance that these efforts will achieve IRS' vision or improve its operations.

## Progress

IRS has made some progress in addressing the problems we have identified in the four high-risk areas. For example, IRS is finalizing a comprehensive strategy to maximize electronic filing and has begun initiatives to develop a complete integrated systems architecture. In response to our recommendations, IRS has also begun to plan both short-term and long-term solutions to its financial management problems, has implemented a new administrative accounting system, and has transferred its payroll processing to the Department of Agriculture's National Finance Center.

In dealing with its accounts receivable problems, IRS has streamlined selected notification and collection processes and is developing ways to adjust its collection techniques to address the various characteristics of delinquent taxpayers. IRS' effort to further prevent and deter the filing of fraudulent tax returns has involved increasing the electronic filters and manual checks to (1) screen electronic and paper returns for problems, (2) determine the suitability of those who want to serve as preparers or transmitters of electronic returns, and (3) better identify questionable refund claims.

## Outlook for the Future

While we are encouraged by IRS' and Treasury's actions, we remain concerned because continued progress is needed to fully implement essential improvements. This is particularly true of IRS' modernization efforts because of their key role in resolving the other issues, such as the problems identified in IRS' revenue accounting systems. At the same time, the nation's tax debt inventory will continue to grow, and filing fraud will continue to be a concern. Until IRS sustains an agencywide commitment and devotes the necessary management attention to addressing the challenges it faces in modernizing its processes and systems, it cannot hope to solve its high-risk problems.

Recent increased oversight of IRS reflects the broad-based concern over these issues. Congress has signaled its concern over IRS' slow progress in modernizing its processes and systems by (1) cutting IRS' budget requests for funds to support its modernization efforts, (2) withholding additional modernization funding until IRS successfully addresses certain identified problems, and (3) directing Treasury to assess and report on IRS' progress in taking corrective action. Likewise, Treasury has attempted to assist in IRS' overall modernization planning and decision-making by directing IRS to rely more heavily on the technical expertise of outside contractors and by establishing a review board to monitor IRS' information technology investments.

In addition, Congress established the National Commission on Restructuring IRS and gave the Commission a broad charter for reviewing IRS' management and operations.

# High-Risk Areas

The four areas in IRS that we have deemed high risk require comprehensive business strategies to ensure that IRS' new and revised processes drive systems development and acquisition. These areas also require accurate and reliable information systems and performance measures to track IRS' progress and provide the data necessary to make informed management decisions.

## Tax Systems Modernization

Over the last decade, IRS has been attempting to overhaul its timeworn, paper-intensive approach to tax return processing. In 1995, we identified serious management and technical weaknesses in the modernization program that jeopardize its successful completion, recommended many actions to fix the problems, and added IRS' modernization to our high-risk list. Since then, IRS and Treasury have together taken several steps to implement our recommendations, but much remains to be done. At stake is the over $3 billion that IRS has spent or obligated on this modernization since 1986, as well as any additional funds that IRS plans to spend on modernization.

In July 1995, we reported that IRS (1) did not have a comprehensive business strategy to cost-effectively reduce paper tax return filings and (2) had not yet fully developed and put in place the requisite management, software development, and technical infrastructure necessary to successfully implement its ambitious, world-class modernization. We also reported that IRS lacked an overall systems architecture, or blueprint, to guide the modernization's development and evolution.

At that time, we made over a dozen recommendations to the IRS Commissioner to address these weaknesses. Collectively, the recommendations called for IRS to (1) formulate a comprehensive business strategy for maximizing electronic filings, (2) improve its strategic information management by implementing a process for selecting, prioritizing, controlling, and evaluating the progress and performance of all major information systems and investments, (3) implement disciplined, consistent procedures for software requirements management, quality assurance, configuration management, and project planning and tracking, and (4) complete and enforce an integrated systems architecture and security and data architectures. IRS agreed to implement our recommendations.

