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Report to the Chairman, Permanent Subcommittee on Investigations Committee on Governmental Affairs U.S. Senate

September 1994

# TAX ADMINISTRATION

# Compliance Measures and Audits of Large Corporations Need Improvement

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GAO

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**General Government Division**

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The Honorable Sam Nunn
Chairman, Permanent Subcommittee
on Investigations
Committee on Governmental Affairs
United States Senate

Dear Mr. Chairman:

This report responds to your request on the Internal Revenue Service's (IRS) program to audit tax returns of the largest corporations—the Coordinated Examination Program (CEP). It makes recommendations to IRS on improving CEP and the appeals process.

This report is the third and final phase of our work on CEP. In April 1991, we testified on our initial observations. In April 1992, we issued our report on trends in CEP audits and a profile of CEP corporations.

As agreed with the Committee, unless you publicly release its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies to the Commissioner of Internal Revenue; the Chairmen of the Senate Committee on Finance, the House Committee on Ways and Means, and the Joint Committee on Taxation; and other interested parties. Copies will also be made available to others on request.

This report was prepared under the direction of Natwar M. Gandhi, Associate Director, Tax Policy and Administration Issues. Other major contributors are listed in appendix VII. If you have any questions about this report, please contact me on (202) 512-5407.

Sincerely yours,

Jennie S. Stathis

Jennie S. Stathis
Director, Tax Policy and
Administration Issues

# Executive Summary

## Purpose

While the nation's 1,700 largest corporations pay billions of dollars in taxes, do they pay all they owe? To address this question, the Internal Revenue Service (IRS) audits these corporations under its Coordinated Examination Program (CEP). Of the sizable sums IRS auditors recommend in additional taxes, how much is collected after appeals and litigation? What factors reduce amounts collected? And what is the status of IRS' ongoing changes to CEP to address those factors? This report, the third in response to a request by the Chairman of the Permanent Subcommittee on Investigations, Senate Committee on Governmental Affairs, focuses on these questions.

## Background

Taxes paid by CEP corporations play an important role in funding government programs. Excluding refunds, these corporations each year pay income taxes of about $55 billion. Nevertheless, IRS' revenue agents annually recommend that they pay billions of dollars of additional taxes—roughly two-thirds of the total recommended from all IRS audits. Thus, it is easy to understand why IRS considers CEP to be its most important audit program.

CEP consumes about 20 percent of IRS' total audit resources. Yet the 1,700 audit staff years devoted to the program are modest compared to the formidable task of auditing the 1,700 largest, most complex corporations. Given this task, CEP audits may not start for several years after the return is filed and take several more years to be completed.

Corporations may challenge the recommended tax assessments in IRS' Office of Appeals and the courts. IRS estimates that CEP corporations appeal 80 to 90 percent of the recommended taxes. IRS' Appeals settles almost 90 percent of those amounts, with the remainder going to court. These recommended taxes are assessed only after the corporation agrees to them, the corporation does not respond to the deficiency notices, or the Tax Court rules on them. Because GAO found that these corporations almost always pay what they are assessed after the appeals process, GAO in this report considers assessed taxes to be equivalent to collected taxes.

CEP audits, unlike most other IRS audits, are conducted using a team approach. A case manager, at the GS-14 level, may be responsible for several CEP audits. An on-site GS-13 or GS-14 team coordinator supervises one or two revenue agents assigned to the audit. The team coordinator may call on engineers, economists, international specialists, and revenue agents in other districts—all of whom report separately to their

supervisors. CEP audits are planned, staffed, and managed at 59 of IRS' 63 district offices. IRS' National Office provides overall direction.

GAO's review included database analyses, surveys, and in-depth case studies. GAO computer matched two IRS databases to calculate the percentage of taxes recommended by CEP teams that was eventually collected. One database provided data on taxes recommended from CEP audits closed in fiscal years 1983 through 1991; the other showed taxes collected from those audits, after any appeals or litigation, as of the end of fiscal year 1992. GAO surveyed 308 IRS and corporation officials involved in all 108 CEP audits that closed agreed at audit or appeals levels and recommended at least $30 million of additional taxes in fiscal years 1989 through 1991.

Using various criteria, GAO judgmentally selected 12 of the 108 audits for case studies. The 12 audits accounted for $1.5 billion of the $8.5 billion of recommended taxes in the 108 audits. For the 12 audits, GAO reviewed documents and interviewed key IRS and corporation officials. Overall, GAO interviewed 85 corporation and IRS officials in 5 regions, 7 districts, and the IRS National Office.

## Results in Brief

IRS' mission is to collect the proper amount of taxes at the least cost to the federal government and taxpayers. However, due to the complexity of the tax law and the conflicting incentives that IRS employees face in administering the law, it is impossible to determine the proper amount of tax that should be collected through CEP. GAO computed that, historically, IRS has actually collected 22 percent of the additional taxes that IRS revenue agents have recommended in CEP audits. GAO does not know what the proper amount should be, but believes that it is reasonable to assume that collecting 22 cents per dollar leaves room for improvement either in the audit recommendation process or in the appeals process, or both.

Another avenue for improvement lies with simplifying the tax code. Reducing tax law complexity would improve the collection rate while benefiting both IRS and taxpayers. Both would have more certainty about what the proper amount of tax should be, which would reduce time spent on audits and in appeals. The complexity and ambiguity of the tax code causes legitimate differences in interpretation. This has resulted in IRS repeatedly auditing some of the same issues and taxpayers repeatedly disputing IRS' audit findings.

Neither the appeals process nor litigation have proven effective in resolving recurring issues. GAO found that 14 tax code sections accounted for 45 percent of 12,000 disputed issues facing IRS' Appeals Office as of September 1992 and for 57 percent of the $99 billion in disputed dollars for those issues. GAO believes that IRS should more aggressively seek legislative changes to resolve recurring disputes.

The tax system also creates a tension in seeking a proper balance between the tax administrator's need for information and the taxpayer's burden in providing information. Such information often involved much earlier tax years—sometimes over 10 years prior to the audit. Recognizing the tension issue, GAO noted instances in which CEP audit teams' legitimate needs for taxpayer-provided information were not met. GAO also noted instances in which taxpayers were permitted to introduce information in the appeals process that was not made available to the CEP audit teams. GAO believes that IRS needs better tools for obtaining legitimately needed information to ensure that audit recommendations for additional taxes are adequately supported.

IRS revenue agents and appeals officers face conflicting measures—measures which create incentives that contribute to the large gap between taxes recommended and taxes collected after appeals.

- IRS agents are charged with protecting the government's revenue. They are instructed to make their audit recommendations without deviating from IRS' legal positions or considering the hazards of litigation. A key measure of the work of the Examination function as a whole is the amount of additional taxes recommended per audit hour.
- Appeals officers, on the other hand, are charged with resolving tax controversies without litigation to the extent possible while being fair and impartial to both the government and the taxpayer. They are instructed to consider the hazards of litigation and may concede the recommended taxes in part or in whole on that basis even if their decision deviates from an IRS legal position. In measuring the Appeals function as a whole, IRS focuses on the number of cases settled without litigation.

GAO recognizes the merit of both objectives but believes that adding the common measure of dollars collected to the existing measures for each function would better balance the incentives in the overall system and contribute to an improved collection rate while permitting each function to continue pursuing its primary objective.

GAO also noted opportunities for improvement through changes in the way IRS allocates and brings CEP resources to bear, trains revenue agents to enhance their knowledge of the industries they audit, and controls the coordination between Appeals and other IRS functions. These improvements would supplement the 10 changes to CEP that IRS approved in 1990 and that GAO also views as being needed.

# GAO's Analysis

## CEP's Collection Rate Was Low

An important output measure is the amount of additional taxes collected as a result of CEP. CEP corporations voluntarily pay about $55 billion in income taxes annually. Because of limitations in IRS' databases, IRS did not know how much additional revenue was actually collected as a result of CEP audits.

GAO worked with IRS' data to compute the collection rate. GAO's computer match of taxes recommended in fiscal years 1983 through 1991 showed only a 22 percent collection rate. Specifically, IRS collected $7.1 billion of $32.4 billion in recommended taxes. Assuming a collection rate of 22 percent for fiscal year 1992, CEP's $16 billion in recommended taxes would eventually yield $3.5 billion. Because IRS' data were incomplete, this 22-percent rate could be too high or too low. Accounting for other factors, such as claims for net operating losses and refunds, would allow IRS to compute a more accurate collection rate. (See pp. 30 and 34-35.)

IRS has been developing a system and new measures to track CEP's results. While new measures are needed, GAO believes IRS' efforts will be enhanced if IRS also accurately measures the collection rate over time. (See pp. 33-34.)

Although CEP corporations voluntarily pay $55 billion in taxes each year, no one knows whether this is the full amount owed. Appeals' settlements on disputed taxes cannot be used as a measure of the amount owed by CEP corporations or their ultimate compliance. Appeals can settle for a lower amount of taxes if it believes litigation would be too risky or that the CEP team's recommendations were not adequately supported—regardless of whether a corporation complied with the tax laws. Determining compliance is also confounded by ambiguities in the tax law. To fully estimate the portion of taxes owed but not paid, IRS would have to audit all

tax issues on a sample of CEP tax returns and be assured that it had properly interpreted the tax law. IRS does not do this largely because of time and resource constraints. (See pp. 35-37.)

## Examination Factors Reducing the Collection Rate

### CEP Director Did Not Control Field Resources

The CEP Executive Director did not have authority to control the budget resources needed for effective CEP audits. Instead, this authority resided with the 59 IRS district offices, where CEP competes with other programs for resources.

GAO found that this lack of central authority has allowed districts to redirect resources from CEP, leaving CEP teams ill-equipped to comprehensively audit enormous corporations that have become more complex and diversified. Funds for travel, training, and private sector experts were insufficient. (See pp. 45-50.)

Decentralization also limited the impact of the 10 changes IRS approved in 1990. The changes focused in better communication, training, and supervision. GAO found that IRS had not consistently implemented the changes in the 59 Districts participating in CEP. GAO believes these changes have potential but that such potential will not be reached if implementation continues to vary across districts. (See pp. 43-45.)

A program as large and important as CEP is less likely to succeed without central control over resources and staff allocation. Centralization, however, need not encompass all aspects of CEP cases. IRS may choose to leave authority for specific case decisions in the hands of District officials, who tend to know more about the cases.

### CEP Productivity Measures Provided Little Incentive

IRS mainly measured CEP's productivity by the amount of additional taxes that audit teams recommended per hour. This measure encouraged CEP teams to recommend as many taxes in the shortest time possible, even if doing so meant bypassing audit steps or not waiting for missing data. Relying on this measure has contributed to a low collection rate,

inefficient uses of CEP resources, and unnecessary burdens on Appeals and corporations.

Also, focusing on recommended taxes as a measure provided little incentive for CEP teams to meet with Appeals officials before the appeals process to explain their audit findings or to meet afterwards to determine why Appeals did not sustain their recommended taxes. Although not required by IRS for all nine appealed cases that GAO reviewed, only four teams met with Appeals beforehand, and none met with Appeals after the case was settled. CEP team members said such meetings would take time and reduce recommended tax amounts. (See pp. 50-53.)

## IRS' Methods to Obtain Taxpayer Data Did Not Always Work

CEP teams and corporations may disagree on the types and amount of information needed for an audit. Some IRS requests for information may be overly broad or vague. Other requests sought information from many years earlier, which complicated efforts to satisfy the request. Recognizing these pitfalls, CEP teams still need a certain amount of information to determine whether all income is reported and all deductions and credits are allowable.

GAO found that two methods CEP teams have to obtain needed taxpayer information—information document requests and summonses—did not work well. For example, 85 percent of CEP team coordinators responding to GAO's survey reported they did not receive requested information from corporations in a timely manner; 30 percent said they had to close audits without receiving all requested information. Without such information, CEP teams could not fully support their recommended taxes, resulting in Appeals ruling in favor of taxpayers' positions.

Rather than providing CEP teams with needed data during the audit, about half of the corporations GAO surveyed said they introduced new data in Appeals. For example, in two case studies where this occurred, Appeals conceded disputed adjustments of about $30 million. CEP officials said they would not have recommended some of the taxes had they received the data during the audit.

GAO believes that IRS could use better tools to encourage corporations to provide requested data in a timely manner. For example, corporations that do not provide requested data to CEP teams without reasonable cause could be prohibited from using the data at Appeals. (See pp. 53-57.)

## Revenue Agents Need to Have Knowledge of the Industries They Audit

IRS did not encourage CEP revenue agents to specialize in auditing certain industries. Instead, IRS rotated them on about a 6-year schedule to different corporations that often involved different industries and different accounting standards and issues. GAO believes that rotating agents among corporations is necessary to reduce potential conflicts of interest. But rotating them to audit corporations in different industries hindered their ability to fully develop audit issues that could be sustained in Appeals.

Over one-quarter of the corporate survey respondents said they were dissatisfied with the audit team's knowledge of their industry. Similarly, 15 of 23 CEP officials from the case studies said revenue agents often lacked the necessary industry knowledge. GAO supports allowing revenue agents to specialize in certain industries but recognizes that such a policy may increase travel costs and would not be practical in every district. (See pp. 57-59.)

# Appeals Factors Reducing the CEP Collection Rate

## Mismatched Goals Set the Stage for a Low Collection Rate

Appeals' mission is to settle tax disputes without litigation while being fair and impartial to both the government and the taxpayer. CEP teams are charged with protecting the government's revenue and instructed to make their audit recommendations without considering the hazards of litigation. Given complex tax laws, these mismatched goals laid the foundation for a low collection rate.

Specifically, IRS' measure for CEP encouraged CEP teams to recommend more taxes. Appeals focused on settling cases. This focus encouraged appeals officers to negotiate settlements on a portion of the taxes that CEP teams recommended to avoid the probability of losing all such taxes in court. Settlements also avoided overloading the courts as well as incurring the costs and time of litigation.

Adding a common measure for both functions, such as the collection rate, would better balance these incentives. A common measure would enhance communication so that CEP teams are less likely to recommend taxes that Appeals will not sustain, while Appeals would be more likely to sustain

supported tax recommendations. Applying this measure only to CEP audit teams would undercut the incentive to communicate.

Also, because IRS has litigated few CEP cases, an imbalance seemed to exist in resolving disputed issues. Knowing this, corporations could negotiate settlements in Appeals from a stronger position. If IRS were to show more willingness to litigate, its negotiation stance could improve. However, GAO recognizes that litigation imposes burdens and risks, and resource constraints may preclude any significant increase in litigation.

Appeals' settlements do not set a precedent for resolving tax disputes beyond those disputes on which the settlement is reached. Without legislative changes that will resolve the disputes or litigation that sets a precedent, the same disputed issues get appealed year after year, creating rework for all affected parties. As of September 1992, Appeals had 12,000 disputed issues, worth $99 billion in adjustments, waiting to be resolved. IRS officials did not know the portion associated with CEP but believed that most were. Of the 12,000 disputed issues, GAO found that 5,279 (45 percent) involved just 14 tax code sections.

GAO believes that IRS needs to focus more attention on proposing legislative changes that would stem recurring issues and improve administration of tax laws as well as the collection rate. Legislative solutions to recurring issues could reduce burdens on corporations and IRS as well as expedite the audit and appeals processes. (See pp. 64-69.)

## Internal Control Lapses in Appeals Gave an Edge to CEP Corporations

Appeals' controls to ensure coordination with other IRS functions did not always work or exist in the cases GAO reviewed. Insufficient coordination gave an edge to CEP corporations and led to inconsistent settlements. Specifically, corporations had an advantage during negotiations whenever Appeals

- used new evidence submitted by corporations after audit without letting CEP officials evaluate it and
- settled issues contrary to IRS legal positions without obtaining the views of the Office of Chief Counsel.

More coordination within IRS may raise concerns about Appeals' independence to settle tax disputes objectively and impartially. On the other hand, more coordination does not need to undercut Appeals' independence and authority. In fact, coordinating on new facts and legal

interpretations before settling a case, while adding some time, can be viewed as upholding objectivity. (See pp. 69-75.)

## Recommendations

To better ensure that IRS meets its mission and improves the CEP collection rate, GAO makes recommendations to the Commissioner of Internal Revenue in chapters 2, 3, and 4, including the following:

- Provide the CEP Director with authority over CEP resources in the districts.
- Expand measures in CEP and Appeals to include consideration of a common measure, such as the collection rate.
- Increase revenue agents' knowledge of specific industries in which they do CEP audits.
- Ensure that Appeals seeks CEP teams' evaluation of new information from corporations and coordinates with Counsel officials before conceding taxes in opposition to IRS legal positions.
- Propose legislative changes that will permanently resolve more recurring tax disputes.
- Use the 22 percent collection rate, when needed, until IRS has corrected the databases for accurately tracking CEP collections.
- Test ways to measure CEP corporate compliance.

## Comments

In a January 11, 1994, letter, the Commissioner of Internal Revenue provided comments on a draft of this report.

The Commissioner agreed to implement some recommendations but not others. For example, she opposed using the 22 percent collection rate when estimating and testing ways to measure corporate compliance. She agreed with recommendations on CEP audit teams, except for giving the CEP Executive Director line and budget authority. GAO still recommends this authority for allocating budget resources but made language changes to clarify its position on line authority. GAO did not intend that the CEP Director control all aspects of CEP, such as specific case decisions.

Finally, the Commissioner agreed with GAO's recommendations on better controls and clearer Appeals' summaries as well as resolving recurring issues by proposing tax law changes. However, she did not agree with some suggestions for balancing incentives in the Appeals process. GAO still believes that more balance is needed in the incentives but recognizes that this goal can be achieved through different means.

The Commissioner's comments on recommendations and report sections and GAO's evaluations of these can be found at the end of chapters 2, 3, and 4 of the report. Appendix VI contains IRS' complete comment letter and an interspersed point-by-point GAO evaluation.

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## Abbreviations

| | |
|---|---|
| AIMS | Audit Information Management System |
| BMF | Business Master File |
| CEP | Coordinated Examination Program |
| ERIS | Enforcement Revenue Information System |
| IDR | information document request |
| IRS | Internal Revenue Service |
| ISP | Industry Specialization Program |
| JCT | Joint Committee on Taxation |
| NOL | net operating loss |
| ROI | return on investment |
| SOI | Statistics of Income Division |
| TEI | Tax Executives Institute |
| TIN | taxpayer identification number |

# Introduction

The mission of the Internal Revenue Service (IRS) includes collecting the proper amount of taxes at the least cost. In doing so, IRS attempts to minimize the burden on taxpayers. Driven by this mission, IRS audits the majority of tax returns filed by about 1,700 of the nation's largest corporations. Excluding any refunds, these corporations voluntarily pay about $55 billion in annual income taxes.

These relatively few audits, compared to the 1.1 million individual and corporate audits done annually, account for the majority of IRS' additional recommended taxes (65 percent in 1992) from all IRS audits. But how much of the additional taxes recommended are truly owed and will be collected after any appeals or litigation?

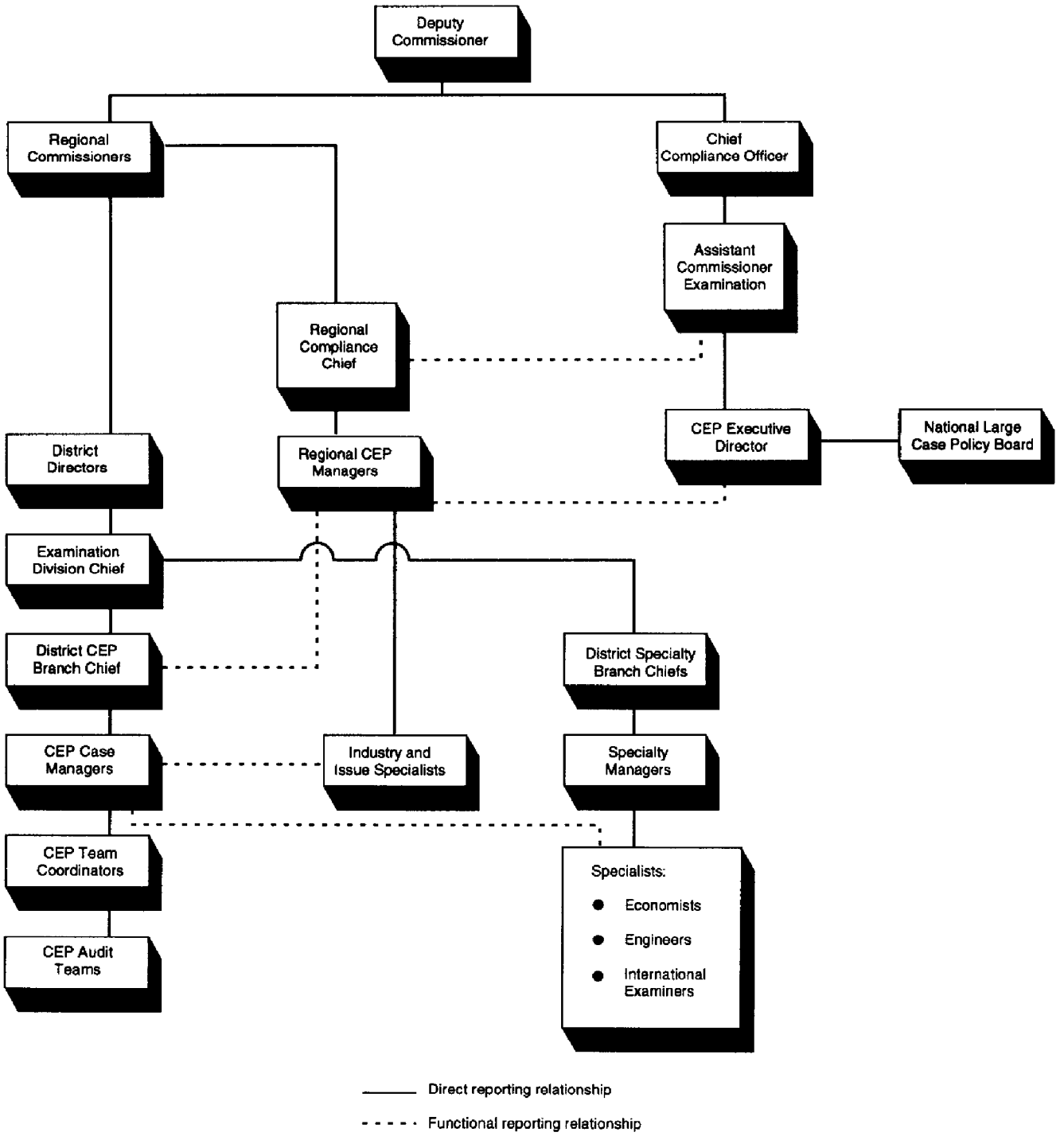
## IRS' Compliance Program for Large Corporate Taxpayers

In 1966, IRS established the Coordinated Examination Program (CEP) to audit the nation's largest and most complex corporations, each with assets usually exceeding $250 million. IRS established the program because of the growth in these corporations during the 1950s and 1960s and because of the realization that IRS' traditional "one case, one agent" approach no longer resulted in effective tax audits of large businesses.

IRS' Examination Division is the function responsible for CEP. IRS has organized CEP in a decentralized manner with Examination staff located in 59 district offices. Examination staff in IRS' National Office provide program direction and oversight. Figure 1.1 shows CEP's decentralized organizational structure. It shows that the highest ranking official in CEP—the Executive Director —does not have line authority over CEP audit teams. Rather, the district director and Examination division chief in each district evaluate the performance of CEP audit team members and control the budget and staffing resources needed for CEP audits.[1]

[1]As of March 1994, IRS was considering additional changes to CEP's organization. For example, CEP may be expanded to include all corporations with assets greater than $10 million. We have not evaluated these proposed changes.

**Figure 1.1: CEP Organization Chart**




(Figure notes on next page)

Source: Prepared by GAO on the basis of IRS documents.

IRS' compliance program for CEP corporations can involve more than the CEP audits in the Examination Division. In addition, IRS' Office of Appeals and Office of Chief Counsel, along with the federal court system, can affect the additional taxes ultimately collected.

## The CEP Audit Process

To determine which large corporations to select for CEP, IRS scores income tax returns on various criteria, such as corporate structure, assets, and income. Once IRS selects the CEP corporations, it uses a team to audit each one because of the complexity of the corporations and their tax returns.

A CEP audit team usually has an on-site GS-13 or GS-14 team coordinator, one or more revenue agents, and specialists. A team coordinator directs the work of the agents and reports to a GS-14 CEP case manager, who usually oversees several audits. Specialists—such as actuaries, economists, engineers, and international and industry specialists—work with the team but do not report directly to the case manager. Rather, specialists report to their own managers.

The Industry Specialization Program (ISP) provides technical advice and information to CEP audit teams. As of 1993, it had 25 industry specialists and 7 issue specialists. They identify tax issues within major industries having audit potential and help revenue agents treat tax issues as well as taxpayers consistently. These specialists, however, have no line authority over the agents. ISP specialists also assist the Office of Chief Counsel in proposing legislative changes and developing revenue rulings and procedures.

CEP audit teams usually remain on-site at the corporation's headquarters for extended periods. The team generally examines two or three annual tax returns in a single audit cycle; each audit cycle takes an average of 2 to 3 years to complete. Although the time lag varies, teams generally begin auditing CEP returns 5 to 6 years after they are filed. IRS is attempting to reduce the time lag by auditing more CEP returns over the same audit cycle.

According to IRS procedures, a CEP team plans its audit by reviewing the corporation's tax returns, financial statements, historical data from past

audits, and other pertinent documents to identify potential areas of tax noncompliance. These areas of potential noncompliance are referred to as "issues." The team develops the audit plan with approval from CEP management. IRS shares the administrative portions of its audit plan with the taxpayer to facilitate the audit process.

After identifying the audit issues, CEP teams use information document requests (IDR) to request documents from taxpayers that relate to their tax liability. Generally, the team submits several IDRs during the audit cycle.

If IRS has problems getting documents, it may issue a legal summons to compel taxpayers to provide them. IRS may issue a summons if taxpayers do not provide all requested documentation in a reasonable period without a valid excuse. When a CEP team cannot determine what information is available, IRS may issue a summons requiring the taxpayer to provide information on what records exist and their location. The Department of Justice works with IRS to enforce the summons in court.

For each issue, if the evidence collected by the audit team does not support the income or deduction shown on the return, the team is to recommend adjustments to the return and compute a corrected tax liability. IRS presents this information to the taxpayer through a "Notice of Proposed Deficiency." After receiving the notice, the taxpayer may (1) agree with the recommendations, (2) provide additional information, or (3) state why the proposed deficiency should be reduced or eliminated. If the taxpayer agrees, the recommended amount becomes a tax assessment.

## Taxpayers Can Protest Audit Adjustments Through IRS' Appeals Function or the Courts

At the close of the audit, if the taxpayer does not agree with IRS' recommended tax adjustments, the taxpayer can (1) file a protest on some or all of the proposed adjustments with IRS' Office of Appeals, (2) take the dispute to Tax Court without paying the recommended tax increase, and/or (3) pay the tax increase and claim a refund in the U.S. Court of Federal Claims or a federal district court. After these options have been exercised, any additional taxes are assessed against the taxpayer. CEP corporations almost always pay the amount assessed.

Of these options, IRS has estimated that CEP taxpayers protest 80 to 90 percent of all recommended taxes to IRS Appeals. All types of taxpayers appeal billions of dollars in tax adjustments from IRS audits. As of September 30, 1992, we reported that Appeals had about 12,000 disputed

issues with $99 billion in proposed tax adjustments waiting to be resolved.[2] IRS' databases did not identify the amounts that CEP corporations appealed.

## Protested CEP Cases Often Go to Appeals' Large Case Program

Appeals has a special Large Case Program for disputes involving recommended tax adjustments of $10 million or more. As of August 1992, the large case inventory had about 2,540 cases. In fiscal year 1992, Appeals took about 2 years to close a large case. The number of protested issues in 1 large case has exceeded 200.

To take an issue to Appeals, the taxpayer must provide a written protest outlining the reasons for disagreement. Before the case is submitted to Appeals, the CEP team is required to write a rebuttal to the taxpayer's protest.

Because of the size and complexity of its large cases, Appeals uses a team approach. Each team has a team chief—a senior GS-15 appeals officer—and two or more appeals officers selected according to the team's needs. Team members do not have to work in the same office as the team chief. IRS industry specialists may also assist the team.

After receiving a large case, the team chief arranges a conference with the CEP taxpayer. The team chief may hold a preconference meeting with CEP team members to hear their positions on the facts and issues. In all interactions, Appeals' staff are to remain objective, find a fair and reasonable basis for resolving disputes, and treat consistently all taxpayers with similar circumstances.

During an appeal, the Appeals' team reviews the CEP team's report and workpapers as well as the taxpayer's protest and CEP team's rebuttal. A taxpayer may present new information to support its position on a protested issue. The team chief is supposed to send that information to the CEP team for evaluation before settling the dispute.

To settle a tax dispute, an appeals officer has authority to consider the hazards of litigation (i.e., the chance of losing in court). To do so, an appeals officer is to review the facts of each case, relevant laws and regulations, and pertinent court cases to judge the probable result if the case were to be litigated. The officer is to evaluate the relative strengths of the taxpayer's and CEP team's positions, using the documentation

[2]Tax Administration: Recurring Tax Issues Tracked by IRS' Office of Appeals (GAO/GGD-93-101, May 4, 1993).

submitted by each side and the results of informal conferences with the taxpayer. The appeals officer is then to negotiate mutual concessions in an attempt to arrive at a settlement that approximates the probable dollar results if the case were to be litigated. To facilitate settlement of large cases, IRS allows team chiefs to approve any final settlement without higher level approval.

At the end of a case, the team chief writes a summary to document how the case was handled. This summary usually discusses issues raised, pertinent facts, applicable regulations and rulings, and relative merits of each side. If agreement with the taxpayer was reached, it also includes Appeals' recommendations and reasons for settlement. Appeals gives a copy of the summary to the taxpayer and the CEP team. If agreement is not reached on the proposed deficiency, Appeals issues a notice of deficiency, and the taxpayer has 90 days to file a petition with the Tax Court.

## Taxpayers May Take Disputes to Tax Court

Taxpayers have the right to not pay the additional recommended taxes and instead take protested issues to the Tax Court, either directly after the audit is closed or if the case is not completely settled in Appeals. Cases pending in Tax Court are called docketed cases. In fiscal year 1992, 46,600 cases were docketed involving all types of taxpayers (e.g., individuals and corporations). The Tax Court has 19 judges who hold court sessions at various locations in the United States. In addition, the chief judge can appoint special trial judges and recall retired judges for a maximum of 90 days each per year.

After a case is docketed, IRS District Counsel should transfer the case to Appeals for possible settlement unless Appeals issued the notice of deficiency. Even then, District Counsel still can return the case but may chose not to do so if settlement seems unlikely. Regardless, Appeals has limited jurisdiction to settle a docketed case independent of District Counsel.

If a docketed case involves a deficiency of more than $10,000, Appeals should return the case to District Counsel when (1) settlement of all or part of the case is not progressing or (2) the case appears on a trial calendar. A case with a lower deficiency should be referred to Appeals for 6 months or until 1 month before the call of the trial calendar. At that point, the case returns to District Counsel unless it and Appeals agree to extend the time for Appeals' consideration. While a case is with Appeals or District Counsel, that office has sole settlement authority. If District

Counsel requests the case file to prepare for trial, District Counsel may also agree that Appeals should continue working on a settlement during this preparation.

After a trial, Tax Court decisions may be appealed to 1 of 11 regional circuit courts or the Circuit for the District of Columbia. Decisions of the circuit courts may be reviewed by the Supreme Court on a writ of certiorari.

## Taxpayers May Pay Taxes and Claim Refunds Through the Courts

A CEP taxpayer may pay all of the recommended taxes and file a claim for refund unless the taxpayer entered into a closing agreement with IRS. The taxpayer must file the claim within 2 years from the date the taxes were paid. IRS' audits of claims generally follow the same pattern as audits of income tax returns. Revenue agents should evaluate claims to determine whether the taxpayer is entitled to a refund. If agents decide that the taxpayer is entitled to a refund, IRS will return the overpayment. If agents decide that the refund claim is unfounded or excessive, the taxpayer can refer the claim to Appeals or sue for the refund in a federal district court or the U.S. Court of Federal Claims.

A taxpayer who loses in district court may appeal the decision to the appropriate circuit court. Taxpayers may appeal a court of claims decision to the Court of Appeals for the Federal Circuit.

## Previous GAO Work

This report presents the results of the third phase of our work on CEP. The first phase was completed in April 1991, when we testified before the Subcommittee on our initial observations about CEP management problems that had persisted for many years.[3] These persistent problems, as identified from various IRS testimony and internal studies done from 1977 to 1990, included

- lack of reliable data on the amount of CEP-recommended taxes that are actually assessed and ultimately collected;
- insufficient training for revenue agents on CEP teams;
- delays in starting CEP audits, which pressures CEP teams to quickly audit multiple tax returns filed years earlier—usually under different tax laws;
- insufficient support audits from other IRS districts in which a CEP corporation has a major operation;

[3] IRS' Efforts to Ensure Corporate Tax Compliance (GAO/T-GGD-91-21, Apr. 17, 1991).

- poor audit planning, which hampers the ability to audit the most significant issues and adequately support any related recommended taxes;
- poor use of specialists who can help teams identify and support significant audit findings on tax issues; and
- poor coordination among IRS functions in doing the CEP audits.

The second phase was completed in April 1992, when we issued a briefing report that provided (1) trends in CEP audit results for fiscal years 1987 through 1991, (2) CEP audit coverage estimates, and (3) a profile of CEP taxpayers.[4] We found that CEP involves very large corporations and generates billions in potential tax revenues. Some of our findings were:

- Total CEP-recommended taxes grew from $7 billion in fiscal year 1987 to $18 billion in fiscal year 1991, a 157-percent increase. The 1991 figure included one case worth $6.5 billion; excluding that case, recommended taxes grew 71 percent over the 5-year period. In fiscal year 1987, IRS recommended $4,372 in additional tax per direct examination hour and in fiscal year 1990, $4,268 per hour—much higher than any other IRS audit program. In fiscal year 1991, the measure increased to $6,875 per hour because of the effect of the $6.5 billion case. Excluding that case, however, CEP recommendations averaged $4,460 per hour in fiscal year 1991—an amount that closely parallels the recommended tax per hour for the previous 4 fiscal years.
- Contrary to IRS testimony, IRS does not audit every CEP taxpayer every year. Using IRS' method of calculating audit coverage for other groups of taxpayers, we found that CEP audit coverage ranged from 66 percent in 1987 to 77 percent in 1991. This coverage included tax returns that were audited solely to resolve a single issue that was carried back or forward from another tax year. IRS officials said they do not believe that an audit coverage measure is applicable to CEP because every CEP return is reviewed for audit potential before being excluded from that year's audit inventory.
- On 1988 corporate income tax returns, CEP taxpayers' reported assets averaged $6.5 billion. They also reported an average of about $1.5 billion in total income, $179 million in taxable income, and an average income tax of $61 million based on taxable income. After claiming tax credits and other tax adjustments, their reported net tax liability averaged $42 million, or 23 percent of average taxable income.

[4]Tax Administration: IRS Efforts to Improve Corporate Compliance (GAO/GGD-92-81BR, Apr. 17, 1992).

## IRS Approved CEP Changes in 1990

IRS has been concerned about CEP's effectiveness since the 1970s, when it began evaluating CEP. On the basis of recent studies, IRS announced 10 changes to CEP in July 1990 that were intended to

- relieve taxpayer burden through tax simplification and improved systems and procedures,
- resolve most factual issues at the audit level,
- provide proper and timely training and resources to all staff,
- improve the effectiveness and efficiency of audits, and
- substantially improve the currency of audits.

The 10 changes are briefly described next.

### National Policy Board

IRS established a national policy board composed of executives from several of its functions and offices: Examination, International, Appeals, and Counsel. Its charter is to (1) establish policy for CEP, (2) ensure that CEP is properly focused and managed, and (3) promote coordination among the functions represented.

### National CEP Director and Regional CEP Managers

IRS filled the position of Executive Director for CEP to provide program development, oversight, and evaluation. In addition, CEP managers were selected in each IRS region to oversee and direct CEP and to coordinate within the region, among regions, and with the executive director. Appeals and Counsel created and filled similar regional positions with the same expectations.

### Top Field Management Involvement in Planning and Support Audits

IRS decided that district and regional management needed to be more involved in CEP to improve the planning process and control of support audits.

### More Managerial Oversight to Increase Taxpayer Cooperation

IRS decided that more top management involvement was needed to develop a cooperative relationship with CEP taxpayers.

### More Industry and Issue Specialization

IRS concluded that CEP teams needed assistance in addressing the increasing complexity of corporate tax law and the growth of international corporate activity. In response, IRS decided to establish more industry and issue specialists.

## More CEP Training

Due to the complex technical and legal issues in CEP cases, IRS recognized the need to set up a cross-functional training program for Examination, Appeals, and Chief Counsel personnel involved in CEP cases. The training was to ensure a common understanding in addressing IRS positions and CEP issues.

## More Effective Communication Systems

IRS decided it needed to improve communications on industry practices and other CEP issues to ensure consistent application of the law. IRS envisioned creating a tracking system to monitor major issues arising in CEP and an electronic bulletin board system to communicate technical information.

## Expedited Legal and Technical Assistance

Due to the complexity of CEP issues and the need for prompt legal and technical assistance, IRS intended for Counsel to provide that assistance from the start of CEP audits. Counsel is to serve as a legal advisor to the CEP team on matters of law and tax policy as well as on the development of issues during audits. Counsel's purpose is not to prepare for litigation.

## Quality Assurance and Measurement Systems

IRS decided that the overall quality of CEP would be improved by developing standard measures and goals for Examination, International, Appeals, and Counsel. In addition, IRS established a CEP Quality Peer Review and a CEP Oversight Committee.

## Early Settlement Offers and Improved Functional Coordination

IRS decided that it needed to (1) facilitate earlier resolution of audit issues with CEP taxpayers and (2) improve coordination among Appeals, Counsel, and Examination. The changes included giving case managers authority to settle recurring issues previously resolved by Appeals.

To offer them more access to Appeals, IRS decided that a CEP team and Counsel should meet with Appeals before a case is settled to discuss the team's positions on audit issues. In addition, Appeals should meet with a CEP team after the settlement to discuss the resolution of the issues. This is intended to help a team to audit later returns.

# Objectives, Scope, and Methodology

Our objectives were to determine (1) the portion of taxes recommended in CEP audits that are collected after any appeals or litigation; (2) what factors, if any, reduce the percentage of recommended taxes ultimately

collected; and (3) the status and preliminary results of IRS' ongoing changes to improve CEP.

## Computer Data Match Used to Calculate Collection Rate

To determine the portion of audit teams' recommended additional taxes ultimately paid by CEP corporations (i.e., the CEP collection rate), we obtained two IRS databases to match corporate income tax return information. The first database, IRS' Audit Information Management System (AIMS), contains information on Examination staff resources and accomplishments, including taxes recommended from audits closed during fiscal years 1983 through 1991. The second database, IRS' Business Master File (BMF), contains tax return account information on taxes collected as well as taxable income, tax liability, penalties, interest, refunds, and audit actions for corporate tax returns. To extract the data, we used a list of taxpayer identification numbers (TIN) for the 1,684 corporations in CEP as of May 1991.

Of 16,641 records we extracted from AIMS, we matched 8,874 records with recommended tax increases to related BMF accounts on the taxes collected through fiscal year 1992 after all appeals and litigation. We could not match the other 7,767 AIMS records to BMF accounts because (1) the account was no longer available on the BMF or (2) the account existed, but the collection information was not yet available on the BMF because the case was still in Appeals or being litigated.

We also did analyses of our matched data set to determine the collection rate by industry and by IRS district and for foreign controlled corporations. To determine the collection rate of CEP cases that IRS' Office of Chief Counsel litigated, we obtained and analyzed a database on the large case disputes closed in litigation for fiscal years 1988 through 1992. In addition, we analyzed the BMF to determine the portion of CEP corporations' income tax payments that resulted from audits as well as the unpaid balance and the penalties for CEP tax returns.

## Surveys and Case Studies

We used two methods to identify factors that affect the percentage of CEP-recommended taxes that are collected and the status of IRS' 1990 changes to CEP. First, we surveyed IRS team coordinators, case managers, and appeals officers and taxpayer representatives involved in a universe of 108 closed CEP cases. Second, we did in-depth case studies of 12 of the 108 cases.

Our survey covered 308 IRS and corporate employees involved in 108 CEP audits. These 108 were IRS' universe of cases that each had $30 million or more in additional taxes recommended and were closed by agreement at the audit or Appeals levels in fiscal years 1989 through 1991. We selected the $30 million cut-off point for several reasons: (1) the 108 cases accounted for nearly $8.5 billion dollars in recommended taxes and (2) the universe size was manageable given the number and complexity of the surveys we used.