In May 1996, Treasury reported to the House and Senate Appropriations Committees on steps under way and planned to exert greater management oversight over IRS' modernization efforts.[1] For example, it established a Modernization Management Board as the primary review and decision-making body for modernization and for policy and strategic direction. In addition, Treasury scaled back the overall size of the modernization by approximately $2 billion and is working with IRS to obtain additional contractor help to accomplish the modernization.

Pursuant to congressional direction, we assessed IRS' actions to correct its management and technical weaknesses, as delineated in Treasury's report on tax systems modernization. We reported in June and September 1996 that IRS had initiated many activities to improve its modernization efforts but had not yet fully implemented any of our recommendations. Consequently, in order to minimize the risk attached to continued investment in its systems modernization, we suggested to Congress that it consider limiting modernization funding exclusively to cost-effective efforts

[1]Report to House and Senate Appropriations Committees: Progress Report on IRS's Management and Implementation of Tax Systems Modernization, Department of the Treasury, May 6, 1996.

that (1) support ongoing operations and maintenance, (2) correct IRS' pervasive management and technical weaknesses, (3) are small, represent low technical risk, and can be delivered quickly, and (4) involve deploying already developed and fully tested systems that have proven business value and are not premature given the lack of a completed architecture.

To help oversee IRS' modernization, Congress in the fiscal year 1997 Omnibus Consolidated Appropriations Act[2] directed IRS to (1) submit by December 1, 1996, a schedule for transferring a majority of its modernization development and deployment to contractors by July 31, 1997, and (2) establish a schedule by February 1, 1997, for implementing our recommendations by October 1, 1997. In its conference report on the act, Congress directed the Secretary of the Treasury to (1) provide quarterly reports on the status of IRS' corrective actions and modernization spending[3] and (2) submit by May 15, 1997, a technical architecture for the modernization that has been approved by

[2]Public Law 104-208, September 30, 1996.

[3]H.R. Report No. 863, 104th Cong., 2d sess. (1996). Congress also included the requirement that Treasury provide a milestone schedule for developing and implementing all modernization projects in Treasury's fiscal year 1996 appropriations act (Public Law 104-52, Nov. 19, 1995).

Treasury's Modernization Management Board. Additionally, the Board was directed to prepare a request for proposals by July 31, 1997, to acquire a prime contractor to manage modernization deployment and implementation.

IRS has continued to take steps to address our recommendations and respond to congressional direction. For example, IRS hired a new Chief Information Officer. It also created an investment review board to select, control, and evaluate its information technology investments. Thus far, the board has reevaluated and terminated selected major modernization development projects, such as the Document Processing System (DPS).

Additionally, IRS (1) provided a November 26, 1996, report to the Congress that set forth IRS' strategic plan and schedule for shifting modernization development and deployment to contractors, (2) is finalizing a comprehensive strategy to maximize electronic filing that is scheduled for completion in early 1997, and (3) is updating its system development life cycle methodology and working across various IRS organizations to define disciplined processes for software requirements management, quality assurance, configuration management, and project planning and tracking. Additionally, IRS is developing a technical architecture for the modernization and plans to provide this to Congress by May 15, 1997. Further, IRS is preparing a schedule for implementing our recommendations and plans to provide it to Congress in February 1997.

While we recognize IRS' and Treasury's actions to address these problems, we remain concerned. Much remains to be done to fully implement essential improvements. Increasing the use of contractors, for example, will not automatically increase the likelihood of successful modernization because IRS does not have the technical capability needed to manage all of its current contractors. As a case in point, IRS' Cyberfile—a system development effort led by contractors to enable taxpayers to personally prepare and file their tax returns electronically—exhibited many undisciplined software acquisition practices as well as inadequate financial and management controls. Eventually, IRS canceled the Cyberfile project after spending over $17 million and without fielding any of the system's promised capabilities. Therefore, if IRS is to use additional contractors effectively, it will have to first strengthen and improve its ability to manage those contractors.

In addition, IRS needs to continue to make concerted, sustained efforts to fully implement our recommendations and respond effectively to the requirements outlined by Congress. It will take both management commitment and technical discipline for IRS to do this effectively. Accordingly, we plan to continue assessing IRS' progress in its critical endeavor to modernize.