IRS' database originally showed 128 cases meeting our selection criteria. We subsequently excluded 20 of these cases from our analysis when new information showed that the cases did not meet our selection criteria because, for example, they were still open in Appeals, involved additional tax recommendations less than $30 million, or involved an audit of a return type other than corporate income tax. Similarly, 75 individuals were eliminated from the relevant survey universes because the designated respondent was no longer with IRS or the taxpayer. Results in chapters 3 and 4 are based on the 308 surveys received from 85 team coordinators, 72 case managers, 78 appeals officers, and 73 corporations.[5] Table 1.1 summarizes the universe size and response rates for each group.

**Table 1.1: Universe and Response Rate Information by Survey Group**

| | Team coordinator | Case manager | Appeals officer | Taxpayer |
|---|---|---|---|---|
| Cases meeting selection criteria | 108 | 108 | 108 | 108 |
| Adjusted universe | 89 | 74 | 83 | 96 |
| Surveys received | 85 | 72 | 78 | 73 |
| Response rate | 96% | 97% | 94% | 76% |

In the surveys, we asked about factors such as the sufficiency and quality of IRS staff, training, issue identification and development, taxpayer cooperation, and case delays. The team coordinator, appeals, and taxpayer surveys also had questions on the case's three largest dollar issues. All four surveys asked for the respondents' opinions of recent changes to CEP and Appeals' Large Case Program. We also asked respondents whether, in

[5]Survey results are reported as percentages of respondents answering the relevant question. At times, respondents neglected to answer a certain question. As a result, the percentages reported in the chapters may be based, for example, on 84 rather than 85 team coordinator responses. Our text does not report these small deviations. However, we do report the number of respondents answering a question when the question was directed at a subgroup of respondents (e.g., those with cases that went to appeals). Appendixes II through V show the number of responses for each question on each survey.

their opinion, the case outcome would have been different had some recent changes to CEP been in effect at the time.

To better understand IRS' processes and the 1990 changes, we did in-depth case studies of 12 of the 108 cases. In three cases, taxpayers fully agreed with CEP audit recommendations; the remaining nine were closed by Appeals. The 12 cases accounted for $1.5 billion (18 percent) of the $8.5 billion of additional taxes recommended in our universe of 108 cases. We did three case studies in each of four IRS districts—Chicago, Houston, Los Angeles, and Manhattan. These four districts accounted for about 30 percent of CEP's staff years and over 40 percent of additional taxes recommended in fiscal year 1991. The 12 cases also reflected a geographic cross section of the nation and covered a variety of industries, including financial services, petroleum, food, construction, and utilities.

In our 12 cases, CEP teams raised between 50 and 300 issues. To narrow our scope, we focused on the three issues having the largest amounts of additional tax recommended. Much of our analysis focused on these 36 issues over the 12 cases.

For each case, we reviewed up to 13 case documents, including the audit plan, information document requests, specialist reports, and the revenue agent report that summarizes the audit findings. When applicable, we reviewed up to an additional 11 documents, such as IRS standard position papers, taxpayer protests, CEP rebuttals, and Appeals case memoranda and summaries. Appendix I includes a list of all 24 documents.

We interviewed IRS employees and taxpayer representatives who were involved with each case and IRS district, regional, and National Office staff responsible for CEP and Appeals management. These interviews involved 85 people, including 6 branch chiefs, 8 case managers, 13 team coordinators, 4 technical specialists, 6 industry specialists, 11 appeals officers, 11 taxpayer representatives, and 26 others. Our interviews focused on the effect of (1) CEP policies and practices about the audits, (2) Appeals policies and practices about the resolution of disputed issues, (3) the 1990 changes to CEP on improving the collection rate, (4) IRS' efforts such as task force studies and process reviews, and (5) other case-specific details that were not addressed by past or present policies.

In reviewing IRS' changes to CEP since 1990, we reviewed the Large Case Policy Board Report, eight CEP task force reports, the CEP Quality Peer

Review for fiscal year 1992, and the Appeals Process Review for fiscal year 1992.

IRS National Office and district officials and representatives of CEP corporations reviewed our surveys and case study methodology before we began. They acknowledged the validity of our approach and reviewed our surveys for comprehensiveness and technical accuracy. District office officials told us our selected cases were representative of typical audits and appeals of CEP corporations in those districts.

We obtained written comments from IRS on a draft of our report. Appendix VI contains these comments and our evaluation of them. We also sent our draft report to three former IRS Commissioners, the Tax Executives Institute (TEI), and other knowledgeable parties for review and made changes in the report on the basis of their comments where appropriate.

TEI represents tax executives of corporations, including most of those in CEP. TEI submitted its comments in a November 12, 1993, letter. We are pleased that TEI participated in our review. In summary, TEI's president said that TEI agreed with our recommendations on enhancing training of CEP revenue agents and on changing the measures of success but opposed others. TEI also expressed concerns about the tone and beliefs underlying some of our conclusions. We have made changes to better balance the tone and address concerns about recommendations in chapter 4 on the Appeals process. However, we disagree with TEI statements about our preconceptions and other recommendations. We have summarized TEI's comments and our evaluation of them at the end of chapters 2, 3, and 4.

Overall, we conducted our work at IRS' National Office, 5 regional offices, and 7 of 59 district offices active in CEP. Appendix I provides a detailed description of our methodology. We did our audit work from February 1992 to September 1993 in accordance with generally accepted government auditing standards.

# IRS Did Not Know the Collection or Compliance Rate Among CEP Corporations

CEP audits consumed over 20 percent (about 1,700 audit staff years) of Examination's audit resources in fiscal year 1992. Although this investment produced additional billions of dollars in recommended taxes, IRS did not know what portion of the taxes it actually collected. We found that IRS assessed and collected 22 percent of the CEP-recommended taxes.[1]

To compute the 22-percent rate, we had to overcome problems with IRS' databases. The databases did not show the taxes actually collected from each CEP audit, excluding the effects of any nonaudit related factors, such as corporate claims for net operating losses (NOL) and refunds from other years. Knowing the taxes collected from audits can help measure the effectiveness of IRS' enforcement programs and the large corporation tax gap.

Even so, our 22 percent collection rate is not a measure of CEP tax compliance or the CEP tax gap. Although IRS' mission is to collect the proper amount of taxes, no one knows what that amount is for CEP corporations. For various reasons, IRS cannot compute the total tax liability for CEP corporations.

## IRS Collected Few of the Taxes Recommended From CEP Audits

IRS did not have databases that showed the actual amount of CEP-recommended taxes that it collected.[2] To compute the actual collection rate we had to merge IRS' AIMS and BMF data. We found that IRS collected $7.1 billion, or 22.1 percent, of the $32.4 billion in taxes recommended during fiscal years 1983 through 1991 for large corporations that were still in CEP as of May 1991 and whose records were closed on both databases through fiscal year 1992.

No one knows what the current collection rate is, but the 22.1-percent rate is the only actual computation available. Until IRS develops a better, more current collection rate, IRS can use this 22.1-percent rate whenever it wants to estimate the amount of additional tax revenues that CEP actually produces. For example, in fiscal year 1992 CEP audit teams recommended about $16 billion in taxes. Given the 22.1-percent rate, these CEP audits could be expected to eventually generate about $3.5 billion in tax collections.

[1]CEP corporations in our BMF database had tax assessments of about $380 billion of which only $348 million (.09 percent) was unpaid. As a result, we considered taxes assessed for CEP corporations to be collected.

[2]IRS has been attempting to collect better data to estimate a collection rate, particularly for CEP corporations. IRS officials briefed us on their new data through its Enforcement Revenue Information System (ERIS)—which we have not evaluated—in December 1993, after we completed our audit.

## Collection Rates Varied Widely Among Industries and Districts

We found that the CEP collection rate varied significantly depending on industry and district. Various factors could explain this, including differences in the cooperation of taxpayers, the complexity of relevant tax laws, the prevalence of unresolved legal issues in certain industries or international issues, the quality of CEP audits, and the practices within and between IRS districts or Appeals offices. Chapters 3 and 4 will discuss these and other factors in more detail.

### Collection Rate by Industry

Table 2.1 shows collection rates in descending order for the 10 industries with the largest amounts of CEP-recommended taxes.

**Table 2.1: 10 Industries With the Largest Recommended Taxes in Descending Collection Rate Order, Fiscal Years 1983 to 1991**

Dollars in millions

| | Taxes recommended | Taxes collected | Collection rate |
|---|---|---|---|
| 1. Wholesale trade of motor vehicle equipment | $678 | $414 | 61.06% |
| 2. Drug manufacturing | 873 | 492 | 56.36 |
| 3. Manufacturing— motor vehicles and equipment | 1,111 | 443 | 39.87 |
| 4. Mutual life insurance | 1,608 | 523 | 32.52 |
| 5. Manufacturing—petroleum refining | 2,988 | 570 | 19.08 |
| 6. Office, computing, and accounting machines | 1,159 | 198 | 17.08 |
| 7. Electric services | 1,413 | 211 | 14.93 |
| 8. Manufacturing—certain electrical equipment | 948 | 75 | 7.91 |
| 9. Bank holding companies | 2,843 | 115 | 4.05 |
| 10. Manufacturing—aircraft, missiles, and parts | 1,298 | 48 | 3.70 |
| **Results for top 10** | **$14,919** | **$3,089** | **20.71%** |

Source: GAO analysis using IRS data.

For all industries in our database the collection rate ranged from a positive 114.7 percent for holding and investment companies to a negative 162 percent for taxpayers in the cement and hydraulic industries.[3]

Collection rates that exceeded 100 percent indicated that appeals officers collected more taxes than recommended by CEP teams. This can occur

[3]This range excludes collection rates exceeding plus or minus 200 percent.

when the tax liability increases while the case is under Appeals' jurisdiction. For example, the liability may increase because of a carryover adjustment from another audit period that affects the tax years being appealed or because of an amended return filed by the taxpayer.

Negative collection rates occur when the appeals officer not only concedes all taxes recommended by a CEP team but also gives the taxpayer a tax refund because the taxpayer filed a claim for a refund or the reported tax liability was reduced. For example, the appeals officer can decrease tax liability because of a computation error in the dollars recommended or a carryover adjustment from another tax period to the tax year in Appeals.

## Collection Rate by District

The collection rate also varied among IRS districts. Table 2.2 shows collection rates in descending order for the 10 IRS districts with the largest amount of CEP recommended taxes.

**Table 2.2: 10 Districts With the Largest Amounts of CEP-Recommended Taxes in Descending Order of Collection Rate, Fiscal Years 1983 to 1991**

Dollars in millions

| District | Taxes recommended | Taxes collected | Collection rate |
|---|---|---|---|
| 1. Newark | $1,161 | $509 | 43.84% |
| 2. Detroit | 1,542 | 595 | 38.59 |
| 3. Boston | 1,087 | 287 | 26.40 |
| 4. Chicago | 1,418 | 348 | 24.54 |
| 5. Manhattan | 5,518 | 1,004 | 18.19 |
| 6. Dallas | 1,121 | 198 | 17.66 |
| 7. Hartford | 1,184 | 192 | 16.22 |
| 8. Los Angeles | 2,162 | 294 | 13.60 |
| 9. Houston | 1,693 | 223 | 13.17 |
| 10. St. Louis | 1,173 | 111 | 9.46 |
| **Result for top 10** | **$18,059** | **$3,761** | **20.83%** |

Source: GAO analysis using IRS data.

The collection rate for all IRS districts with CEP audits ranged from a high of 75.04 percent in Albuquerque, NM, to a low of a negative 52.23 percent in Salt Lake City, UT.

## Foreign Versus U.S.-Owned Corporations

Our computer match showed that the collection rate for the 144 foreign-owned CEP corporations was 33 percent compared to 21 percent

for 1,124 U.S.-owned corporations. IRS officials said a possible reason for this disparity is that foreign-owned corporations often feel a greater need to quickly resolve tax disputes, diverting negative public attention from what could be perceived as tax evasion. They may fear this attention could result in lower sales or trigger new restrictive legislation.

## Promising Trends in Large Corporations Agreeing to Pay CEP Recommended Taxes

IRS is developing new CEP measures and a new management information system. CEP officials believe this new system will provide better information on CEP results. To the extent it works, the system will provide the recommended adjustment for each audit issue and the amount of protected revenue. A CEP team protects tax revenues already in the Treasury when it determines that a taxpayer's request for a tax refund has no merit.

This new system has produced some data on these new measures. For example, IRS data showed an increase in the percent of CEP-recommended taxes that large corporations agreed to pay (and not appeal) at the end of the audit. According to IRS' data, agreed payments were 5.3 percent in fiscal year 1990, 11.1 percent in 1991, and 15 percent in 1992. During these 3 years, the percent of CEP cases in which corporations agreed with all audit findings were 3 percent, 4.7 percent, and 6 percent, respectively.[4]

We believe these trends are promising. If they continue, IRS and taxpayers will spend fewer resources settling tax disputes. In addition, the collection rate should increase. However, we did not analyze the corporate cases leading to these trends. We do not know whether these corporations agreed with a greater portion because the CEP teams better supported their recommended taxes or simply to avoid the more contentious, complex tax issues.

Instead of evaluating these new measures and system, our review focused on computing the collection rate of CEP-recommended taxes. We envision the collection rate as an additional CEP measure worth tracking in this new system. If the system eventually tracks the rate, we view that as a positive enhancement. Even so, we believe that more changes in CEP are needed, which chapters 3 and 4 discuss.

[4]Because taxpayers may file a claim for refund of taxes after taxes were paid, agreement rates may need to be lowered.

## IRS Databases Should Be Changed to Better Capture CEP Collections

We had to make several adjustments to overcome problems in the IRS databases that we used to compute the collection rate. The databases need improvements to track actual CEP results and eliminate the need to estimate. Without improvements, the rate will be understated or overstated, depending on various factors. Although these factors may offset each other, IRS and Congress have no way of knowing how much tax is actually collected from CEP unless the problems are corrected.[5]

The 22 percent collection rate understates the taxes generated from CEP audits when Appeals subtracts NOL from other tax years.[6] Although the corporation may owe additional taxes as a result of the CEP audit, BMF records only the net amount instead of the amount generated from the audits.

For example, a CEP audit of taxpayer A's 1987 tax return may have resulted in $100 million in recommended taxes that the taxpayer appeals. After appeals, the taxpayer agrees to a liability of $50 million. However, the taxpayer files a claim with the appeals officer for a tax refund of $40 million based on an NOL from another tax year. BMF will record only a net $10 million payment for audit related collections. This understates the contributions of CEP because the collection rate will appear to be 10 percent rather than the actual 50 percent. About 3 percent of the appeals officers we surveyed said this understatement occurred in their cases.

On the other hand, the CEP collection rate was overstated when subsequent events led to refunds of recommended taxes that the corporation had already paid. Again, BMF did not record this effect to allow a truer measure of the CEP collection rate.

For example, a taxpayer agrees in appeals to pay $40 million of $100 million in recommended taxes—a collection rate of 40 percent. In doing so, the taxpayer reserves the right to file a claim on certain issues involving $20 million because of a pending court decision. If the court later rules against IRS, the taxpayer may file the claim and receive a refund of $20 million. IRS' databases would record the $20 million refund but not

[5]Since 1990, IRS has attempted to create a system called ERIS to track the amount of recommended taxes from all enforcement programs that IRS eventually collects. As of December 1993, IRS officials said they hoped to have reliable collection data in 3 to 5 years. We believe our experience may offer ways to expedite the creation of ERIS.

[6]An NOL occurs when allowable deductions exceed gross income for a tax year. Taxpayers can save and deduct NOLs to reduce taxable income for up to 15 years or claim a refund of taxes paid in the preceding 3 years.

associate it with an audit. Instead, IRS' databases would record the $40 million as an audit result, leading to a 40 percent collection rate rather than the adjusted rate of 20 percent (the $20 million divided by the $100 million).

## The Collection Rate Does Not Measure Corporate Compliance or Tax Gap

It is important to recognize what the collection rate does and does not represent. In general, the rate measures the portion of recommended tax assessments that ultimately gets collected. On the other hand, the rate does not measure corporate compliance or the tax gap. Specifically, the new CEP collection rate does not mean that CEP corporations paid just 22 percent of their tax liability for reasons explained in the next section.

None of IRS' databases contained data for precisely measuring CEP corporations' tax compliance. For example, in a separate analysis of BMF, we found that audited CEP corporations paid $379 billion in taxes of which $21.5 billion, or 5.7 percent, resulted from CEP audits.[7] For various reasons, this does not mean that the voluntary compliance of these CEP corporations was 94.3 percent (100 percent less 5.7 percent). The 94.3 percent only represents the voluntary portion of these corporations' tax payments—not of their total tax liabilities. It excludes any additional taxes that may be owed due to noncompliance that IRS had not identified.

Currently, IRS' data on CEP audit results only capture the amount of additional taxes recommended from auditing certain issues on selected tax returns. IRS does not know about any additional tax liabilities from (1) CEP tax returns that are not audited or (2) issues missed on returns that are audited. Our April 1992 report stated that IRS does not audit every CEP return. Using IRS' method to calculate audit coverage, we found that IRS audited from 66 percent of CEP returns in fiscal years 1987 to 77 percent in fiscal year 1991.

Regarding noncompliance not audited or missed during an audit, we reported in April 1992 that IRS applied an average of one direct examination staff year to each CEP return examined for fiscal years 1987 through 1991.[8] This modest level of effort to audit complex corporations with billions of dollars in assets and income will undoubtedly miss some noncompliance. In April 1991, the IRS Commissioner testified that he

[7]The number of years covered in this analysis varied for different taxpayers. See appendix I for a discussion of this analysis.

[8]Tax Administration: IRS Efforts to Improve Corporate Compliance (GAO/GGD-92-81BR, Apr. 17, 1992).

believed IRS was not finding all the issues on CEP tax returns. Likewise, taxpayers and other IRS officials have said that IRS is missing audit issues on these returns.

Among audited returns, CEP teams may identify noncompliance and recommend additional taxes. IRS did not have the data to allow us to determine the extent to which any recommended taxes from CEP audits truly represented additional noncompliance. On one hand, Appeals may concede some or all of these taxes because the CEP team lacked enough information to fully support additional taxes. Or, although the team supported the additional tax liabilities, Appeals may concede them to settle disputes. On the other hand, Appeals may concede some CEP-recommended taxes that teams raised in error and, as such, do not represent additional tax liabilities.

For these reasons, not only is the voluntary compliance rate of CEP corporations unknown but the tax gap for these corporations cannot be precisely measured. The tax gap is the difference between the amount of income tax owed for a tax year and the amount paid voluntarily. For CEP corporations, IRS assumed that the amount of CEP-recommended taxes equals the tax gap.

IRS estimated a $23.7 billion tax gap for 1992 among all large corporations, including those in CEP. Just as with the voluntary compliance being understated, IRS' estimate of the tax gap would be understated to the extent that IRS audits did not account for additional noncompliance on CEP returns. Conversely, the tax gap would be overstated to the extent that the additional tax recommended did not represent true noncompliance.

Although not known, the voluntary compliance of CEP corporations may be decreasing, which increases the tax gap, according to at least one indicator. In our April 1992 report on corporate compliance, IRS officials said trends in recommended taxes can be an indicator of CEP corporate compliance. If their compliance increases, IRS officials said CEP-recommended taxes should decrease to an extent. Although factors other than compliance can affect recommended tax amounts, CEP-recommended taxes increased 47 percent—from $10.9 billion to $16 billion—over fiscal years 1990 to 1992. No one knew all the reasons for this increase, including the effect of possible lower voluntary compliance.

In the context of the tax gap, IRS officials believed that auditing the unaudited returns would have little effect. They said IRS staff reviews

unaudited returns for noncompliance before excluding them. Nonetheless, IRS officials said they have not tested their judgment about the amount of noncompliance on these unaudited returns.

In the final analysis, IRS' estimates of voluntary compliance and the tax gap among CEP corporations are rough guesses, not precise measures. We believe that IRS could increase the precision of its voluntary compliance and tax gap estimates if it (1) tested its judgment to not audit some CEP returns every year and (2) developed a method for quantifying the noncompliance not detected during CEP audits.

As one way to begin to quantify the amount of undetected noncompliance, IRS could continue auditing CEP taxpayers after the normal close of the audit. The CEP team could probe further into certain (1) corporate subsidiaries that received a cursory review, or (2) tax return lines that were not audited in depth. Doing such probes, however, would increase the costs and burdens on IRS and corporations.

## Complexity Affects Measurements of Tax Compliance and the Collection Rate

Tax law complexity makes measurements of tax compliance and the collection rate very difficult. Complex laws provide opportunities for different interpretations that may lead to different calculations of corporate liability. As a result, it is reasonable to assume that CEP teams are likely to recommend additional taxes and that CEP corporations are likely to challenge them. In addition, complexity can muddle Appeals' determination of tax liability.

Because disclosure restrictions in section 6103 of the tax code prohibit a discussion of issues that we reviewed in our cases, we can only highlight some examples of complexity in laws or regulations that complicate decisions for CEP teams and taxpayers. We also discuss how complexity has resulted in some tax disputes continuing for over 30 years.

For example, before the Revenue Reconciliation Act of 1993, taxpayers could deduct the cost of purchased intangible assets, such as customer or subscription lists, that had a readily determinable useful life. Goodwill was not amortizable because it does not have a determinable useful life. Therefore, to amortize an intangible asset, the taxpayer was required to distinguish the intangible from goodwill.

Taxpayers have battled for more than 60 years over amortization of intangibles. In the last 20 years, taxpayers have been more successful in

identifying, valuing, and establishing useful lives for a variety of intangibles. Recent court cases have been decided on the taxpayer's ability to prove that the asset exists and is separate from goodwill. In 1993, the Supreme Court held that a taxpayer may depreciate the asset if it can be valued and has a limited useful life that can be determined with reasonable accuracy.

In our August 1991 report, we recommended that Congress consider revising current tax law to allow amortization of purchased intangibles, including goodwill, over specific statutory recovery periods.[9] In 1993, legislation was passed to allow 15-year amortization for many newly purchased intangible assets, including goodwill and going concern value.[10]

Another complex area of law includes provisions existing before the Tax Reform Act of 1986. Because many of our cases involved tax years before the 1986 act, different corporate tax rates applied to "capital" and "ordinary" income.[11] The tax code defined capital asset very broadly as "property held by the taxpayer (whether or not connected with his trade or business)" and excluded five categories of property from capital asset status.

While court decisions have set out guidelines for determining whether an asset is capital or ordinary, those decisions depend on the kind of asset and whether it fits within an enumerated exception. Because the character of the asset may depend on whether the taxpayer purchased and held it with a business or investment motivation, classifying assets is often difficult.

These are just a few examples of the legal ambiguity in cases we reviewed. Complexity also arose from extremely detailed statutes and regulations.

[9]Tax Administration: Issues and Policy Proposals Regarding Tax Treatment of Intangible Assets (GAO/GGD-91-88, Aug. 9, 1991).

[10]The new rules generally apply to property acquired after August 10, 1993; however, a taxpayer may apply the rules to all property acquired after July 25, 1991. On February 9, 1994, IRS announced that it will offer to settle pending disputes over the tax treatment of intangible assets acquired on or before July 25, 1991. Under guidelines for settling the disputes, taxpayers will generally be able to reduce the basis of acquired intangible assets for which amortization was claimed on their returns. IRS indicated that the Supreme Court decision in Newark Morning Ledger and changes to the tax treatment of intangibles in the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66) led to its settlement decision.

[11]It was more advantageous for a taxpayer who has a gain on the sale of property to argue that the property was a capital asset. If a taxpayer realized a loss, it was more beneficial to argue that the property was not a capital asset.

Specifically, the corporate alternative minimum tax and the uniform capitalization rules have all increased complexity for corporations.

An August 1993 IRS contract study surveyed 365 senior tax officers of CEP corporations on the causes of taxpayer burden.[12] Corporate officials who responded were nearly unanimous in believing that the Tax Reform Act of 1986 added complexity, resulting in higher tax compliance costs and less accurate information being provided to IRS. Although it was beyond the scope of our review to analyze how to simplify the tax code, the corporate tax officials suggested several ideas. These ideas included using the income shown on a corporation's financial statement as the basis for assessing taxes and eliminating the alternative minimum tax.

Taxpayers deserve a tax system with which they can voluntarily comply at minimal burden. Such a system does not exist for CEP corporations. We found CEP tax return issues that have been disputed and remain unresolved after 30 years. As of October 1992, 56 percent (11,459) of 20,564 CEP tax returns in our database were unresolved because of an ongoing activity (audit, litigation, criminal investigation, or claim for a refund). The 11,459 unresolved returns covered various tax years, dating back to 1961, for 1,650 CEP taxpayers. (See table 2.3.)

**Table 2.3: Unresolved CEP Corporate Tax Returns**

| | | Type of activity ongoing[a] (number of returns) | | | |
|---|---|---|---|---|---|
| Tax years | Number of unresolved returns | Audit | Litigation | Criminal investigation | Claims |
| 1961 to 1969 | 196 | 83 | 93 | 1 | 102 |
| 1970 to 1979 | 2,413 | 1,134 | 914 | 5 | 1,374 |
| 1980 to 1989 | 6,734 | 6,169 | 1,149 | 8 | 2,451 |
| 1990 to 1993 | 2,116 | 2,299 | 53 | 2 | 169 |
| **Total** | **11,459** | **9,685** | **2,209** | **16** | **4,096** |

[a]Number of activities exceeds number of returns because more than one activity can occur at the same time. For example, a taxpayer can file a claim for refund while the return is being audited.

Source: GAO analysis from IRS data.

## Conclusions

Although not a perfect measure, our 22 percent collection rate is the only measure of how much IRS actually collects over time from CEP audits. Accordingly, until IRS develops better data, we believe IRS should use this

[12]"Measuring Taxpayer Burden and Attitudes For Large Corporations," by Joel Slemrod, University of Michigan, and Marsha Blumenthal, University of St. Thomas.

rate whenever it needs to estimate how much it collects as a result of CEP audits.

IRS can develop better data to track CEP audit results by improving its databases. Specifically, IRS needs to account for factors causing the rate to be understated or overstated. Afterwards, IRS can update the collection rate.

For various reasons, IRS did not know the extent to which CEP corporations complied in paying their tax liabilities, much less their total tax liability. For example, CEP teams did not (1) audit all returns or (2) audit all issues on audited returns. Improved compliance measurement is possible if IRS tests its assumption on not auditing CEP tax returns that appear to have little revenue potential. For taxpayers who are audited, IRS should test whether more in-depth audits to detect missed issues would be cost effective. Both tests will increase costs and burdens for IRS and corporations. However, due to the potential taxes lost if IRS' assumptions are wrong, we believe limited tests are warranted.

## Recommendations to the Commissioner of Internal Revenue

We recommend that the Commissioner of Internal Revenue

- use a 22.1 percent collection rate when estimating the taxes that will ultimately be collected from CEP audits until more reliable information becomes available;
- correct the factors in IRS' databases that caused the CEP collection rate to be understated or overstated (i.e., NOLs and refund claims after settlement) and use the corrected results to update the collection rate; and
- test the cost-effectiveness and accuracy of measuring CEP corporate compliance and the related tax gap by auditing samples of (1) unaudited CEP returns and (2) audited CEP returns in greater depth.

## Comments and Our Evaluation

### IRS Comments

In commenting on a draft of this report, the IRS Commissioner did not agree to use a 22 percent collection rate. While the Commissioner agreed that the collection rate concept is useful for estimating revenue, she believes that the 22-percent rate is too low and that IRS' new database, ERIS,

provides more accurate data. We disagree on both points. We acknowledge in our report various factors (e.g., NOLs and refund claims) that could make the collection rate higher or lower and recommend that IRS correct its databases to account for these factors. While we agree that ERIS will be an important data source for IRS, ERIS will not produce actual collection rate data for several years. Until ERIS can produce an actual collection rate, our 22-percent rate is the only computation available.

The Commissioner also criticized our draft report for using the collection rate as the sole measurement of CEP effectiveness. We disagree; our draft report emphasized that the collection rate should be used as one of many measures.

The Commissioner did not specifically agree or disagree with our recommendation to correct problems with IRS' databases that caused the CEP collection rate to be understated or overstated. The Commissioner did state that the collection rate is a viable concept for the budget and resource process and that IRS is developing a baseline voluntary compliance measure using a definition and methodology "very similar" to ours. Given this effort, we are surprised that IRS criticizes our collection rate and we hope that IRS' methodology incorporates our suggestions for improving the relevant databases.

The Commissioner also did not agree to test IRS' assumptions about auditing more CEP returns and doing fuller audits. The Commissioner agreed that such studies would be useful in estimating the tax gap but raised doubts about the overall benefits of such studies. Even so, the Commissioner pointed out that IRS is doing a small-scale project to evaluate the merits of expanding the scope of CEP audits. On the other hand, the Commissioner said doing such projects would be too costly and burdensome. We acknowledge IRS' concerns, but we believe that checking these assumptions is critical given CEP's size and importance.

## TEI's Comments

TEI took issue with what it characterized as the alleged implication in the report that tax noncompliance among CEP corporations was likely to be significant. TEI rejected the proposition of a single correct tax liability from which any variance is evidence of noncompliance. Our report cites examples of CEP corporations not complying. However, before citing these examples, we devoted a major section in chapter 2 to discuss why no one knows the level of tax compliance among CEP corporations. We do not see

how this section or the examples can be construed as evidence of significant noncompliance among CEP corporations.

TEI's letter seemingly acknowledged noncompliance by citing our finding that CEP corporations voluntarily paid 94 percent of taxes collected from them; the other 6 percent resulted from IRS' CEP audits. TEI contended that this 94 percent figure shows that CEP corporations were among the most compliant taxpayers. Although this could be true, we do not view this as evidence of 94-percent compliance among CEP corporations for various reasons as discussed in this report.

Further, TEI suggested that CEP corporations may in fact overpay their taxes because they do not appeal all additional taxes that CEP audit teams recommend. We acknowledge that CEP corporations may not appeal all tax recommendations that they reasonably could have appealed. We do not believe, however, that this means CEP corporations overpay their taxes. Our report points out forces, such as CEP audit teams missing noncompliance or inadequately supporting their claims of noncompliance, that could result in CEP corporations underpaying their taxes. In sum, we reiterate our conclusion—no one knows the full extent of CEP corporations' tax liabilities.

TEI also was concerned with what it believed to be our position that CEP teams audit all tax issues on CEP returns. TEI said that most CEP corporations devote considerable time and energy to voluntarily pay their taxes and already receive heavy IRS scrutiny. TEI also stated that this type of audit would create enormous delays and costs for corporations as well as IRS. We agree, which is why we did not recommend this. Instead, we recommended that IRS audit more issues on a limited sample of returns in order to test IRS' assumption that audit teams do not miss issues on CEP tax returns.

# Many Factors Related to the Audit Process Reduced CEP's Collection Rate

CEP teams audit tax returns as part of IRS' mission to collect the proper amount of taxes at the least cost to the federal government and taxpayers. As a result of these audits, CEP teams recommend additional taxes that they believe the corporations owe. Various problems, attributable to both IRS and corporations, have weakened the chances that these recommendations will survive. These problems also have increased IRS' costs and burdened CEP corporations.

Although IRS has studied ways to improve CEP since the 1970s, serious problems remain that reduced the collection rate. Since 1990, IRS has made changes to minimize some of these problems. Our work indicated that although these changes look promising, they have not been fully implemented because of the decentralized way in which IRS organizes its operations. Even if implemented, the changes may not be enough to address problems such as inadequate resources and tools for doing CEP audits. These changes and problems in the context of the low collection rate are discussed below.

## Most CEP Changes Have Not Been Fully Implemented and May Not Be Enough

In 1990, IRS approved and began implementing 10 changes to enhance CEP audits. Given such recent approval, we did not attempt to fully measure the effects of the 10 changes. However, our case studies, survey results, and on-site visits and interviews at selected IRS districts in 1992 and 1993 did allow us to identify the status of the changes and some preliminary results.

From our work, we concluded that these changes offer the potential to improve CEP. For example, the changes may have contributed, to an extent, to the recent trend in corporations agreeing to pay more recommended taxes after audit, as discussed in chapter 2. We found that most of the changes have not been fully implemented, suggesting the need for action. Table 3.1 summarizes the status of these changes as well as actions needed. Chapters 3 and 4 offer recommendations to address most of the needed actions.

**Table 3.1: GAO Evaluation of the Current Status and IRS Actions Needed in Implementing CEP's 1990 Approved Changes**

| 1990 approved changes | Status | IRS actions needed |
|---|---|---|
| 1. Expedited legal and technical assistance | Ongoing | More consistent district counsel involvement |
| 2. Expanded ISP to clarify IRS positions | Complete | Further expansion to improve revenue agents' industry knowledge |
| 3. Training revenue agents on issue development | Ongoing | More training |
| 4. Improved communication between CEP and Appeals | Ongoing | Better incentives for improved communications |
| 5. More involvement by IRS field managers to improve (a) taxpayer cooperation, (b) audit currency, and (c) issue resolution | Ongoing | Managers still need to become more involved for improvements to occur |
| 6. Field manager involvement in audit planning, support audits, and oversight | Ongoing | Managers still need to become more involved in these areas |
| 7. Better communications for audit teams through laptop computers and electronic bulletin board | Ongoing | Districts GAO visited had not received funds for laptop computers |
| 8. Establish national policy board to ensure CEP is properly managed | Complete | None |
| 9. Establish a national CEP director and CEP managers to provide CEP leadership and responsibility | Complete | Has provided overall leadership, but lacks authority |
| 10. Develop standards and measures for a successful CEP | Ongoing | Needs revision; see chapter 2 |

Source: IRS documents and GAO analysis.

On the basis of our surveys and interviews, the two approved changes to provide more central direction over CEP—establish a national CEP director and a national policy board—appear to have been fully implemented. IRS has also fully implemented its approved expansion to the Industry Specialization Program (ISP). Such changes seem to have improved communication and coordination among the IRS functions as well as oversight of CEP.

However, IRS could make these changes even more effective. We believe that IRS could do more to improve revenue agents' industry knowledge. Further, although IRS established the position of CEP director to provide development, oversight, and evaluation, the director has no line authority over CEP revenue agents or resources. In March 1994, IRS officials said that they would soon expand the director's responsibilities beyond the 1,700 CEP corporations. These responsibilities would cover IRS' audits (about 50,000) of all corporations with assets exceeding $10 million but would not cover the authority over field staff or resources. The effects of this expansion on CEP audits and related resources were not known.

Similarly, the National Large Case Policy Board recently reviewed the 10 changes.[1] The Board's 1993 report noted marked improvement in many areas, such as the increase in functional cooperation among Appeals, District Counsel, and CEP. However, the report identified the decentralized CEP structure and budget as a key concern. It pointed to six CEP areas, which cut across many of the 10 changes, needing improvement: (1) a more centralized budget, (2) an improved measurement system, (3) more issue agreements and case resolutions, (4) better issue identification, (5) more timely audits, and (6) accelerated tax collections. The CEP Executive Director said that these six areas affect CEP's ability to finish implementing the 1990 changes.

We found inconsistent and incomplete implementation of the remaining seven changes. Our work showed that IRS' decentralized structure hindered implementation of the seven changes; district offices have been responsible for implementing most changes. The CEP Executive Director said that if he had line authority over CEP teams and a separate budget, he could have ensured more complete and consistent implementation of the seven changes.

IRS' decentralized structure has evolved over time to protect against concentrated power that could be abused. In this structure, IRS' districts acquired the major responsibility for operating various programs. Although IRS has been exploring ways to more effectively operate in a modern environment, its decentralized structure has become rooted.

These 10 changes, even if fully implemented, will not solve certain problems that contribute to CEP-recommended taxes not being collected. These problems included the following: (1) CEP audit teams lack needed resources, (2) CEP's measures of success skew the incentives for audit teams in supporting tax recommendations, (3) CEP's methods for obtaining needed data from corporations do not work well, and (4) CEP teams lack knowledge about industries covered in audits.

## Lack of Budget Resources Hampered CEP Audits

IRS considers CEP to be one of its highest priority enforcement programs. However, in the four districts we visited, CEP did not receive a commensurate priority in resource allocation. The decentralized structure allowed districts to shift resources to meet other needs. Our work showed that CEP teams often lacked funds for training, traveling to corporate

[1] "The State of the Large Case Program," report of the IRS National Large Case Policy Board, January 13, 1993.

offices to obtain data, and hiring private sector experts. Such resource shortfalls hindered CEP teams' ability to audit large, diverse corporations with operations scattered worldwide.

## Training

Officials in CEP, Appeals, and District Counsel in the four districts we visited generally said that CEP revenue agents need more training on how to support recommended taxes. These officials said that audit issues were not fully developed, in part, because the agents were not sure about what documents or expert testimony were needed.

Only 26 percent of the 85 team coordinators responding to our survey said they had been trained before being placed in their positions. About 33 percent of them reported that they needed more training, such as on industry tax and accounting issues, to improve their ability to do audits. Further, none of the team coordinators in our 12 case studies had received extensive training on the level of evidence needed to support tax assessment recommendations. The advanced corporate training course, which is required for CEP revenue agents, covered such evidence standards only briefly. We are concerned about the lack of training for team coordinators. As case managers become responsible for other CEP audits, the team coordinators continue to receive more responsibility for managing audits. (See ch. 1 for a description of CEP staff roles.)

We also found a need for more training on industries that CEP corporations cover. About two-thirds of the case managers and team coordinators responding to our survey had not received training on industries they audited. In our survey, a team coordinator who had specialized in the insurance industry since 1986 had the following comments about the lack of such training.

"From May 1986 until the present time, I have only received about 8 days of continuing professional education training in insurance (examination of insurance cases is my specialty). This is despite the fact that there were major changes in the tax law for life insurance companies in 1984 and property and casualty companies in 1986. We have a number of newer agents who have been assigned to the insurance group for more than 1 year. These agents have not yet received any formal classroom training."

During our work, a revenue agent told us how the lack of industry training can hurt an audit. The revenue agent had been rotated from a CEP team doing audits in one industry to a team in another industry without any training on the new industry. This agent erred in computing an additional

tax assessment because he did not know enough about the tax laws for that industry. The corporation had to train the agent on how to compute the tax.

An appeals officer who had done many CEP audits as a revenue agent told us the training in Appeals has been much more extensive than what Examination provided him. The appeals officer said issue development and collection rates would be improved if revenue agents received similar training.

CEP officials have long known about problems with training. IRS' CEP Quality Peer Review Report for 1991 stressed the importance of training to keep revenue agents updated on tax laws and industry trends. The report concluded that a lack of funding had resulted in revenue agents not receiving the training to do highly competent work. The report recommended that IRS develop industry, issue, and tax law training for all CEP staff.

A 1992 report by an IRS task force on CEP training concluded that a lack of training puts revenue agents at a severe disadvantage during CEP audits.[2] The report recommended that CEP officials develop a training plan to cover tax law changes and to focus training on industries being audited as well as other issues commonly raised during audits.

This task force also recommended establishing a specific budget for CEP training. Accordingly, IRS set aside about $4 million in fiscal year 1993 for CEP training. However, we found that three CEP training courses to be funded through this budget were cancelled as of May 1993 due to other district office priorities. The CEP Executive Director told us that training needs cannot remain unmet year after year without harming audit quality.

## Travel and Support Audits

In addition to training, district office decisions to allocate resources to other areas have limited CEP travel and support audits. In one of the four districts in our review, audit teams lacked the funds to travel to major subsidiaries of large corporations being audited. As a result, the teams could not collect information to fully develop potential audit issues. One CEP official commented on the effect of inadequate travel funds on one audit.

[2]"A Roadmap To Quality CEP Focused Training," National CEP Training Task Force, Final Report, September 1992.

"The taxpayer suggested a meeting every other month at the support site; however, due to lack of travel funds the case manager had to reduce these to quarterly meetings. In addition, the case manager recommended that at a minimum the case manager and team coordinator travel to the support sites to attend these meetings. Due to district restrictions on travel, only one IRS person, the team coordinator, is allowed to travel to these meetings. Therefore, the case manager, who has ultimate authority and responsibility for that case and support audit, is not allowed to participate in key meetings which will determine the success of the examination."

If a district provides insufficient travel funds, its CEP teams responsible for the audit could have a greater need for audit support from other districts. That is, revenue agents in other districts, where the taxpayer being audited also conducts business, could help by doing the audit work in their districts.

In our survey, a team coordinator noted the following problems in getting support audits when the district budget for CEP was too limited to allow visits to a taxpayer's subsidiary operations.

"My current assignment has a member corporation whose home office is in another region. This corporation has not been examined since joining the consolidated group — at least 10 years. Its records for both book and tax are maintained in the other region. Circumstances such as these warrant at least a limited scope audit. I requested a support audit during the pre-audit stage of the cycle, and the case manager never forwarded the request. I was told that since the support districts no longer receive credit for their work, and with budgetary restrictions, they would be reluctant to devote the manpower necessary to perform the requested work. This would necessitate our going to the support district and doing the audit ourselves, and that wasn't going to happen."

The fiscal year 1992 CEP peer review found completed support audits in 24 percent of the cases. The peer review noted that support audits allow CEP teams to utilize IRS-wide talent to meet audit needs. However, case managers and other CEP officials in all four districts we reviewed were reluctant to request support audits. They said resource constraints and differing priorities across districts meant that agents assigned to do support audits may not be qualified for the job or be able to do the work when needed. In summary, they were not confident that they would receive work of as high quality as they received when using agents from their own districts.

## Private Sector Experts

CEP teams also had difficulty obtaining district office funds for private sector experts to assist on the audits. Our work showed that using experts could help CEP teams support their recommended assessments. Appeals officers said they perceived IRS' specialists as less credible than taxpayers' experts and generally conceded audit findings developed by IRS specialists. They added that contracting private sector experts would help increase the collection rate.

In our follow-up with survey respondents, 20 percent of 82 team coordinators told us that they needed but could not obtain a private sector expert (e.g., an economist) for their cases. In these cases, district management did not agree that an expert was needed, given available IRS specialists and insufficient funds. Also, district officials said needed experts were not readily available, and waiting was impractical.

CEP teams did not use private sector experts on any of the 36 top-dollar issues in the 12 cases we reviewed. Of the 11 District Counsel and Appeals officials who worked on these cases, 10 told us that CEP needs to hire more experts to develop complex audit issues. They said taxpayers' experts have much greater influence in Appeals and Tax Court than IRS' specialists.

In one case involving the depreciation of assets, IRS' specialist alleged that the taxpayer overstated the value of the assets. The appeals officer said he conceded most of over $150 million of recommended adjustments because the courts would be unlikely to uphold IRS' position when the taxpayer had hired a reputable appraisal firm. The appeals officer also said the courts generally would not perceive IRS' specialists as credible in this case.

In another example, the appeals officer said the CEP taxpayer hired famous tax attorneys whose writings on taxation were often cited in court. Knowing this, the appeals officer said he felt obligated to accept the taxpayer's position and conceded over $100 million in recommended adjustments. He said the credibility of the taxpayer's experts exceeded that of IRS' specialists.

IRS' fiscal year 1992 CEP peer review report found a similar problem. CEP used private sector experts in 16 percent of the cases reviewed compared to 43 percent by the corporations audited. The report recommended that CEP teams obtain experts early in the audit to facilitate information gathering and improve audit quality. Further, the report recommended that CEP officials in the National Office seek additional funds to contract experts.

IRS has allocated separate funds to CEP for contracting with experts since fiscal year 1991. According to National Office officials, although these funds have helped to alleviate some of the pressures on the districts when they requested experts, the funds were still too limited to have a large impact.

Having a central budget would facilitate the transfer of CEP funds during the year from one district to another. In our case studies, 19 of 24 CEP district officials agreed that the National Office should directly control CEP resources, such as training, travel, and private sector experts. They generally supported having a central CEP budget to deter districts from shifting CEP funds to other district programs.

In summary, no IRS program can get all of the resources that it needs, particularly when budgets are tight. But our work suggested that CEP had some serious unmet needs and that resources would be more certain under a centrally managed CEP budget. With such certainty, CEP team members and other IRS staff could be better developed and utilized. Although IRS would need to protect against overcentralizing and thus undercutting other district programs, CEP would be more likely to meet its mission in auditing large, complex corporations if resource allocation were more centralized. One protection could be to leave the responsibility for specific decisions about CEP audits and technical aspects at the district level.

## CEP Productivity Measures Need to Provide More Incentive to Revenue Agents

IRS measured CEP's productivity by the amount of additional taxes that audit teams recommend and the time it takes to complete the audit. We agree with the Internal Revenue Service Manual that the intent of an audit is to determine the true tax liability without concern about the hazards of litigation. It is not IRS' manual that needs to be expanded, but rather its measurement of CEP. For various reasons discussed below, we believe that CEP teams also need to consider the rate at which their recommended taxes are collected.

Considered separately, we believe that IRS' current two measures have some validity. Using recommended taxes as one measure can encourage revenue agents to identify more areas of potential noncompliance, especially when complex tax laws make determining the true tax liability difficult. Measuring the time to complete audits is likely to encourage audit teams to use their time effectively.

On the other hand, we found that these two measures alone did not provide adequate incentive. Attempting to generate the most recommended tax in the shortest amount of time can induce CEP teams to bypass audit steps and not fully develop support for their recommended taxes. Thus, CEP teams had little incentive to review all areas of tax returns, track down valuable data, or seek feedback on its audits from Appeals. We believe this lack of incentive led to some poorly supported recommended taxes that could not be sustained in Appeals. Having the collection rate as another measure could alter this incentive and result in CEP teams better supporting their tax recommendations.

## Little Incentive to Identify and Fully Develop Recommended Taxes

IRS' measures provided little incentive for CEP audit teams to adequately identify and develop recommended taxes that can be sustained after audit. By focusing on recommended taxes and audit cycle time, these measures can pressure teams to use the same audit plan year after year—particularly if the old plan produced high recommended taxes (regardless of whether Appeals had sustained these recommended taxes). CEP teams in 11 of our 12 cases generally followed the same plan across audit cycles. Limited time to complete audits may help explain this tendency.

We found that following the old audit plan can result in CEP teams missing issues, overstating recommended taxes, and using resources ineffectively. For example, corporate officials told us that the taxes recommended repeatedly by revenue agents often involved timing issues that should not be developed in subsequent years once the adjustment is agreed to and made.

The most negative aspect of CEP audits cited by both the corporate and IRS officials surveyed was the revenue agents' failure to adequately support issues they raised during the audit. An appeals officer said: "To create dollars, Exam (Examination Division) raises too many weak issues. This clouds the entire case. Exam should focus on solid issues and not be pressured to create tax." Also, a case manager commented: "Instead of encouraging agents to fully develop their issues so that the government can eventually collect the tax, ROI (return on investment using recommended taxes) encourages agents to set up big deficiencies. Finding issues is probably easier than developing them."

## CEP Teams Had Little Incentive to Coordinate With Appeals

Measuring success by the amount of recommended taxes per hour also gave CEP teams little incentive to coordinate with Appeals on how it settled disputes over recommended taxes. We found inconsistent coordination between CEP teams and appeals officers. Such coordination could inform CEP teams about the reasons that Appeals conceded recommended taxes from prior audits. Without this knowledge, agents may continue to recommend taxes that are likely to be conceded.

One of IRS' 10 changes in 1990 required CEP teams and Appeals to meet before and after the case is decided by Appeals. CEP teams can explain their position on disputed issues and allow Appeals to ask questions about the team's positions. The teams may also use this information to more fully develop their positions in the next audit. By May 1991, both functions had changed their procedures to require these meetings.

Before IRS required these two functions to meet before and after settlements, our surveys indicated that communications between Appeals and CEP teams on settlements were inconsistent. Although 64 percent of the appeals officers said Appeals provided feedback to CEP teams on the settlements, only about 40 percent of both the 56 case managers and 73 team coordinators who had cases that went to Appeals said Appeals provided feedback. CEP officials said a possible reason for the disparity could be that the feedback provided to Examination was not provided to the CEP teams.

Our case studies also showed this inconsistency. For the nine cases in Appeals we reviewed (most audited and settled before IRS implemented its CEP changes), four CEP teams did not hold preconference meetings with Appeals. In addition, none of the nine teams met with Appeals after the case was settled to find out why recommended taxes were not sustained. Moreover, the revenue agents working on five of the nine cases said they had neither read the written Appeals' report on the resolution of past audits of the same taxpayer nor coordinated with Appeals before or after the audit. They said doing so takes time away from current audits and offers little potential to recommend more taxes.

In summary, we believe that measuring CEP on taxes collected in addition to taxes recommended would balance competing incentives and serve as a control against overstated recommended taxes. With both measures, CEP teams should feel less pressure to recommend taxes that are unlikely to be sustained in Appeals or the courts. They also would have more of an

incentive to fully develop issues that they do audit. As a result, the collection rate should increase from 22 percent.

A January 1993 report issued by the Treasury Inspector General illustrates what can happen by emphasizing recommended taxes over taxes collected—IRS' overall mission.[3] The report described how IRS managers in the Buffalo district manipulated statistics. They shifted recommended taxes from CEP audits to another audit program that was falling short of its goal. Because the CEP goal had been met, they artificially enhanced the other program's results to attain better performance evaluations and receive merit pay increases.[4] Although IRS prohibits using numerical goals to evaluate individual performance, IRS holds managers accountable for meeting the program goals. The Inspector General concluded that problems he found may exist throughout IRS.

## Audit Methods to Obtain Taxpayer Data Did Not Work Effectively or Were Rarely Used

CEP teams need corporate information to determine whether all income is reported and all deductions and credits are allowable. But corporations can have difficulty finding information when IRS' requests are vague or are for an old tax year. To the extent that CEP teams poorly planned the audit, vague requests are more likely. Also, the CEP teams and corporations may disagree on the types and amount of information needed for the audit. Such disagreements are the normal product of the tension existing between tax administrators and taxpayers in a complex tax system that depends on voluntary compliance.

We found that the two methods—IDRs and summons authority—that CEP teams have to obtain needed taxpayer data were not working well. IDRs were not effective; and summons authority was seldom used because of the time required to obtain a summons. As a result, CEP teams need more effective tools to use when corporations do not provide requested information in a timely manner. Such tools would help ensure that CEP teams develop supportable recommended taxes that can be sustained in Appeals.

In our survey, 85 percent of team coordinators reported they did not receive requested information in a timely manner, while about 30 percent

[3]"Management Inquiry Into the Buffalo District of the Internal Revenue Service," Department of the Treasury, Inspector General report, (OIG-OQA-93-003, Jan. 12, 1993).

[4]Although the Inspector General report did not indicate whether CEP's collection rate as discussed in chapter 2 would be affected by this shift in program results, we doubt that our computation of the rate was affected. We tracked the taxes recommended for each specific CEP corporation, which would not be affected by the manipulation of aggregated results.

said they had to close audits without receiving the information. Further, 76 percent of the 57 team coordinators and 61 percent of the 55 case managers who reported that their cases closed later than planned said problems getting information from the taxpayer caused the delay to a great or very great extent. One team coordinator responded to our survey with the following comments.

"The taxpayer procrastinated and was able to control the pace of the examination. [IRS] management's decision to close the case with undeveloped, unagreed issues was a poor decision. Exam should have fought for the records and issued summonses where required to properly develop issues."

Our case studies also showed the difficulty that CEP teams had in getting information. Out of the 12 cases, 5 teams extended the time to complete the audits because the corporation did not provide needed data. In all, four teams had not received the data by the time the audit ended.

Rather than providing information to CEP teams during the audits, corporations sometimes provided it only to Appeals. In our survey, about half of the 63 corporate respondents whose cases went to Appeals said they introduced new information only to Appeals. In the 9 appealed cases we reviewed, the corporations provided new information to Appeals for 17 of the 27 top-dollar issues. In two of these cases, CEP officials told us they would never have recommended additional taxes if they had received the related information during the audit. The information convinced Appeals officials to concede about $30 million in disputed adjustments to taxable income. If the teams had not recommended these adjustments upon receiving the requested information, the collection rate would have been higher.

Overall, providing information to Appeals and not to CEP teams significantly affected the collection rate. In the 9 appealed case studies, Appeals sustained almost 70 percent of the recommended taxes when corporations provided the information to CEP teams compared to none of those taxes recommended when the corporations provided the information directly to Appeals.

The fiscal year 1992 CEP peer review study also found that requested information was provided by the due date in only one-third of the requests, even though the team and the taxpayer had agreed on an acceptable response time. The peer review report viewed the efficient exchange of

information as essential to a quality audit and recommended higher management attention.

When corporations did provide requested information, many case managers and team coordinators who responded to our survey were not satisfied with taxpayers' responses. About 40 percent were dissatisfied with the completeness of the information. CEP, Appeals, and District Counsel officials we interviewed said taxpayers' failure to provide requested information in the audit resulted in undeveloped recommended assessments. Our analysis of the nine case studies showed that such recommendations were likely to be conceded by Appeals.

Both taxpayers and district CEP officials indicated that corporations encountered difficulties responding to IRS' information requests. About 40 percent of the taxpayer respondents reported that they were dissatisfied with the clarity and conciseness of the teams' requests. They believed that the IDRs were too wide-ranging or vague to be processed quickly and accurately. According to a report by an organization whose members include CEP corporations, CEP teams request irrelevant information when they are "fishing" for issues to audit.

IRS officials said while IDRs may be broad and vague, CEP corporations did not always leave an audit trail that allows CEP teams to identify the specific documents needed. On the other hand, CEP officials in the four districts we visited said they recognized the corporations' difficulty in responding to IDRs. They pointed out that corporations had more difficulty when the requests involved tax returns from many years ago, particularly if the taxpayers retained tax information in multiple locations or lacked personnel to find the information.

Although the case managers and team coordinators in our survey expressed dissatisfaction with taxpayers' overall cooperation in responding to information requests, they rarely issued summons to obtain the information. In the survey, only seven case managers and five team coordinators said they used IRS' summons authority to obtain needed information. Instead, they said they relied on meetings with taxpayers to resolve delays or they reissued the original request for data.

We found this same condition in our case studies. In the nine protested cases, CEP officials met with the taxpayers to discuss delays in obtaining requested information. The CEP teams had not used their summons authority in any cases, despite their difficulties. Most teams did not receive

the requested information in a timely manner, if at all. In one case, however, a team used a summons during a subsequent audit cycle when the corporation said the information requested could not be located. After receiving the summons, the corporation located the records overnight. However, according to revenue agents in some of the districts we visited, a summons generally does not provide such immediate results.

Revenue agents in three of the four districts we visited said they were reluctant to use the summons authority. Under pressure to close audits quickly, they said a summons must be enforced, which can take from 6 to 24 months. The agents also said they did not want to harm good relationships with the corporations. However, as a District Counsel noted, agents do not have good relationships when corporations do not provide requested information.

We recognize that IRS' IDRs can cross the bounds of what would seem reasonable to an independent observer. As a result, we do not believe that IRS should necessarily be able to obtain all of the information that it requests.

However, our case work showed examples in which even reasonable requests for information were not met in a timely manner or at all. Given the practical difficulties of using a summons, the inadequate corporate responses to IDRs, and the frequency with which corporations provided new information to Appeals, we believe CEP teams need more effective tools to gain better access to the information for which their request is appropriate. We have identified the following options that could be used by IRS if a corporation did not provide requested information without reasonable cause:

- Prohibit the corporation from introducing such information during appeals or trial. A similar requirement exists in section 982 of the Internal Revenue Code for foreign-based documentation. This section can prohibit taxpayers from introducing that documentation in a civil tax case.
- Provide IRS with the authority to assess a penalty for noncompliance with a request for certain information. This authority could be similar to section 6038A, which allows penalties against certain foreign-owned corporations that fail to furnish requested information.
- Give CEP the authority to impose penalties on corporations that willfully fail to produce requested data by the end of the audit. No such penalty exists now. Under this penalty option, Appeals and the courts could rule

on whether the corporation had reasonable cause for not providing the data to CEP. If so, the penalties imposed by CEP would be abated.

We have not studied the cost-effectiveness of these three options. And IRS may want to examine ways to make the summons authority more useful, by devising a more timely process or progressive steps leading to its use. Any of these approaches may improve IRS' ability to obtain the necessary information. Yet, all of them should be considered as a last resort. Working cooperatively with taxpayers to clarify the IDRS and obtain the necessary information should be tried first. However, we believe enhancing IRS' tools as we suggest may increase cooperation so that the new tools would rarely be needed.

## Revenue Agents Were Not Adequately Informed About Industry Audit Issues

We found that CEP revenue agents generally did not specialize in a particular industry. IRS policy has long required that agents rotate from audits of one corporate taxpayer to another about every 6 years. We support the concept of rotation as an internal control to safeguard the integrity of CEP, but whether the current 6-year standard is appropriate today is another question. IRS officials told us that IRS is considering lengthening this period.

We also believe that rotation is more important among corporations than among industries. In rotating among corporations on the 6-year schedule, IRS' revenue agents have tended to also switch from doing audits within one industry to audits within another. Switching industries, along with corporations, requires agents to learn different accounting practices and audit issues. As a result, agents have more difficulty doing a quality audit under tight time frames.

District CEP officials in our 12 case studies cited a need for more industry knowledge. Of 23 officials, 15 told us CEP revenue agents often lacked the necessary knowledge of the industry environment, tax accounting practices, and issues. They believed this lack of knowledge hindered revenue agents' ability to develop supportable audit positions. These officials said a portion of revenue agents should specialize in industries to help CEP teams more effectively audit corporations in the same industry.

In addition, 11 percent of team coordinators and 27 percent of taxpayers responding to our survey reported that they were dissatisfied with the audit team's knowledge of the taxpayer's industry. One corporate official we surveyed said that the

"Technical ability of Examining agents is woefully inadequate. They just don't have the background or expertise to handle complex technical issues of CEP taxpayers. To deal with an agent who has 'a little knowledge' is a frustrating experience, since much time is taken up by responding to irrelevant questions."

The 1990 IRS quality improvement team for CEP recognized the need for more knowledge of industries covered by CEP audits. The team found that ISP had not kept pace with the changing corporate world. ISP lacked effective communication across IRS districts. Nor did it adequately ensure consistency among audit teams in developing positions on similar industry issues. The team cited needed improvements to ISP to deal with multi-industry corporations. For example, the team believed that an ISP that relies on each district to coordinate its industry issues without national management will not meet its intended purpose. This team concluded that such an approach lacked a mechanism to ensure that audit plans and industry issues are uniformly developed.

IRS expanded ISP, on the basis of its 1990 change, by having ISP industry coordinators accumulate and disseminate information on selected industries as well as IRS' audit positions. IRS' goal was to ensure a more consistent treatment of taxpayers. IRS also created electronic bulletin boards to improve communications among audit teams in developing industry issues. However, IRS did not develop controls to ensure that revenue agents would use the information as intended.

We found ISP had not ensured that CEP teams would raise and develop coordinated industry issues. Three of four industry coordinators we interviewed said their span of responsibility is too vast for them to be adequately involved in all audits in their industry or to provide all audit teams with needed assistance. The industry coordinators said they rely on audit teams to request their assistance when problems arise. However, they acknowledged that audit teams usually did not have enough industry knowledge to know when to ask for help.

Not having revenue agents who know about an industry can hamper audits. One CEP branch chief said an adequate understanding of the taxpayer's industry is paramount for effective audits. In 1 of our 12 cases, the lack of industry knowledge significantly hindered the audit. The district assigned three revenue agents to an audit involving an industry about which they had no knowledge. The team coordinator had to spend time coaching the agents on the industry and its accounting standards. At

the same time, the coordinator was tasked with developing complex audit issues but lacked enough time to accomplish this task.

According to the team coordinator, this audit was inefficient. The agents only began to understand the industry and accounting standards when the audit ended. As a result, the major issues were poorly developed and Appeals completely conceded two of the three top-dollar issues, totaling over $800 million. The corporation is litigating the third issue.

We believe developing industry specialization among revenue agents would improve their abilities to audit CEP corporations. IRS is already developing a program to have agents specialize for non-CEP audits of businesses. So far, IRS believes this program has improved audits. We believe that this program can provide a road map to help CEP meet challenges it may encounter through specialization. Believing that IRS still should rotate agents among corporations, we favor a similar type of industry specialization for CEP audits.

## Conclusions

CEP is IRS' most important audit program given its complexity and revenue implications. Since the 1970s, CEP has been plagued by various problems. To correct these problems, IRS approved CEP changes in 1990. IRS districts, which have the major responsibility for CEP audits, have not fully implemented all of these changes. We believe these changes are positive and need greater support from a central authority for them to work effectively.

The decentralized management of CEP has also contributed to these problems. This structure has allowed districts to shift CEP resources to meet other needs. Having fewer resources, CEP teams are ill-equipped to do quality audits of large corporations with complex operations. In particular, we found that CEP teams needed more consistent training on industry issues and audit practices. More centralized control over budget and staff resources, while balancing other resource needs in the districts, could improve the audits as well as the audit team's support for recommended taxes. To protect against excessive centralization, authority for making specific case decisions could be left in District Office hands.

IRS' measure of CEP—recommended tax increases per hour of audit time—may encourage CEP teams to recommend tax increases not likely to be sustained in Appeals. Contributing factors include time pressures to close audits and ineffective tools for obtaining needed information from

CEP corporations. We believe that adding a new measure—the rate in collecting recommended taxes—could provide needed balance in discouraging CEP teams from continuing to recommend taxes that Appeals is likely to concede.

CEP teams and corporations may disagree on the types and amounts of information needed for an audit. While some IRS requests for information may be overly broad or vague, CEP teams need information to determine whether all income is reported and all deductions and credits are allowable. The CEP teams had problems getting timely and complete information from taxpayers using IDRs and did not often use IRS' summons authority—the current two methods of obtaining information. While we believe that CEP teams should first try working cooperatively with taxpayers to clarify data requests and obtain needed information, we also believe that IRS' tools do not work well enough when corporations do not provide requested information in a timely manner.

Concessions of recommended tax increases in Appeals also arose because CEP teams lacked knowledge about the industries that their audits covered. Our work showed that CEP revenue agents did not know enough about industry trends and practices. We believe that having more such knowledge would improve CEP audits along with the chances for recommended taxes being upheld in Appeals. Given increasingly complex corporations, specialized agents rotated among corporations in the same industry would improve CEP audits.

If the IRS changes are successful, CEP teams will be more likely to improve their audits and recommend tax increases that can be supported and sustained. However, we see a need for other changes to the CEP budget, training, and measures as well as CEP teams' access to corporate data and their knowledge of industries.

## Recommendations to the Commissioner of Internal Revenue

We recommend that the Commissioner of Internal Revenue

- give the CEP Executive Director authority over CEP budget resources and staff allocations at the district office level,
- ensure that CEP's revenue agents receive adequate training on the industry they specialize in as well as on tax laws and basic auditing skills such as standards of evidence,
- expand the measures of CEP productivity to include the percent of recommended taxes that is ultimately collected,

- issue regulations or propose legislation to strengthen IRS' ability to obtain needed data from CEP corporations during the audit after evaluating options for obtaining needed data from corporations as discussed on page 56, and
- modify CEP's policy to allow revenue agents to rotate among corporations in the same industries to the extent possible.

# Comments and Our Evaluation

## IRS Comments

The Commissioner agreed with our recommendations on training CEP revenue agents. She also agreed to modify CEP policy on rotating revenue agents to the extent that circumstances and resources permit. In addition, she said that in fiscal year 1994, IRS will study the three options that we suggested to increase IRS' ability to obtain needed data from corporations during CEP audits.

The Commissioner did not agree with our recommendation to give line and budget authority to the CEP Executive Director. We believe that IRS assumed our recommendation was similar to ones made by IRS study groups in 1990, which recommended major centralization. The intended scope of our recommendation was not as great. We agree that full centralization generates problems as well as benefits. We clarified our report recommendation to focus on centralizing authority over resource allocation, not over CEP cases themselves.

The Commissioner also did not agree with our recommendation to use the collection rate as one measure of CEP productivity. Even so, the Commissioner said, in commenting on a recommendation in chapter 2, that IRS is developing a voluntary compliance baseline measure using a methodology similar to ours. We continue to believe that this recommendation is needed and IRS' proposed measure would suffice.

The Commissioner also said we did not put enough emphasis on changes that IRS was making to CEP, such as the continual involvement and control by regional CEP managers and the new measures that IRS was developing. We added report language to further acknowledge these changes and our support for IRS' efforts. However, neither our survey of 108 CEP cases nor our work during 1992 and 1993 at IRS offices in 5 IRS regions provided

evidence that regional CEP managers' involvement had significantly improved the selection of audit issues or resource allocation.

## TEI Comments

TEI raised concerns about whether we would be "jumping the gun" in suggesting new penalties or sanctions if CEP corporations did not adequately provide data that CEP teams requested. TEI pointed to many problems with these IRS requests, which our report has discussed. We also saw evidence of corporations not responding adequately to reasonable requests.

We differ slightly with TEI on these points. In turn, our recommendations asked IRS to evaluate the various options for improving CEP teams' ability to obtain needed data. We do not view this as "jumping the gun." Our work did not lead us to conclude that IRS' changes to CEP since 1990 will solve the problem, even though they may lead to improvements.

Regarding these ongoing changes to CEP, TEI characterized our report as "more a historical portrait" of CEP in 1993. TEI questioned whether our findings from cases closed a number of years ago would still be valid because of the many ongoing changes to CEP. We agree that much of our work focused on cases audited and settled in Appeals before IRS approved changes to CEP in 1990. This fact, however, did not preclude us from analyzing the status of these changes as well as the recent state of CEP. We surveyed various IRS officials as well as taxpayer officials involved in 108 cases—some settled in Appeals after 1990. In all cases, we asked questions about each of IRS' changes. Further, we interviewed 85 IRS and corporate officials in various field locations up through mid-1993. We drew on all of this information in reaching our conclusions about the recent state of CEP as well as IRS' changes.

# Appeals' Mission and Controls Contributed to a Lower Collection Rate and Unbalanced Incentives

When corporations disagree with the additional taxes CEP teams recommend, they usually challenge the taxes in Appeals. If a CEP team does not or cannot adequately support its recommended taxes, Appeals has little choice but to concede these taxes. Even if Examination's position is supported, Appeals may concede the taxes in full or in part on the basis of an assessment of the hazards of litigating the issue.

We found that Appeals has been striving to meet its stated mission

"to resolve tax controversies, without litigation, on a basis which is fair and impartial to both the Government and the taxpayer and in a manner that will enhance voluntary compliance and public confidence in the integrity and efficiency of the Service."

While IRS may be meeting its mission to settle disputes without litigation, we believe that this emphasis along with other factors contributed to the 22 percent collection rate and challenged Appeals' ability to meet other parts of its stated mission—to reach settlements fair to both the government and the taxpayer and to promote voluntary compliance. Specifically:

- Differing interpretations of complex tax laws led to extensive rework in resolving disputes year after year, which Appeals' settlements generally cannot resolve beyond the years in dispute.
- The inherent conflict between Appeals' mission to settle disputes without litigation and Exam's mission to protect the government's interest by recommending taxes laid the groundwork for a low collection rate.
- Appeals' controls for coordinating with other IRS offices, such as Exam and Counsel, either did not always work or did not exist, creating inconsistencies in settling tax disputes.

Appeals has taken steps to improve the settlement process, such as requiring opening conferences with CEP teams, sharing its settlement results and rationales with CEP teams, and initiating an industry specialization program. We support such efforts and cite them throughout this chapter. Even so, further changes are needed to balance incentives and tighten controls while allowing Appeals to stay independent and impartial. Besides reducing rework, our changes should help improve the collection rate and consistent application of tax law. In sum, IRS should be better able to meet its mission of collecting the proper amount of tax at the least cost and burden to IRS and taxpayers.

## Complex Tax Laws Combined With Appeals' Mission Allow Tax Disputes to Recur

Both IRS and taxpayers consider the corporate tax code complex and ambiguous, causing legitimate differences in opinion over how the law should be interpreted. As a result, IRS has repeatedly audited the same issues and corporations have repeatedly disputed IRS' audit findings. This cycle has drained IRS and corporate resources without putting the disputes to rest. Neither the appeals process nor litigation are particularly effective means of resolving these recurring audit issues; a better means may be tax law changes.

As of September 1992, about 12,000 disputed issues with $99 billion in proposed adjustments were waiting to be resolved by Appeals.[1] We found that 14 tax code sections account for 5,279 (45 percent) of these disputed issues and $56 billion (57 percent) of these proposed adjustments. IRS officials said they believed most were appealed by CEP corporations.[2]

Complex, ambiguous laws have created opportunities to characterize transactions in order to achieve a desired outcome. This flexibility, in turn, increases the likelihood of tax disputes. Without clear tax laws, resolution of these disputes can get complicated and can ultimately rely on the negotiating skills of those persons representing IRS and CEP taxpayers.

This was illustrated during our review. We attempted to evaluate whether Appeals' decisions on the 27 highest-valued issues in our 9 appealed cases were reasonable according to the tax code. Tax law ambiguity and complexity combined with Appeals officers' broad discretion to settle disputes made this attempt inconclusive.

Our survey results also indicated that ambiguity in the tax code is a problem in resolving disputes over CEP audit results.

- Hazards of litigation was the primary reason cited by appeals officers for partially or fully conceding issues. They believed that litigation was too risky, given uncertainty over how the court would interpret tax laws.
- About 90 percent of the corporations said they appealed CEP-recommended taxes because they disagreed with Examination's legal interpretation instead of its presentation of the facts.

[1]Tax Administration: Recurring Tax Issues Tracked by IRS' Office of Appeals (GAO/GGD-93-101, May 4, 1993).

[2]The issues are being appealed by corporations, partnerships, estates, and individuals. Because of limitations in IRS' database, we could not determine how many were appealed by CEP corporations without doing a time-consuming analysis of all 5,279 open issues.

This lingering ambiguity on tax issues reduces CEP's collection rate. It also increases IRS' costs as CEP teams continue to raise the same audit issues—recommending additional taxes—while Appeals continues to settle disputes over the same issues. Such rework also increases corporations' costs.[3] Overall, the effects of complex corporate tax laws contradict IRS' mission to collect the proper amount of taxes at the least cost.

Given the resource drain and burden imposed from reworking tax disputes, we believe that IRS and Treasury should more actively seek to permanently resolve these disputes. We also believe that proactively pursuing tax law changes, rather than relying on the appeals process or litigation, is the best means of resolving recurring issues.

For example, Appeals' settlements do not produce binding precedents for resolving similar disputes in future years. Instead, they generally resolve tax issues for just the years in dispute. In addition, case-by-case settlements have produced dissimilar treatment for the same tax issue.

Litigation also does not necessarily establish clear legal precedent. Several factors complicate the resolution of disputes through the tax litigation system. Because this system involves the Tax Court, Court of Federal Claims, and federal district courts, conflicts among the court decisions may arise. It may take years before the Supreme Court reviews conflicting decisions, if it ever does. Litigation, therefore, may not fully resolve the dispute but will add substantial time and costs.

IRS and Treasury already have a process that can be used more proactively to propose tax law changes to Congress. IRS annually generates a list of legislative proposals that the Treasury Department reviews and approves for the administration's consideration. Given the recurrence of many corporate tax disputes, CEP officials said they annually offer proposals to permanently resolve disputed tax issues. The few proposals that survive these steps are officially submitted to Congress. We believe that these proposals must be well supported, clearly presented, and seriously considered.

[3]An IRS-contracted study by the University of Michigan concluded that 1,300 CEP corporations together incurred costs totaling $2 billion a year to comply with federal, state, and local tax laws.

## Differing Incentives Laid Groundwork for Low Collection Rate at Appeals Stage

Appeals' mission to settle disputes without litigation can conflict with CEP teams' desire to recommend additional taxes. Given that tax law is open to interpretation, this difference led to more recommended taxes that CEP corporations were likely to dispute and Appeals was likely to concede. Such differences not only produced rework but laid the groundwork for the low CEP collection rate.

Consistent with its mission, Appeals' goal in the mid-1980s was to settle 85 percent of all types of cases without litigation. Appeals dropped this numerical goal in 1988 because its staff strove to achieve the number instead of reasonable and fair settlements. Even without this goal, the settlement rates for CEP cases ranged from 84 to 93 percent in fiscal years 1990 to 1992.

Such high settlement rates diverged from CEP teams' focus. As chapter 3 discusses, a key CEP measure was the amount of additional taxes recommended per hour. This measure provided a strong incentive for CEP teams to recommend additional taxes if they had doubts about a corporation's liability. Conversely, Appeals emphasized settling cases out of court. This encouraged appeals officers to concede recommended taxes to settle the case.

With this imbalance, CEP's focus burdens "downstream" functions like Appeals. Similarly, Appeals' focus burdens "upstream" functions like CEP because Appeals settlements do not set a precedent to follow as do some court decisions. A 1992 IRS study discussed the need to examine its functional organization.[4] It concluded that a functional organization does not maximize effectiveness. The study proposed using a systems approach to find ways to better organize work and increase cooperation between functions. It also proposed developing measures to determine how well IRS meets its overall mission of collecting the proper amount of tax at the least cost to the public.

We believe one way IRS could increase cooperation and balance between CEP and Appeals is to provide a common measure that applies to them as well as meets IRS' overall mission. That common measure could be the collection rate. If IRS added this measure to both functions, appeals officers would have more incentive to

[4]"The Internal Revenue Service Plan for Improving Customer Satisfaction and Organizational Performance," Document 9039, September 24, 1992.

- meet with CEP teams before settling cases to better understand the audit findings, request any missing data, or provide any new taxpayer data; and
- clearly communicate to CEP teams as soon as possible the reasons why recommended taxes were not sustained so that the team can avoid raising the same issues in the same manner, thus reducing taxpayer burden and saving IRS resources.

National Office Appeals' officials believed that using the collection rate as a measure could induce some appeals officers to forget about settling disputes fairly and just focus on collecting the taxes. Measures can affect behavior. That is why they are important. However, for various reasons, we expect this added measure to have overall positive rather than negative effects.

First, Appeals already measures the portion of recommended tax that it "recovers" rather than concedes. As our work showed, this measure did not induce appeals officers to focus on collection to the exclusion of their mission. Our idea of a common measure simply extends this existing measure in Appeals throughout IRS. Doing so would allow IRS to see the total portion of recommended taxes collected across all stages—including agreements at the Exam level as well as Appeals and litigation results.

Second, National Office Appeals officials raised concerns about relying on the collection rate measure when separate adjustments to taxes owed, such as net operating loss carryover or carryback, can confound settlement amounts for the actual issues being disputed. These officials did not know the extent to which these separate adjustments skew the collection rate. In chapter 2, we recommend changes to IRS' databases in order to keep these adjustments from overstating or understating the collection rate.

Third, by tracking the collection rate across functions instead of as a goal within each function, IRS employees would feel less pressure to ignore their function's mission. Even if some pressure started to arise, appeals officers still would be subjected to other measures and be expected to negotiate fair and objective settlements. Given their role of assessing hazards of litigation, the officers may continue to use their independence to settle for a portion of the disputed taxes rather than lose them all in court. The difference would be that IRS would measure such results overall.

To the extent that a common measure encourages Appeals to share taxpayer information with CEP teams and consider their interpretations, more efficient audits with better supported recommended taxes would become more likely. Less rework and burden on corporations would also be likely if Appeals' enhanced communication led CEP teams to not recommend taxes that are unlikely to be sustained due to inadequate support.

In sum, these forces could better balance the incentives without detracting from Appeals' independence and impartiality. In fact, applying the collection rate only to CEP teams would be unfair to them and undercut the balance and incentive to communicate.

Appeals' mission also involved another imbalance. The pressure to settle cases without litigation increased the incentive for CEP taxpayers to appeal and hold out for more favorable settlements, especially under differing interpretations of law. Three of four IRS District Counsel officials we interviewed favored more litigation to guide IRS' tax positions on selected issues.

We confirmed that IRS litigation is infrequent, relative to the number of issues that the 1,700 CEP corporations appeal each year.[5] Counsel records showed that federal Tax, Claims, and District Courts in fiscal year 1992 decided 46 CEP income tax cases of which 29 were decided in Tax Court. During fiscal years 1988 to 1992, Counsel closed 96 income tax cases from Tax Court.

However, litigation has a downside. Neither IRS nor the courts can handle major increases in litigation. Litigation also adds costs for the corporations and IRS as well as time and risk to dispute resolution. CEP taxpayers said any IRS willingness to litigate more will force them to bypass Appeals and go to Tax Court. Having the ultimate decision over litigating, taxpayers may tend to litigate if they see their cases as strong.[6]

Resolving disputes at a lower level is preferable—particularly given limited resources. However, the propensity to litigate few CEP cases may put IRS at a disadvantage in its negotiations and increase the likelihood that CEP corporations will appeal and reach favorable settlements. Because

[5]We did our analysis using a list of taxpayers in CEP as of May 1991.

[6]Even so, Chief Counsel data on 96 Tax Court cases closed from 1988 to 1992 for CEP corporations we surveyed showed a higher collection rate, about 35 percent, than our 22-percent rate for a broader universe of closed CEP cases.

litigation adds costs, time, and risks for all parties, any IRS decision to litigate more disputed issues must consider these factors.

## Appeals Needs Better and More Controls to Ensure Consistent Application of Tax Laws and a Level Playing Field

We found that Appeals did not have sufficient controls to meet its policies on coordinating with IRS functions. The controls did not always work or exist. Without coordination, IRS is at a disadvantage when Appeals does not share new information with CEP teams. Or, if Appeals' settlements conflict with Counsel's positions, inconsistent applications of tax laws can arise. We also found weaknesses in other internal controls, such as those to prevent conflicts of interest.

Officials from Appeals and CEP corporations acknowledged the need for Appeals to coordinate within IRS. However, they raised concerns that more coordination would create the perception that Appeals is less independent and impartial. We agree that Appeals must be independent and impartial. Before spending money to litigate, corporations need to be able to contact an objective party at IRS who can review CEP teams' support for recommended taxes. However, we do not believe that Appeals' coordination with other IRS offices will reduce its independence or authority to objectively settle disputes.

### IRS Can Improve Controls to Allow CEP Teams to Review New Corporate Information That Appeals Received

In May 1991, Appeals formalized its policy to ask CEP teams to evaluate new, significant information that corporations provide during the appeals process. The policy in effect for the cases we reviewed, however, gave appeals officers the discretion to request this evaluation. Not allowing CEP teams to evaluate such information created the potential for noncompliance to go undetected and for Appeals to arrive at an incorrect settlement.

Corporations often provided new information to Appeals. Our survey showed that over half of the 63 corporate respondents that appealed provided new information. Also, corporations provided new information on 17 of the top 27 issues in our 9 case studies.

We found that Appeals frequently did not give new information to the CEP audit team for evaluation. In analyzing the 17 issues in which corporations provided new information, we found that Appeals did not ask CEP teams to evaluate new information for 8 of the issues. District Counsel officials said they believed that corporations, knowing Appeals usually did not ask for such evaluations, have withheld information until the Appeals process.

For example, on one of these eight issues, Appeals received new evidence to counter an adjustment to taxable income worth more than $5 million. The appeals officer told us that he accepts at face value the information that any corporation provides unless some reason exists to question it. CEP officials said that they had not seen the information and that this corporation has a history of submitting questionable evidence to support its tax return. They believed that Appeals should have provided the new information to them for verification.

IRS studies have uncovered similar problems under the current policy. A 1992 IRS review found that the policy to send new information to CEP teams was not followed in over half of 28 Appeals cases reviewed.[7] In these cases, CEP corporations provided new information on 25 issues, but Appeals shared the information for just 9 issues with the CEP teams.

A 1991 quality review by one district caused it to establish procedures for sending all new information from corporations to CEP teams. An appeals official in that district said this initiative appears to have given corporations an incentive to cooperate at the audit level. In this district, 55 of 63 case managers and revenue agents perceived that Appeals favored taxpayers. They had not been given a chance to rebut new facts and arguments. On this point, the report on this quality review stated that some Appeals officers were reluctant to return cases to CEP teams due to time delays or to teams' concerns about reworking the case.

Our work confirmed these reasons. Team chiefs told us Appeals' reluctance stems from the increased time to close the case, which can harm their performance evaluations. Similarly, a CEP case manager told us CEP teams may be reluctant to consider new corporate information if doing so will reduce the additional taxes recommended and increase their time charges to the case.

Despite the added time it may take to close the case, we believe IRS' policy is sound. CEP teams need to see the new information to round out their audits. Given appeals officers' role to settle cases, they should not have to also audit the new information. Yet, without better controls to ensure that CEP teams have a chance to evaluate new information, taxpayers will have somewhat of an advantage during the appeals process.

We considered new controls to ensure that CEP teams not only received new information but had a chance to comprehensively review it in the

[7]National Office Appeals' 1992 Large Case Process Review, January, 15, 1993.

context of Appeals' final settlement. For example, a control from other dispute resolution processes would involve having CEP and corporate officials attend any meeting Appeals holds. If CEP officials attended Appeals' meetings, they could evaluate new information. They also could react to corporate presentations to Appeals.