## Financial Management

Our audits of IRS' financial statements have outlined the substantial improvements needed in IRS' accounting and reporting in order to comply fully with the requirements of the Chief Financial Officers Act of 1990 (CFO Act). The audits for fiscal years 1992 through 1995 have described IRS' difficulties in properly accounting for its reported $1.4 trillion in tax revenues, in total and by reported type of tax; reliably determining the amount of accounts receivable owed for unpaid taxes; regularly reconciling its Fund Balance With Treasury accounts; and either routinely providing support for receipt of the goods and services it purchases or, where supported, accurately recording the purchased item in the proper period.

IRS has made progress in addressing these problems and has developed an action plan, with specific timetables and deliverables, to address the issues our financial statement audits have identified. This is particularly notable in IRS' administrative accounting operations, which track its over $7 billion appropriation that funds IRS' activities. For example, IRS recently reported that it has identified substantially all of the reconciling items for its Fund Balance With Treasury accounts, except for certain amounts IRS has deemed not to be cost-beneficial to research further. It also has successfully transferred its payroll processing to the Department of Agriculture's National Finance Center and has begun designing both a short-term and a long-term strategy to fix the problems that contribute to its nonpayroll expenses being unsupported or reported in the wrong period.

Further, in the revenue accounting area, IRS has designed an interim approach to capture the detailed support for revenue and accounts receivable until longer-term solutions can be identified and implemented. The issues with IRS' revenue accounting operations are complex, and the remedies needed are multifaceted and encompass organizational, managerial, technological, and procedural improvements. IRS' revenue accounting problems are especially affected and complicated by automated data processing systems that were implemented many years ago and thus not designed to support the financial reporting requirements ushered in by the CFO Act. Some of the longer-term actions needed to correct the long-standing problems in IRS' revenue accounting operations include

- implementing software, hardware, and procedural changes needed to create reliable subsidiary accounts receivable and revenue records that are fully integrated with the general ledger; and
- implementing software changes that allow the detailed taxes reported to be maintained separately from the results of compliance efforts that would not be valid financial reporting transactions in the masterfile, other related revenue accounting feeder systems, and the general ledger.

The requirements of the CFO Act have provided the impetus for ongoing efforts to improve IRS' operations. They led to IRS' top managers having a much better understanding than ever before of IRS' serious accounting and reporting problems, provided information on the magnitude of IRS' tax receivables collection problems, and identified the need for stronger controls over such areas as payroll operations.

IRS has made progress in responding to our recommendations. Over the past 4 years, we have made 59 recommendations to improve IRS' financial management systems and reporting. IRS agreed with these recommendations and has been working to implement them and correct its financial systems and information problems. IRS has completed action on some of these recommendations and has efforts under way to address the remaining areas. IRS has been directed in the appropriations committees' conference report to submit a report by March 1, 1997, that presents a plan to correct the problems identified in our July 1996 audit report. As part of our audit of IRS' fiscal year 1996 financial statements, which was ongoing when this report was being prepared, we are examining and will report on the additional actions IRS has taken to respond to the recommendations we have made.

IRS' efforts are intended to position itself to have more reliable financial statements for fiscal year 1997 and thereafter. To accomplish this, especially in accounting for revenue and the related accounts receivables, IRS will need to institute longer-term solutions involving reprogramming software for IRS' antiquated systems and developing new systems as required.

Follow-through by IRS is essential to ensure that its short-term and long-term plans are carried out and effectively solve financial management problems. While IRS' senior management has resolved to address these issues, in the past IRS has not always provided the follow-through needed to complete necessary corrective measures. Solving these problems is essential to providing reliable financial information and ensuring taxpayers that their federal tax dollars are properly accounted for in accordance with federal accounting standards. The accuracy of IRS' financial statements is also essential to both IRS and Congress for (1) ensuring adequate accountability for IRS programs, (2) assessing the impact of tax policies, and (3) measuring IRS' performance and cost effectiveness in carrying out its numerous tax enforcement, customer service, and collection activities.