Although our work indicated a need for CEP officials to react to corporate presentation of new facts, we decided that requiring CEP officials to attend all meetings with Appeals and corporate officials posed problems. Always having all parties at meetings could cause lengthier meetings as the two sides argue their positions or prove to be too burdensome because of numerous meetings.

Instead, we favored another option. We concluded that CEP officials need one last chance to review all new information in the context of Appeals' settlement—just before it is finalized. This control would allow CEP teams to determine whether they received all new information and learn how appeals officers used it. While this control may increase the time necessary to reach settlement, it should avoid the burdens from having all parties at every meeting. It also allows Appeals to retain its independence and may improve its appearance of impartiality.

## IRS Can Improve Its Controls on Counsel Coordination to Ensure Tax Law Consistency

Appeals also needs to improve a control intended to help ensure consistent application of tax law. This control requires, in certain situations, that Appeals coordinate with Counsel on IRS' standard legal positions before finalizing any settlement.

Counsel at the National Office issues various types of guidance about tax issues. This guidance includes revenue rulings, private letter rulings, and technical advice memoranda, which formally set forth IRS' standard legal position.[8]

CEP teams are required to comply with such standard legal positions in developing issues. Appeals is not required to do so when settling the disputed issue unless these positions support the taxpayer, which can result in inconsistent settlements. Appeals officials said they need the

[8]A revenue ruling offers IRS' official position on a legal issue. A private letter ruling informs a taxpayer how IRS will treat a specific transaction for tax purposes; it must be honored only for the taxpayer to whom it is issued. Technical advice is furnished by National Office to a District or Appeals office in response to a question on the interpretation and proper application of tax laws given the established facts of a specific case. According to a Chief Counsel official, it can take from 6 months to 2 years, and sometimes longer, to issue a revenue ruling or technical advice.

flexibility to deviate from standard positions in order to remain independent.

IRS has established some limits over Appeals' concessions of audit issues for which IRS has a standard position. IRS' manual requires appeals officers to request and consider the views of the appropriate Counsel office before completely conceding an audit issue supported by an IRS standard position but two exceptions exist. The requirement does not apply if (1) the concession is less than 100 percent of the recommended tax or (2) the appeals officer believes that the taxpayer's facts are distinguishable from the facts upon which IRS' standard position was based.

An appeals official pointed to a potential internal control weakness in this manual section. Team chiefs in the field have broad discretion in settling disputes. They can decide both whether their settlements conflict with IRS' standard positions and whether coordination is required. Given their discretion, team chiefs can justify no coordination in such settlements by, for example, conceding less than 100 percent of the recommended adjustments. In sum, Appeals had no internal control system to track cases with standard positions and check how chiefs used their discretion in settling such cases.

We checked disputed issues that relied on standard positions to see whether the exceptions to coordination applied. Of the 27 appealed issues we reviewed, CEP teams raised 9 issues using such positions. Of the nine issues, Appeals fully sustained two issues totaling about $150 million in adjustments to taxable income. Appeals conceded at least 60 percent of the adjustments in each of the seven other issues involving about $800 million; four issues were conceded 100 percent and a fifth issue 90 percent.

Of these seven issues involving IRS' standard positions, Appeals did not have to coordinate with Counsel on three and did have to coordinate on two issues that were conceded 100 percent. Given the breadth of team chiefs' discretion and the exceptions, we could not determine whether coordination was required for the last two issues, both of which were fully conceded.

- For one of these issues, the CEP team had used revenue rulings from earlier years. Because the rulings did not specifically cover this CEP taxpayer, it was difficult to tell whether the rulings' examples applied to the actual facts of the disputed issue.

- In another fully conceded issue, the Appeals team chief conceded $20 million contrary to technical advice issued to the taxpayer. The chief said he saw no need to obtain the views of Chief Counsel because he believed the facts of the case materially differed from those stated in the technical advice. However, Counsel had issued this technical advice to revoke an earlier advice when the CEP team illustrated how the taxpayer misstated material facts used in the earlier technical advice. The team chief told us that the dispute was over the facts of the case and that the CEP team and Counsel were wrong and the taxpayer was right. We disagree that this was just a factual dispute and that the legal merits of this case were not an issue.

To enhance the consistent application of IRS' standard positions, we generally support coordination with Counsel. However, such coordination occurred in only one of seven issues involving these positions—largely because of the two exceptions to coordinating with Counsel. On the basis of our work, we favor changing these exceptions, particularly for standard positions that rely on technical advice and private letter rulings.

In these two types of guidance, the facts apply to a specific taxpayer and should be agreed to by IRS and the taxpayer before IRS issues such guidance. Because of this, the exception for the facts materially differing should not apply. Also, concessions for all seven of the issues reviewed were at least 60 percent. We believe that coordination should occur for such substantial concessions contrary to an IRS standard position. Further, even if IRS changes the exceptions, our work indicates the need to track the resolution of disputes in which technical advice and private letter rulings apply to the contested issues.

Appeals officials we interviewed said they were concerned that more coordination with Counsel would increase the time needed to close cases. However, Appeals already has added a coordination step for its ISP issues. It recently required appeals officers to seek review and approval from the ISP coordinator before conceding ISP issues. These officials believed that this ISP review will save time because the appeals officer could consult with a knowledgeable person about an issue. We support this new step as a way to ensure consistent settlements. We believe that such a coordination step is needed on IRS' standard positions.

IRS spends resources to establish standard legal positions and follow them in audits. If Appeals disagrees with the positions taken, its concerns should be communicated to Chief Counsel in order to make IRS'

enforcement consistent. If Chief Counsel concurs with Appeals, CEP teams may not need to continue to recommend taxes on issues that Appeals will concede. Besides being cost effective and less burdensome to taxpayers, this outcome should improve the collection rate.

One way to communicate concerns about standard positions is through Appeals' written summary of its case decisions. In certain cases, Appeals is required to send this summary to the Joint Committee on Taxation (JCT) for review.[9]

We found that this written summary lacked information that JCT needed to assess quality. In the nine issues that CEP teams raised based on Counsel positions, the summary for eight issues neither referred to the position nor the reason that the position was not followed. For example, one summary made no mention that a CEP team followed a standard position on a tax issue to adjust taxable income by over $300 million.[10] Without mentioning this in the summary, future CEP teams and JCT would not know how Appeals viewed this standard position for the tax years of our case study.

IRS requires these written summaries to explain the related tax law and facts as well as the team chief's rationale for settling an issue. This rationale may include references to standard positions. However, IRS does not require that these summaries specifically identify whether standard legal positions existed and were followed.

These summaries are the only documents received by CEP teams for use in future audits of the taxpayer and by JCT to evaluate the quality of Appeals' decisions. Without discussing the standard positions in the summary, we believe that JCT, or any reviewer relying on this summary, does not have all the facts needed to fully evaluate the quality of the settlement.

## Appeals Can Improve Its Other Controls

IRS has established other internal controls in Appeals to prevent collusion between the Appeals team chief and the taxpayer and to ensure quality settlements. These controls were that (1) no team chief was to be assigned to the same taxpayer for more than 6 successive tax years and (2) Appeals'

[9]Congress requires the JCT to review Appeals' settlements for tax refund cases of $1 million or more and the two largest deficiency cases closed by each region in a 6-month period.

[10]Appeals officials said a written summary for prior tax years had discussed this issue and the applicable technical advice. We do not believe that referring to a written summary for earlier tax years is sufficient notification that CEP had followed a technical advice memorandum for the current case.

managers were to review the quality of all settlements made by the team chiefs.

We found that weaknesses allowed noncompliance with both internal controls. Specifically, in one of our nine case studies, the team chief was assigned to the same taxpayer for 12 successive years, so the first control was not followed. This chief told us he was not aware that any manager had reviewed his settlements since 1980, so the second control was apparently not followed.

The January 1993 IRS Large Case study also found that senior appeals managers were not consistently following this second control by reviewing the quality of the settlements. In 14 of 28 large cases reviewed, team chiefs did "poor" or "fair" in assessing the hazards of litigation on 1 or more issues (i.e., 24 of 128 issues). Even so, 6 of the 14 chiefs said they had not received any feedback. Such feedback could improve subsequent settlements. The study recommended that supervisors provide written feedback during and after the appeals process.

## Conclusions

Appeals has been making some positive changes, such as its policy on sharing its settlements and the bases for them with CEP teams. But its mission and controls have contributed to various imbalances that can grant some advantages to corporations and that have lowered the collection rate. IRS' appellate function for settling tax disputes without litigation where appropriate is crucial, but more changes are needed to improve the balance as well as the collection rate. We believe these changes will allow Appeals to remain independent and do its job in a fair and impartial manner to the benefit of the affected parties.

Our desire to increase the collection rate does not mean that corporations will always pay more taxes. They are likely to pay more taxes if CEP teams have sufficient information and analysis to support their recommended taxes, making Appeals' concessions less likely. They will not pay more taxes when better information leads CEP teams to no longer recommend taxes that Appeals has repeatedly conceded. Thus, IRS and corporations will spend less money reworking the disputed tax issues.

Clear tax laws would also play a major role in reducing rework. Clarity would make voluntary compliance more likely, reducing the issues that IRS revenue agents raise and that corporations dispute. In the long run, this would ease the burden on CEP corporations of complying as well as reduce

the costs for all parties. Unfortunately, certain tax issues continue to be audited and appealed year after year. Because Appeals' settlements cannot permanently resolve the treatment of a tax issue, these tax disputes are likely to recur. Clearly, more needs to be done to prevent recurring issues. Because litigation can generate high costs and inconsistent rulings, legislative clarification is the preferred alternative. While IRS internally develops some legislative solutions, few are aggressively pursued and ultimately recommended to Congress.

Further, the inherent imbalance between the missions of CEP audit teams and Appeals contributed to rework and a low collection rate. Incentives encouraged CEP teams to recommend taxes and CEP corporations to appeal them—particularly given ambiguities in tax laws. Appeals' mission was to settle cases without litigation. The imbalance can be mitigated without revamping the appeals process. Within the context of Appeals' mission to be fair and independent, establishing a shared measure such as the collection rate should improve the balance. If so, Appeals and CEP teams would be more likely to communicate. IRS and corporate costs should decrease as CEP teams recommend fewer taxes on issues that Appeals has repeatedly conceded. Also, CEP teams would be more likely to recommend taxes that can be supported. Both effects would improve the collection rate.

Better controls would help ensure Appeals' compliance with IRS policies on (1) sending new corporate information to CEP teams and (2) asking for Counsel's views before deviating from standard positions in settling issues. New controls also would help. First, Appeals' written summaries could disclose when standard positions existed and, if the settlement was contrary to this position, the reasons why. Second, a system to track the coordination and settlement of disputed CEP issues involving technical advice and private letter rulings that apply to taxpayers would be beneficial. Third, Appeals' coordination with CEP officials just before settling a case would allow the officials to check all new facts, given the proposed settlement, at one time.

## Recommendations to the Commissioner of Internal Revenue

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

- More strongly propose legislative changes to resolve more recurring CEP tax disputes.

- Better balance incentives to encourage communication among Appeals, CEP teams, and Chief Counsel. In addition to IRS' current program measures, consideration should be given to a cross-functional standard measure, such as the collection rate, that encourages all units to work toward the overall IRS mission to collect the proper amount of tax at the least cost.
- Improve controls to ensure that Appeals provides CEP teams with (1) new information that taxpayers submit and (2) an opportunity to comment just prior to settling a case.
- Improve controls to ensure that Appeals coordinates with Counsel before deviating from standard positions on CEP tax issues by (1) requiring coordination when Appeals concedes a substantial portion, (2) eliminating the exception on facts differing materially when Appeals settles an issue contrary to an applicable technical advice or private letter ruling, and (3) tracking settlements and coordination on disputed issues involving technical advice or private letter rulings.
- Improve communication of settlement decisions and aid quality control efforts by requiring Appeals to identify the existence and effects of, and any deviations from, standard positions in its written summaries on CEP settlements.

# Comments and Our Evaluation

## IRS Comments

The Commissioner agreed with our recommendation to advocate legislative changes to help resolve complex tax laws. She added that IRS regularly recommends changes to the tax laws with input from Appeals. Although we revised our original recommendation that IRS attempt to litigate more CEP issues, the Commissioner concurred that litigation may be necessary to resolve disputed interpretations of the law.

The Commissioner opposed some of our suggestions in the draft report for better balancing incentives in Appeals. Her concern was that these steps would hamper Appeals' ability to settle cases in a fair and impartial manner. We had suggested in the draft report that IRS measure Appeals by the collection rate and delete the phrase "without litigation" from Appeals' mission statement. We continue to believe that more balance is needed. We have, however, revised our recommendation to recognize the need for IRS discretion in how to get all functions working toward IRS' common goal.

One option could be to use the collection rate as a common measure for both Appeals and CEP teams. Although the Commissioner raised concerns about this option, she also noted that IRS already is developing and using similar measures. Acknowledging IRS' concerns, we also deleted the suggestion that IRS change Appeals' mission statement.

The Commissioner agreed with our recommendations on better controls to ensure that Appeals coordinates with CEP teams on new information but raised concerns about ways to meet this end. We no longer recommend that Appeals invite CEP officials to meetings with corporate representatives. Although we believe that such a practice has merit, we recognize its potential downside, as reflected in IRS' comments. Instead, we now recommend that Appeals coordinate with CEP just before finalizing its settlement to ensure that CEP teams have seen all new information provided by CEP corporations and how it was used. If IRS implements this recommendation and our recommendation on sharing new information with CEP teams, we no longer see the need for having all three parties at Appeals' meetings.

The Commissioner agreed with our recommendation that Appeals coordinate with Chief Counsel on standard legal positions. She also agreed with our recommendation on clarifying Appeals' written summaries of its settlements to specifically discuss the existence of standard legal positions.

However, she did not agree to replace the "full concession" exception on coordinating with Chief Counsel with a "substantial concession" exception. We added language to the report to clarify our bases for this recommendation. Coordination does not usurp Appeals' authority or independence to settle cases. We believe that Counsel needs to know when its standard legal positions have not been followed. Such knowledge may lead Counsel to change these IRS positions, which CEP teams must adhere to during their audits.

The Commissioner also made technical comments about our findings on Appeals' mission and Appeals' coordination with Chief Counsel when standard legal positions exist. We met with Appeals' officials to discuss these technical questions, and we clarified our report language where necessary.

## TEI Comments

TEI raised major concerns with our conclusions and recommendations for the appeals process. TEI believed they would encourage more litigation. Although we do not agree with all of TEI's comments, we have made changes to improve the tone and balance in this chapter.

TEI interpreted our draft report as implying that Appeals "was giving away the store." In fact, we pointed out that we could not evaluate the quality of Appeals' settlements because of its discretion and the ambiguity of tax law.

We have made changes to our report to clarify our view on litigation. We never viewed litigation as a way to collect more taxes. Rather, we viewed litigation as a way, albeit a less desirable one compared to legislative proposals, to clarify tax law and resolve disputes over tax issues that recur year after year. We have expanded our discussion of its costs and burdens compared to its impact on negotiating settlements during the appeals process and no longer recommend more litigation to resolve recurring tax disputes.

Nor do we still recommend that IRS change Appeals' mission statement by dropping reference to settling disputes without litigation. Although we believe this phrase is redundant—given that settlement connotes not litigating—we understand TEI's concerns about Appeals' mission as an impartial, independent forum that taxpayers may use to administratively resolve disputes.

# Objectives, Scope, and Methodology

Our objectives were to determine (1) what portion of taxes recommended in Coordinated Examination Program (CEP) audits are collected after any appeals and litigation; (2) what factors, if any, reduce the percentage of recommended taxes that are collected (i.e., the collection rate); and (3) what the status and initial impact are of the Internal Revenue Service's (IRS) ongoing changes to improve CEP.

## Computer Data Match Used to Calculate Collection Rate

To determine the CEP collection rate—the percentage of CEP-recommended taxes ultimately collected—we did a computer data match of corporate income tax returns between two IRS databases. The first, Audit Information Management System (AIMS), contains information on audit results, including additional taxes recommended at the close of an audit. The second, the Business Master File (BMF), contains information on taxable income, taxes not yet paid, tax liability, penalties, interest, payments, refunds, and audit actions for business tax returns.

In both systems, each record contains the taxpayer identification number (TIN), the tax year, and the return type, which for our purposes is the corporate income tax return. To make AIMS and BMF data more compatible, we sorted the information in both databases by TIN, tax year, and dates of closed audits.[1]

Using a list of TIN for 1,684 corporate taxpayers in CEP as of May 1991, we were able to match 1,650 TINs to BMF. For the 1,650 TINs, we obtained records for 20,564 corporate tax returns for various tax years ranging from 1961 to 1993. The record of a corporate income tax return generally remains on BMF for 5 years after all tax and payment disputes are resolved. We eliminated BMF records of tax returns that had no audit adjustment code. We also eliminated all unnecessary BMF audit transactions that were posted before fiscal year 1983. This step was necessary because AIMS data were not available before 1983.

To use BMF data, we applied our criterion of a "completed audit period." We defined this term as the period in which an IRS audit made at least one tax adjustment, followed by an audit release indicator. As the starting point, we used the last day of the previous audit period or, if not present, the date that IRS posted the return. The BMF audit release indicator identified the end of an audit. We added 30 calendar days to the audit

[1]We converted dates on BMF and AIMS from calendar dates to sequential dates for easier matches. To illustrate, using February 1, 1986, the calendar date is written month/day/year (02/01/86), and the sequential date shows the numerical position that date occupies in sequence for a 365-day year and is written year/day (86032).

release date to identify late posting audit adjustments. IRS also does this adjustment on its new Enforcement Revenue Information System (ERIS) to match tax adjustments to taxes recommended.

BMF showed more than one audit period for some returns. Multiple audit periods can occur when IRS finds it necessary to readjust the tax liability due to (1) a change in another period that affected the tax liability, such as a net operating loss (NOL) carryback or a taxpayer's filing of some other type of claim that was channeled through the audit process.

We also obtained complete AIMS records of corporate tax returns for CEP audits closed by IRS examiners from fiscal years 1983 through 1991, all years for which IRS had complete data tapes as of the end of fiscal year 1991. We wanted AIMS records for the earliest year possible because it generally takes 2 years from the date when a case is closed on AIMS for it to work its way through the appeals process to final resolution before the results appear on BMF. It takes about 6 years for litigated cases.

AIMS has the recommended tax adjustments for each closed audit. We dropped records that showed recommended taxes of $1 because some IRS districts use this amount if, for some reason, they must close the case on AIMS for a second time. As with BMF, AIMS had more than one record for a tax year for some CEP taxpayers. Ultimately, our AIMS database had records of 16,641 audits for 1,572 CEP taxpayers. IRS completed these audits from October 1, 1982, to September 30, 1991, and recommended additional taxes of $60.7 billion.

We matched the AIMS data to BMF using TINs and tax years, beginning with our earliest AIMS records. The BMF audit release indicator date had to be the same as or later than the AIMS closing date. We also matched 8,874 AIMS records having recommended tax increases, totalling $32.4 billion, to BMF. This match showed that IRS collected $7.1 billion of $32.4 billion, a collection rate of 22.08 percent after the appeals process.

## Collection Rate by Industry

To determine the collection rate by industry, we obtained a Statistics of Income Division (SOI) tape that provided industry codes by TIN. Some taxpayers have no industry code because not all TINs fit within an SOI industry group. We matched the industry codes with those tax returns that had the same codes on AIMS and BMF. This match allowed us to allocate 86 percent (about $28 billion) of the $32.4 billion in tax recommendations and related collections to 141 industries. Because high tax recommendations

have the greatest impact on the collection rate, we focused on the 10 industries for which IRS recommended the greatest amount of additional taxes.

## Collection Rate by District

To determine the collection rate by IRS district office, we sorted the $32.4 billion in recommended taxes (and related collections) by districts, using the two-digit district codes on related AIMS records. Because high tax recommendations have the greatest impact on the collection rate, we focused on the 10 districts with the highest tax recommendations.

## Collection Rate of Foreign-Controlled Corporations

To determine the collection rate for foreign-controlled corporations in CEP, we used IRS information that had been manually compiled by IRS' International Division. We matched TINs with tax returns that had the same TINs on AIMS and BMF. We were able to associate 9 percent of the $32.4 billion with 144 of the 206 CEP foreign-controlled corporations identified by IRS.

## Collection Rate of Litigated CEP Cases

To determine the collection rate of CEP cases that taxpayers pursued through litigation, we obtained data from IRS' Office of the Chief Counsel's management information system on large case disputes closed in litigation for fiscal years 1988 through 1992. The Chief Counsel's database showed the amount of taxes and penalties both before and after litigation. We matched our database of CEP TINs with the Chief Counsel's information to develop the collection rate.

# Other Analyses of BMF Data

We developed additional information on CEP taxpayers using data from our BMF database. The following BMF analyses excluded data on taxes recommended or any other data from AIMS. We analyzed

- transaction codes that identified tax payments from all sources to determine the percentage of total taxes paid by CEP corporations that audits generated;
- transaction codes for audits, litigation, criminal investigations, and claims to identify CEP audited returns that were not yet resolved;
- taxes due in order to compute the portion of CEP assessments unpaid; and
- transaction codes for penalties such as negligence, substantial understatement, and fraud to determine the number and amounts of enforcement penalties for CEP returns.

## Surveys and Case Studies

To determine what factors affected the percent of CEP-recommended taxes that are collected and the impact of IRS' recent changes to CEP, we surveyed IRS and taxpayer officials involved in a universe of 108 closed CEP cases and did in-depth case studies of 12 CEP cases, 9 of which had been appealed. We also interviewed 85 IRS officials in 7 districts and 5 regions.

### Surveys for 108 Closed CEP Cases

To identify factors affecting case settlement and the impacts of recent changes to CEP, we surveyed IRS case managers, team coordinators, appeals officers, and taxpayer representatives for 108 CEP cases. Each case had $30 million or more in taxes recommended and was closed by agreement with the Examination Division or closed out of Appeals in fiscal years 1989 through 1991. The threshold of $30 million in recommended taxes enabled us to focus on the largest cases with the greatest impact on the collection rate. The 108 cases in our universe involved $8.5 billion in taxes recommended by CEP teams. The threshold also produced a manageable universe size given the number and complexity of our four surveys.

The surveys asked about factors such as the sufficiency and quality of IRS staff, training, issue identification and development, taxpayer cooperation, and case delays. The team coordinator, appeals officers, and taxpayer representative surveys also asked about each case's three largest dollar issues. All four surveys asked for the respondents' opinions of recent changes to CEP and Appeals' Large Case Program. We also asked respondents if the case outcome would have been different had some recent changes to CEP been in effect at the time. To get information on IRS use of outside consultants, we did a follow-up telephone survey of respondents to our team coordinator questionnaire.

IRS' database on closed cases originally gave us a universe of 128 cases that met our criteria. After mailing the surveys, we received new information from respondents showing that 20 did not meet our selection criteria—for example, that cases were still open in Appeals, were closed before fiscal year 1989, or involved tax recommendations under $30 million. We also adjusted the universe sizes for each survey group when the designated respondent was no longer with the IRS or was no longer a taxpayer representative. The universe included cases closed by agreement at the audit level; by definition, these cases were excluded from the Appeals survey universe. Table I.1 shows the adjusted universe sizes for each of the four surveys.

**Table I.1: Adjusted Universe Sizes for Team Coordinator, Case Manager, Appeals Officer, and Taxpayer Surveys**

| | Team coordinator | Case manager | Appeals officer | Taxpayer |
|---|---|---|---|---|
| Original universe size | 128 | 128 | 128 | 128 |
| Cases not meeting universe criteria | 20 | 20 | 20 | 20 |
| Respondents not available | 19 | 34 | 10 | 12 |
| Cases agreed at the examination level | 0 | 0 | 15 | 0 |
| **Total unusable** | **39** | **54** | **45** | **32** |
| Adjusted universe size | 89 | 74 | 83 | 96 |

IRS provided the names of the case managers, team coordinators, and Appeals officers for each case. We mailed the case manager, team coordinator, and Appeals officer surveys in April 1992. We mailed a second one in May 1992 to those who did not respond initially. We asked case managers to send us the name and address of the taxpayer representative for that audit case. For cases in which the case manager was not available, we followed up to identify the taxpayer contact. We mailed the taxpayer surveys in August 1992 with a follow-up mailing in September 1992.

During October and November 1992, we telephoned taxpayers who still had not responded to encourage them to do so. Our response rates, based on usable responses received by January 1993, ranged from 76 percent for taxpayers to 97 percent for case managers. Table I.2 summarizes our response rates for each type of survey.

**Table I.2: Response Rates for Each Type of Survey**

| | Team coordinator | Case manager | Appeals officer | Taxpayer |
|---|---|---|---|---|
| Adjusted universe size | 89 | 74 | 83 | 96 |
| Surveys received | 85 | 72 | 78 | 73 |
| Response rate | 96% | 97% | 94% | 76% |

## Case Studies

To better understand the CEP audit and appeals processes and the factors that affect the collection rate, we did in-depth studies of 12 closed cases. We judgmentally selected the 12 cases from the universe of 108 cases that closed by agreement with Examination or Appeals in fiscal years 1989 to 1991 and that had recommended additional taxes of $30 million or more.

We used several criteria to select our cases for detailed review: (1) location of the auditing district, (2) availability of case documents and

IRS staff (cases closed from CEP after 1986), (3) collection rate for the audit, and (4) taxpayer's primary industry. On the basis of these criteria, we identified 26 cases available from which to choose our 12 case studies. (See table I.3).

**Table I.3: Total Number of Cases From the Four Districts We Visited, Selection Criteria by Collection Rate Range**

| | Collection rate | | | | |
|---|---|---|---|---|---|
| **District** | **0 to 9%** | **10 to 39%** | **40 to 99%** | **100%** | **Total** |
| Chicago | 0 | 0 | 0 | 5 | **5** |
| Houston | 1 | 3 | 1 | 0 | **5** |
| Los Angeles | 3 | 2 | 0 | 0 | **5** |
| Manhattan | 8 | 2 | 1 | 0 | **11** |
| **Total** | **12** | **7** | **2** | **5** | **26** |

We selected 12 cases from 4 IRS districts—Chicago, IL; Houston, TX; Los Angeles, CA; and Manhattan, NY. These four districts accounted for about 30 percent of the CEP's staff years and over 40 percent of the taxes recommended in fiscal year 1990. These cases also provided a cross section of the nation and industries, including financial services, food, petroleum, construction, and utilities as well as conglomerates.

The 12 cases used an average of 7 CEP audit staff years to complete. We could not obtain data on Appeals' staff years for these cases. However, the 1992 Appeals Process Review reported that Appeals' large cases averaged about one-half staff year and 2-1/2 calendar years to complete. The 12 cases accounted for $1.5 billion (18 percent) of the $8.5 billion of additional taxes recommended in our universe of 108 cases.

As shown in table I.4, our selection covered three of the four ranges of collection rates. We selected three cases closed at the Examination level and nine closed out of Appeals. Table I.4 shows the distribution of the 12 cases selected by rate and district.

**Table I.4: Collection Rates of GAO-Selected Cases, by District Visited**

| | Collection rate | | | | |
|---|---|---|---|---|---|
| **District** | **0 to 9%** | **10 to 39%** | **40 to 99%** | **100%** | **Total** |
| Chicago | 0 | 0 | 0 | 3 | **3** |
| Houston | 1 | 2 | 0 | 0 | **3** |
| Los Angeles | 2 | 1 | 0 | 0 | **3** |
| Manhattan | 1 | 2 | 0 | 0 | **3** |
| **Total** | **4** | **5** | **0** | **3** | **12** |

In our 12 cases, CEP teams raised at least 70 and as many as 280 issues. Given so many issues, we focused on the top three issues for each case in terms of dollars raised. Specifically, we reviewed which issues were involved, how they were developed, and how they were resolved. We used these 36 issues to structure our review in analyzing case documents and IRS databases.

For each case, we reviewed the following case documents:

- Revenue Agent Report (Form 4549)
- Reasons for Proposed Adjustments (Form 886A)
- Audit Plan (Form 4764A/B)
- CEP Case Status Report (Form 4451)
- Large Case Identity Record (Form 4143)
- Information Document request log, when available
- Examination Closing Record (Form 5344)
- Case Manager's activity log
- Records of opening and closing conferences, when available
- Specialists' reports, when applicable
- Corporate income tax return
- BMF transcripts

When applicable, we reviewed the following additional documents:

- Request for National Office technical advice
- Technical advice memorandums, Determination Letters, and Private Letter Rulings
- Taxpayer protests and Examination's related rebuttals
- Appeals' Audit Statement and Case Memorandum
- Appeals' transmittal letter to Joint Committee on Taxation (JCT)
- Closing agreements
- Examination dissents to Appeals' settlements

Using standard formats, we interviewed IRS and corporate officials for each case and IRS district, regional, and National Office staff responsible for CEP and Appeals management. Our interviews focused on the impacts of (1) CEP audit policies and practices, (2) Appeals' policies and practices, (3) the 1990 changes to CEP, (4) IRS' task force studies and process reviews, and (5) other relevant case details. Overall, we interviewed 85 people at least once—including 6 branch chiefs; 8 case managers; 13 team coordinators; 4 technical specialists; 6 industry specialists; 11 appeals

officers; and 26 other IRS district, regional, and national officials as well as 11 taxpayer representatives.

IRS national and district officials and corporate representatives reviewed our surveys and case study approach. They acknowledged the validity of our approach and surveys. District officials said our selected cases were typical of their CEP audits and appeals. In addition to IRS, we sent our draft report to three former IRS Commissioners, the Tax Executive Institute (which represents CEP taxpayers), and other knowledgeable parties. We incorporated their comments in the report where appropriate.

We did our work at the IRS National Office, 5 regional offices, and 7 of 59 district offices active in CEP. The five regions included Midwest, North Atlantic, Southeast, Southwest, and Western; the seven districts included Boston, Chicago, Houston, Los Angeles, Manhattan, New Orleans, and St. Louis.

# Survey of CEP Team Coordinators

U.S. General Accounting Office

## Coordinated Examination Program - Team Coordinator Questionnaire

### INTRODUCTION

The U.S. General Accounting Office (GAO), an investigative agency of Congress, is conducting a study of IRS's Coordinated Examination Program (CEP). The overall objective of our review is to determine what factors affect the rate at which taxes recommended by CEP revenue agents get assessed. We are surveying the audit teams who worked on each of the CEP cases which had recommended additional taxes of $30 million or more and were closed agreed in Exam or closed in Appeals from 1989 to 1991.

You have been selected to complete this survey due to your involvement with the corporate returns and the tax years indicated below. Because of your work on this case, your response to this survey will help us to identify all the factors which impact the resolution of CEP audits, both positively and negatively.

This questionnaire is confidential. The control number is included only to aid us in our follow-up efforts. Your response will be combined with those of other respondents and will be reported only in summary form. We will not identify specific CEP taxpayer information in our report.

Most of the questions in this questionnaire can be easily answered by checking boxes or filling in blanks. You will need to refer to the Revenue Agent Report (RAR) to complete some questions. Further, you may need to refer to other IRS workpapers or documents when answering certain questions on this questionnaire because of the lapse of time since this audit was closed.

This questionnaire should take about 2 hours to complete. If you have any questions concerning any part of this survey, please call Ms. Deborah Junod at (202) 272-7904.

Please return the completed questionnaire in the enclosed pre-addressed envelope within 2 weeks from the time you receive it. In the event the envelope is misplaced, the return address is:

U.S. General Accounting Office
General Government Division
Attn: Mr. James Fremming
441 G Street, N.W., Room 3126
Washington, D.C. 20548

Thank you for your assistance.

### Case Information:

***After completing the questionnaire, please remove the case information sticker before returning your completed questionnaire.***

**Total number of team coordinators responding = 85**

**I. RESPONDENT INFORMATION**

Please provide the following information:

Your current work telephone number - (_____)_____

Were you assigned to audit these CEP corporate returns during any part of the Exam timeframe shown on page 1? (CHECK ONE.) (8)

85 Yes --> **Please continue with question 1.**

-0 No --> **STOP: Do not continue if you were not assigned to this audit during the Exam timeframe shown above. Please return the questionnaire in the enclosed envelope.**

1. Please answer the following as it applied to you at the time you began the above audit: *(Enter "00" if none or under 1 year.)* (9-18)

**Years reported are means.**

a. Total number of years of IRS experience in the Examination Division N=85 __19__ Years

b. Number of years as a CEP team coordinator N=85 ..... __8__ Years

c. Number of years working on CEP examinations at positions other than team coordinator N=84 ..... __3__ Years

d. Total number of years of RA/IE experience examining corporations prior to being assigned to CEP examinations N=85 ..... __7__ Years

e. Number of years of RA/IE experience listed in d above that you were examining corporations with assets of $100 million or more N=85 ..... __3__ Years

2. What grade level were you when you were first assigned to the audit? (ENTER NUMBER.)

GS - _____ (19-20) or GM - _____ (21-22)

80 GS-13
5 Other

3. What was your educational background at the time you were assigned to this examination? (CHECK ALL THAT APPLY.) (23-29)

2 24 Hours of Accounting with no degree

67 BS/BA Accounting/Taxation

9 BS/BA Other (Specify: _____)

9 MA Accounting/Taxation

5 MA Other (Specify: _____)

- Ph.D. (Specify: _____)

2 Other (Specify: _____)

4. Were you a CPA when you were assigned to this examination? (CHECK ONE.) (30)

30 Yes

55 No

5. Did you receive the following training/experience in CEP procedures or issues before you were assigned to this audit or within 1 year of your assignment? (CHECK ONE BOX IN EACH ROW.) (31-35)

| | Yes (1) | No (2) | Not available at time (3) |
|---|---|---|---|
| a. Advanced corporate training or equivalent of Phase 5 | 79 | 2 | 3 |
| b. Team coordinator training | 22 | 33 | 30 |
| c. IRS training (3 days or more) related to the taxpayer's primary industry | 28 | 42 | 15 |
| d. Non-IRS training/seminars on any issues related to the taxpayer | 12 | 60 | 12 |
| e. Previous non-IRS experience related to the industry | 8 | 71 | 5 |

6. Was there any other training that you had not received that you felt you needed to improve your ability to conduct this CEP audit? (CHECK ONE.) (36)

57 No

28 Yes ---> Please explain:

_____

_____

7. At the time of this audit, was training on issues and industries provided jointly for Examination, Appeals, and Counsel? (CHECK ONE.) (37)

11 Yes

73 No

In your opinion, did/would this type of joint training improve the quality and timeliness of this audit in any way? (CHECK ONE.) (38)

57 Yes

25 No

Please explain your response.

_____

_____

_____

_____

8. At the time of this audit, did IRS obtain outside specialists to develop and deliver advanced training on complex technical and/or legal issues? (CHECK ONE.) (39)

11 Yes

73 No

In your opinion, did/would obtaining outside specialists to deliver advanced training improve the quality and timeliness of this audit in any way? (CHECK ONE.) (40)

57 Yes

24 No

Please explain your response.

_____

_____

_____

_____

## II. CASE MANAGEMENT

9. Overall, how satisfied or dissatisfied were you with the amount of time the case manager devoted to this case? (CHECK ONE.) (41)

33 Very satisfied
42 Generally satisfied
(SKIP TO QUESTION 11.)

10 Generally dissatisfied
- Very dissatisfied
(CONTINUE WITH QUESTION 10.)

10. In your opinion, what factors affected the time the case manager devoted to this audit? (CHECK ALL THAT APPLY.) (42-45)

2 Number of taxpayers/points in your inventory
7 Collateral duties
1 Logistical problems
6 Other (Please explain): _____

11. To what extent, if at all, were you involved with the following on this audit cycle? (CHECK ONE BOX IN EACH ROW.) (46-54)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) |
|---|---|---|---|---|---|
| a. The preparation of the audit plan | 67 | 8 | 2 | 2 | 5 |
| b. The selection of issues for audit | 67 | 8 | 3 | 1 | 5 |
| c. The review of workpapers | 45 | 24 | 6 | 5 | 4 |
| d. The opening conference with the taxpayer | 57 | 17 | 3 | 2 | 5 |
| e. The closing conference with the taxpayer | 61 | 19 | 2 | - | 2 |
| f. Interim meetings with the taxpayer | 63 | 18 | 4 | - | - |
| g. The review of proposed adjustments and tax computations | 68 | 16 | - | - | 1 |
| h. Resolution of problems between the taxpayer and revenue agents | 63 | 16 | 4 | - | 1 |
| i. Assistance in resolving difficult issues | 64 | 16 | 4 | - | 1 |

12. At the time of this audit, was a system such as electronic bulletin board or issue tracking available for case managers to communicate case managers on other districts on special industries and/or issues to ensure that all parties were equally informed? (CHECK ONE.) (55)

24 Do not know

29 Yes

31 No

In your opinion, did/would using such a system improve the development of issues in this case? (CHECK ONE.) (56)

42 Yes

17 No

Please explain your response.

_____ _____

_____ _____

_____

13. Overall, how satisfied or dissatisfied were you with management's involvement with the audit? (CHECK ONE BOX IN EACH ROW.) (57-60)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. District Director | 6 | 1 | 15 | - | 1 | 62 |
| b. Chief or Assistant Chief of Examination | 7 | 2 | 15 | 5 | 3 | 53 |
| c. Branch Chief | 21 | 13 | 25 | 3 | 4 | 19 |
| d. Case Manager | 44 | 21 | 12 | 6 | 1 | 1 |

14. At the time of this audit, was your district office management involved in the planning of the audit and/or requesting support examinations in this case? (CHECK ONE.) (61)

30 Yes

55 No

In your opinion, did/would this type of district office involvement ensure better planning of this audit or more thorough support examinations? (CHECK ONE.) (62)

28 Yes

52 No

Please explain your response.

_____

_____

**III. STAFFING/SPECIALISTS**

15. At any time during the audit, did you have insufficient revenue agent staff? (CHECK ONE.) (63)

22 Yes

63 No

16. Did turnover in staff or specialists negatively impact the development of issues? (CHECK ONE.) (64)

25 Yes

60 No

***If your responses to both questions 15 and 16 are "No", skip to question 18.***
***If you answered "Yes" to either question 15 or 16, continue with question 17.***

17. What were the reasons that your staffing level was insufficient or why staff turned over? (CHECK ALL THAT APPLY.) (65-72)

11 Staff were not available when the audit began

13 Staff were temporarily diverted to other activities/ collateral duties during the course of the audit

- Staff were permanently removed due to P-4-5 rotation policy

1 Staff were permanently removed from audit due to incompatibility

15 Staff were permanently removed from audit due to other reasons

3 My request(s) for additional staff to be assigned was denied

2 My request(s) for additional staff to be assigned was granted, but the staff was (were) assigned later than appropriate

14 Other (Please specify) _____

_____

18. In your opinion, were the services of specialists obtained when you felt they were needed to help you develop your issues? (CHECK ONE.) (73)

68 Yes, for all my issues --> (SKIP TO QUESTION 22.)

14 Yes, in some cases

2 No

(CONTINUE WITH QUESTION 19.)

19. In your opinion, which specialist services were needed but were not obtained? (CHECK ALL THAT APPLY.) (74-82)

5 Outside consultant(s)
4 Industry/Issue specialist(s)
3 Economist(s)
4 Engineer(s)
2 Computer audit specialist(s)
3 International specialist(s)
- EPEO specialist(s)
- Payroll specialist(s)
1 Excise specialist(s)
1 Counsel (83-84)
2 Other - Specify: _____ (85-86)

20. What were the reason(s) that the needed specialists were not obtained? (CHECK ALL THAT APPLY.) (87-90)

- District office management denied the request(s)
4 The needed specialists were not available to the district
- The needed specialists could not be borrowed from another district
11 Other - Specify: _____

21. For those specialists that were needed for this audit cycle but were not obtained, to what extent, if at all, did not having the services of this (these) specialist(s) negatively impact the results of the audit? (CHECK ONE BOX IN EACH ROW. CHECK BOX 1, "N/A" IF THE SPECIALIST WAS NOT NEEDED OR WAS NOT OBTAINED ON THE AUDIT.) (91-99)

| | Not Applic-able (1) | To a very great extent (2) | To a great extent (3) | To a moderate extent (4) | To some extent (5) | To little or no extent (6) | No basis to judge (7) |
|---|---|---|---|---|---|---|---|
| a. Outside consultant | 10 | - | - | 3 | - | - | 2 |
| b. Industry/Issue specialist | 9 | 1 | 1 | 1 | 2 | - | 1 |
| c. Economist | 11 | 1 | - | 1 | 1 | - | - |
| d. Engineer | 9 | 1 | 2 | 1 | 1 | - | - |
| e. Computer audit specialist | 11 | - | 1 | - | 1 | 1 | 1 |
| f. International specialist | 11 | 2 | - | - | - | - | 1 |
| g. EPEO specialist | 12 | - | - | - | 1 | - | 1 |
| h. Counsel | 11 | - | 2 | - | 1 | - | - |
| i. Other (Please specify) N=8 | | | | | | | |

Repeat ID - 2 (1-7)

22. In your opinion, what was the quality of work performed by the following individuals on this audit cycle? (CHECK ONE BOX IN EACH ROW. CHECK BOX 1, "N/A" IF THE POSITION WAS NOT USED ON THE AUDIT.) (8-19)

| | Not Applic-able (1) | Excellent (2) | Good (3) | Adequate or marginal (4) | Poor (5) | Very poor (6) | No basis to judge (7) |
|---|---|---|---|---|---|---|---|
| a. Case Manager | 1 | 33 | 33 | 14 | 1 | - | 1 |
| b. Other Exam revenue agents | 5 | 23 | 47 | 8 | 1 | - | - |
| c. Computer audit specialist | 2 | 28 | 41 | 11 | 2 | - | - |
| d. Industry/issue specialist | 29 | 13 | 27 | 8 | 5 | 1 | 1 |
| e. Engineer | 8 | 22 | 25 | 21 | 4 | 2 | 1 |
| f. International specialist | 12 | 29 | 30 | 8 | 2 | 1 | 3 |
| g. Economist | 64 | 6 | 6 | 3 | - | 2 | 3 |
| h. Outside consultant | 76 | 1 | 3 | - | - | - | 4 |
| i. EPEO specialist | 49 | 6 | 13 | 8 | 1 | 1 | 4 |
| j. Appeals | 22 | 7 | 16 | 11 | 6 | 9 | 13 |
| k. Counsel | 38 | 12 | 6 | 7 | - | 2 | 17 |
| l. Other (Please specify) N=20 | | | | | | | |

23. Did an industry or an issue specialization program exist at the time of this audit? (CHECK ONE.) (20)

75 Yes

10 No

In your opinion, did/would this program improve the audit team's ability to develop complex organizational or technical issues? (CHECK ONE.) (21)

63 Yes

20 No

Please explain your response.

_____

_____

_____

## IV. CASE DELAYS

24. Was this case closed out of Exam later than planned? (CHECK ONE.) (22)

57 Yes ---> (CONTINUE WITH QUESTION 25.)

27 No ---> (SKIP TO QUESTION 26.)

25. To what extent, if at all, did the following factors cause delays in closing the case in Exam? (CHECK ONE BOX IN EACH ROW.) (23-34)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) |
|---|---|---|---|---|---|
| a. Obtaining staff or specialists | 2 | 2 | 8 | 10 | 35 |
| b. Turnover in staff or specialists | 7 | 4 | 8 | 7 | 32 |
| c. Obtaining technical advice | 2 | 1 | 3 | 2 | 48 |
| d. Receiving specialists' reports | 6 | 3 | 3 | 8 | 36 |
| e. Issuing a summons | 1 | 3 | 1 | - | 50 |
| f. Diverting staff or specialist to collateral duties | 6 | 1 | 13 | 8 | 29 |
| g. Obtaining information from the taxpayer | 24 | 20 | 6 | 4 | 4 |
| h. Obtaining access to the taxpayer's computer file | 2 | 7 | 6 | 8 | 35 |
| i. Having access to the taxpayer's representative | - | 2 | 7 | 5 | 44 |
| j. Delays by the taxpayer in starting the examination | 3 | 4 | - | 5 | 45 |
| k. Delays by IRS in starting the examination | - | - | 1 | 5 | 50 |
| l. Other (Please specify) N=23 | | | | | |

26. If the taxpayer caused delays by not supplying the information requested on the IDR's or allowing access to computer files in a timely manner (or at all), what means were used to obtain the information? (CHECK ALL THAT APPLY.) (35-39)

13 Not applicable, all requested information was received in a timely manner

---

5 Summons

64 Informal means such as meetings between IRS management and the taxpayer

56 Follow-up IDR's

12 Other - Please specify: _____

**V. INFORMATION DOCUMENT REQUESTS**

27. Was all needed information requested on the IDR's received before the case was closed in exam? (CHECK ONE.) (40)

60 Yes

24 No

28. What percentage of the total number of IDR's requesting new information were issued within 90 days of the close of the audit? (ENTER PERCENT.)

_____ Percent (41-43)

25 0 percent
3 1 percent
4 2 percent
6 5 percent
1 10 percent
1 15 percent
1 25 percent
1 80 percent
1 100 percent

42 Do not know (44)

29. Overall, how satisfied or dissatisfied were you with the following? (CHECK ONE BOX IN EACH ROW.) (45-54)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. The timeliness of taxpayer responses to IDR's | 9 | 22 | 11 | 24 | 19 | - |
| b. The completeness of the information provided by taxpayer in response to IDR's | 12 | 29 | 9 | 24 | 11 | - |
| c. The relevance of the information provided by taxpayer in response to IDR's | 14 | 39 | 16 | 13 | 3 | - |
| d. That IDR's were issued in a timely manner | 50 | 29 | 5 | 1 | - | - |
| e. That IDR's were clearly and concisely prepared | 47 | 34 | 4 | - | - | - |
| f. That the information requested was obtainable by the taxpayer (e.g., information not available because of a merger, too old, etc.) | 31 | 29 | 5 | 11 | 2 | 4 |
| g. The overall cooperation of taxpayer to IDR's | 16 | 28 | 10 | 19 | 10 | - |

30. To the best of your knowledge, did the taxpayer provide information during the appeals process which Exam had requested but was not received? (CHECK ONE.) (55)

26 Yes ---> (CONTINUE WITH QUESTION 31.)

20 No
26 Do not know
(SKIP TO QUESTION 32.)

13 Not applicable, agreed case ---> (SKIP TO QUESTION 34.)

31. Did Appeals involve Exam further in case development because the taxpayer provided additional information, filed a claim, or raised new issues? (CHECK ONE.) (56)

4 Yes, Appeals relinquished jurisdiction of the case back to Exam

17 Yes, Appeals involved Exam in further case development without relinquishing jurisdiction of the case

5 No

- Do not know

32. Did the taxpayer provide information during the appeals process which Exam had or had not requested that reduced the proposed tax deficiency? (CHECK ONE.) (57)

26 Yes

14 No

31 Do not know

33. Did your district office management such as the District Director, Chief or Assistant Chief (Exam), or Branch Chief meet with high level taxpayer officials during this audit? (CHECK ONE.)

(58)

34 Yes ---> Please specify the position or role of those who met with high level taxpayer officials.

_____ (59)

37 No ---> In your opinion, would increased managerial oversight have improved the taxpayer's level of cooperation (e.g., prompt response to IDR's or meetings to discuss disagreements between the taxpayer and IRS)? (60)

8 Yes

30 No

Please explain your response.

_____

_____

_____

## VI. TECHNICAL ADVICE

34. Was any formal technical advice still in effect from a prior audit cycle? (CHECK ONE.) (61)

10 Yes

64 No

11 Do not know

35. Was formal technical advice requested on this cycle? (CHECK ONE.) (62)

8 Yes

75 No

2 Do not know

**If formal technical advice was not still in effect from a prior audit cycle and/or was not requested for this audit cycle, please skip to question 41.**

36. How long did it take to receive a response to the request for formal technical advice? (ENTER NUMBER OF MONTHS.)

_____ Months (63-64) or - Do not know (65)

N=3
3 Months
30 Months
41 Months

37. Was the formal technical advice followed in full by Exam, Counsel, Appeals, and by the taxpayer? (CHECK ONE BOX IN EACH ROW.) (66-69)

| | Yes (1) | No (2) | Not applicable (3) |
|---|---|---|---|
| a. Followed by Exam | 3 | - | - |
| b. Followed by Counsel | - | - | 2 |
| c. Followed by Appeals | - | 1 | 1 |
| d. Followed by the taxpayer | 1 | 1 | - |

38. In your opinion, how helpful or not was the formal technical advice for developing issues and resolving disputes with the taxpayer? (CHECK ONE BOX IN EACH ROW.) (70-71)

| | Very helpful (1) | Somewhat helpful (2) | Of little or no help (3) | Do not know (4) |
|---|---|---|---|---|
| a. For developing issues | 2 | - | 1 | - |
| b. For resolving disputes with taxpayer | 1 | - | 1 | - |

39. Did the taxpayer request a private letter ruling(s) or determination letter(s) on any issue during these tax years? (CHECK ALL THAT APPLY.) (72-75)

1 Yes, a private letter ruling or rulings

1 Yes, a determination letter or letters

1 Neither a private letter ruling or determination letter

1 Do not know

40. Was legal and/or technical assistance provided from the start of this audit to educate the audit team on matters of tax law and policy or overall issue development? (CHECK ONE.) (76)

1 Yes

3 No

In your opinion, did/would this assistance improve the development of issues in this case? (CHECK ONE.) (77)

- Yes

2 No

Please explain your response.

_____

_____

_____

**VII. ADDITIONAL INFORMATION ABOUT THE CASE**

41. Did this CEP taxpayer file a consolidated corporate return? (CHECK ONE.) (78)

81 Yes

4 No

- Do not know

42. In general, how satisfied or dissatisfied were you with the following factors during the audit? (CHECK ONE BOX IN EACH ROW.) (79-90)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | Not Applicable (6) |
|---|---|---|---|---|---|---|
| a. Access to needed IRS supplies | 30 | 31 | 12 | 4 | 8 | - |
| b. Access to IRS research material | 26 | 27 | 12 | 16 | 4 | - |
| c. Access to professional industry manuals | 13 | 10 | 22 | 16 | 14 | 10 |
| d. Access to IRS computers | 29 | 19 | 8 | 4 | 6 | 19 |
| e. Access to IRS printers | 29 | 17 | 9 | 4 | 4 | 22 |
| f. Access to IRS office support staff | 26 | 22 | 16 | 8 | 2 | 10 |
| g. Space provided by the taxpayer for the audit team | 37 | 26 | 6 | 12 | 4 | - |
| h. Access to taxpayer's supplies | 27 | 6 | 12 | 1 | 6 | 33 |
| i. Access to taxpayer's library or other public research materials | 30 | 23 | 6 | 10 | 9 | 7 |
| j. Access to taxpayer's computers | 17 | 11 | 18 | 8 | 8 | 23 |
| k. Access to taxpayer's printers | 15 | 9 | 15 | 3 | 8 | 35 |
| l. Access to taxpayer's photocopiers | 53 | 15 | 5 | 7 | 5 | - |

43. Did the taxpayer agree to extend the date on the statute of expiration? (CHECK ONE.) (91)

2 No

83 Yes ---> Was/Were the extension(s) granted sufficient to allow you to develop all the issues you believed needed to be developed prior to completing the audit? (CHECK ONE.) (92)

79 Yes

2 No

44. Did the taxpayer disclose controversial issues at the beginning of the audit? (CHECK ONE.) (93)

51 No

30 Yes --> Was this disclosure specific to the issues that should be examined? (CHECK ONE.) (94)

26 Yes

4 No

45. Did the taxpayer provide you with a list of adjustments to taxable income or credits for those tax years being audited? (CHECK ONE.) (95)

47 Yes ---> (CONTINUE WITH QUESTION 46.)

37 No --> (SKIP TO QUESTION 47.)

46. Who did the adjustments favor? (CHECK ONE.) (96)

- IRS only

6 The taxpayer only

40 Both IRS and the taxpayer

1 Do not know

Repeat ID - 3 (1-7)

## VII. CASE CLOSINGS

47. Please provide the following CEP recommended tax results separately for each tax year included in this case. Please be sure to enter the tax year at the top of each column. *(You will need the Revenue Agent Report to complete this table.)*

***Please round to the nearest dollar.***

| | Primary Tax Years (As shown on page 1.) | | |
|---|---|---|---|
| | (8-9) Tax Year 19____ | (10-11) Tax Year 19____ | (12-13) Tax Year 19____ |
| a. Total net adjustments to taxable income per Exam | $ _____ | $ _____ | $ _____ |
| b. Total net adjustments to tax credits per Exam | $ _____ | $ _____ | $ _____ |
| c. Total taxable income per Exam | $ _____ | $ _____ | $ _____ |
| d. Corrected tax liability per Exam | $ _____ | $ _____ | $ _____ |
| e. Less: Tax credits per Exam | $ _____ | $ _____ | $ _____ |
| f. Plus: Recapture of prior year ITC per Exam | $ _____ | $ _____ | $ _____ |
| g. Total corrected tax liability per Exam | $ _____ | $ _____ | $ _____ |
| h. Less: Total tax shown on return or as previously adjusted | $ _____ | $ _____ | $ _____ |
| i. Deficiency/(Overassessment) per Exam | N=76 (14-23) Mean = $22,391,102 Range = $-59,468,005 to $102,415,024 | N=79 (24-33) Mean = $286,797,297 Range = $-305,897 to $171,786,866 | N=38 (34-43) Mean = $29,145,249 Range = $-382,037 to $116,779,138 |
| j. Total penalties per Exam List Type: | (44-51) N=6 Mean = $2,976,955 | (52-59) N=4 Mean = $9,215,622 | (60-67) N=3 Mean = $2,319,279 |
| k. Claims for tax decrease considered during examination | N=55 (68-77) Mean = $6,182,525 Range = $0 to $87,504,859 | N=57 (78-87) Mean = $6,358,570 Range = $0 to $145,175,185 | N=23 (88-97) Mean=$2,726,786 Range = $0 to $16,675,131 |
| l. Corporation Application for Tentative Refund (Form 1139) considered during Exam process | N=51 (98-107) Mean = $9,774,100 Range = $0 to $150,149,391 | N=57 (108-117) Mean = $17,300,022 Range = $0 to $613,500,377 | N=23 (118-127) Mean = $15,854,364 Range = $0 to $109,171,450 |

Continued on next page

**Question 47 (Continued)** Repeat ID - 4 (1-7)

Be sure to enter the tax year at the top of each column.

***Please round to the nearest dollar.***

| | Carry Over Years (Forward/Backward) | | |
|---|---|---|---|
| | (8-9) Tax Year 19____ | (10-11) Tax Year 19____ | (12-13) Tax Year 19____ |
| a. Total net adjustments to taxable income per Exam | $ _____ | $ _____ | $ _____ |
| b. Total net adjustments to tax credits per Exam | $ _____ | $ _____ | $ _____ |
| c. Total taxable income per Exam | $ _____ | $ _____ | $ _____ |
| d. Corrected tax liability per Exam | $ _____ | $ _____ | $ _____ |
| e. Less: Tax credits per Exam | $ _____ | $ _____ | $ _____ |
| f. Plus: Recapture of prior year ITC per Exam | $ _____ | $ _____ | $ _____ |
| g. Total corrected tax liability per Exam | $ _____ | $ _____ | $ _____ |
| h. Less: Total tax shown on return or as previously adjusted | $ _____ | $ _____ | $ _____ |
| i. Deficiency/(Overassessment) per Exam | N=23 (14-23)<br>Mean = $6,469,657<br>Range = $-7,887,532 to $40,187,338 | N=16 (24-33)<br>Mean = $4,535,846<br>Range = $-31,297,792 to $56,272,281 | N=12 (34-43)<br>Mean = $6,398,877<br>Range = $-4,402,462 to $37,477,688 |
| j. Total penalties per Exam List Type: | (44-51)<br>None | (52-59)<br>N=1 | (60-67)<br>N=1 |
| k. Claims for tax decrease considered during examination | N=13 (68-77)<br>Mean = $7,412,578<br>Range = $0 to $83,265,754 | N=8 (78-87)<br>Mean = $2,417,904<br>Range = $0 to $19,343,228 | N=7 (88-97)<br>Mean = $7,836,381<br>Range = 0 to $46,415,065 |
| l. Corporation Application for Tentative Refund (Form 1139) considered during Exam process | N=16 (98-107)<br>Mean = $10,562,558<br>Range = $0 to $83,785,039 | N=10 (108-117)<br>Mean = $11,791,867<br>Range = $0 to $54,962,636 | N=8 (118-127)<br>Mean = $7,428,067<br>Range = $0 to $35,780,396 |

Repeat ID - 5 (1-7)

48. Please provide the following information on the three top dollar adjustments to taxable income/credits in this case.

| | Issue #1 | Issue #2 | Issue #3 |
|---|---|---|---|
| a. IRC | _____ | _____ | _____ |
| b. Adjustment to: *(Check one per issue.)* | (8)<br>72 Taxable income<br>7 Credit | (9)<br>68 Taxable income<br>12 Credit | (10)<br>66 Taxable income<br>11 Credit |
| c. Dispute involved: *(Check one or both.)* | (11-12)<br>65 Interpretation of law<br>46 Based on merit/facts | (13-14)<br>61 Interpretation of law<br>44 Based on merit/facts | (15-16)<br>48 Interpretation of law<br>39 Based on merit/facts |
| d. Type of adjustment *(Check all that apply.)* | (17-23)<br>16 Unreported income<br>29 Overstated deductions<br>39 Timing<br>7 Valuation<br>11 Allocation<br>1 Whipsaw<br>18 Other (Specify)<br>_____ | (24-30)<br>8 Unreported income<br>37 Overstated deductions<br>27 Timing<br>11 Valuation<br>7 Allocation<br>1 Whipsaw<br>18 Other (Specify)<br>_____ | (31-37)<br>12 Unreported income<br>30 Overstated deductions<br>22 Timing<br>11 Valuation<br>11 Allocation<br>- Whipsaw<br>20 Other (Specify)<br>_____ |
| e. Original adjustment proposed by Exam | N=82 (38-48)<br>Mean = $115,271,508<br>Range = $-26,511,591 to $1,941,237,337 | N=82 (49-59)<br>Mean = $65,644,009<br>Range = $-156,114,992 to $1,772,956,719 | N=81 (60-70)<br>Mean = $30,169,295<br>Range = $-346,803 to $266,707,891 |
| f. Amount of signed formal agreement reached between Exam and the taxpayer | N=73 (71-81)<br>Mean = $15,868,198<br>Range = $-26,511,591 to $180,000,000 | N=74 (82-92)<br>Mean = $3,029,545<br>Range = $-156,114,992 to $56,787,710 | N=75 (93-103)<br>Mean = $9,271,378<br>Range = $-2,766,411 to $219,317,285 |

Repeat ID - 6 (1-7)

49. Were these issues Exam Coordinated Issues (ECI's)? (CHECK ONE BOX IN EACH ROW.) (8-10)

| | Yes (1) | No (2) | The ECI program didn't exist at that time (3) | Do not know (4) |
|---|---|---|---|---|
| a. Issue #1 | 19 | 52 | 5 | 3 |
| b. Issue #2 | 17 | 54 | 5 | 3 |
| c. Issue #3 | 11 | 59 | 5 | 3 |

50. For these three issues, was there a need for a specialist or outside consultant that was not obtained? (CHECK ONE.) (11)

75 No

(SKIP TO QUESTION 52.)

4 Do not know

6 Yes, there was a need but they were not obtained ---> *Please list the positions not used that you feel should have been used but were not, and check the issue number(s).*

| Position Not Used | Issue Number | | |
|---|---|---|---|
| 3 Economist | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 (14) |
| 2 Engineer | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 (17) |
| 1 Actuary | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 (20) |
| 1 Industry specialist | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 (23) |
| _____ | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 (26) |
| _____ | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 (29) |

51. For any of the three issues that you identified that were protested on this case, which of the following factors do you feel caused the taxpayer to protest the issue? (**CHECK YES OR NO FOR EACH ROW FOR EACH ISSUE.** IF THE ISSUES WERE AGREED, CHECK THE NOT APPLICABLE BOX IN THE FIRST ROW AND GO ON TO THE NEXT ISSUE.)

**We did not analyze responses to this question due to an erroneous skip instruction on question 50.**

| | Issue #1 | | Issue #2 | | Issue #3 | |
|---|---|---|---|---|---|---|
| | Yes (1) | No (2) | Yes (1) | No (2) | Yes (1) | No (2) |
| If issue agreed, check box under the agreed issue . . . | 1. ☐ N/A | | 1. ☐ N/A | | 1. ☐ N/A | |
| a. Disagreement over interpretation of the law | | | | | | |
| b. Disagreement over facts | | | | | | |
| c. Amount supported by taxpayer documentation exceeds the amount allowed by Exam | | | | | | |
| d. Disagreement on timing issues | | | | | | |
| e. Disagreement on valuation issues | | | | | | |
| f. Disagreement on allocation issues | | | | | | |
| g. Disagreement on whipsaw issues | | | | | | |
| h. Appeals settlement on prior cases | | | | | | |
| i. Appeals settlement of same issue for a different taxpayer | | | | | | |
| j. Other (Specify) _____ | | | | | | |
| k. Other (Specify) _____ | | | | | | |

**Please note:** The following questions pertain to the overall case results.

52. Did you secure a signed formal agreement from the taxpayer on the proposed adjustments at the time the case was closed out of Exam? (CHECK ONE.) (66)

13 Yes, the taxpayer agreed to all issues (full agreement)

23 Yes, the taxpayer agreed to some issues (partial agreement)

49 No

- Do not remember

53. If the case manager would have had settlement authority (Delegation Order 236) for "rollover" and "recurring" issues for which Appeals had already established a settlement practice based on the facts of the issue, do you believe this would have had a positive effect, no effect, or a negative effect on the recovery rate of these returns? (CHECK ONE.) (67)

28 A positive effect on the recovery rate

38 No effect on the recovery rate

4 A negative effect on the recovery rate

15 Do not know

54. Do you believe case managers or other Examination officials should be actively attempting to settle more audit issues based on the merits (facts) of a case? (CHECK ONE.) (68)

64 Yes

Please explain: _____

18 No

_____

_____

55. How satisfied or dissatisfied were you with Appeals overall settlement of this audit cycle? (CHECK ONE.) (69)

5 Very satisfied

17 Generally satisfied (SKIP TO QUESTION 57.)

15 Neither satisfied nor dissatisfied

13 Generally dissatisfied

14 Very dissatisfied (CONTINUE WITH QUESTION 56.)

20 No basis to judge/Agreed case ---> (SKIP TO QUESTION 59.)

56. Did you use the dissent process to protest Appeal's settlement of this case? (CHECK ONE.) (70)

2 Yes

24 No

57. Did Examination and Counsel discuss the taxpayer's protest with Appeals to ensure that Appeals was able to consider all of the relevant facts in this case? (CHECK ONE.) (71)

35 Yes

38 No

In your opinion, to what extent, if at all, did/would the discussion enhance Appeals' ability to sustain dollars recommended by Exam? (CHECK ONE.) (72)

8 To a very great extent

11 To a great extent

11 To a moderate extent

10 To some extent

19 To little or no extent

14 Do not know

Please explain your response.

_____

_____

_____

58. Did appeals discuss the final resolution of unagreed issues to provide Examination with information for auditing the subsequent tax returns for this taxpayer? (CHECK ONE.)

(73)

32 Yes --> If yes, was the feedback provided to the revenue agents working on the subsequent audit? (CHECK ONE.) (74)

28 Yes

Please explain: _____

3 No

41 No --> If no, in your opinion, would this feedback have improved the planning or the timeliness of subsequent audit cycles? (CHECK ONE.) (75)

16 Yes

Please explain: _____

23 No

## IX. OVERALL PERCEPTION OF AUDIT CYCLE

59. Regarding the team collectively, how satisfied or dissatisfied were you with the following factors on this audit? (CHECK ONE BOX IN EACH ROW.) (76-90)

| | Very satisfied (1) | Generally satisfied (2) | Neither satisfied nor dissatisfied (3) | Generally dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Number of staff assigned to the audit | 36 | 36 | 5 | 7 | - | - |
| b. Number of staff days allotted to the audit | 33 | 40 | 7 | 4 | - | - |
| c. Adequacy of the team's experience and skills in auditing large corporations | 31 | 40 | 11 | 3 | - | - |
| d. Adequacy of the team's knowledge in tax laws, rules and regulations | 34 | 42 | 6 | 3 | - | - |
| e. Adequacy of the team's knowledge of the industry involved in the audit | 17 | 38 | 20 | 8 | 1 | 1 |
| f. Adequacy of support audits | 4 | 16 | 7 | 6 | 2 | 47 |
| g. Level of cooperation of team members with one another | 37 | 41 | 1 | 4 | - | 1 |
| h. Level of cooperation you received from the team | 42 | 37 | 4 | - | - | 2 |
| i. Level of cooperation between the taxpayer and the team members | 10 | 46 | 12 | 10 | 7 | - |
| j. Length of time it took to complete the audit | 10 | 32 | 19 | 17 | 7 | - |
| k. Extent to which team members fully developed the issues assigned to them | 22 | 51 | 9 | 3 | - | - |
| l. Extent to which team members accurately developed the issues assigned to them | 22 | 55 | 4 | 2 | 2 | - |
| m. Extent to which management was involved in the case | 20 | 36 | 16 | 9 | 2 | 2 |
| n. Other (Please specify) N=6 | | | | | | |
| o. Other (Please specify) N=4 | | | | | | |

60. How satisfied or dissatisfied were you with the overall quality of the performance of the IRS team (including specialists) during the audit of this taxpayer identified on page 1 of this questionnaire? (CHECK ONE.) (91)

31 Very satisfied

50 Generally satisfied

2 Neither satisfied nor dissatisfied

2 Generally dissatisfied

- Very dissatisfied

61. How satisfied or dissatisfied were you with the overall attitude/level of cooperation of the taxpayer? (CHECK ONE.) (92)

7 Very satisfied

37 Generally satisfied

13 Neither satisfied nor dissatisfied

24 Generally dissatisfied

4 Very dissatisfied

62. In your opinion, has the establishment of a National CEP Director had a positive impact, no impact, or a negative impact on program development, oversight, and/or evaluation within CEP? (CHECK ONE.) (93)

18 A positive impact

13 No impact

11 A negative impact

42 Do not know

Please explain your response:

_____

_____

_____

63. In your opinion, has the establishment of Regional CEP Managers had a positive impact, no impact, or a negative impact on program development, oversight, and/or evaluation within CEP? (CHECK ONE.) (94)

11 A positive impact

18 No impact

6 A negative impact

49 Do not know

Please explain your response:

_____

_____

_____

64. In your opinion, has the establishment of a multi-functional National Policy Board had a positive impact, no impact, or a negative impact on promoting taxpayer cooperation through improved coordination between Examination, Appeals, International and Counsel? (CHECK ONE.) (95)

20 A positive impact

55 No impact

2 A negative impact

65. In your opinion, would the development of standard goals and measures for Examination, Appeals, International, and Counsel have had a positive effect, no effect, or a negative effect on this audit? (CHECK ONE.) (96)

40 A positive effect

29 No effect

15 A negative effect

66. In your opinion, would CEP quality peer reviews have improved this audit in any way? (CHECK ONE.) (97)

11 Yes --> Please explain:

_____

_____

_____

71 No

67. Please briefly discuss in the space below what you feel was the most positive thing about this audit as well as the most negative thing about this audit.

**Positive:** N=78 _____ (98)

_____

_____

_____

_____

**Negative:** N=74 _____ (99)

_____

_____

_____

_____

68. Please list any other recent changes to the Large Case Program which would have impacted on the resolution of these returns had they been in effect at the time these returns were worked. Also, describe in what ways they would have impacted the resolution of the returns. (100)

Change: _____

Impact on case: _____

_____

_____

_____

Change: _____

Impact on case: _____

_____

_____

_____

Change: _____

Impact on case: _____

_____

_____

_____

69. Are there any other changes to the CEP/Large Case Program that you would like to suggest here? (101)

N=57

_____

_____

_____

_____

_____

_____

_____

_____

_____

Thank you for your assistance. Please return the questionnaire in the pre-addressed envelope.

Thank you.

# Survey of CEP Case Managers

U.S. General Accounting Office

## Coordinated Examination Program - Case Manager Questionnaire

### INTRODUCTION

The U.S. General Accounting Office (GAO), an investigative agency of Congress, is conducting a study of IRS's Coordinated Examination Program (CEP). The overall objective of our review is to determine what factors affect the rate at which taxes recommended by CEP revenue agents get assessed. We are surveying the audit teams who worked on each of the CEP cases which had recommended additional taxes of $30 million or more and were closed agreed in Exam or closed in Appeals from 1989 to 1991.

You have been selected to complete this survey due to your involvement with the corporate returns and the tax years indicated below. Because of your work on this case, your response to this survey will help us to identify all the factors which impact the resolution of CEP audits, both positively and negatively.

This questionnaire is confidential. The control number is included only to aid us in our follow-up efforts. Your response will be combined with those of other respondents and will be reported only in summary form. We will not identify specific CEP taxpayer information in our report.

Most of the questions in this questionnaire can be easily answered by checking boxes or filling in blanks. You will need to refer to the Revenue Agent Report (RAR) to complete some questions. Further, you may need to refer to other IRS workpapers or documents when answering certain questions on this questionnaire because of the lapse of time since this audit was closed.

This questionnaire should take about 2 hours to complete. If you have any questions concerning any part of this survey, please call Ms. Deborah Junod at (202) 272-7904.

Please return the completed questionnaire in the enclosed pre-addressed envelope within 2 weeks from the time you receive it. In the event the envelope is misplaced, the return address is:

U.S. General Accounting Office
General Government Division
Attn: Mr. James Fremming
441 G Street, N.W., Room 3126
Washington, D.C. 20548

Thank you for your assistance.

**Case Information:**

***After completing the questionnaire, please remove the case information sticker before returning your completed questionnaire.***

**Total number of case managers responding = 72**

**I. RESPONDENT INFORMATION**

Please provide the following information:

Your current work telephone number - (_____)_____

Were you assigned to audit these CEP corporate returns during any part of the Exam timeframe shown on page 1? (CHECK ONE.) (8)

72 Yes --> **Please continue with question 1.**

- No --> **STOP: Do not continue if you were not assigned to this audit during the Exam timeframe shown above. Please return the questionnaire in the enclosed envelope.**

1. Please answer the following as it applied to you at the time you began the above audit: *(Enter "00" if none or under 1 year.)* (8-18)

**Years reported are means.**

a. Total number of years of IRS experience in the Examination Division N=71 __22__ Years

b. Number of years as a CEP case manager N=72 . . . . . __7__ Years

c. Number of years working on CEP examinations at positions other than case manager N=72 . . . . . __3__ Years

d. Total number of years of RA/IE experience examining corporations prior to being assigned to CEP examinations N=72 . . . . . __8__ Years

e. Number of years of RA/IE experience listed in d above that you were examining corporations with assets of $100 million or more N=71 . . . . . __3__ Years

2. What grade level were you when you were first assigned to the audit? (ENTER NUMBER.)

GS - _____ (19-20) or GM - _____ (21-22)

9 GS-14
57 GM-14
6 Other

3. What was your educational background at the time you were assigned to this examination? (CHECK ALL THAT APPLY.) (23-29)

2 24 Hours of Accounting with no degree

52 BS/BA Accounting/Taxation

12 BS/BA Other (Specify: _____)

11 MA Accounting/Taxation

4 MA Other (Specify: _____)

- Ph.D. (Specify: _____)

2 Other (Specify: _____)

4. Were you a CPA when you were assigned to this examination? (CHECK ONE.) (30)

37 Yes

33 No

5. Did you receive the following training/experience in CEP procedures or issues before you were assigned to this audit or within 1 year of your assignment? (CHECK ONE BOX IN EACH ROW.) (31-35)

| | Yes (1) | No (2) | Not available at time (3) |
|---|---|---|---|
| a. Advanced corporate training or equivalent of Phase 5 | 66 | 6 | - |
| b. Case manager training | 63 | 7 | 1 |
| c. IRS training (3 days or more) related to the taxpayer's primary industry | 22 | 38 | 11 |
| d. Non-IRS training/seminars on any issues related to the taxpayer | 9 | 55 | 7 |
| e. Previous non-IRS experience related to the industry | 3 | 67 | 2 |

6. Was there any other training that you had not received that you felt you needed to improve your ability to conduct this CEP audit? (CHECK ONE.) (36)

62 No

10 Yes ---> Please explain:

_____

_____

7. At the time of this audit, was training on issues and industries provided jointly for Examination, Appeals, and Counsel? (CHECK ONE.) (37)

6 Yes

66 No

In your opinion, did/would this type of joint training improve the quality and timeliness of this audit in any way? (CHECK ONE.) (38)

38 Yes

32 No

Please explain your response.

_____

_____

_____

_____

8. At the time of this audit, did IRS obtain outside specialists to develop and deliver advanced training on complex technical and/or legal issues? (CHECK ONE.) (39)

5 Yes

67 No

In your opinion, did/would obtaining outside specialists to deliver advanced training improve the quality and timeliness of this audit in any way? (CHECK ONE.) (40)

39 Yes

31 No

Please explain your response.

_____

_____

_____

## II. CASE MANAGEMENT

9. Overall, how satisfied or dissatisfied were you with the amount of time you devoted to this case? (CHECK ONE.) (41)

18 Very satisfied
45 Generally satisfied
(SKIP TO QUESTION 11.)

8 Generally dissatisfied
1 Very dissatisfied
(CONTINUE WITH QUESTION 10.)

10. In your opinion, what factors affected the time you devoted to this audit? (CHECK ALL THAT APPLY.) (42-45)

5 Number of taxpayers/points in your inventory
3 Collateral duties
2 Logistical problems
5 Other (Please explain): _____

11. To what extent, if at all, were you involved with the following on this audit cycle? (CHECK ONE BOX IN EACH ROW.) (46-54)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) |
|---|---|---|---|---|---|
| a. The preparation of the audit plan | 17 | 28 | 12 | 2 | 10 |
| b. The selection of issues for audit | 11 | 33 | 13 | 4 | 9 |
| c. The review of workpapers | 8 | 21 | 26 | 13 | 4 |
| d. The opening conference with the taxpayer | 44 | 15 | - | - | 10 |
| e. The closing conference with the taxpayer | 52 | 16 | 2 | - | 1 |
| f. Interim meetings with the taxpayer | 36 | 31 | 5 | - | - |
| g. The review of proposed adjustments and tax computations | 28 | 37 | 6 | - | 1 |
| h. Resolution of problems between the taxpayer and revenue agents | 43 | 25 | 4 | - | - |
| i. Assistance in resolving difficult issues | 37 | 27 | 7 | - | 1 |

12. At the time of this audit, was a system such as electronic bulletin board or issue tracking available for case managers to communicate with case managers in other districts on special industries and/or issues to ensure that all parties were equally informed? (CHECK ONE.) (55)

20 Yes

52 No

In your opinion, did/would using such a system improve the development of issues in this case? (CHECK ONE.) (56)

41 Yes

22 No

Please explain your response.

_____

_____

_____

13. Overall, how satisfied or dissatisfied were you with management's involvement with the audit? (CHECK ONE BOX IN EACH ROW.) (57-59)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. District Director | 10 | 4 | 19 | - | 1 | 38 |
| b. Chief or Assistant Chief of Examination | 15 | 7 | 20 | - | 1 | 29 |
| c. Branch Chief | 28 | 18 | 16 | - | 2 | 5 |

14. At the time of this audit, was your district office management involved in the planning of the audit and/or requesting support examinations in this case? (CHECK ONE.) (60)

23 Yes

47 No

In your opinion, did/would this type of district office involvement ensure better planning of this audit or more thorough support examinations? (CHECK ONE.) (61)

20 Yes

49 No

Please explain your response.

_____

_____

**III. STAFFING/SPECIALISTS**

15. At any time during the audit did you have insufficient revenue agent staff? (CHECK ONE.) (62)

13 Yes

59 No

16. Did turnover in staff or specialists negatively impact the development of issues? (CHECK ONE.) (63)

12 Yes

60 No

***If your responses to both questions 15 and 16 are "No", skip to question 18.***
***If you answered "Yes" to either question 15 or 16, continue with question 17.***

17. What were the reasons that your staffing level was insufficient or why staff turned over? (CHECK ALL THAT APPLY.) (64-71)

4 Staff were not available when the audit began

8 Staff were temporarily diverted to other activities/ collateral duties during the course of the audit

1 Staff were permanently removed due to P-4-5 rotation policy

- Staff were permanently removed from audit due to incompatibility

8 Staff were permanently removed from audit due to other reasons

2 My request(s) for additional staff to be assigned was denied

4 My request(s) for additional staff to be assigned was granted, but the staff was (were) assigned later than appropriate

9 Other (Please specify) _____

_____

18. In your opinion, were the services of specialists obtained when you felt they were needed to help you develop your issues? (CHECK ONE.) (72)

65 Yes, for all my issues --> (SKIP TO QUESTION 22.)

3 Yes, in some cases

4 No

(CONTINUE WITH QUESTION 19.)

19. In your opinion, which specialist services were needed but were not obtained? (CHECK ALL THAT APPLY.) (73-81)

1 Outside consultant(s)

2 Industry/Issue specialist(s)

2 Economist(s)

2 Engineer(s)

- Computer audit specialist(s)

- International specialist(s)

1 EPEO specialist(s)

- Payroll specialist(s)

- Excise specialist(s)

- Counsel (82-83)

3 Other - Specify: _____ (84-85)

20. What were the reason(s) that the needed specialists were not obtained? (CHECK ALL THAT APPLY.) (86-89)

- District office management denied the request(s)

3 The needed specialists were not available to the district

- The needed specialists could not be borrowed from another district

5 Other - Specify: _____

21. For those specialists that were needed for this audit cycle but were not obtained, to what extent, if at all, did not having the services of this (these) specialist(s) negatively impact the results of the audit? (CHECK ONE BOX IN EACH ROW. CHECK BOX 1, "N/A" IF THE SPECIALIST WAS NOT NEEDED OR WAS NOT OBTAINED ON THE AUDIT.) (90-98)

| | Not Applic-able (1) | To a very great extent (2) | To a great extent (3) | To a moderate extent (4) | To some extent (5) | To little or no extent (6) | No basis to judge (7) |
|---|---|---|---|---|---|---|---|
| a. Outside consultant | 5 | - | - | - | 1 | - | - |
| b. Industry/Issue specialist | 5 | 1 | - | - | - | - | - |
| c. Economist | 4 | 1 | - | 1 | - | - | - |
| d. Engineer | 3 | 1 | - | 1 | - | - | - |
| e. Computer audit specialist | 5 | - | - | - | - | - | - |
| f. International specialist | 5 | - | - | 1 | - | - | |
| g. EPEO specialist | 5 | - | - | - | - | - | 1 |
| h. Counsel | 5 | - | 1 | - | - | - | |
| i. Other (Please specify) N=2 | | | | | | | |

Repeat ID - 2 (1-7)

22. In your opinion, what was the quality of work performed by the following individuals on this audit cycle? (CHECK ONE BOX IN EACH ROW. CHECK BOX 1, "N/A" IF THE POSITION WAS NOT USED ON THE AUDIT.) (8-19)

| | Not Applic-able (1) | Excellent (2) | Good (3) | Adequate or marginal (4) | Poor (5) | Very poor (6) | No basis to judge (7) |
|---|---|---|---|---|---|---|---|
| a. Team coordinator(s) | 1 | 54 | 15 | 2 | - | - | - |
| b. Other Exam revenue agents | 4 | 22 | 40 | 4 | - | 1 | 1 |
| c. Computer audit specialist | 1 | 21 | 36 | 13 | - | - | 1 |
| d. Industry/issue specialist | 16 | 6 | 29 | 9 | 2 | - | 8 |
| e. Engineer | 7 | 12 | 31 | 18 | 1 | - | 2 |
| f. International specialist | 11 | 26 | 20 | 7 | 4 | - | 3 |
| g. Economist | 43 | 7 | 7 | 1 | 2 | - | 9 |
| h. Outside consultant | 53 | 2 | 3 | - | - | - | 12 |
| i. EPEO specialist | 40 | 3 | 11 | 9 | - | - | 6 |
| j. Appeals | 19 | 6 | 13 | 13 | 5 | 3 | 10 |
| k. Counsel | 25 | 8 | 11 | 9 | 1 | - | 14 |
| l. Other (Please specify) N=12 | | | | | | | |

23. Did an industry or an issue specialization program exist at the time of this audit? (CHECK ONE.) (20)

59 Yes

13 No

In your opinion, did/would this program improve the audit team's ability to develop complex organizational or technical issues? (CHECK ONE.) (21)

48 Yes

15 No

Please explain your response.