## Accounts Receivable

IRS is the government's primary tax collection agency and routinely collects over a trillion dollars annually. But many taxpayers are either unable or unwilling to pay their taxes when due, and as a result, IRS estimates that its accounts receivable amount to tens of billions of dollars. Unfortunately, IRS' long-term efforts to efficiently and effectively collect the billions of dollars taxpayers owe in delinquent taxes and to prevent taxpayers from becoming delinquent have been seriously hampered, primarily by outdated equipment and processes, incomplete information needed to better target collection efforts, and the absence of a comprehensive strategy and detailed plan that address the systemic nature of the underlying problems.

On the other hand, short-term results in collecting delinquent taxes have shown some promise. In fiscal year 1996, for example, IRS reported the collection of $29.8 billion in delinquent taxes—the most ever by IRS. Furthermore, for the first time since 1989, IRS also reported that its collection employees took in more money than they classified as "currently not collectible." While these results are encouraging, IRS needs to know more about its inventory of tax assessments and the types of taxpayers who become delinquent each year to develop effective strategies to efficiently target its collection resources and to prevent future delinquencies.

IRS' collection efforts have been hampered by the age of the delinquent tax accounts. Because of the outdated equipment and processes used to match tax returns and related information documents, it can take IRS several years to identify potential delinquencies and then initiate collection actions. In addition, according to IRS, the 10-year statutory collection period generally precludes it from writing off uncollectible receivables until that period has expired. As a result, the receivables inventory includes many relatively old accounts that will never be collected because the taxpayers are deceased or the companies defunct.

IRS has undertaken many initiatives to deal with its accounts receivable problems. These initiatives include correcting errors in the masterfile records of tax receivables, developing more information on the makeup of the inventory of tax debts, developing research systems to identify characteristics of delinquent taxpayers and appropriate collection techniques, attempting telephone contact earlier in the collection process, speeding up the collection process for repeat delinquents, revising the format of bills sent to delinquent taxpayers, automating many of the processes carried out by collection employees in field offices, and attempting to collect compliance-generated delinquencies earlier. While some of these efforts appear to have had some impact on collections and the tax debt inventory, others are long term in nature, and their effectiveness may not be determined for years. Further, the problems with IRS' data and information systems will continue to hinder its ability to effectively measure the results of these efforts.

Congress has recently taken actions that could help deal with the collection of delinquent taxes and the prevention of future delinquencies. Legislation requiring more electronic deposits of employment taxes, expanding voluntary withholding, and authorizing IRS to test the use of private debt collectors could help reduce posting errors, prevent taxpayers from becoming delinquent, and collect more money. Other actions in areas such as tax delinquencies related to independent contractors—a group of taxpayers that is proportionately more delinquent than other groups of taxpayers—could, if adopted, also help IRS deal with its collection problems.

Although the results cannot generally be quantified or traced back to specific actions or improvements, some of IRS' efforts reportedly have resulted in increased collections and reduced delinquencies in the short term. For example, during fiscal year 1996, IRS revised the bills sent to taxpayers to make them clearer and easier to understand, and reported that collections from the billing process increased from $11.8 billion in fiscal year 1995 to $14.7 billion in fiscal year 1996. IRS has also placed more emphasis on collecting examination assessments at the close of an audit, and preliminary results have been favorable.

Until fiscal year 1996, IRS' inventory of tax assessments increased at a faster pace than collections. For example, during the period 1991-1996, the inventory increased an average of 16 percent each year, from $104 billion at the end of fiscal year 1991 to about $216 billion at the end of fiscal year 1996. Reported collection of delinquent taxes, however, averaged only a 4.5-percent increase, from $24.3 billion to $29.8 billion, during that same period.

We recognize that the growth in the gross inventory is not the best measure of IRS' performance because it includes penalty and interest charges that continue to accrue on delinquent accounts, potentially invalid accounts, and accounts that are truly uncollectible; however, better figures are not available. IRS is working toward better defining its receivables inventory. For its fiscal year 1995 financial statements, IRS developed a methodology to differentiate financial accounts receivable from the amounts it has assessed for compliance purposes. While the methodology appeared sound, mistakes in performing the analysis and errors in the underlying data made the sample results unreliable.

A number of IRS initiatives hold some potential for future improvements in both collections and compliance. For example, IRS is developing a number of research and evaluative tools that are intended to determine the most efficient and effective way to handle cases by identifying those taxpayer characteristics that could predict the possible outcome of the cases. In addition, research databases are being constructed that are intended to allow for identification of particular groups, and a research structure has been developed to allow for studies dealing with different groups of taxpayers. However, the completion dates for full development of the databases are currently unknown due to the uncertainty of funding for IRS' Tax Systems Modernization program. Even if funding was assured, it would still take a number of years to identify the root causes of delinquencies and to develop, test, and implement courses of action to deal with the causes. Once the analyses and planning are completed, it will still be some time before full results of the new initiatives are realized.

Nevertheless, the recent increase in reported collections is a good sign. As previously mentioned, the $29.8 billion reported in fiscal year 1996 is the most ever collected. This sum represents a 19-percent increase over the $25.1 billion reported in fiscal year 1995 and a 17-percent increase over the $25.5 billion reported in fiscal year 1990—the previous best year. However, as we said earlier, IRS does not have the data to determine which actions or improvements generate changes in program performance such as this.

Correcting the problems and improving collections will require long-term and continuous efforts. To ensure that these efforts are on the right track, IRS needs a comprehensive strategy that involves all aspects of IRS' operations. As part of this strategy, IRS needs to set priorities; modernize outdated equipment and processes; and establish goals, timetables, and a system to measure progress.

## Filing Fraud

When we first identified filing fraud as a high-risk area in February 1995, the amount of filing fraud being detected by IRS was on an upward spiral. From 1991 to 1994, the number of fraudulent returns that IRS detected rose from 11,168 to 77,781, and the total amount of fraudulent refunds detected rose from $42.9 million to $160.5 million. In 1995, after being urged to take immediate action by us, Congress, and a Treasury task force, IRS introduced new controls and expanded existing controls in an attempt to reduce its exposure to filing fraud. Those controls were directed toward either (1) deterring the filing of fraudulent returns or (2) identifying questionable returns after they have been filed.

To deter the filing of fraudulent returns, IRS took several steps that were focused on electronic filers. As a result of these steps, IRS (1) expanded the number of upfront filters in the electronic filing system designed to screen electronic submissions for problems, such as missing or incorrect Social Security Numbers (SSN), to prevent returns with those problems from being filed electronically and (2) strengthened the process for checking the suitability of persons applying to participate in the electronic filing program as return preparers or transmitters by requiring fingerprint and credit checks.

To better identify fraudulent returns once they have been filed, IRS placed an increased emphasis in 1995 on validating SSNs on filed paper returns and delayed any related refunds to allow time to do those validations and to check for possible fraud. IRS also improved its Questionable Refund Program by (1) revising the computerized formulas used to score all tax returns as to their fraud potential and (2) upgrading the Electronic Fraud Detection System (EFDS) to give staff better research capabilities.

IRS' efforts produced some positive results. For example, the number of SSN problems identified by the electronic filing filters increased from about 1 million in 1994 to about 4.1 million in 1995. In addition, about 350 persons who applied to participate in the electronic filing program for 1995 were rejected because they failed the new fingerprint and credit checks. IRS' efforts to validate SSNs on paper returns produced over $800 million in reduced refunds or additional taxes. Unfortunately, IRS identified many more SSN problems than it was able to deal with and released about 2 million refunds without resolving the problems.

Despite the generally positive results, there is insufficient information available to determine which of IRS' actions have had a significant impact on either detecting or deterring filing fraud. IRS conducted some studies in 1995 and 1996 that may shed some light on the effects of its changes and upgrades, but IRS has not released the results of these studies.

The number of fraudulent returns identified by IRS has declined recently, from 77,781 fraudulent returns involving refunds of $160.5 million in 1994 to 62,309 fraudulent returns with refunds of $131.7 million in 1995. That downward trend continued in 1996, at an even more significant pace.