_____

_____

_____

## IV. CASE DELAYS

24. Was this case closed out of Exam later than planned? (CHECK ONE.) (22)

55 Yes ---> (CONTINUE WITH QUESTION 25.)

17 No ---> (SKIP TO QUESTION 26.)

25. To what extent, if at all, did the following factors cause delays in closing the case in Exam? (CHECK ONE BOX IN EACH ROW.) (23-34)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) |
|---|---|---|---|---|---|
| a. Obtaining staff or specialists | 4 | 1 | 7 | 8 | 34 |
| b. Turnover in staff or specialists | 6 | 3 | 2 | 3 | 40 |
| c. Obtaining technical advice | 2 | 2 | 5 | - | 44 |
| d. Receiving specialists' reports | 3 | 6 | 5 | 10 | 28 |
| e. Issuing a summons | 2 | 1 | 1 | 4 | 45 |
| f. Diverting staff or specialist to collateral duties | 1 | 5 | 5 | 6 | 35 |
| g. Obtaining information from the taxpayer | 12 | 21 | 9 | 8 | 4 |
| h. Obtaining access to the taxpayer's computer file | 1 | 7 | 5 | 7 | 34 |
| i. Having access to the taxpayer's representative | 1 | 3 | - | 7 | 43 |
| j. Delays by the taxpayer in starting the examination | 1 | 2 | 1 | - | 50 |
| k. Delays by IRS in starting the examination | 1 | 3 | 1 | 1 | 48 |
| l. Other (Please specify) N=21 | | | | | |

26. If the taxpayer caused delays by not supplying the information requested on the IDR's or allowing access to computer files in a timely manner (or at all), what means were used to obtain the information? (CHECK ALL THAT APPLY.) (35-39)

12 Not applicable, all requested information was received in a timely manner

7 Summons

52 Informal means such as meetings between IRS management and the taxpayer

46 Follow-up IDR's

17 Other - Please specify: _____

## V. INFORMATION DOCUMENT REQUESTS

27. Was all needed information requested on the IDR's received before the case was closed in exam? (CHECK ONE.) (40)

55 Yes

17 No

28. What percentage of the total number of IDR's requesting new information were issued within 90 days of the close of the audit? (ENTER PERCENT.)

_____ Percent (41-43)

21 0 percent
3 1 percent
5 2 percent
5 5 percent
2 10 percent
1 95 percent

35 Do not know (44)

29. Overall, how satisfied or dissatisfied were you with the following? (CHECK ONE BOX IN EACH ROW.) (45-54)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. The timeliness of taxpayer responses to IDR's | 7 | 20 | 14 | 19 | 12 | - |
| b. The completeness of the information provided by taxpayer in response to IDR's | 7 | 27 | 8 | 22 | 8 | - |
| c. The relevance of the information provided by taxpayer in response to IDR's | 6 | 41 | 10 | 13 | 2 | - |
| d. That IDR's were issued in a timely manner | 33 | 31 | 5 | 3 | - | - |
| e. That IDR's were clearly and concisely prepared | 34 | 33 | 3 | 2 | - | - |
| f. That the information requested was obtainable by the taxpayer (e.g., information not available because of a merger, too old, etc.) | 21 | 27 | 11 | 5 | 2 | 6 |
| g. The overall cooperation of taxpayer to IDR's | 8 | 30 | 10 | 15 | 9 | - |

30. To the best of your knowledge, did the taxpayer provide information during the appeals process which Exam had requested but was not received? (CHECK ONE.) (55)

18 Yes ---> (CONTINUE WITH QUESTION 31.)

19 No
21 Do not know
(SKIP TO QUESTION 32.)

14 Not applicable, agreed case ----> (SKIP TO QUESTION 35.)

31. Did Appeals involve Exam further in case development because the taxpayer provided additional information, filed a claim, or raised new issues? (CHECK ONE.) (56)

2 Yes, Appeals relinquished jurisdiction of the case back to Exam

11 Yes, Appeals involved Exam in further case development without relinquishing jurisdiction of the case

3 No

1 Do not know

32. Did the taxpayer provide information during the appeals process which Exam had or had not requested that reduced the proposed tax deficiency? (CHECK ONE.) (57)

16 Yes

17 No

25 Do not know

33. Did your district office management such as the District Director, Chief or Assistant Chief (Exam), or Branch Chief meet with high level taxpayer officials during this audit? (CHECK ONE.) (58)

28 Yes ---> Please specify the position or role of those who met with high level taxpayer officials.

_____ (59)

29 No ---> In your opinion, would increased managerial oversight have improved the taxpayer's level of cooperation (e.g., prompt response to IDR's or meetings to discuss disagreements between the taxpayer and IRS)? (60)

3 Yes

25 No

Please explain your response.

_____

_____

_____

## VI. ADDITIONAL INFORMATION ABOUT THE CASE

34. Did this CEP taxpayer file a consolidated corporate return? (CHECK ONE.) (61)

67 Yes

3 No

- Do not know

35. In general, how satisfied or dissatisfied were you with the following factors during the audit? (CHECK ONE BOX IN EACH ROW.) (62-73)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | Not Applicable (6) |
|---|---|---|---|---|---|---|
| a. Access to needed IRS supplies | 29 | 25 | 9 | 4 | 5 | - |
| b. Access to IRS research material | 25 | 24 | 8 | 7 | 8 | - |
| c. Access to professional industry manuals | 7 | 25 | 23 | 7 | 7 | 3 |
| d. Access to IRS computers | 19 | 27 | 8 | 4 | - | 14 |
| e. Access to IRS printers | 21 | 25 | 8 | 3 | - | 15 |
| f. Access to IRS office support staff | 16 | 32 | 10 | 5 | - | 7 |
| g. Space provided by the taxpayer for the audit team | 30 | 25 | 10 | 5 | 2 | - |
| h. Access to taxpayer's supplies | 17 | 11 | 16 | 1 | 1 | 26 |
| i. Access to taxpayer's library or other public research materials | 22 | 21 | 15 | 6 | 2 | 6 |
| j. Access to taxpayer's computers | 5 | 23 | 17 | 5 | 3 | 19 |
| k. Access to taxpayer's printers | 5 | 19 | 17 | 4 | 3 | 24 |
| l. Access to taxpayer's photocopiers | 39 | 25 | 2 | 1 | 5 | - |

36. Did you secure a signed formal agreement from the taxpayer on the proposed adjustments at the time the case was closed out of Exam? (CHECK ONE.) (74)

14 Yes, the taxpayer agreed to all issues (full agreement)

16 Yes, the taxpayer agreed to some issues (partial agreement)

39 No

3 Do not remember

37. If the case manager would have had settlement authority (Delegation Order 236) for "rollover" and "recurring" issues for which Appeals had already established a settlement practice based on the facts of the issue, do you believe this would have had a positive effect, no effect, or a negative effect on the recovery rate of these returns? (CHECK ONE.) (75)

20 A positive effect on the recovery rate

43 No effect on the recovery rate

2 A negative effect on the recovery rate

7 Do not know

38. Do you believe case managers or other Examination officials should be actively attempting to settle more audit issues based on the merits (facts) of a case? (CHECK ONE.) (76)

62 Yes

9 No

Please explain: _____

_____

_____

39. How satisfied or dissatisfied were you with Appeals overall settlement of this audit cycle? (CHECK ONE.) (77)

6 Very satisfied

14 Generally satisfied (SKIP TO QUESTION 41.)

10 Neither satisfied nor dissatisfied

11 Generally dissatisfied

7 Very dissatisfied (CONTINUE WITH QUESTION 40.)

24 No basis to judge/Agreed case ---> (SKIP TO QUESTION 43.)

40. Did you use the dissent process to protest Appeal's settlement of this case? (CHECK ONE.) (78)

2 Yes

16 No

41. Did Examination and Counsel discuss the taxpayer's protest with Appeals to ensure that Appeals was able to consider all of the relevant facts in this case? (CHECK ONE.) (79)

29 Yes

28 No

In your opinion, to what extent, if at all, did/would the discussion enhance Appeals' ability to sustain dollars recommended by Exam? (CHECK ONE.) (80)

6 To a very great extent

4 To a great extent

10 To a moderate extent

8 To some extent

14 To little or no extent

10 Do not know

Please explain your response.

_____

_____

_____

42. Did appeals discuss the final resolution of unagreed issues to provide Examination with information for auditing the subsequent tax returns for this taxpayer? (CHECK ONE.) (81)

21 Yes —> If yes, was the feedback provided to the revenue agents working on the subsequent audit? (CHECK ONE.) (82)

18 Yes

Please explain: _____

1 No

35 No —> If no, in your opinion, would this feedback have improved the planning or the timeliness of subsequent audit cycles? (CHECK ONE.) (83)

11 Yes

Please explain: _____

17 No

**VII. OVERALL PERCEPTION OF AUDIT CYCLE** Repeat ID - 3 (1-7)

43. Regarding the team collectively, how satisfied or dissatisfied were you with the following factors on this audit? (CHECK ONE BOX IN EACH ROW.) (8-22)

| | Very satisfied (1) | Generally satisfied (2) | Neither satisfied nor dissatisfied (3) | Generally dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Number of staff assigned to the audit | 28 | 41 | 1 | 2 | - | - |
| b. Number of staff days allotted to the audit | 21 | 44 | 4 | 2 | 1 | - |
| c. Adequacy of the team's experience and skills in auditing large corporations | 30 | 37 | 3 | 2 | - | - |
| d. Adequacy of the team's knowledge in tax laws, rules and regulations | 34 | 35 | 3 | - | - | - |
| e. Adequacy of the team's knowledge of the industry involved in the audit | 24 | 33 | 12 | 3 | - | - |
| f. Adequacy of support audits | 4 | 19 | 5 | 4 | - | 38 |
| g. Level of cooperation of team members with one another | 30 | 32 | 5 | 4 | 1 | - |
| h. Level of cooperation you received from the team | 41 | 30 | - | 1 | - | - |
| i. Level of cooperation between the taxpayer and the team members | 11 | 31 | 17 | 11 | 2 | - |
| j. Length of time it took to complete the audit | 7 | 30 | 14 | 20 | 1 | - |
| k. Extent to which team members fully developed the issues assigned to them | 26 | 43 | 2 | 1 | - | - |
| l. Extent to which team members accurately developed the issues assigned to them | 27 | 41 | 4 | - | - | - |
| m. Extent to which management was involved in the case | 17 | 30 | 20 | - | - | 5 |
| n. Other (Please specify) N=8 | | | | | | |
| o. Other (Please specify) N=3 | | | | | | |

44. How satisfied or dissatisfied were you with the overall quality of the performance of the IRS team (including specialists) during the audit of this taxpayer identified on page 1 of this questionnaire? (CHECK ONE.) (23)

25 Very satisfied

44 Generally satisfied

1 Neither satisfied nor dissatisfied

2 Generally dissatisfied

- Very dissatisfied

45. How satisfied or dissatisfied were you with the overall attitude/level of cooperation of the taxpayer? (CHECK ONE.) (24)

5 Very satisfied

37 Generally satisfied

12 Neither satisfied nor dissatisfied

16 Generally dissatisfied

2 Very dissatisfied

46. In your opinion, has the establishment of a National CEP Director had a positive impact, no impact, or a negative impact on program development, oversight, and/or evaluation within CEP? (CHECK ONE.) (25)

34 A positive impact

12 No impact

13 A negative impact

13 Do not know

Please explain your response:

_____

_____

_____

47. In your opinion, has the establishment of Regional CEP Managers had a positive impact, no impact, or a negative impact on program development, oversight, and/or evaluation within CEP? (CHECK ONE.) (26)

16 A positive impact

29 No impact

7 A negative impact

20 Do not know

Please explain your response:

_____

_____

_____

48. In your opinion, has the establishment of a multi-functional National Policy Board had a positive impact, no impact, or a negative impact on promoting taxpayer cooperation through improved coordination between Examination, Appeals, International and Counsel? (CHECK ONE.) (27)

30 A positive impact

36 No impact

4 A negative impact

49. In your opinion, would the development of standard goals and measures for Examination, Appeals, International, and Counsel have had a positive effect, no effect, or a negative effect on this audit? (CHECK ONE.) (28)

21 A positive effect

31 No effect

18 A negative effect

50. In your opinion, would CEP quality peer reviews have improved this audit in any way? (CHECK ONE.) (29)

6 Yes --> Please explain:

_____

_____

_____

62 No

51. Please briefly discuss in the space below what you feel was the most positive thing about this audit as well as the most negative thing about this audit.

**Positive:** _____ (30)

_____

_____

_____

_____

**Negative:** _____ (31)

_____

_____

_____

_____

52. Please list any other recent changes to the Large Case Program which would have impacted on the resolution of these returns had they been in effect at the time these returns were worked. Also, describe in what ways they would have impacted the resolution of the returns. (32)

Change: _____

Impact on case: _____

_____

_____

_____

Change: _____

Impact on case: _____

_____

_____

_____

Change: _____

Impact on case: _____

_____

_____

_____

53. Are there any other changes to the CEP/Large Case Program that you would like to suggest here? (33)

_____

_____

_____

_____

_____

_____

_____

_____

_____

# Survey of IRS Appeals Officers

U.S. General Accounting Office

## Closed CEP Case Questionnaire - Appeals

### INTRODUCTION

The U.S. General Accounting Office (GAO), an investigative agency of Congress, is conducting a study of IRS's Coordinated Examination Program (CEP). The overall objective of our review is to determine what factors affect the rate at which taxes recommended by CEP revenue agents get assessed. We are surveying appeals officers who worked on each of the CEP corporate returns which had recommended additional taxes of $30 million or more and were closed in Appeals from 1989 to 1991.

You have been selected to complete this survey due to your involvement with the corporate tax returns and tax years indicated on this page. Because of your work on these returns, your response to this survey will help us to identify all of the factors which impact the resolution of CEP audits, both positively and negatively.

This questionnaire is confidential. The control number is included only to aid us in our follow-up efforts. Your responses will be combined with those of other respondents and will be reported only in summary form. We will not identify specific CEP taxpayers in our report.

Most of the questions can be easily answered by checking boxes or filling in blanks. You will need to refer to the Audit Statement and the Supporting Statement to complete some questions.

We estimate this questionnaire should take about 2 hours to complete. The actual amount of time it will take to complete depends on the number of tax years involved. If you have any questions concerning any part of this survey, please call Ms. Deborah Junod at (202) 272-7904.

Please return the completed questionnaire in the enclosed pre-addressed envelope within 2 weeks from the time you receive it. In the event the envelope is misplaced, the return address is:

U.S. General Accounting Office
General Government Division
Attn: Mr. James Fremming
441 G Street, N.W., Room 3126
Washington, D.C. 20548

Thank you for your assistance.

**Corporate Tax Return Information:**

***After completing this questionnaire, please remove the case information sticker before returning your completed questionnaire.***

**Total number of Appeals respondents = 78**

I. **RESPONDENT INFORMATION**

Please provide your current work telephone number . . . . . (_____)_____

For these CEP corporate returns, were you assigned to settle disputed issues for the tax years shown on page 1? (CHECK ONE.) (8)

78 Yes --> **Please continue with question 1.**

0 No --> ***STOP:* Do not continue if you were not assigned to resolve disputes on the tax returns shown on page 1. Please return the questionnaire in the enclosed envelope.**

1. Please enter the total number of years of IRS experience you had at the time you were assigned to the above returns.

Mean = 22 Years N=77 (9-10)

2. Were you ever a revenue agent or international examiner with IRS' Examination Division? (CHECK ONE.) (11)

2 No --> (GO TO QUESTION 3.)

69 Yes --> Please answer the following questions as they apply to you at the time you began consideration of the taxpayer's protest of these returns. *(Enter "00" if none or under 1 year.)* (12-23)

**Years reported are means.**

a. Number of years working on CEP examinations as a revenue agent N=76 . . . . . 2 Years

b. Number of years working on CEP examinations as an international examiner N=76 . . . . . * Years

c. Number of years of revenue agent experience examining corporations prior to being assigned to CEP examinations N=76 . . . . . 4 Years

d. Number of years of revenue agent experience listed in c. above that you were examining corporations with assets of $100 million or more N=76 . . . . . 2 Years

e. Number of years of international examiner experience examining corporations prior to being assigned to CEP examinations N=76 . . . . . * Years

f. Number of years of international examiner experience listed in e. above that you were examining corporations with assets of $100 million or more N=76 . . . . . * Years

* Mean is less than one year

3. What grade level were you when you were first assigned to these returns? (ENTER NUMBER.)

GS - _____ (24-25) or GM - _____ (26-27)

37 GS-14
36 GS-15 or GM-15
5 Other

4. Please indicate whether or not you have held the following positions at IRS.
For those you have held, please enter the number of years you have held the position.
*(Enter "00" if none or under 1 year.)*

| Position | Yes (1) | No (2) | Time in Position |
|---|---|---|---|
| a. IRS District Conferee | 31 | 46 | Mean=2 Years |
| b. IRS Exam Case/Group Manager | 9 | 67 | Mean=3 Years |
| c. IRS Exam Quality Reviewer | 9 | 67 | Mean=2 Years |
| d. Other IRS related position(s) (Specify) N=59 | | | _____ Years |
| | | | _____ Years |
| e. Other government position(s) related to tax/auditing N=12 | | | _____ Years |
| | | | _____ Years |
| f. Private industry position(s) related to tax/auditing N=32 | | | _____ Years |
| | | | _____ Years |

5. a. Approximately how long had you been an appeals officer at the time you were assigned to these returns?

N=78 Mean = 13 Years (55-58)

b. How long had you worked on large cases ($10 million or more and at least 20 issues in dispute) as an appeals officer at the time you were assigned to these returns?

N=78 Mean = 8 Years (59-62)

or

1 Did not work on large cases (63)

6. Were you a Team Chief at the time you were assigned to these returns? (CHECK ONE.) (64-71)

37 Yes

41 No

7. What was your educational background at the time you were assigned to these returns?
(CHECK ALL THAT APPLY.) (65-71)

3 24 Hours of Accounting with no degree

58 BS/BA Accounting/Taxation

13 BS/BA Other (Specify: _____)

23 MA Accounting/Taxation

3 MA Other (Specify: _____)

- Ph.D. (Specify: _____)

18 Other (Specify: _____)

8. Were you a CPA when you were assigned to these returns? (CHECK ONE.) (72)

49 Yes

29 No

9. Did you receive the following training/experience in large case CEP procedures or issues before you were assigned to these returns or within 1 year of your assignment? (CHECK ONE BOX IN EACH ROW.) (73-78)

| | Yes (1) | No (2) |
|---|---|---|
| a. Advanced corporate training or equivalent of Phase 5 | 67 | 11 |
| b. Appeals officer training | 75 | 3 |
| c. IRS training (3 days or more) related to the taxpayer's primary industry | 36 | 42 |
| d. Non-IRS training/seminars on any issues related to the taxpayer | 28 | 49 |
| e. Previous non-IRS experience related to the industry | 3 | 71 |
| f. Topical training provided jointly to Examination, Appeals, and Counsel | 58 | 20 |

10. Was there any other training you had not received that you feel would have benefited the quality or timeliness of the settlement on these returns? (CHECK ONE.) (79)

8 Yes --> Please explain below.

70 No

_____

_____

_____

_____

## II. OVERALL CASE RESULTS

11. During the period you were working on these returns, what was the average number of active work units in your inventory? (ENTER NUMBERS.)

Mean = 6 Number of work units with less than $1 million in dispute N=72, Range = 0 to 30 (80-81)

Mean = 4 Number of work units with $1 million to $10 million in dispute N=75, Range = 0 to 15 (82-83)

Mean = 5 Number of work units with over $10 million in dispute N=78, Range = 0 to 10 (84-85)

12. For these returns, how many issues were protested by the taxpayer? (ENTER NUMBER.)

Mean = 53 Issues N=77 (86-88)

Range = 1 to 340 issues

13. If the case manager would have had settlement authority (Delegation Order 236) for "rollover" and "recurring" issues for which Appeals had already established a settlement practice based on the facts of the issue, do you believe this would have had a positive effect, no effect, or a negative effect on the recovery rate of these returns? (CHECK ONE.) (89)

17 A positive effect on the recovery rate

45 No effect on the recovery rate

3 A negative effect on the recovery rate

13 Do not know

14. Do you believe Examination case managers should be actively attempting to settle more audit issues based on the merits (facts) of a case? (CHECK ONE.) (90)

46 Yes

26 No

Please explain: _____

_____

_____

Repeat ID - 2 (1-7)

15. Please provide the following information separately for each tax year included in these returns. Please be sure to enter the tax year at the top of each column. *(You will need the Audit Statement to complete this table.)*

***Please round to the nearest dollar.***

| | Primary Tax Years *(As shown on page 1.)* | | |
|---|---|---|---|
| | (8-9) Tax Year 19____ | (10-11) Tax Year 19____ | (12-13) Tax Year 19____ |
| a. Taxable income proposed by Exam | $ _____ | $ _____ | $ _____ |
| b. Corrected tax liability per Appeals | $ _____ | $ _____ | $ _____ |
| c. Less: Tax credits per Appeals | $ _____ | $ _____ | $ _____ |
| d. Plus: Recapture of prior year ITC per Appeals | $ _____ | $ _____ | $ _____ |
| e. Total corrected tax liability per Appeals | $ _____ | $ _____ | $ _____ |
| f. Less: Total tax shown on return or as previously adjusted | $ _____ | $ _____ | $ _____ |
| g. Deficiency/(Overassessment) per Appeals | $ _____ | $ _____ | $ _____ |
| h. Total penalties per Appeals (List type) _____ _____ _____ _____ _____ | (14-21) None $ _____ | (22-29) None $ _____ | (30-37) N=2 $ _____ |

Continued on next page

**Question 15 (Continued)**

Repeat ID - 3 (1-7)

Be sure to enter the tax year at the top of each column.

***Please round to the nearest dollar.***

| | Carry forward/back Years | | |
|---|---|---|---|
| | (8-9) Tax Year 19____ | (10-11) Tax Year 19____ | (12-13) Tax Year 19____ |
| a. Taxable income proposed by Exam | $ _____ | $ _____ | $ _____ |
| b. Corrected tax liability per Appeals | $ _____ | $ _____ | $ _____ |
| c. Less: Tax credits per Appeals | $ _____ | $ _____ | $ _____ |
| d. Plus: Recapture of prior year ITC per Appeals | $ _____ | $ _____ | $ _____ |
| e. Total corrected tax liability per Appeals | $ _____ | $ _____ | $ _____ |
| f. Less: Total tax shown on return or as previously adjusted | $ _____ | $ _____ | $ _____ |
| g. Deficiency/(Overassessment) per Appeals | $ _____ | $ _____ | $ _____ |
| h. Total penalties per Appeals (List type) _____ _____ _____ _____ _____ | (14-21) N=1 $ _____ | (22-29) None $ _____ | (30-37) None $ _____ |

Repeat ID - 4 (1-7)

16. Did the taxpayer file a claim for a refund, a request for a tentative refund, or was a new issue raised during the Appeals process for these returns? (CHECK ONE.) (8)

36 No, none of these situations apply ----> **(GO TO QUESTION 17.)**

39 Yes ---> **If yes**, how much did you reduce or increase taxable income or credits because of the claim(s), request(s), or new issues? (ENTER DOLLAR AMOUNT. IF NONE, ENTER "00".)

| | Increase | Decrease |
|---|---|---|
| Taxable income | | |
| Credits | | |

**If yes**, was this a claim resulting in a net operating loss carryback from a subsequently filed return? (CHECK ONE.) (53)

5 Yes

32 No

2 Do not know ---> **(GO TO QUESTION 17.)**

17. Overall, how satisfied or dissatisfied were you with the following? (CHECK ONE BOX IN EACH ROW.) (54-57)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Overall attitude/cooperation of the taxpayer | 34 | 27 | 8 | 6 | 3 | - |
| b. The timeliness of taxpayer responses | 28 | 32 | 6 | 9 | 3 | - |
| c. The completeness of the information provided by the taxpayer | 24 | 32 | 13 | 8 | 1 | - |
| d. The relevance of the information provided by the taxpayer | 24 | 34 | 13 | 6 | 1 | - |

## III. PROTESTED ISSUES AND APPEALS RESULTS

18. Did Examination, Appeals, and Counsel discuss the taxpayer's protest to ensure that Appeals was able to consider all of the relevant facts in the resolution of these returns? (CHECK ONE.) (58)

39 Yes

39 No ----> In your opinion, to what extent, if at all, would such a discussion have reduced Appeals' time for processing issues on these returns? (CHECK ONE.) (59)

1 To a very great extent

1 To a great extent

10 To a moderate extent

8 To some extent

10 To little or no extent

9 Do not know

Please explain your response.

_____

_____

_____

19. Did Examination provide Appeals with a written rebuttal for issues protested by the taxpayer? (CHECK ONE.) (60)

40 Yes --> Did this written rebuttal reduce Appeals' time for processing issues on these returns? (61)

25 Yes

11 No

Please explain: _____

36 No --> Would a written rebuttal have reduced Appeals' time for processing issues on these returns? (62)

23 Yes

8 No

Please explain: _____

20. Please provide the following information on the three top dollar adjustments to income/credit protested by the taxpayer for these returns. *(You will need the supporting statement to complete this question.)*

| | Issue #1 | Issue #2 | Issue #3 |
|---|---|---|---|
| a. IRC | _____ | _____ | _____ |
| b. Adjustment to: *(Check one per issue.)* | (63)<br>70 Taxable income<br>6 Credit | (64)<br>68 Taxable income<br>7 Credit | (65)<br>63 Taxable income<br>9 Credit |
| c. Dispute between Exam and taxpayer involved: *(Check one or both.)* | (66-67)<br>60 Interpretation of law<br>54 Based on merit/facts | (68-69)<br>53 Interpretation of law<br>46 Based on merit/facts | (70-71)<br>53 Interpretation of law<br>42 Based on merit/facts |
| d. Type of Adjustment *(Check all that apply.)* | (72-78)<br>10 Unreported income<br>28 Overstated deductions<br>29 Timing<br>7 Valuation<br>12 Allocation<br>- Whipsaw<br>15 Other (Specify) | (79-85)<br>11 Unreported income<br>33 Overstated deductions<br>14 Timing<br>2 Valuation<br>11 Allocation<br>- Whipsaw<br>16 Other (Specify) | (86-92)<br>9 Unreported income<br>26 Overstated deductions<br>14 Timing<br>2 Valuation<br>9 Allocation<br>- Whipsaw<br>20 Other (Specify) |
| e. Adjustment per Exam | N=78 (8-18)<br>Mean = $80,363,225<br>Range = $0 to $631,237,212 | N=75 (19-29)<br>Mean = $46,406,598<br>Range=$-127,738,791 to $566,703,455 | N=74 (30-40)<br>Mean = $26,740,230<br>Range = $-51,577,089 to $168,280,618 |
| f. Adjustment per Appeals | N=78 (41-51)<br>Mean = $16,816,716<br>Range = $-151,102,119 to $170,196,254 | N=75 (52-62)<br>Mean = $23,438,348<br>Range = $-50,873,768 to $475,146,014 | N=74 (63-73)<br>Mean = $13,120,621<br>Range = $-52,000,000 to $129,941,793 |

**Question 21 through 33 relate specifically to these three identified top dollar adjustments to income/credit.**

21. Were these issues Appeals Coordinated Issues (ACI's)? (CHECK ONE BOX IN EACH ROW.) (74-76)

| | Yes (1) | No (2) | ACI program didn't exist at that time (3) | Do not know (4) |
|---|---|---|---|---|
| a. Issue #1 | 4 | 72 | 1 | - |
| b. Issue #2 | 3 | 71 | 1 | - |
| c. Issue #3 | 2 | 71 | 1 | - |

Repeat ID - 5 (1-7)

22. For any of these three issues, was there a need for a specialist or outside consultant that was not obtained? (CHECK ONE.) (8)

73 No

(SKIP TO QUESTION 24.)

1 Do not know

4 Yes, Exam should have used some specialist(s) or outside consultant(s) but did not ---->

*Please list the type of specialist or consultant that you feel should have been used but were not and check the issue number(s).*

| Specialist/Consultant Not Used | Issue Number | | |
|---|---|---|---|
| 2 Economist | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 |
| 2 Engineer | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 |
| _____ | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 |
| _____ | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 |
| _____ | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 |
| _____ | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 |

23. For the specialist(s) and/or outside consultant(s) that you listed in the prior question, was one subsequently obtained in all instances? (CHECK ALL THAT APPLY.) (27-30)

- Yes, by Examination
- Yes, by Appeals
- Yes, by District Counsel

4 No ----> Please explain: _____

24. For these issues that you indicated above, should formal technical advice have been obtained that was not obtained? (CHECK ONE BOX IN EACH ROW.) (31-33)

| | Yes (1) | No (2) |
|---|---|---|
| a. Issue #1 | 1 | 77 |
| b. Issue #2 | - | 76 |
| c. Issue #3 | 1 | 74 |

25. For the three issues that you identified for these returns, which of the following factors caused the taxpayer to protest the issue? (CHECK YES OR NO FOR EACH ROW FOR EACH ISSUE THAT WAS PROTESTED.)

| | Issue #1 | | Issue #2 | | Issue #3 | |
|---|---|---|---|---|---|---|
| | Yes (1) | No (2) | Yes (1) | No (2) | Yes (1) | No (2) |
| a. Disagreement over interpretation of the law | 65 | 12 | 61 | 15 | 62 | 10 |
| b. Disagreement over facts | 49 | 28 | 45 | 29 | 40 | 32 |
| c. Amount supported by taxpayer documentation exceeds the amount allowed by Exam | 13 | 60 | 24 | 47 | 13 | 57 |
| d. Disagreement on timing issues | 28 | 46 | 20 | 52 | 23 | 45 |
| e. Disagreement on valuation issues | 12 | 62 | 8 | 60 | 9 | 59 |
| f. Disagreement on allocation issues | 17 | 56 | 14 | 57 | 15 | 54 |
| g. Disagreement on whipsaw issues | - | 73 | 1 | 70 | - | 69 |
| h. Appeals settlement on prior work units | 19 | 54 | 12 | 59 | 11 | 57 |
| i. Appeals settlement of same issue for a different taxpayer | 6 | 67 | 4 | 67 | - | 69 |
| j. Pending litigation of same issue for a different taxpayer | 15 | 59 | 7 | 64 | 4 | 65 |
| k. Other (Specify) _____ | | | | | | |
| l. Other (Specify) _____ | | | | | | |

26. For each of the three issues that you identified, did the taxpayer provide additional documentation to Appeals to support its protest on the issue? (CHECK APPROPRIATE BOXES FOR EACH ISSUE.)

| | Yes (1) | No (2) | If yes, had the Exam staff requested this information while these returns were still under Exam? *(Check one box for each issue.)* | | |
|---|---|---|---|---|---|
| | | | Yes (1) | No (2) | Don't know (3) |
| a. Issue #1 | 45 | 33 | 11 | 15 | 18 |
| b. Issue #2 | 41 | 35 | 11 | 15 | 14 |
| c. Issue #3 | 33 | 41 | 5 | 7 | 20 |

27. After these returns were in Appeals, did you relinquish their jurisdiction back to Exam for further development of these issues? (CHECK APPROPRIATE BOXES FOR EACH ISSUE.)

| | Yes (1) | No (2) | If yes, did Exam provide additional information or a supplemental RAR which helped you arrive at a settlement of the issue? *(Check one box for each issue.)* | |
|---|---|---|---|---|
| | | | Yes (1) | No (2) |
| b. Issue #1 | 3 | 75 | 2 | 1 |
| b. Issue #2 | 7 | 69 | 5 | 2 |
| c. Issue #3 | 3 | 70 | 3 | - |

28. While these returns were under jurisdiction of Appeals, was Exam involved in further development of these issues? (CHECK APPROPRIATE BOXES FOR EACH ISSUE.)

| | Yes (1) | No (2) | If yes, did Exam provide additional information or a supplemental RAR which helped you arrive at a settlement of the issue? *(Check one box for each issue.)* | |
|---|---|---|---|---|
| | | | Yes (1) | No (2) |
| a. Issue #1 | 29 | 49 | 27 | 1 |
| b. Issue #2 | 29 | 47 | 27 | 3 |
| c. Issue #3 | 17 | 57 | 17 | 1 |

29. Please identify the reason code(s) (from those listed below) which best describe the resolution of these issues. (PLEASE ENTER THE LETTER CORRESPONDING TO THE REASON IN THE APPROPRIATE BOX.)

*Please note: In many cases a single reason will be adequate. However, you may select up to three codes, if necessary, to adequately describe the action taken on these issues. If more than one reason code is selected, please list them in the order of impact on the resolution of these issues.*

**The two most frequently cited responses are listed for each issue.**

| | Reason Code #1 (Highest Impact) | Reason Code #2 (2nd Highest Impact) | Reason code #3 (3rd Highest Impact) |
|---|---|---|---|
| a. Issue #1 | 23 E<br>19 C | 14 C<br>12 E | 3 A<br>3 C |
| b. Issue #2 | 19 E<br>14 C | 9 C<br>8 E | 3 A<br>3 C |
| c. Issue #3 | 20 J<br>19 E | 9 C<br>5 E | 3 A<br>2 C |

**REASON CODES ARE AS FOLLOWS:**

**A** = New facts/evidence obtained and evaluated by Appeals/Counsel
**B** = New facts/evidence obtained and evaluated by Exam
**C** = Hazards - Facts/evidence are open to judgement
**D** = Conflict
**E** = Hazards - Application or interpretation of law
**F** = Changes in law
**G** = Whipsaw issue
**H** = Offsetting considerations
**I** = Technical error
**J** = Appeals/Counsel sustains the issue in full
**K** = Tax Court decision
**L** = Returned to District for additional development
**M** = Returned to District for consideration of new evidence

Repeat ID - 6 (1-7)

30. Were all protested issues on these returns *(not just the three issues identified)* settled by Appeals? (CHECK ONE.) (8)

69 Yes, all issues on these returns were resolved by Appeals or Exam.

9 No, some or all of the issues on these returns were forwarded to Counsel for resolution.

31. Did Appeals discuss the final resolution of unagreed issues *(not just the three issues identified)* with Examination officials to provide them with information for auditing subsequent returns? (CHECK ONE.) (9)

48 Yes --> Was the feedback provided to the revenue agents who proposed the adjustments? (10)

36 Yes

Please explain: _____

6 No

27 No --> In your opinion, would this feedback have improved the planning or the timeliness of audits on subsequent returns? (11)

5 Yes

Please explain: _____

13 No

## IV. IMPLEMENTED OR PROPOSED CHANGES IN THE LARGE CASE PROGRAM

32. The following matrix contains changes to the Large Case Program that have been proposed or implemented. For the top three dollar issues, had these changes been implemented at the time you worked on these tax returns, do you feel they would have (1) increased the sustention rate and (2) decreased the time for processing of these issues?
(CHECK TWO BOXES FOR EACH ROW.)

| Changes | This change would have increased the sustention rate for the top three dollar issues. *(Check one box for each row.)* | | | This change would have decreased the time for processing the top three dollar issues. *(Check one box for each row.)* | | |
|---|---|---|---|---|---|---|
| | Yes (1) | No (2) | Don't know (3) | Yes (1) | No (2) | Don't know (3) |
| a. Establishment of a National Policy Board to improve coordination between Exam, International, Appeals, and Counsel. | 4 | 53 | 19 | 6 | 55 | 15 |
| b. Establishment of a National Executive Director for CEP. | 1 | 55 | 21 | 1 | 57 | 17 |
| c. Increased involvement by Exam district office management to ensure better planning and provide more support while audits are conducted. | 21 | 30 | 26 | 27 | 25 | 23 |
| d. Establishment of Assistant Regional Directors of Appeals for the Large Case Program. | 7 | 55 | 15 | 9 | 52 | 14 |
| e. Expansion of Team Chief authority to settle disputes. | 15 | 50 | 12 | 16 | 48 | 12 |
| f. Standardized goals and measures for Exam, International, Appeals, and Counsel. | 14 | 44 | 19 | 13 | 43 | 20 |
| g. Establishment of the Office of Large Cases in the National Office. | 5 | 51 | 21 | 4 | 52 | 20 |
| h. Formal pre-conferences between Exam and Appeals. | 31 | 34 | 12 | 41 | 26 | 9 |
| i. Formal post-conferences between Exam and Appeals. | 23 | 43 | 11 | 23 | 41 | 11 |
| j. Establishment of an Industry Specialization Program. | 32 | 31 | 14 | 25 | 40 | 11 |
| k. Provision of legal and/or technical assistance from the start of all audits in Examination. | 42 | 26 | 9 | 37 | 29 | 9 |
| l. Receiving written rebuttals from Exam for issues protested by the taxpayer. | 44 | 28 | 5 | 49 | 24 | |

Question 32 (Continued)

| Changes | This change would have increased the sustention rate for the top three dollar issues. (Check one box for each row.) | | | This change would have decreased the time for processing the top three dollar issues. (Check one box for each row.) | | |
|---|---|---|---|---|---|---|
| | Yes (1) | No (2) | Don't know (3) | Yes (1) | No (2) | Don't know (3) |
| m. Providing case managers increased settlement authority for "rollover" and "recurring" issues. | 22 | 41 | 14 | 22 | 41 | 13 |
| n. Implementing cross-functional training for Exam, Appeals, and Counsel. | 29 | 37 | 11 | 30 | 34 | 12 |

33. Taking everything into consideration, how would you rate the overall quality of Exam's development of each of the top three dollar issues that you identified? (CHECK ONE BOX IN EACH ROW.) (40-42)

| | Excellent (1) | Good (2) | Adequate (3) | Poor (4) | Very poor (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Issue 1 | 10 | 30 | 26 | 8 | 3 | 1 |
| b. Issue 2 | 7 | 35 | 20 | 7 | 5 | 2 |
| c. Issue 3 | 10 | 33 | 22 | 4 | 3 | 2 |

If you wish to explain any of your responses, please use the space below.

Issue 1: _____

Issue 2: _____

Issue 3: _____

## V. GENERAL QUESTIONS RELATING TO THESE RETURNS

34. Taking everything into consideration, how would you rate the overall quality of Exam's **identification** of the audit issues on these returns? (CHECK ONE.) (43)

18 Excellent

35 Good

12 Adequate

4 Poor

2 Very poor

7 No basis to judge

Please explain your response:

_____

_____

_____

35. Taking everything into consideration, how would you rate the overall quality of Exam's **development** of the audit issues on these returns? (CHECK ONE.) (44)

8 Excellent

28 Good

30 Adequate

9 Poor

2 Very poor

- No basis to judge

Please explain your response:

_____

_____

_____

36. Please list any other recent changes to the Large Case Program which would have impacted the resolution of these returns had they been in effect at the time these returns were worked. Also, describe in what ways they would have impacted the resolution of the returns. (45)

Change: _____

Impact on resolution of returns: _____

_____

_____

_____

Change: _____

Impact on resolution of returns: _____

_____

_____

_____

Change: _____

Impact on resolution of returns: _____

_____

_____

_____

37. Are there any other changes to the Large Case Program that you would like to suggest here? (46)

N=26

38. Please briefly discuss in the space below what you feel was the most positive thing as well as the most negative thing about the resolution of these returns.

**Positive:** N=67 (47)

**Negative:** N=46 (48)

# Survey of CEP Corporations

U.S. General Accounting Office

## Closed CEP Case Survey - Taxpayer Questionnaire

### INTRODUCTION

The U.S. General Accounting Office (GAO), an investigative agency of Congress, is conducting a study of IRS's Coordinated Examination Program (CEP). The overall objective of our review is to determine what factors affect the rate at which taxes recommended by CEP revenue agents get assessed. We are surveying taxpayers who filed each of the CEP corporate returns which had recommended additional taxes of $30 million or more and were closed, agreed in Exam, or closed in Appeals from 1989 to 1991.

You have been selected to complete this survey because you were identified by IRS as the point of contact for the audit of the corporate tax returns and tax years indicated on this page. Because of your work assisting IRS with the audit of these returns, your response to this survey will help us to identify the factors which affect the resolution of CEP audits, both positively and negatively.

This questionnaire is confidential. The control number is included only to aid us in our follow-up efforts. Your responses will be combined with those of other respondents and will be reported only in summary form. We will not identify specific CEP taxpayers in our report.

Most of the questions can be easily answered by checking boxes or filling in blanks. We estimate this questionnaire should take about 2 hours to complete. The actual amount of time it will take to complete depends on the number of tax years involved and the availability of data. If you have any questions concerning any part of this survey, please call Ms. Deborah Junod at (202) 272-7904.

Please return the completed questionnaire in the enclosed pre-addressed envelope within 2 weeks from the time you receive it. In the event the envelope is misplaced, the return address is:

U.S. General Accounting Office
General Government Division
Attn: Ms. Valerie Caracelli
441 G Street, N.W., Room 3126
Washington, D.C. 20548

Thank you for your assistance.