During the first 9 months of 1996, IRS reported detecting 20,521 fraudulent returns involving refunds of $55.4 million, compared with 59,241 returns totaling $124.8 million in the first 9 months of 1995. There is insufficient information available to determine whether the decline was the result of staff reductions, changes in the program's operating and reporting procedures, or a general decline in the incidence of fraud.

IRS' efforts to control filing fraud are also constrained by the relatively short time available, after a return is filed and before any refund is issued, in which to identify a questionable return. Therefore, it is critically important for IRS to (1) optimize the controls, such as upfront filters, that are intended to prevent the filing of fraudulent returns and (2) maximize the effectiveness of available staff. Modernization is the key to achieving these objectives, and electronic filing is the cornerstone of that modernization.

As discussed previously, one of the benefits of electronic filing is the ability to build controls into the system, in the form of filters, that prevent returns with certain problems (such as incorrect SSNs) from being filed electronically. IRS cannot identify those kinds of problems on paper returns until after the returns are filed and, as happened in 1995, is limited in the number of cases it can pursue by the number of staff available. One solution to this dilemma is to increase the percentage of returns filed electronically. IRS' business vision calls for increasing the number of electronic returns to 80 million by 2001. However, our analysis of recent filing trends indicated that only about 33 million returns are expected to be filed electronically by 2001. To achieve its goal, IRS must first identify those groups of taxpayers who offer the greatest opportunity to reduce IRS' paper-processing workload and operating costs if they were to file electronically. IRS must then develop strategies that focus its resources on eliminating or lessening impediments that inhibit those groups from participating in the program. As of early January 1997, IRS was finalizing its electronic filing strategy.

The EFDS enables IRS to use its staff more effectively by automating a process that had been labor and paper intensive and by enhancing the staff's research and query capabilities. To date, EFDS has been used primarily on electronic returns, which accounted for only about 13 percent of all individual income tax returns filed in 1996. IRS had planned to expand EFDS to all paper returns, but it is unclear how those plans will be affected by IRS' recent decisions to terminate its major paper processing modernization project (the Document Processing System) and to consider other options for processing paper returns.

# Further Action Needed

For years, IRS has struggled to collect the nation's tax revenue using outdated processes and technology. The result has often been inefficient and ineffective programs and operations that are vulnerable to waste, fraud, abuse, and mismanagement. Of particular concern to us, Congress, and others have been IRS' efforts to modernize its tax systems, manage its administrative and revenue accounting systems, identify and collect taxes owed the government, and detect and prevent the filing of fraudulent tax returns.

These areas of concern share common characteristics that IRS must address in the very near future. Specifically, these high-risk areas lack an overall implementation strategy to guide IRS in the selection, acquisition, control, integration, security, and evaluation of modern information systems that would improve its efficiency and effectiveness. Program officials in these areas also do not always have the information needed for their management decisions. As a result, any expectation of significant and immediate improvement in these areas seems unrealistic.

We believe that IRS must take prompt and determined action to identify and meet its planning, modernization, and information needs. At a minimum, IRS needs an implementation strategy that includes both performing cost-benefit analyses when prioritizing its needs in the context of its overall business vision and developing reasonable estimates of the extent, time frames, and resources required to align its program areas with its vision. IRS also needs to better plan for the purchase and integration of new systems and technologies. In addition, IRS must ensure that its administrative and revenue accounting systems fully comply with government accounting standards and that it develops performance measures that will allow its managers, Congress, and us to track its progress.

# Related GAO Products

## Tax Systems Modernization

Tax Systems Modernization: Actions Underway But Management and Technical Weaknesses Not Yet Corrected (GAO/T-AIMD-96-165, Sept. 10, 1996).

IRS Operations: Critical Need to Continue Improving Core Business Practices (GAO/T-AIMD-96-188, Sept. 10, 1996).

Internal Revenue Service: Business Operations Need Continued Improvement (GAO/AIMD/GGD-96-152, Sept. 9, 1996).

Tax Systems Modernization: Cyberfile Project Was Poorly Planned and Managed (GAO/AIMD-96-140, Aug. 29, 1996).