**Corporate Tax Return Information:**

***After completing this questionnaire, please remove the case information sticker before returning your completed questionnaire.***

**Total number of taxpayer respondents = 73**

I. RESPONDENT INFORMATION

Please provide your current work telephone number . . . . . (_____)_____

Were you assigned to assist with the IRS audit of the tax years shown on page 1? (CHECK ONE.) (8)

73 Yes --> **Please continue with question 1.**

- No --> **STOP: Do not continue if you were not assigned to assist with the IRS audit of the tax returns shown on page 1. Please return the questionnaire in the enclosed envelope.**

1. Please provide your position title at the time you were assigned to the audit of the above returns. (9-10)

11 Vice-President, Tax
6 Tax Counsel
20 Director of Taxes
30 Tax Manager
3 Tax Accountant
2 Other

2. Please enter the total number of years you had held the position entered above at the time you were assigned to the audit of the above returns.

N=73
Mean=5 Years (11-12)

3. Please indicate whether or not you have held the following positions at this corporation. For those positions you have held, please enter the number of years you held that position. *(Enter "0" if none or under 1 year.)*

| Position | Yes (1) | No (2) | Time in position | |
|---|---|---|---|---|
| a. Vice-President - Taxes | 17 | 50 | Mean=6 Years | (13-15) |
| b. Director of Taxes | 30 | 37 | Mean=9 Years | (16-18) |
| c. Tax Manager | 48 | 23 | Mean=8 Years | (19-21) |
| d. Tax Attorney | 11 | 56 | Mean=7 Years | (22-24) |
| e. Tax Accountant | 26 | 40 | Mean=5 Years | (25-27) |
| f. Other tax-related positions with this corporation. (Please specify) N=18 | | | _____ Years | (28-30) |
| | | | _____ Years | (31-33) |
| g. Other tax-related position(s) with other companies. (Please specify.) N=34 | | | _____ Years | (34-36) |
| | | | _____ Years | (37-39) |

4. Were you ever employed by the Internal Revenue Service? (CHECK ONE.) (40)

62 No ——> **(GO TO QUESTION 5.)**

11 Yes ——> Please indicate whether or not you held the following positions at IRS. For those positions you have held, please enter the number of years you held the position. *(Enter "0" if none or under 1 year.)*

| Position | Yes (1) | No (2) | Time in position | |
|---|---|---|---|---|
| a. Revenue Agent | 7 | 3 | Mean=6 Years | (41-43) |
| b. IRS Exam Case/Group Manager | - | 7 | _____ Years | (44-46) |
| c. IRS Appeals Officer | 1 | 5 | 1 Year | (47-49) |
| d. Other IRS position(s) related to corporate audits. (Please specify) N=5 | | | _____ Years | (50-52) |
| | | | _____ Years | (53-55) |
| e. Other government position(s) related to tax/auditing (Please specify) N=3 | | | _____ Years | (56-58) |
| | | | _____ Years | (59-61) |

5. What was your educational background at the time you were assigned to assist IRS with the audit of these returns? (CHECK ALL THAT APPLY.) (62-70)

1 24 Hours of Accounting with no degree

52 Bachelors - Accounting/Taxation

11 Bachelors - Other (Specify: _____)

15 Masters - Accounting/Taxation

9 MBA

1 Masters - Other (Specify: _____)

20 J.D. or LL.B.

- Ph.D. (Specify: _____)

7 Other (Specify: _____)

6. Were you a CPA when you were assigned to assist IRS with the audit of these returns? (CHECK ONE.) (71)

32 Yes

38 No

7. How many staff resources did your corporation use to assist IRS in the audit and Appeals process for these tax years. *(Please enter the actual number of staff days used for each type of position listed below. If actual data is not available, please enter N/A in the spaces below and go to question 8.)* (72-95)

a. Attorneys . . . . . Mean=263 Staff Days
N=19

b. Accountants & Tax Specialists Mean=749 Staff Days
N=23

c. Outside specialists/consultants . Mean=37 Staff Days
N=11

d. Administrative/support . . . . . Mean=156 Staff Days
N=11

e. Other - Please specify:
N=0

_____ _____ Staff Days

_____ _____ Staff Days

**TOTAL** . . . . . Mean=1190 Staff Days
N=23

## II. IRS EXAMINATION CASE MANAGEMENT

Repeat ID4/Rec 2 (1-7)

8. Overall, how satisfied or dissatisfied were you with the following? (CHECK ONE BOX IN EACH ROW.) (8-20)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Adequacy of the IRS audit team's experience and skills in auditing large corporations. | 18 | 25 | 14 | 13 | 3 | - |
| b. Adequacy of the IRS audit team's knowledge of tax laws, rules, and regulations. | 15 | 21 | 20 | 11 | 5 | - |
| c. Adequacy of the IRS audit team's knowledge of international issues associated with your corporation. | 8 | 22 | 13 | 11 | 7 | 12 |
| d. Adequacy of the IRS audit team's knowledge of your corporation's primary industry. | 13 | 22 | 18 | 13 | 7 | - |
| e. Level of cooperation between your staff and the IRS team. | 31 | 20 | 7 | 7 | 7 | - |
| f. Length of time it took to complete the audit. | 7 | 20 | 16 | 12 | 18 | - |
| g. Corporation's involvement in discussing the audit plan. | 9 | 13 | 22 | 13 | 11 | 5 |
| h. Substance of issues discussed at the opening conference. | 9 | 10 | 29 | 8 | 9 | 8 |
| i. Substance of issues discussed at the closing conference. | 11 | 15 | 20 | 10 | 8 | 6 |
| j. Extent to which you had interim discussions with the IRS team members. | 20 | 28 | 13 | 6 | 6 | - |
| k. Adequacy of IRS' equipment. | 5 | 10 | 27 | 4 | 5 | 22 |
| l. Adequacy of IRS's research material. | 3 | 9 | 28 | 4 | 5 | 24 |
| m. Adequacy of IRS' supplies. | 5 | 9 | 28 | 3 | 3 | 25 |

9. In your opinion, what was the quality of work performed by the following IRS personnel who worked on this audit? (CHECK ONE BOX IN EACH ROW. CHECK BOX 1 IF THE POSITION WAS NOT USED ON THIS AUDIT.) (21-33)

| IRS Personnel | Position not used (1) | Excellent (2) | Good (3) | Adequate or marginal (4) | Poor (5) | Very poor (6) | No basis to judge (7) |
|---|---|---|---|---|---|---|---|
| a. Case manager | - | 16 | 32 | 9 | 11 | 5 | - |
| b. Team coordinator(s) | - | 18 | 29 | 12 | 11 | 1 | 2 |
| c. Other Exam revenue agents | 2 | 4 | 37 | 21 | 4 | 1 | 2 |
| d. Computer audit specialist | 3 | 10 | 29 | 23 | 3 | 1 | 3 |
| e. Industry/issue specialist | 32 | 1 | 11 | 6 | 6 | 4 | 11 |
| f. Engineer | 6 | 6 | 19 | 22 | 11 | 6 | 3 |
| g. International specialist | 8 | 3 | 30 | 13 | 9 | 4 | 4 |
| h. Economist | 43 | 1 | 3 | 6 | 8 | 3 | 7 |
| i. Outside consultant | 54 | - | - | - | - | 1 | 15 |
| j. EP/EO specialist | 36 | 3 | 13 | 5 | - | 1 | 12 |
| k. Appeals staff | 10 | 22 | 27 | 3 | 3 | - | 3 |
| l. Counsel | 38 | 3 | 5 | 5 | 4 | 1 | 14 |
| m. Other (Please specify) N=7 | | | | | | | |

10. In your opinion, what was the quality of the case manager's supervision of IRS personnel assigned to this audit? (CHECK ONE.) (34)

14 Excellent

31 Good

11 Adequate or marginal

9 Poor

5 Very poor

3 No basis to judge

11. Overall, how satisfied or dissatisfied were you with IRS management's involvement with the audit? (CHECK ONE BOX IN EACH ROW.) (35-38)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Case manager | 24 | 15 | 11 | 12 | 10 | 1 |
| b. Branch Chief | 4 | 4 | 10 | 1 | 2 | 51 |
| c. Chief or Assistant Chief of Examination | 1 | 1 | 6 | 1 | 2 | 60 |
| d. District Director | 1 | 1 | 4 | 1 | 1 | 64 |

12. In your opinion, would increased IRS managerial oversight by the Branch Chief, Chief of Examination, or District Director have improved working relationships and the flow of information between your corporation and IRS (e.g., prompt response to IDRs or meetings to discuss disagreements between you and IRS)? (CHECK ONE.) (39)

16 Yes

38 No

18 Does not need improvement

Please explain your response.

_____

_____

13. To what extent, if at all, did IRS involve your corporation's representatives in the following activities? (CHECK ONE BOX IN EACH ROW.) (40-45)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Preparation of the audit plan | 1 | 6 | 7 | 13 | 45 | 1 |
| b. Reaching agreement on how the audit of certain issues would proceed | 1 | 16 | 19 | 18 | 18 | 1 |
| c. Interim meetings with the IRS team | 6 | 27 | 20 | 11 | 9 | - |
| d. Informal resolution of problems with the revenue agents | 6 | 22 | 15 | 11 | 16 | 2 |
| e. Discussions with IRS management | 2 | 7 | 11 | 16 | 28 | 9 |
| f. Setting the audit completion date | 3 | 14 | 12 | 12 | 30 | 1 |

14. To what extent, if at all, did your corporation provide the following assistance to IRS? (CHECK ONE BOX IN EACH ROW.)

(46-50)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) | Do not know (6) |
|---|---|---|---|---|---|---|
| a. Access to supplies | 13 | 19 | 13 | 8 | 17 | 3 |
| b. Access to research materials | 24 | 18 | 16 | 6 | 9 | - |
| c. Access to computers | 6 | 13 | 13 | 9 | 30 | 1 |
| d. Access to printers | 6 | 12 | 9 | 6 | 37 | 2 |
| e. Access to photocopiers | 43 | 20 | 4 | 3 | 1 | - |

15. Did IRS raise a new issue within 90 days of the targeted closing date of the audit? (CHECK ONE.)

(51)

31 Yes

32 No

10 Do not know

16. Did you raise a new issue within 90 days of the targeted closing date of the audit? (CHECK ONE.)

(52)

12 Yes

55 No

6 Do not know

17. Was this case closed out of Exam later than planned? (CHECK ONE.)

(53)

34 Yes —> (CONTINUE WITH QUESTION 18.)

22 No

(SKIP TO QUESTION 19.)

17 Do not know

18. To what extent, if at all, did the following factors cause delays in closing the case in Exam? (CHECK ONE BOX IN EACH ROW.)

(54-67)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. IRS difficulty obtaining staff or specialists | 1 | 3 | 3 | 5 | 13 | 9 |
| b. Turnover of your corporations' staff or specialists | - | 2 | 2 | 7 | 21 | 2 |
| c. Turnover of IRS staff or specialists | 1 | - | 2 | 7 | 18 | 6 |
| d. Diversion of your corporation's staff to other duties | 1 | 5 | 5 | 8 | 15 | - |
| e. Diversion of IRS staff to other duties | 1 | 1 | 7 | 7 | 12 | 6 |
| f. Obtaining technical advice | 1 | 1 | 1 | 3 | 21 | 7 |
| g. Issuance of a summons | - | 1 | 1 | 1 | 23 | 8 |
| h. Responding to IDRs | 2 | 8 | 8 | 8 | 7 | 1 |
| i. Granting IRS access to computer files | - | - | - | 1 | 30 | 3 |
| j. Having access to IRS officials | - | - | 2 | 4 | 22 | 6 |
| k. Delays by IRS in starting the examination | - | 2 | 1 | 2 | 26 | 3 |
| l. Delays by your corporation in starting the examination | - | - | - | 2 | 28 | 3 |
| m. Delays in development of international issues | 5 | 5 | 4 | 5 | 11 | 4 |
| n. Other - Specify: N=8 | | | | | | |

19. Did IRS include you in developing a schedule for issuance of IDRs as part of the audit planning process? (CHECK ONE.)

(68)

49 No

22 Yes ----> Did IRS deviate significantly from this schedule? (CHECK ONE.)

(69)

6 Yes

15 No

1 Do not know

20. Overall, how satisfied or dissatisfied were you with the following? (CHECK ONE BOX IN EACH ROW.) (70-72)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. That IDRs were issued in a timely manner | 13 | 26 | 17 | 14 | 2 | 1 |
| b. That IDRs were clearly and concisely prepared | 6 | 28 | 11 | 19 | 9 | - |
| c. That the information requested through IDRs was obtainable (e.g., information was not too old or missing due to merger, etc.) | 6 | 21 | 19 | 20 | 4 | 2 |

21. Did IRS submit an IDR within 90 days of the targeted closing date of the audit? (CHECK ONE.) (73)

32 Yes

25 No

16 Do not know

22. Did your corporation agree to extend the statute expiration date? (CHECK ONE.) (74)

0 IRS did not request an extension

72 Yes --> *How many times did you agree to extend the statute?* Mean=4 Times (75-76)

1 No --> Please explain why your corporation did not agree. _____

_____

_____

23. Did your corporation request a private letter ruling(s), determination letter(s), or technical advice on any issue for these tax years? (CHECK ALL THAT APPLY.) (77-81)

6 Yes, a private letter ruling or rulings

3 Yes, a determination letter or letters

9 Yes, technical advice

52 None of the above

3 Do not know

24. Pursuant to IRC Section 6662, did your corporation disclose issues at the beginning of the audit? (CHECK ONE.) (82)

39 Yes

32 No

25. Did your corporation provide IRS with a list of adjustments to taxable income or credits for those tax years being audited? (CHECK ONE.) (83)

63 Yes ---> (CONTINUE WITH QUESTION 26.)

10 No ---> (SKIP TO QUESTION 27.)

26. Who did the adjustments favor? (CHECK ONE.) (84)

1 IRS only

1 The taxpayer only

61 Both IRS and the taxpayer

- Do not know

27. Did your corporation sign a formal agreement (Form 870) on the proposed adjustments at the time the case was closed out of Exam? (CHECK ONE.) (85)

9 Yes, we agreed to all issues (full agreement)

22 Yes, we agreed to some issues (partial agreement)

41 No

- Do not remember

28. Were there certain audit issues for which you agreed with Examination's resolution but for which you did not sign a formal agreement (Form 870)? (CHECK ONE.) (86)

33 No

40 Yes --> Please explain why you did not sign a formal agreement.

_____

_____

_____

_____

_____

_____

29. Taking everything into consideration, how would you rate the overall quality of Exam's **identification** of the audit issues on these returns? (CHECK ONE.) (87)

10 Excellent

25 Good

25 Adequate

6 Poor

3 Very poor

2 No basis to judge

Please explain your response:

_____

_____

_____

_____

_____

30. Taking everything into consideration, how would you rate the overall quality of Exam's **development** of the audit issues on these returns? (CHECK ONE.) (88)

9 Excellent

16 Good

25 Adequate

16 Poor

6 Very poor

- No basis to judge

Please explain your response:

_____

_____

_____

_____

_____

## III. APPEALS INFORMATION

31. Did you protest any issues contained in this audit? (CHECK ONE.) (89)

62 Yes --> (CONTINUE WITH QUESTION 32.)

9 No --> (SKIP TO QUESTION 39.)

32. Overall, how satisfied or dissatisfied were you with the following aspects of the appeals process? (CHECK ONE BOX IN EACH ROW.) (90-94)

| | Very satisfied (1) | Somewhat satisfied (2) | Neither satisfied nor dissatisfied (3) | Somewhat dissatisfied (4) | Very dissatisfied (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Adequacy of the Appeals team's knowledge of tax laws, rules, and regulations | 26 | 26 | 5 | 1 | - | 4 |
| b. Adequacy of the Appeals team's knowledge of your corporation's primary industry | 20 | 21 | 14 | 2 | - | 5 |
| c. Level of cooperation between your staff and the Appeals team | 35 | 18 | 4 | 1 | 1 | 3 |
| d. Length of time it took to reach a settlement on the disputed issues | 13 | 23 | 5 | 15 | 4 | 2 |
| e. Fairness of the settlement reached | 20 | 24 | 11 | 2 | 1 | 3 |

33. Did your corporation provide new information or documentation regarding disputed issues at the Appeals level that you did not provide during the audit? (CHECK ONE.) (95)

29 No

34 Yes --> Please explain why this information was not provided during the audit.

_____

_____

_____

Repeat ID#/Rec 3 (1-7)

34. For protested issues, IRS provided the following information on the three top dollar adjustments per the revenue agent's report to income/credits that impacted the corporate income tax liability in this case. Please refer to these issues when answering questions 35 to 38.

*If we have not identified the issues, please provide the requested data in the matrix below for the top three dollar adjustments for protested issues and continue with question 35.*

| | Issue #1 | Issue #2 | Issue #3 |
|---|---|---|---|
| a. IRC *[Enter IRC Section Number(s)]* | _____ _____ ___ ___ ___ ___ (8-11) _____ _____ ___ ___ ___ ___ (20-23) _____ _____ ___ ___ ___ ___ (32-35) | _____ _____ ___ ___ ___ ___ (12-15) _____ _____ ___ ___ ___ ___ (24-27) _____ _____ ___ ___ ___ ___ (36-39) | _____ _____ ___ ___ ___ ___ (16-19) _____ _____ ___ ___ ___ ___ (28-31) _____ _____ ___ ___ ___ ___ (40-43) |
| b. Adjustment to: *(Check one per issue.)* | (44) 59 Taxable income 4 Credit | (45) 57 Taxable income 5 Credit | (46) 48 Taxable income 10 Credit |
| c. Dispute involved: *(Check one or both.)* | (47-48) 48 Interpretation of law 43 Based on merit/facts | (49-50) 42 Interpretation of law 39 Based on merit/facts | (51-52) 45 Interpretation of law 31 Based on merit/facts |
| d. Type of Adjustment *(Check all that apply.)* | (53-58) 11 Unreported income 24 Overstated deductions 25 Timing 2 Valuation 9 Allocation 12 Other (Specify) _____ | (59-64) 7 Unreported income 24 Overstated deductions 12 Timing - Valuation 9 Allocation 18 Other (Specify) _____ | (65-70) 6 Unreported income 20 Overstated deductions 10 Timing 1 Valuation 8 Allocation 18 Other (Specify) _____ |
| e. Adjustment to income or credits proposed by Exam | N=62 (8-18) Mean = $102,466,171 Range = $0 to $1,070,320,853 | N=60 (19-29) Mean = $49,512,963 Range = $-127,738,791 to $566,703,455 | N=58 (30-40) Mean = $23,882,207 Range = $-51,511,089 to $168,280,618 |
| f. Amount of adjustment agreed to with Appeals. | N=61 (41-51) Mean = $18,918,423 Range = $-151,102,119 to $525,516,383 | N=59 (52-62) Mean = $25,786,337 Range = $-50,873,768 to $475,146,014 | N=57 (63-73) Mean = $9,548,409 Range = $-52,000,000 to $105,233,259 |

35. How many staff days did your corporation use to assist IRS on each issue through the examination and appeals process?

| Issue #1 | Issue #2 | Issue #3 |
|---|---|---|
| N=14<br>Mean=32 Staff days (74-76)<br>or<br>48 Do not know (77) | N=14<br>Mean=26 Staff days (78-80)<br>or<br>47 Do not know (81) | N=13<br>Mean=21 Staff days (82-84)<br>or<br>47 Do not know (85) |

Repeat ID#/Rec 5 (1-7)

36. For each of the identified three issues, which of the following factors caused your corporation to protest the issue? **(CHECK YES OR NO FOR EACH ROW FOR EACH ISSUE.)**

| | Issue #1 | | Issue #2 | | Issue #3 | | |
|---|---|---|---|---|---|---|---|
| | Yes (1) | No (2) | Yes (1) | No (2) | Yes (1) | No (2) | |
| a. Disagreement over interpretation of the law | 58 | 5 | 55 | 5 | 50 | 7 | (8-10) |
| b. Disagreement over facts | 27 | 35 | 25 | 34 | 28 | 29 | (11-13) |
| c. Amount supported by taxpayer documentation exceeds the amount allowed by Exam | 19 | 40 | 20 | 37 | 20 | 32 | (14-16) |
| d. Disagreement on timing issues | 23 | 37 | 18 | 38 | 15 | 38 | (17-19) |
| e. Disagreement on valuation issues | 4 | 54 | 6 | 50 | 5 | 48 | (20-22) |
| f. Disagreement on allocation issues | 11 | 49 | 12 | 43 | 9 | 42 | (23-25) |
| g. Appeals settlement on prior cases | 22 | 38 | 10 | 47 | 9 | 45 | (26-28) |
| h. Appeals settlement of the same issue for a different taxpayer | 8 | 52 | 4 | 53 | 5 | 49 | (29-31) |
| i. Other (Specify) _____ | | | | | | | (32-34) |
| j. Other (Specify) _____ | | | | | | | (35-37) |

37. Did your corporation use any internal or outside specialists (including attorneys, economists, accountants, engineers, appraisers, etc.) to assist with any of these three issues? (CHECK ONE.) (38)

10 No

1 Do not know

51 Yes ——> *Please list the type of specialists used and check the issue number(s).*

| Specialist | | Issue Number | | | |
|---|---|---|---|---|---|
| 64 Attorney | (39-40) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (41) |
| 18 Accountant | (42-43) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (44) |
| 5 Economist | (45-46) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (47) |
| 5 Engineer | (48-49) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (50) |
| 2 Actuary | (51-52) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (53) |
| 5 Other | (54-55) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (56) |

38. For any of these three issues, did IRS need any specialists (i.e., attorneys, economists, accountants, engineers, appraisers, etc.) that were not used? (CHECK ONE.) (57)

33 No

23 Do not know

5 Yes, there was a need but they were not used ------> *Please list the type of specialist not used that you feel IRS should have used and check the issue number(s).*

| Specialist Needed But Not Used By IRS | | Issue Number | | | |
|---|---|---|---|---|---|
| 2 Attorney | (58-59) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (60) |
| 2 Actuary | (61-62) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (63) |
| 1 Economist | (64-65) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (66) |
| 1 Industry specialist | (67-68) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (69) |
| _____ | (70-71) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (72) |
| _____ | (73-74) | ☐ Issue #1 | ☐ Issue #2 | ☐ Issue #3 | (75) |

## IV. IMPLEMENTED OR PROPOSED CHANGES IN THE IRS COORDINATED EXAMINATION PROGRAM

39. The following matrix contains changes to IRS' Coordinated Examination Program that have been proposed or implemented. Had these changes been implemented at the time IRS audited these tax returns, do you feel they would have had a positive, negative, or no impact on; (1) IRS' identification and development of audit issues and (2) the timeliness of the audit? (CHECK ONE BOX UNDER EACH COLUMN FOR EACH ROW.)

| CHANGES | Impact this change would have had on identifying and developing issues. *(Check one box for each row.)* | Impact this change would have had on the timeliness of the audit. *(Check one box in each row.)* |
|---|---|---|
| a. Establishment of a National Policy Board to improve coordination between Exam, International, Appeals, and Counsel. | 21 Positive impact (76)<br>23 No impact<br>8 Negative impact<br>20 Do not know | 17 Positive impact (77)<br>27 No impact<br>10 Negative impact<br>17 Do not know |
| b. Establishment of a National Executive Director for CEP. | 9 Positive impact (78)<br>33 No impact<br>4 Negative impact<br>25 Do not know | 8 Positive impact (79)<br>32 No impact<br>10 Negative impact<br>20 Do not know |
| c. Increased involvement by Exam district office management to ensure better planning and provide more support while audits are conducted. | 25 Positive impact (80)<br>23 No impact<br>9 Negative impact<br>14 Do not know | 30 Positive impact (81)<br>21 No impact<br>10 Negative impact<br>9 Do not know |
| d. Establishment of Regional CEP Managers. | 9 Positive impact (82)<br>24 No impact<br>9 Negative impact<br>29 Do not know | 10 Positive impact (83)<br>22 No impact<br>15 Negative impact<br>22 Do not know |
| e. Standardized goals and measures for Exam, International, Appeals, and Counsel. | 13 Positive impact (84)<br>14 No impact<br>15 Negative impact<br>29 Do not know | 14 Positive impact (85)<br>16 No impact<br>12 Negative impact<br>28 Do not know |
| f. IRS Counsel involvement at the start of all audits in Examination. | 11 Positive impact (86)<br>13 No impact<br>33 Negative impact<br>15 Do not know | 9 Positive impact (87)<br>15 No impact<br>36 Negative impact<br>11 Do not know |

40. Do you believe IRS case managers or other Examination officials should be actively attempting to settle more audit issues based on the merits (facts) of a case? (CHECK ONE.) (88)

66 Yes

3 No

Please explain: _____

Repeat ID#/Rec 6 (1-7)

## V. IMPLEMENTED OR PROPOSED CHANGES IN IRS' APPEALS LARGE CASE PROGRAM

41. The following matrix contains changes to IRS' Appeals Large Case Program that have been proposed or implemented. Had these changes been implemented at the time you appealed disputed issues on these tax returns, do you feel they would have had a positive, negative, or no impact on; (1) the process of settling disputed issues and (2) the timeliness of the appeals process? (CHECK ONE BOX UNDER EACH COLUMN FOR EACH ROW.)

| CHANGES | Impact this change would have had on the process of settling disputed issues. *(Check one box for each row.)* | Impact this change would have had on the timeliness of the appeals process. *(Check one box in each row.)* |
|---|---|---|
| a. Establishment of a National Policy Board to improve coordination between Exam, International, Appeals, and Counsel. | 17 Positive impact (8)<br>13 No impact<br>12 Negative impact<br>25 Do not know | 14 Positive impact (9)<br>17 No impact<br>13 Negative impact<br>23 Do not know |
| b. Establishment of Assistant Regional Directors of Appeals for the Large Case Program. | 8 Positive impact (10)<br>24 No impact<br>3 Negative impact<br>32 Do not know | 8 Positive impact (11)<br>20 No impact<br>9 Negative impact<br>30 Do not know |
| c. Expansion of Appeals Team Chief authority to settle cases. | 44 Positive impact (12)<br>13 No impact<br>- Negative impact<br>11 Do not know | 41 Positive impact (13)<br>16 No impact<br>1 Negative impact<br>10 Do not know |
| d. Standardized goals and measures for Exam, International, Appeals and Counsel. | 12 Positive impact (14)<br>12 No impact<br>13 Negative impact<br>31 Do not know | 11 Positive impact (15)<br>11 No impact<br>14 Negative impact<br>32 Do not know |
| e. Establishment of Appeals' Office of Large cases in IRS' National Office. | 7 Positive impact (16)<br>12 No impact<br>17 Negative impact<br>32 Do not know | 7 Positive impact (17)<br>12 No impact<br>21 Negative impact<br>28 Do not know |
| f. Establishment of an Industry Specialization Program for Appeals. | 13 Positive impact (18)<br>14 No impact<br>22 Negative impact<br>19 Do not know | 11 Positive impact (19)<br>14 No impact<br>24 Negative impact<br>19 Do not know |
| g. Formal pre-conferences between Exam and Appeals. | 14 Positive impact (20)<br>20 No impact<br>13 Negative impact<br>21 Do not know | 17 Positive impact (21)<br>16 No impact<br>16 Negative impact<br>19 Do not know |
| h. Formal post-conferences between Exam and Appeals. | 17 Positive impact (22)<br>19 No impact<br>8 Negative impact<br>24 Do not know | 17 Positive impact (23)<br>20 No impact<br>9 Negative impact<br>22 Do not know |

42. If IRS became "current" in the tax years they have under audit, to what extent, if at all, do you believe the following could be accomplished? (CHECK ONE BOX IN EACH ROW.)

(24-28)

| | To a very great extent (1) | To a great extent (2) | To a moderate extent (3) | To some extent (4) | To little or no extent (5) | No basis to judge (6) |
|---|---|---|---|---|---|---|
| a. Delays in your response to IDR's could be decreased. | 10 | 25 | 20 | 12 | 5 | - |
| b. IRS's development of audit issues could be improved. | 7 | 15 | 13 | 14 | 16 | 7 |
| c. The number of audit issues agreed to at the Exam level could be increased. | 7 | 15 | 11 | 11 | 22 | 6 |
| d. The working relationship between IRS and your corporation could be improved. | 7 | 17 | 12 | 12 | 20 | - 4 |
| e. Other (Specify) N=3 | | | | | | |

## VI. GENERAL QUESTIONS

43. Are there any other changes to the Coordinated Exam Program or Appeals' Large Case Program that you would like to suggest here? (29)

N=39

44. Please briefly discuss in the space below what you feel was the most positive thing as well as the most negative thing about the CEP audit of these returns.

**Positive:** N=42 (30)

**Negative:** N=52 (31)

45. Please briefly discuss in the space below what you feel was the most positive thing as well as the most negative thing about IRS Appeals' resolution of protested issues.

**Positive:** N=49 (32)

**Negative:** N=39 (33)

# Comments From the Internal Revenue Service and Our Evaluation

Note: We have retyped verbatim pages 1 through 18 of IRS' general concerns portion of its letter to facilitate interspersement of GAO comments, which are in boldface type.

COMMISSIONER

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

January 11, 1994

Ms. Jennie S. Stathis
Director, Tax Policy and
Administration Issues
United States General Accounting Office
Washington, DC 20548

Dear Ms. Stathis:

Thank your for the opportunity to review your recent draft report entitled "Tax Administration: IRS Cannot Measure or Assure Compliance by Large Corporations".

Enclosed are our detailed comments concerning the draft report. Our general concerns, clarifying the report text on key aspects of the Coordinated Examination Program and the Appeals process precede our response to the report's specific recommendations. It is important to note that GAO's review focused on cases closed in fiscal years '89, '90 and '91. These cases were generally received in Appeals two to three years before they were closed. The structure of the program reviewed and commented on by GAO is not the same as the present one.

We hope you find these comments useful.

Sincerely,

Margaret Milner Richardson

Enclosure

IRS COMMENTS ON GAO DRAFT REPORT ENTITLED "TAX ADMINISTRATION: IRS CANNOT MEASURE OR ASSURE COMPLIANCE BY LARGE CORPORATIONS"

GENERAL CONCERNS

The Large Case Programs in Appeals and Examination have greatly changed since the cases reviewed by GAO started through the process. The GAO review focused on cases closed in fiscal years '89, '90 and '91. Those cases were generally received in Appeals two to three years before they were closed. Since 1991 their have been many changes to the Large Case program - particularly as a result of the Appeals Management Initiative of fiscal year 1991. The structure of the program reviewed and commented on by GAO is not the same one that now exists. In this respect the report is merely a historical record of the large case program that was and it is not an accurate description or assessment of the current program.

GAO reviewed a sample of 12 cases - 9 of which went forward to Appeals unagreed. That is rather small when compared to the approximately 600 Large Cases closed by Appeals during the years in question. GAO's sample was neither randomly drawn nor statistically accurate. It was too small to constitute a valid sample for purposes of drawing any conclusions regarding the process that existed during the years in question. Yet GAO used that sample - supplemented by anecdotal information - to recommend fundamental changes to the Appeals process. The anecdotal information ranged from a single comment by an Appeals employee to statistics that seem to conflict with IRS published information.

**GAO COMMENT 1: IRS said our report is merely an historical record of CEP and not an accurate depiction of the current CEP. IRS questioned whether our work allows us to make any conclusions and recommendations. IRS also criticized us for using a nonrandom sample of 12 CEP cases.**

**We disagree with IRS' positions. Our methodology allowed us to evaluate the recent state of CEP--including the initial effects of IRS' changes since 1990--and draw conclusions. Although we support many of IRS' ongoing changes to CEP, we recommend other changes that we view as necessary.**

**We added language throughout our report to further describe the basis for our conclusions and recommendations, but a summary may be helpful here. Through most of 1993, our work included case studies, standard surveys of IRS and corporate officials, IRS and**

corporate interviews, and the collection rate computation. Details on each approach follow.

First, a case study approach is an acceptable research method, particularly when drawing a representative sample would be difficult and seeking in-depth data and personal perspectives is desired. Although nonrandom, our selection of the 12 CEP cases followed rigorous criteria. We selected our 12 cases from the 108 cases in our survey universe. The 12 cases accounted for $1.5 billion (18 percent) of $8.5 billion in additional taxes recommended in the 108 cases. Also, each case had to come from one of four districts we visited. These districts generated over 40 percent of all CEP taxes recommended in fiscal year 1990.

As described in the draft report, our methodology extended beyond 12 case studies. The 108 cases in our survey universe covered the CEP audit cases closed in fiscal years 1989 through 1991 that had $30 million or more in additional taxes recommended (see pp. 27 and 85-89). This threshold of $30 million enabled us to focus on large cases with the greatest impact on the collection rate. Responses from 308 IRS and corporate officials in the 108 cases gave us a broad overview of CEP.

Further, we separately interviewed 74 IRS officials, some more than once, who had responsibility for CEP or our 12 cases. We also interviewed corporate officials for 11 of our 12 cases; 1 corporation would not meet with us. The IRS and corporate interviews provided insights on the factors affecting our 12 cases and on the current status of CEP.

Knowing that IRS has been changing CEP, we designed each approach to allow us to evaluate past and current processes for audits and appeals. Doing so enabled us to capture the status and initial effects of IRS' changes (see p. 43).

We discussed our entire methodology with high-level Appeals and Examination officials responsible for CEP before doing our field work. They acknowledged the validity of our case study and survey methodologies at that time. Officials in the four districts told us our cases represented their typical CEP audits and appeals. They commented on our IRS and corporate surveys for the 108 cases, which helped to ensure that the surveys were technically correct.

**Also, IRS criticized us for using "anecdotal" information and statistics that conflict with published IRS information. We disagree that our results are anecdotal. Our examples of remarks made by IRS officials demonstrate typical attitudes we heard from those surveyed or interviewed. The officials had responsibility for CEP audits or appeals and decisions about millions in tax revenues. Moreover, we are not aware of any conflicts with IRS published information.**

The Service does not concur that the 22.1% collection rate reported by GAO accurately reflects the current status of CEP. Therefore, the Service does not concur with the GAO recommendation that the 22.1% rate should be used to project large case revenue. First, GAO's 22.1% rate is not a collection rate, anyway; it is an assessment rate. Second, recent data suggest that both the assessment rate and the corresponding collection rate are much higher that 22.1%. These data are from the Enforcement Revenue Information System (ERIS) for CEP closures from Examination or Appeals in FY91, FY92, and FY93 (partial year), and reflect the effects of tax law changes and CEP improvement initiatives. ERIS data are the most current and accurate data available to the Service, and as such, should be relied on to project CEP revenue.

As the ERIS database becomes increasingly comprehensive, covering five years or more, we will track and adjust the assessment and collection rates accordingly. It should be remembered that data from any one year could skew the CEP collection-to-recommendation ratio significantly. For revenue projection, analysis of a multi-year average is the correct approach, and ERIS is the correct database.

**GAO COMMENT 2: First, IRS suggested that our collection rate is an assessment rate. As explained in our text (see p. 30), we used the terms "assessed" and "collected" interchangeably because we found that CEP corporations paid almost all tax assessments. Our analysis of all CEP corporate income tax returns on BMF at the end of fiscal year 1992 showed that CEP corporations paid 99.91 percent of $380 billion in assessments.**

**Second, IRS said our 22-percent rate is too low and should not be used to project revenue. As support, IRS used ERIS data. IRS believes these data reflect recent tax law changes and CEP changes since 1990.**

**We did not intend for our collection rate to be used to project revenues. IRS is developing ERIS to help do so. We encourage IRS to continue to develop that capability.**

We revised our recommendation to clarify our intent.

ERIS may be appropriate for projecting revenue, but we question use of ERIS data to challenge our collection rate. Although we did not attempt to evaluate ERIS, we met with IRS officials and reviewed summary ERIS data through December 1993 after IRS shared its draft comments. This work allowed us to conclude that IRS could not know whether 22 percent is too low or too high. As discussed in our draft report, IRS officials said they did not know the actual rate (see pp. 30 and 34). While we acknowledge that our rate will rarely reflect recent tax law and CEP changes, neither will ERIS data.

Unlike IRS, we computed the actual collection rate. Our computation relied on IRS data and recognized that CEP audits and the resolution of any disputes typically span at least 8 years. Knowing this, we focused on about 9,000 CEP audits that IRS closed between fiscal years 1983 and 1991. For these audits, we measured the portion of the additional taxes recommended that IRS ultimately collected through fiscal year 1992 after completing any appeals or litigation.

On the other hand, ERIS data do not yet allow IRS to compute the actual collection rate. So far, ERIS has been tracking taxes recommended for audits closed in fiscal years 1991 to 1993. ERIS has captured the amount of recommended taxes that taxpayers agreed to pay (not the amount paid) after audits. This agreed amount has roughly averaged 15 percent of all recommended taxes and would be more current than data we used, particularly fiscal years 1992 and 1993.

The other 85 percent of the recommended taxes are being disputed, usually in Appeals. Because IRS does not yet know the collection rate for these taxes, IRS has estimated amounts it would collect over future years, using the results of recently settled cases in Appeals. For example, IRS assumed that the Appeals settlement rate for fiscal year 1991 would apply to disputed taxes from fiscal year 1991 audits. These disputed taxes will take years to settle and collect given the IRS estimate of 2 to 3 years for CEP disputes to be resolved in Appeals.

By using such Appeals' settlements to estimate the rate for 85 percent of the recommended taxes, ERIS' estimates cannot be much more current than our actual rate. We used similar Appeals' results through fiscal year 1992. Our analyses showed that these recent Appeals' results largely

**covered tax years before 1987. Thus, we do not believe that ERIS' data adequately reflect recent tax law and CEP changes.**

**In summary, our rate measures the portion of taxes recommended during fiscal years 1983 through 1991 that IRS actually collected through fiscal year 1992 after any appeals or litigation. ERIS attempts to project revenues that IRS can expect to collect in future fiscal years for CEP audits closed since fiscal year 1991.**

**Further, IRS said as ERIS' data begin covering 5 years or more, it will track and adjust the rate. Later, IRS acknowledged that ERIS cannot yet compute the collection rate because it has not been in place long enough. With enough data, IRS also said ERIS can be used to estimate future collections.**

**We support IRS' efforts and believe that a complete ERIS database could help compute the collection rate and estimate revenues from CEP audits. Our recommendation on correcting IRS' databases will improve the data that enter ERIS for these purposes. We also agree that data from any 1 year can skew the rate, which is why we computed the actual rate over a number of years.**

APPEALS

Appeals conducted its first Large Case Process Review in 1992 and the results of that review point up the need for some changes to the process. The Appeals review consisted of a representative sample of the Large Cases closed during 1992. We recommended changes to the process based on that review and have started our review of the 1993 case closures. The 1992 review established a baseline of information on the Appeals process. We intend to continue the reviews and to compare the results with the established baseline so that we can measure the impact of any changes made to the organization as a result of those reviews.

The GAO report indicated that they had not reviewed the sampled issues for technical correctness. However, at a meeting held May 5, 1993 GAO, representatives stated that their counsel had reviewed the 27 issues in their sample and found none that were technically incorrect.

**GAO COMMENT 3: We disagree with IRS' assertion that GAO Counsel had found no technical problems with Appeals' settlements for the 27 disputed issues we analyzed. As stated in this report, we attempted to evaluate Appeals' settlements but could not conclusively determine the**

**technical correctness because of complex laws and IRS team chiefs' discretion to settle tax disputes. We clarified our final report to alleviate any confusion (see p. 67).**

Overall the report exhibits a misunderstanding of Appeals and the Appeals mission.

**GAO COMMENT 4: We do not believe that our draft report exhibited a misunderstanding of Appeals. However, we added language in chapter 4 to clarify our findings and recommendations.**

Some of the components in the Appeals process that are not treated clearly in the report are:

- What constitutes "Official Service Position" within the meaning of the Internal Revenue Manual;

  **GAO COMMENT 5: We disagree that our draft report did not clearly define "official service position." Our definition came from IRS manuals, and we continue to use that definition (see p. 71).**

- What the Appeals' mission is and where it comes from - specifically the Code of Federal Regulations;

  **GAO COMMENT 6: We disagree that the draft report did not clearly discuss Appeals' mission. We cited the mission verbatim from the IRS manual. However, we made changes in chapter 4 to more clearly discuss Appeals' mission.**

- The difference between settling cases to "avoid litigation" and settling issues - based on the hazards of litigation - to reach a fair result;

  **GAO COMMENT 7: We revised the draft report to address IRS' concerns over our characterization of the basis for Appeals' settlements (see pp. 66-69).**

- What precedential value the settlement of an issue does or does not carry. The report seems to indicate that settling an issue adds to the ambiguity of the tax law rather than simply reflecting the hazards inherent in that ambiguity; and

  **GAO COMMENT 8: Our report acknowledged that the Appeals' settlements cannot resolve the ambiguity of tax laws. We have added language to clarify the "precedential value" of Appeals' settlements given**

**ambiguous tax laws (see pp. 64-65).**

- Recognition that Appeals' mission and process were structured to accommodate the approximately 60,000 cases that the function settles each year - not just the approximately 300 CEP cases that are settled each year in Appeals. CEP cases need to be viewed in the context of the total Appeals program and the purpose of its mission.

**GAO COMMENT 9: IRS indicated that our draft report did not clearly recognize Appeals' mission and process for about 60,000 non-CEP cases that it settles annually. We acknowledge this fact. Our work for more than 2 years has dealt only with CEP cases. Further, Appeals already treats CEP cases differently. It established a separate Office of Large Case to coordinate work on appeals of large dollar amounts such as those by corporations. Thus, we saw no need to discuss how Appeals considers tax disputes by non-CEP taxpayers. Also, we found no basis to support the IRS citation of 300 CEP cases closed annually in Appeals.**

One of our concerns with the GAO report is an apparent misunderstanding on GAO's part of what constitutes "Official Service Position." It is important to remember that not every informal opinion of Counsel is the official Service position. Only published issuances, such as Regulations, Revenue Rulings and Procedures constitute official position. Counsel and the Assistant Commissioner Employee Plans and Exempt Organizations often provide informal advice on issues. These "advisories" are not binding precedent or Service position.

**GAO COMMENT 10: IRS again said we had a misunderstanding of what constitutes official service positions and informal advice. As mentioned earlier (see comment 5), we disagree. Our analysis did not include informal advice.**

It is important to recognize the "precedential" limitations of the various types of Service issuances. Technical advice deals with a specific case and the facts agreed to by both the government and the taxpayer. A Technical Memorandum represents the Service's determination of the tax effects of a specific taxpayer's transaction. It is not binding precedent for another taxpayer or transaction. A Revenue Ruling deals with a set of hypothetical facts and the law at the time the ruling was issued - which may have changed by the time another case raises the specific issue. Such distinctions weaken any analogy made from the published position to the case, and thus increase the hazards of litigation.

The statement on page 92 of the GAO draft report that Appeals' authority to deviate from Service position may improperly favor the taxpayers' position underscores GAO's fundamental misunderstanding of Appeals' authority to deviate from formal IRS position. Appeals proposes a settlement varying from Service position when the hazards of litigation increase the chance that the taxpayer's position would be more likely to be upheld by a court.

**GAO COMMENT 11: We disagree that our discussion on Appeals' deviation from an official service position reflected a misunderstanding of Appeals. Still, we revised our report (see pp. 74-75) to more clearly recognize that Appeals is not required to follow official service positions in settling disputed tax issues.**

The GAO draft report states that in five instances Appeals settled matters contrary to Service position without appropriate consultation with the National Office. We do not believe that this conclusion is correct. We have reviewed all five of those cases - and discussed them with the GAO. Four of them did not involve full concessions or were not contrary to official Service position. One of them may have arguably varied from a previously issued technical advice, however, even that situation is not clear.

In the single case where Appeals might be open to criticism, the technical advice revoked a private letter ruling issued ten years prior to Appeals' action. The facts as presented for purposes of the technical advice being retroactive were not, in the judgment of the Appeals Officer, the facts as they were later developed. Since the technical advice denied section 7805(b) relief on facts that turned out to be incorrect or misleading, the Appeals Officer found that the revocation should be applied only prospectively. The legal merits of the technical advice were not at issue.

**GAO COMMENT 12: IRS disagreed that Appeals settled five cases contrary to IRS' official positions without required coordination, but it acknowledged that in one of the cases, Appeals may be open to criticism. After not reaching agreement on the five cases in discussions with Appeals officials through December 1993, we believe that the confusion about whether coordination was required illustrates the need for more internal controls.**

**Accordingly, we refocused our discussion. Instead of focusing on whether Appeals should have coordinated the settlements, we concentrated on internal controls as well as the expansion of coordination. IRS did not agree to**

**expand coordination to cover substantial concession of issues supported by official service positions. Our report now more fully discusses the merits of this expansion (see pp. 72-74).**

All Appeals decisions must be firmly grounded and supported by (1) the statutory authority and (2) by the delegated power to exercise an independent judgment to resolve interpretive and evidentiary disputes resulting from a complex tax system. The ability to render independent judgments is fundamental to an effective dispute resolution process. We are quick to note, however, that independence without a careful consideration of the merits of opposing views is never effective or appropriate for good tax administration.

It is also important to remember the scope of what we do in Appeals. Last year, we successfully resolved more than 250,000 issues in Appeals. The Large Case Program, while it does generate a great deal of revenue, covers, from a numbers standpoint, only one percent of the cases and issues handled in Appeals. Furthermore, the protocol for contrary-to-Service-position settlement situations extends to all cases. Since a very large percentage of the issues in all resolved cases involve some compromise of some Service position, the GAO proposal, as written, would result in a lengthy delay. For these reasons, we feel the benefits derived from a mandated review of partial compromises would be outweighed by the negative impact on the perception of the independence of Appeals and the delays that would result from those reviews.

**GAO COMMENT 13: We believe that Appeals' Large Case program is much more significant than stated in IRS' comments. By focusing on the number of cases, IRS undercuts the importance of the Large Case program. Other IRS data on the dollar value of the cases highlight their importance. According to Appeals' data at the end of fiscal year 1993, its Office of Large Case accounted for just 455 of the 49,080 cases. Yet, these 455 cases constituted over $39 billion (85 percent) of $46 billion in proposed deficiencies.**

**Also, we disagree that coordinating substantial concessions contrary to official service positions will cause unnecessary delays or infringe on Appeals' independence. Our report discusses this (see p. 76). Also, we did not recommend or imply that every "partial" concession should be coordinated because, as IRS states, a very large portion of every disputed issue is conceded to an extent (see comment 12).**

Appeals does not concede issues to avoid litigation as stated in the draft report. Appeals considers issues on their merits and settles them when necessary based on the hazards of litigation.

**GAO COMMENT 14: IRS said Appeals does not concede issues to avoid litigation. We clarified this issue in our report (see comments 7 and 11).**

EXAMINATION

With respect to the measurement of success in the Coordinated Examination Program the report did not recognize that the Service is in the process of changing the measurement system used to monitor CEP at the national and regional levels. It also appears that GAO did not evaluate and the report did not address the activities of the seven Regional CEP Program Managers and their very active oversight of the program for all districts with CEP workload. The Regional CEP Program Managers, under the direction of the Executive Director, CEP, have actively assumed functional authority and management responsibilities for their programs. Just to provide some insight with respect to the measurements tracked and currently monitored by CEP, we offer the following:

| | | FY92 | FY93 |
|---|---|---|---|
| Total Cases Closed | | 580 | 486 |
| Full/Partially Agreed | | 356 | 347 |
| Percent Full/Partially Agreed | | 61% | 71% |
| Settlement Authority Cases | | 45 | 49 |
| Settlement Authority Dollars | | $459,222,447 | $295,555,843 |
| Accelerated Issue Resolution Agreements: | Cases | 21 | 42 |
| | Dollars | $769,507,386 | $551,343,343 |

It should be noted that these numbers differ significantly from the limited percentages shown by GAO for only fully agreed CEP cases (FY90 - 3%; FY91 - 4.7%; and FY92 - 6%). In addition, CEP has significantly increased the percentage of agreed dollars at the Examination level from approximately 5% in FY90 to 11% in FY91 to 18% in FY92.

**GAO COMMENT 15: IRS said our report ignored its new statistical measures and measurement system for CEP. We did not review them because we focused on the collection rate and they did not exist when we started. We revised the text to mention IRS' new measures and system (pp. 33-34).**

**The IRS letter cited statistics from this system. Because the statistics did not relate to the collection**

**rate, we have not used them, except for the percentage of agreed dollars at the close of CEP audits for fiscal years 1990 to 1992. However, we found that the 1992 agreement rate was 15 percent (see p. 33)--not 18 percent as cited by IRS.**

The Regional Managers have ensured through their monitoring process that key issues which arise within their districts, are being addressed and that there are adequate resources to do the job. They continuously stress to district management the need for their involvement in ongoing risk analysis. Since 1990 more District Directors have become involved with CEP taxpayers in their districts. Continuous meetings have been held over matters such as, record retention problems, delays in responding to information document requests, resolution of issues at the lowest levels, statute of limitations concerns and one stop service concepts.

The Regional CEP Managers have been instrumental in coordinating concerns with Appeals and Counsel over the management of unagreed issues and have had significant overall involvement for a wide range of agreed issues. They have served as chairpersons on over ten major task forces involved with addressing the major concerns in the CEP Quality Improvement Project (QIP). Through their Assistant Regional Commissioners (Examination), the Regional CEP Managers have monitored travel and line item budget activities directly related to CEP and related programs.

**GAO COMMENT 16: Although regional CEP managers may have a role in CEP, our surveys and interviews with district officials showed that district managers--not regional managers--had authority and accountability for CEP. Further, CEP officials told us that they did not have national resource information for CEP and that we should contact the districts (not regions) for it.**

GAO, for a fuller understanding, needs to review the final products and recommendations of these efforts and interview the national chairpersons of the following CEP initiatives undertaken in FY91, FY92 and FY93:

1. CEP Critical Success Factors, Standards and Measures Task Force.
2. CEP Return on Investment Task Force.
3. CEP Support Audit Task Force.
4. CEP Voluntary Compliance Baseline Measures Task Force.

**GAO COMMENT 17: We reviewed all final reports that were available on CEP initiatives. A week after sending its official comments, IRS still could not provide a final report on CEP Voluntary Compliance Baseline Measures. Of the reports received, we understand and generally support them.**

GAO's analysis included post closure abatements which can significantly distort the Assessed to Recommended ratio. Abatements, such as net operating losses and credits, have nothing to do with CEP effectiveness, and should not be considered in measuring CEP Assessed to Recommended ratio. ERIS data does not include abatements.

**GAO COMMENT 18: We agree that our collection rate included postclosure abatements such as NOLs and other claims. Our report explained that we had to include them because IRS' databases did not account for them. Further, ERIS officials told us in December 1993 that the ERIS database also does not account for factors such as NOLs. They could not tell us the effect that such factors have on the collection rate. Our recommendation on correcting IRS' databases will help to identify these factors so they cannot skew the rate one way or the other.**

GAO's focus is on Recommended Tax and Penalty and Assessed Tax and Penalty. The Draft Report does not address Interest Assessed or Interest Collected. Interest is not included in the Recommended Amount from Examination. However, even given that interest represents the time value of tax and penalty owed, the amount of interest assessed and collected is significant and should be recognized. For example, ERIS reports that the interest collected on CEP closures (CEP Corporations $250 million and over) in FY 1991, FY 1992, and FY 1993 (partial year) was $4.241 billion. Consequently, an analysis of CEP effectiveness should include mention of the resulting interest assessed and collected.

**GAO COMMENT 19: IRS believes that we should recognize the interest collected on taxes recommended in audits. We agree that tracking interest amounts can help project audit revenues. But we do not favor including interest amounts in computing the taxes collected from taxes recommended. Because CEP audits do not recommend interest, including it would improperly inflate the collection rate.**

**Response to Report Recommendation**

Chapter 2 Recommendations:

Recommendation 1:

Use a 22.1 percent collection rate when estimating the additional tax revenues expected from CEP audits until more reliable information becomes available.

Response:

See comments under General Concerns.

In their report, GAO uses the 22.1 percent collection rate as a catch all not only for estimating revenue but to measure effectiveness and productivity in the Coordinated Examination Program. We do not agree that the collection rate, as used by GAO, should be used as the sole measurement of CEP effectiveness or productivity.

> **GAO COMMENT 20: IRS said our report viewed the collection rate as the way to estimate revenue and the sole measurement of CEP effectiveness or productivity. We intended neither connotation. We clarified our recommendation on using the collection rate (see comment 2). However, our report has envisioned the collection rate as one of many measures.**

Collection rates do not measure CEP effectiveness or CEP productivity. GAO acknowledged that Net Operating Loss and Credit Carrybacks as well as post closure abatements distort the recommended tax to collected tax ratio. Despite this distortion they continue to assert that it should be used to measure CEP productivity and effectiveness. These abatements, which in the CEP can be significant, have no role to play in measuring the efforts of the examination team. More accurately, the correct measure of effectiveness and productivity is the ratio of the CEP tax and penalties assessed (agreed at the examination stage or sustained in the Appeals and litigation process) to the amount of tax and penalties recommended.

Events beyond the control of the Service (NOLs, post closure abatements and claims) should not play a role in measuring the success of the program. Despite GAO acknowledging in the report that these items influence the collection rate, the report discounts or ignores these factors and continues to stress the collection rate for measurement purposes for virtually all objectives. The report needs to reflect properly the importance of the collection rate for budget and resource purposes but it needs to make clear that it alone is not a proper measurement for effectiveness and productivity.

**GAO COMMENT 21: IRS suggested that we ignored postclosure abatements such as NOLs and that these factors should not play a role in measuring CEP. We disagree for reasons discussed in comments 2 and 18. We believe that IRS must correct its databases so that these factors cannot skew the rate. We also disagree that postclosure claims have no role in measuring CEP audits. Claims filed with the Claims Court and District Court have a role if they involved CEP audit results.**

**We agree that "the" (if not the only one) correct measure of CEP effectiveness and productivity is the rate at which CEP-recommended taxes and penalties are assessed after appeals and litigation (see comments 2 and 20). As our draft discussed, this is our definition of the collection rate.**

**Finally, IRS again said we viewed the collection rate as the only measure, and the rate does not measure CEP effectiveness or productivity. As discussed earlier, we disagree (see comments 2 and 20). We agree that the collection rate is important for budget and resource purposes.**

In footnote 1 on page 36 and again on page 53 of the draft report, GAO states that the IRS estimated it collected 44.5 percent of the taxes recommended from CEP audits. This is incorrect and needs to be removed from the report. This percentage is used in estimating the revenue that would be generated from a resource initiative and reflects the amount of the recommendation that ultimately would be assessed on large, non-CEP cases with assets greater that $250 million. We have not, and would not, use this number in any estimate of the collections that would be realized from CEP work.

**GAO COMMENT 22: We have made changes (see pp. 30 and 34) to represent more clearly IRS' efforts to estimate CEP-related revenues.**

Since Fiscal Year 1991, the Enforcement Revenue Information System (ERIS) has tracked CEP closures from Examination and Appeals/Chief Counsel, including each of the following elements:

Original Recommended Tax and Penalty or Agreed and Partially Agreed CEP Cases;

Unagreed Recommended Tax and Penalty on Unagreed CEP Cases;

Tax, Penalty and Interest Assessed; and,

Tax, Penalty and Interest Paid.

ERIS data (FY 1991, FY 1992 and FY 1993 to date) are more accurate than those used by GAO (FY 1983 to FY 1991) and are therefore more indicative of current CEP accomplishments as well as more reliable in predicting future accomplishments. ERIS can be used to estimate collections for future years. The accuracy of these estimates will be significantly improved as the ERIS data base expands.

ERIS data include significantly fewer pre-1987 CEP cases than does GAO's data. The problem with using the older pre-1987 CEP case information is that it does not reflect the 1986 Tax Reform Act changes nor the effects of the implemented CEP changes. Thus some of the GAO recommendations are predicated on data that no longer are representative of the CEP.

**GAO COMMENT 23: IRS said its ERIS data are more accurate and indicative of the current CEP. For reasons discussed in comment 2, we disagree for the most part. IRS also said ERIS data are more reliable for revenue estimates, which will improve as ERIS expands its database and becomes more complete. Although we cannot yet comment on ERIS' reliability, we agree that such estimates will improve as ERIS becomes more complete. Finally, for reasons discussed in comments 1 and 2, we disagree that ERIS data use significantly fewer pre-1987 CEP cases and that our recommendations rely on data that no longer reflect CEP.**

Recommendation 2:

Correct the factors in IRS' databases that caused the CEP collection rate to be understated or overstated (i.e. net operating losses and refund claims after settlement) and use the corrected results to estimate CEP tax revenues.

Response:

Much of our response to Recommendation 1 above, is also appropriate here. We continually update the parameters in the Interim Model, which we believe is the most accurate way currently available to estimate collections.

We agree that the collection rate is a viable concept for application to the budget and resource process. The Service has established a system (ERIS) to provide collection rate information. The system has not been in place long enough to collect the necessary data and we have resisted reporting any

accomplishment data for CEP in collected dollars until it can provide additional data.

> **GAO COMMENT 24: We agree that the collection rate is applicable to the budget and resource allocation process. We also agree that ERIS has not been in place long enough to compute an actual collection rate (also see comments 2, 20, 21, and 23).**

We also have a task force working to establish appropriate Voluntary Compliance Baseline Measures for the CEP. The methodology used is very similar to the one employed by GAO. Extracted data from the Business Master File, Master File Tax Return Accounts and our own in-house Management Information System (CEMIS) are utilized to track CEP returns from filing through Examination, Appeals and Counsel for ultimate sustention and recovery rates. Baseline measures will be computed on a semi-annual basis and returns will be tracked from filing year 1981 forward. This system will provide management with information to assess program effectiveness.

> **GAO COMMENT 25: IRS acknowledged that it is using a methodology similar to ours as well as the same databases to develop the ultimate recovery rate across IRS functions. This measure approximates our definition of the collection rate; currently, IRS' recovery rate only tracks how much recommended tax under appeal is "recovered" after settlement. IRS said it will use this ultimate, IRS-wide measure to assess CEP effectiveness. We agree, which is why we have recommended that IRS track the collection rate (see comments 2, 20, 21, 23, and 24).**

Recommendation 3:

Examine a sample of skipped CEP returns and use the results to re-visit the policy to not audit a significant portion of CEP returns filed annually and to adjust the tax gap estimate.

Response:

We do not agree that such a study should be initiated. Although such a study could provide useful information for improving our tax gap estimates, resource constraints preclude our undertaking such a study at this time. Furthermore, for the following reasons we believe that such a study would have little benefit in regard to CEP administrative practices and policies. First, the audit coverage rate for CEP corporations was far greater than any other taxpayer category from 1983 through 1991. Second, each CEP return filed receives an in-depth review by a case manager and

skilled examiners to determine its audit potential. This review process incorporates a "risk analysis" which is a process where mathematical models are employed. It is based on experience, judgment, and objective analysis of the return data. Overall the analysis considers the potential benefits and utilization of resources. This recommendation would cause unnecessary additional burden on taxpayers with minimal additional tax assessments.

**GAO COMMENT 26: IRS disagreed with our recommended test of its policy on not auditing all CEP returns. IRS acknowledged that such a study would be useful but is precluded by resource constraints. We acknowledge these points but simply want IRS to check its assumption about not auditing all CEP returns. We have revised our recommendations accordingly, letting IRS decide how to test the assumption (see p. 40).**

**Further, IRS said it audits a higher portion of CEP returns than other types of returns. While true, IRS does not audit about one-quarter of CEP returns.**

Recommendation 4:

Examine in greater depth a sample of audited CEP returns and use the results to adjust the tax gap estimate and to evaluate the cost-effectiveness of doing this fuller audit.

Response:

We do not agree that such a study should be initiated. While the project suggested would provide information for improving our large corporation tax gap methodology it is important to note that these types of studies are low priority items because of very real resource constraints. Depending on the depth of such a study, it could impose a significant burden on both taxpayers and the IRS. It should be noted that Research and CEP have recently attempted a very small scale project similar to the one suggested. Although the results from the project may have limited usefulness for improving the tax gap methodology because the 13 cases studied were not selected randomly, the project was undertaken to gather information about the effect of expanding the scope of and the time spent on CEP audits. We will be examining the information and results from this project in greater detail during the development of our updated and revised corporation income tax gap estimates.

**GAO COMMENT 27: IRS opposed our recommendation to test its assumption about doing more in-depth audits of CEP returns because of concerns about resources and**

**burdens. We acknowledge these concerns and are pleased that IRS has recently started such a test on a small scale. We believe it is reasonable to check this assumption for such an important program as CEP.**

Chapter 3 Recommendations

Recommendation 1:

Give the CEP Executive Director line and budget authority down to the district office level.

Response:

We do not agree with this recommendation. This same concept was proposed by the formal CEP QIP in FY90. However, the feedback from Regional Commissioners, ARCs Examination, and Regional Counsel expressed concern that the adoption of this recommendation would not deal with the root causes of the problems identified by the CEP QIP.

Their response indicated that implementation of this recommendation would create other significant operational and managerial problems. They also stated that the National Office has responsibility for establishing policy and oversight, and that responsibility should not be diffused to line management over CEP at the regional and district levels. During FY94, the Service is continuing to implement major organizational changes at both the regional and district levels, based upon extensive studies conducted during the past two fiscal years. This recommendation is in conflict with the recommendations in those studies.

**GAO COMMENT 28: IRS opposed our recommendation on centralizing CEP to some extent. We believe that our recommendation is less encompassing than IRS envisioned. Our report acknowledges potential problems with centralization and clarifies the limited scope of our recommendation (see pp. 45, 50, and 60).**

Recommendation 2:

Ensure that CEP's revenue agents receive adequate training on the industry they specialize in as well as on tax laws and basic auditing skills such as standards of evidence.

Response:

We agree with the above recommendation. Training is an integral part of the development of our examiners and is a cornerstone of

CEP initiatives. The Executive Committee Decision Document stated "the Service must act to set up the very best training it can afford for Examination, Appeals and Counsel personnel involved in CEP cases. Training should be cross functional to ensure that all personnel have a common base of understanding from which to develop Service positions on CEP issues."

During FY91, the Executive director, CEP convened a task group to make recommendations on improving the process of funding, planning and delivery of quality CEP training. A final report was approved and issued in September 1992.

We are currently in the process of implementing a new educational approach entitled "Corporate Education", which is a restructured all encompassing approach to training. It provides for career-long education for all employees. The Service recognizes that every employee must acquire and demonstrate a portfolio of skills/knowledge to fully perform the job. We would welcome the opportunity to provide GAO with a complete overview of our Corporate Education effort.

Recommendation 3:

Expand the measures of CEP productivity to include the percent of recommended taxes that is ultimately collected.

Response:

Refer to our response to Chapter 2, Recommendation 1 for greater detail. The collection rate ultimately is not the proper tool to measure productivity.

GAO throughout their report wants the Service to use the ultimate collection rate to measure program effectiveness and productivity. We do not believe this is an appropriate measure.

**GAO COMMENT 29: IRS said that our draft report viewed the collection rate as the ultimate measure of CEP and that this rate should not be used. We disagree for reasons discussed in comments 2, 20, and 23-25.**

For example: An examiner recommends $100 in taxes which the taxpayer agrees to and pays. The collection rate is 100%. If in another example the taxpayer pays $100 in taxes and files a net operating loss carryback for $75 in taxes (assuming it is allowable and results from an economic downturn) the $100 deficiency is reduced to $25. The collection rate is now 25% Were both examinations effective? Was the examiner in the first scenario more productive than in the second scenario?

Even though the collection rate dropped from 100 percent to 25 percent in the above examples, were either of the examinations less effective or productive than the other one? The answer is obvious, no. GAO needs to revise their report and clarify their inferences about the collection rate. It does not and should not be used to measure CEP productivity or effectiveness.

**GAO COMMENT 30: IRS' example implies that IRS would use the collection rate to evaluate individuals. We oppose this use. Our report has neither recommended nor implied that the rate be used to evaluate individuals or audit teams. Instead, we viewed the rate as an IRS-wide measure. In fact, our report has used a similar example to illustrate the IRS inability to separate NOL claims from other assessments on its databases, leading us to recommend that IRS correct its databases. Also, IRS opposed using the collection rate. We continue to support the rate (especially when IRS is trying to develop it) for reasons stated in comments 2, 18, 20, 21, 23-25, and 29.**

GAO ignores the statistical indicators and critical elements adopted by the CEP in the last three years. We believe these indicators truly measure our productivity. Some of which include the percentage of agreed cases and dollars, use of Delegation Order 236, Accelerated Issue Resolution, cycle time and last but not least our Peer Review process.

**GAO COMMENT 31: IRS said we ignored its new CEP measures over the last 3 years. We did not focus on these measures, given our collection rate objective. We have, however, acknowledged IRS' new measures as discussed in comment 15.**

GAO has made only casual reference to the Peer Review. However much of what GAO is recommending comes from our Peer Review recommendations. Our Peer Review process has been in place for three years. During each Peer Review, teams of experienced CEP managers, examiners and specialists perform in-depth reviews of closed CEP cases to measure issue development, audit competency and procedural accuracy. We have now compiled the results of the three reviews as a baseline. The reviews covered approximately 150 examinations compared to the 12 studies GAO performed during their review.

**GAO COMMENT 32: IRS said we made only casual reference to its peer reviews, whose recent recommendations are similar to ours. IRS implied that its peer review results on 150 audit cases are a better basis for any recommended changes to CEP than our 12 case studies.**

**We agree that our work and IRS' peer reviews involved many of the same weaknesses and recommendations for CEP. We cite results from IRS' peer reviews and other studies that relate to our recommendations. Even so, the basis for our recommendations goes beyond IRS' peer reviews and our 12 case studies as discussed in comment 1.**

Using the Peer Review results and our other statistical indicators and critical elements to measure productivity and effectiveness is far more meaningful than the ultimate collection rate.

Recommendation 4:

Modify CEP's policy to allow revenue agents to rotate among corporations in the same industries to the extent possible.

Response:

We agree with this recommendation when circumstances permit keeping key team coordinators, team members and specialists within the same industries. However, CEP does not have sufficient resources for travel expenses that would be incurred on extended assignments of our personnel in multi-state locations. We believe we can improve our examiners' knowledge of various industries through improved training and use of the industry specialization program related to their assignments. The Executive Director of CEP has devoted numerous efforts to improve the industry training of our personnel, including joint training initiatives with various industry organizations and the effort of the CEP Training Task Force. We have also expanded joint training efforts by including our professional stakeholders such as TEI and ABA.

Recommendation 5:

Issue regulations or propose legislation to strengthen IRS' ability to obtain needed data from CEP corporations during the audit. This effort should include an evaluation of the pros and cons of the 3 options for obtaining needed data, as GAO discussed on page 79.

Now on p. 56.

Response:

We agree that the proposal by GAO needs to be thoroughly examined. The Executive Director, Office of Coordinated Examination Program, will establish a work group during FY94 to evaluate the pros and cons of this GAO recommendation. It should be noted that in recent responses to the Service regarding tax

penalty administration policies, various tax professional groups discouraged the further expansion of legislative penalties as enforcement tools in tax administration.

Chapter 4 Recommendations

Recommendation 1:

Establish controls to ensure that CEP teams have an opportunity to review new information provided by the taxpayer during the Appeals process.

Response:

We agree with this recommendation and, in fact, identified the problem in the Appeals Process Review Report published January 15, 1993. A recommendation was made as part of that report to strengthen current IRM procedures which we hope will solve the problem.

Recommendation 2:

Require Appeals' supporting statements to clearly identify when relevant national office guidance exists, whether it was followed, and, if not, why. Also, eliminate the exceptions for coordination based on (1) concessions less than 100 percent and (2) an official's opinion that the facts of the case are materially different.

Response:

We agree that Appeals Officers need to discuss all relevant authority so that the basis for settlement can be evaluated by Appeals management, Examination and other independent reviewers such as the Joint Committee on Taxation. However, the rule for settling issues contrary to Service position requires only that a full concession of an issue contrary to official Service position need to be coordinated with the National Office. That rule should not be changed. The courts consider Revenue Rulings and Technical Advice memorandums to be the opinion of the Service. They may and often do choose to ignore the opinion of the Service in deciding an issue.

**GAO COMMENT 33: IRS agreed with our recommendation on discussing the basis for Appeals' settlements but not on coordinating substantial concessions of issues supported by official service positions. We still recommend coordination for substantial concessions for reasons discussed in comments 5 and 10-13.**

Recommendation 3:

Better balance incentives in the Appeals process by (1) expanding the measures of Appeals' success to include the present of CEP recommended taxes that are collected; (2) resolving more recurring tax disputes by proposing legislative changes or, as a last resort, litigating more; (3) deleting the phrase "without litigation" from the Appeals' mission statement; and, (4) requiring a CEP official to attend Appeals' conferences with CEP corporations, or at least the initial and final conferences if attending all of them becomes burdensome.

Response:

We do not agree with recommendation part (1). To include in the management objectives of Appeals a goal that measures the amount of tax collected strikes at the heart of the Appeals mission. GAO pointed out in their draft report that having an 85 percent agreement rate in Appeals' objectives has, at a minimum, created the perception with Examination that settlements were less than they might have been because of Appeals' attempts to meet the goal. Appeals eliminated that stated objective 5 years ago because they had the same concern.

CEP taxpayers and their representatives might well have the same perception from the opposite point of view. That is, that Appeals is measured by the amount collected and, therefore, Appeals is more concerned with recovering tax than being fair and impartial.

The "measures of success" for Appeals have already been expanded to include an analysis of our recovery rate. Recovery rate, at this time, is a comparison of the deficiency and penalty recommended by Examination to the deficiency and penalty agreed to after Appeals' consideration of the case. Appeals continues to look at the definition of recovery rate in order to capture a meaningful and accurate measure of Appeals on the amounts assessed. The Appeals' annual business plan for FY 94 includes an analysis of both the recovery rate and the sustention rate (the sustention rate is the percentage of adjustment sustained in Appeals, rather than the percentage of tax - it is measured on an issue basis).

The Chief Counsel Large Case briefings - held at least twice a year since 1990 - have also focused in part on the low sustention and recovery cases. The lowest cases were regularly analyzed in an attempt to identify and understand the reasons for the low amounts. The idea is to identify issues or other systemic problems causing low rates.

However, the analysis called for in the business plan and the case analysis in the briefings focus on specific issues and cases rather than the overall percentage for the organization. We think that approach is appropriate; but broad goals or measures of success based on a recovery rate are dangerous.

**GAO COMMENT 34: IRS opposed using the collection rate as a measure in Appeals. IRS said that this measure would strike at Appeals' mission and that Appeals eliminated a goal to settle 85 percent of its cases because of the problems it created.**

**For reasons stated in earlier comments, we continue to favor applying the collection rate across IRS' functions--including Appeals--particularly when IRS is developing a collection rate and Appeals is using the recovery rate. We added text (see pp. 67-68) to address IRS' concerns and clarify our reasoning. Our report also addresses Appeals' 85-percent settlement goal. Although Appeals eliminated it, the settlement rate increased to as high as 93 percent in fiscal year 1992. Regardless, we view the collection rate as simply one measure--not the overriding goal.**

**Although IRS uses the recovery rate, IRS said broad goals or measures based on the recovery rate are dangerous. We agree, which is why we viewed the collection rate as one of many measures and not as a goal.**

We agree in part with part 2 of this recommendation. The tax laws are complex and they often need to be simplified to clear up areas of controversy. The Internal Revenue Service (with Appeals as a participant) regularly recommends changes to the tax laws. The Chief Counsel now has a Special Counsel (Legislation) whose job is to facilitate the exchange of ideas between the Counsel branch of the Service and Congress.

On the other hand when legislation is not feasible, litigation may be necessary to resolve disputed interpretations of the law. Though costly and often unpredictable, litigation may produce the necessary clarification.

**GAO COMMENT 35: IRS agreed that litigation may be necessary to clarify tax law. We agree but revised our report to downplay the extent to which IRS should litigate to clarify tax laws (pp. 64-65). We much prefer clarifying tax laws through legislative action because of the costs and risks of litigation.**

We do not agree with part 3 of this recommendation. Deletion of the phrase "without litigation" from the Appeals mission statement is not necessary and indeed it seems to conflict with GAO's prior recommendation that litigation be used as a "last resort" to resolve issues. Using litigation as a last resort, we settle most of the cases, trying only those that might set a precedent in an area of the tax law that is particularly confusing. Settlements never set a precedent or clarify the law. They reflect the ambiguities in the law and the effect those ambiguities would have on a court decision if the issue were tried. So Appeals settlements do not add to the ambiguities - they just reflect the ambiguities that already exist.

The Service currently has a procedure for bypassing Appeals if Counsel thinks a case should be tried. This procedure - designating issues for litigation - has existed for many years. It allows the Service to identify key issues in specific cases to be tried - and it prevents Appeals from settling those issues. So the mechanism already exists and has been used to limit the settlements in Appeals where litigation is needed.

**GAO COMMENT 36: IRS disagreed with deleting the phrase "without litigation" from Appeals' mission statement. Our report recognizes that Appeals' mission is to settle--not litigate--cases. As a result, we believed this phrase was redundant. Also, because Appeals does not litigate, deleting this phrase would not conflict with the previous recommendation on IRS litigating as a last resort to clarify tax laws (see comment 35).**

**To avoid confusion, we deleted this from our recommendation. Instead, we now discuss the need for IRS to show more willingness to litigate. We believe that IRS puts itself at a disadvantage by litigating so few CEP cases and could use the IRS procedure for bypassing Appeals in choosing cases to litigate. We still discuss the downsides to litigation, such as the added costs, burdens, and risks for IRS, the courts, and corporations (see pp. 68-69).**

The mission statement is written for all of Appeals - not just the Large Case Program. Appeals overall disposed of over 60,000 cases last year - most of them agreed. The tax courts decided about 1500 cases. If Appeals did not settle the vast majority of cases, the courts would soon be over run with work.

Finally, Appeals does not concede issues to avoid litigation as stated in the report. We want to make it clear that Appeals considers issues on their merits and settles them when necessary

based on the hazards of litigation. Appeals does not concede issues simply because we do not want to try the case. Appeals does not try cases. Settlements reflect our assessment of the litigating hazards. If the taxpayers and Appeals can not agree on a settlement based on a reasonable assessment of the hazards, the taxpayer may initiate litigation.

We think it is important to keep in mind that it has been, to this point, the government's general policy to allow taxpayers to resolve their disputes without litigation whenever possible. Only under fairly narrow circumstances has it been the government's policy to force litigation. This option to settle has become part of the process that is expected by taxpayers.

> **GAO COMMENT 37: IRS said Appeals must settle cases, judging the hazards of litigation, to avoid burdening the courts--not to avoid litigation. We clarified this point in the report as discussed earlier (comment 7). IRS also pointed to its general policy to allow taxpayers to choose to settle disputes in Appeals rather than litigate. We favor this policy but still believe IRS must show more willingness to litigate for the reasons discussed in comment 36.**

GAO's figures indicate a "collection" rate on tried cases of 35 percent. While that figure does not agree with previously published recovery rates for recently tried Large Cases, it still reflects significant hazards to the government when cases are tried. Remember, cases that are tried have been fully developed and represent the government's best attempt to win the issue in court.

> **GAO COMMENT 38: IRS questioned a 35-percent collection rate that we cited for litigated CEP cases. We did so to counter an opinion of an IRS official on litigated cases having a lower collection rate. Because we no longer discuss that opinion, we downplayed discussion of the 35-percent rate, even though it is accurate.**

We do not agree with part 4 of this recommendation. We feel that bringing the Examiner into the conference will often upset the settlement atmosphere depending on the level of contention between the examiner and the taxpayers. The two parties do not agree - otherwise they would not be in Appeals. Forcing them back together may only aggravate the situation. Appeals does not have the authority to decide cases - like a judge or arbitrator - and so the Appeals representatives may often end up as referee. Even professional mediators separate the parties when they are trying to gain concessions from one or both. Concessions are often more easily granted when the parties are not in each

other's presence.

**GAO COMMENT 39: IRS raised concerns about bringing CEP officials into Appeals' meetings with CEP taxpayers. We expanded our discussion of these concerns and revised our recommendation. Our work indicated a need for CEP officials to have more opportunities to react to new facts from corporations. Thus, we now favor giving CEP officials one last chance to review all new information in the context of Appeals' settlement--just before it is finalized (see pp. 69-71).**

We do agree that Appeals needs to listen to both sides so that it can make a fully informed decision about the relative merits of a particular issue. But we do not need to do that simultaneously. We already require that new information presented at the conference be returned to Examination pursuant to IRM 8628.7(2). We have also made changes to the process (1991) to require a meeting on all Large Cases between Appeals and Examination before the Appeals hearings with the taxpayer begin. We wanted to ensure that Appeals fully understood Examination's position on the issues. Examination has the opportunity to fully explain its position - beyond what is stated in the Revenue Agent's Report and Appeals has an opportunity to discuss the issue with Examination. The FY92 Process Review for Appeals confirmed that these meetings are being held.

The Service also mandated a post-closing conference between the functions and encouraged continuing dialogue following the pre-conference. The Process Review indicated that the post closing conferences were not being held all of the time. The results of the Appeals process are being conveyed to Examination through the continuing dialogue that exists following the pre-conference meeting.

There are occasions when Examination is invited to attend an Appeals hearing. But this is left to the judgment of the Appeals Officer. To mandate Examination's attendance at Appeals conferences would often create more problems than it solves. Appeals would, therefore, prefer to keep Examination's participation discretionary. With the increased communication created by the Pre and Post conferences, coupled with the proper feedback of new information to Examination, we think the process will be both fair and effective for the taxpayer and the government.

ADDITIONAL COMMENTS ON REPORT TEXT

GAO criticized Appeals for not revealing to the Joint Committee the full explanation and authority behind a particular decision.

The issue involved was a rollover from a previous cycle. The previous Appeals Case Memorandum had fully discussed the issue, was attached to the report sent to the Joint Committee, and the GAO was told that it was - and acknowledged that this was correct. Knowing that the full explanation they desired was in fact given to the Joint Committee, the GAO nevertheless had included this criticism in their draft report.

**GAO COMMENT 40: IRS said we had not fully discussed an Appeals' settlement in a case reviewed by JCT. We disagree. Nor did we acknowledge that Appeals attached a full explanation of the technical advice to the case memo for the years of our case study. Appeals' case memo had no reference to the technical advice. We do not believe that referring to case memos for earlier tax years notifies JCT, or any reader, about that technical advice. We believe Appeals' recent memo should have shown that (1) settlement was contrary to this technical advice, which the audit team followed; and (2) an explanation of the technical advice was attached to Appeals' earlier case memos. We clarified our concerns with this case in the report (see p. 74).**

Either GAO should clarify the statements that "IRS officials believed that if voluntary compliance had improved, CEP-recommended taxes would have decreased" (p.4 and elsewhere) or remove them entirely. This statement is an oversimplification which is likely to be misinterpreted. Improvements in voluntary compliance do not necessarily imply a reduction in additional tax recommended. If "true" tax liability increases each year (as it generally will even if only because of inflation), voluntary compliance can improve even if taxes not paid voluntarily and taxes recommended increase. Furthermore, voluntary compliance is only one of many factors influencing taxes recommended.

**GAO COMMENT 41: IRS said to delete or clarify an IRS official's statement about CEP tax recommendations decreasing if voluntary compliance increased. We have further acknowledged other factors that could explain any increases in the CEP tax recommendations (see pp. 36-37).**

Throughout the report there is a reference to the Appellate function "conceding" tax issues. The correct phrase should be "compromising". To concede suggests that we are giving up completely on an issue. In most cases we feel we are appropriately compromising the proposed taxes at less than the amount proposed by examination on the basis of litigation hazards either factual or legal.

**GAO COMMENT 42: IRS said the phrase "conceding" was incorrect. We disagree. Since our review started over 2 years ago, IRS officials have referred to a less-than-100-percent sustention of an issue as a partial concession. Also, the Internal Revenue Manual (IRM 8 (14) 40) refers to settlements in favor of the taxpayer as partial or full concessions.**

The report also fails to recognize the importance of our Appellate function in the tax compliance system. We are of course faced with the limited resources of the judicial system in disposing of contested cases. While some increase in the productivity of the judicial system can be expected the total number of cases being audited could quickly overwhelm the courts but for our current settlement system.

**GAO COMMENT 43: We believe that the report recognized the importance of Appeals. We have further acknowledged its importance throughout chapter 4.**

Many areas of the law are turning to "alternate dispute resolution" systems. For 60 years the Service has had a system to dispose of cases without the need for litigation. The bulk of our cases developed by the examination function have been resolved to the satisfaction of the taxpayers by appeals officers without the costs and delays surrounding the litigation process. In other words if we did not have the Appeals function today we would be forced to invent it. While we agree that there are ways to improve the system we should not lose sight of the importance of the Appeals function to tax compliance.

While we appreciate the aspiration that the tax law should be clear enough that dispute resolution does not rely on the negotiating skills of Service personnel we doubt that such a system is achievable in the foreseeable future.

Finally, we think that it is unfortunate that the Joint Committee on Taxation, whose Refund Counsel reviews a significant portion of the IRS Appeals Large Cases that are closed each year, did not participate in this CEP study.

**GAO COMMENT 44: IRS said it was unfortunate that JCT did not participate in our study. We agree. If JCT had participated, as requested, our work in Appeals might have been expedited and refined, particularly on the technical correctness of settlements.**

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