Tax Systems Modernization: Actions Underway But IRS Has Not Yet Corrected Management and Technical Weaknesses (GAO/AIMD-96-106, June 7, 1996).

Security Weaknesses at IRS' Cyberfile Data Center (GAO/AIMD-96-85R, May 9, 1996).

Tax Systems Modernization: Management and Technical Weaknesses Must Be Overcome to Achieve Success (GAO/T-AIMD-96-75, Mar. 26, 1996).

Tax Systems Modernization: Management and Technical Weaknesses Must Be Corrected If Modernization Is to Succeed (GAO/AIMD-95-156, July 26, 1995).

## Financial Management

Financial Management: Challenges Facing the IRS (GAO/T-AIMD-97-34, Jan. 9, 1997).

IRS Financial Audits: Status of Efforts to Resolve Financial Management Weaknesses (GAO/T-AIMD-96-170, Sept. 19, 1996).

Financial Audit: Examination of IRS' Fiscal Year 1995 Financial Statements (GAO/AIMD-96-101, July 11, 1996).

Financial Audit: Actions Needed to Improve IRS Financial Management (GAO/T-AIMD-96-96, June 6, 1996).

IRS Operations: Significant Challenges in Financial Management and Systems Modernization (GAO/T-AIMD-96-56, Mar. 6, 1996).

Financial Audit: Examination of IRS' Fiscal Year 1994 Financial Statements (GAO/AIMD-95-141, Aug. 4, 1995).

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Financial Audit: Examination of IRS' Fiscal Year 1992 Financial Statements (GAO/AIMD-93-2, June 30, 1993).

## Accounts Receivable

IRS Tax Collection Reengineering (GAO/GGD-96-161R, Sept. 24, 1996).

Tax Administration: Tax Compliance of Nonwage Earners (GAO/GGD-96-165, Aug. 28, 1996).

Managing IRS: IRS Needs to Continue Improving Operations and Service (GAO/T-GGD/AIMD-96-170, July 29, 1996).

Financial Audit: Examination of IRS' Fiscal Year 1995 Financial Statements (GAO/AIMD-96-101, July 11, 1996).

Tax Research: IRS Has Made Progress But Major Challenges Remain (GAO/GGD-96-109, June 5, 1996).

Tax Administration: IRS Tax Debt Collection Practices (GAO/T-GGD-96-112, Apr. 25, 1996).

Tax Administration: IRS' Fiscal Year 1996 and 1997 Budget Issues and the 1996 Filing Season (GAO/T-GGD-96-99, Mar. 28, 1996).

Status of Tax Systems Modernization, Tax Delinquencies, and the Potential for Return-Free Filing (GAO/T-GGD/AIMD-96-88, Mar. 14, 1996).

Financial Audit: Examination of IRS' Fiscal Year 1994 Financial Statements (GAO/AIMD-95-141, Aug. 4, 1995).

Taxpayer Compliance: Reducing the Income Tax Gap (GAO/T-GGD-95-176, June 6, 1995).

Reducing the Tax Gap: Results of a GAO-Sponsored Symposium (GAO/GGD-95-157, June 2, 1995).

Tax Administration: Administrative Improvements Possible in IRS' Installment Agreement Program (GAO/GGD-95-137, May 2, 1995).

High-Risk Series: Internal Revenue Service Receivables (GAO/HR-95-6, Feb. 1995).

Tax Administration: Tax Compliance Initiatives and Delinquent Taxes (GAO/T-GGD-95-74, Feb. 1, 1995).

Tax Administration: Changes Needed to Reduce Volume and Improve Processing of Undeliverable Mail (GAO/GGD-95-44, Dec. 7, 1994).

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## Filing Fraud

Earned Income Credit: IRS' 1995 Controls Stopped Some Noncompliance, But Not Without Problems (GAO/GGD-96-172, Sept. 18, 1996).

IRS Efforts to Control Fraud (GAO/GGD-96-96R, Mar. 25, 1996).

The 1995 Tax Filing Season: IRS Performance Indicators Provide Incomplete Information About Some Problems (GAO/GGD-96-48, Dec. 29, 1995).

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