

United States General Accounting Office Washington, DC 20548

April 26, 2001

The Honorable Charles O. Rossotti Commissioner of Internal Revenue Department of the Treasury

Subject: Internal Revenue Service--Status of the Modernized Research Operations

Dear Mr. Rossotti:

In an Internal Revenue Service (IRS) memorandum from December 1999, you highlighted the importance of research in key decision-making processes and in finding ways of improving performance on IRS' strategic goals in light of limited resources.<sup>1</sup> Because we agree that using research in an effective manner is important, we monitored the status of IRS' efforts to improve its research operations. Since 1998, IRS has been undergoing a major effort to modernize its overall structure, which included the creation of four operating divisions that each focus on a particular group of taxpaying customers, such as wage earners or large businesses.<sup>2</sup> In 2000, IRS began to restructure its research organization and created, among others, research units within each of its operating divisions.<sup>3</sup>

During our review, we determined that a detailed study was not warranted at this time because IRS had made few decisions about the modernized research operations. However, from our limited work, we identified issues that present challenges for IRS management when making future decisions about research.

This letter summarizes and transmits to you information we presented in a March 15, 2001, briefing to the Deputy IRS Commissioner and other IRS officials.<sup>4</sup> In particular, this letter discusses the (1) steps IRS has taken to modernize its research operations since October 1, 2000, (2) areas of concern raised in past reports and studies of IRS research operations, and (3) status of IRS' efforts to address these concerns within the new research operations. To address these issues, we identified and summarized past studies on IRS' research organization; reviewed relevant IRS documents, such as research plans; and interviewed key officials responsible for research. We conducted

 $<sup>^{1}</sup>$  IRS' three strategic goals are to (1) provide top-quality service to each taxpayer in every interaction, (2) provide top- quality service to all taxpayers through fair and uniform application of the law, and (3) increase productivity through a quality work environment.

<sup>&</sup>lt;sup>2</sup> The four operating divisions are: (1) Wage and Investment, (2) Small Business/Self-Employed, (3) Large and Mid-Size Business, and (4) Tax Exempt/Government Entities.

<sup>&</sup>lt;sup>3</sup> In addition to the research units in the operating divisions, two other research units were created–a headquarters Office of Research and a research unit for Criminal Investigations. We refer to these units collectively as IRS' research operations.

<sup>&</sup>lt;sup>4</sup> See enc. I for the briefing handout.

our work in accordance with generally accepted government auditing standards. This letter provides information on the status of IRS' efforts through February 2001.<sup>5</sup>

### Results

IRS has begun taking steps to modernize its research operations. As part of this modernization, IRS planned to create research units within each of its operating divisions to work together collaboratively. As of October 1, 2000, the assignment of research staff to the operating divisions was completed. The work for most on-going research projects continued within the new structure using interim procedures. In addition, IRS continued to place staff in key leadership positions.

Regarding the areas of concern raised in past studies of IRS research, our review of five studies conducted between 1995 and 2000 identified many concerns about IRS' research operations. (See enc. II for a list of the studies that we reviewed.) For example, four of the studies discussed the need for IRS to measure the performance of its research organization. We grouped the concerns into six general areas--research leadership, human capital, organization infrastructure, systems and data management, customer focus, and performance measures. While the specific issues from these reports may not apply to the new research structure, the overall concepts are still relevant to the new IRS research units. (See enc. I, page 8 [slides 7 and 8], for summaries of the concerns in the six general areas.)

IRS is just beginning its efforts to address these past areas of concern. IRS officials told us that, in part, they had been waiting for new research leadership to be in place before they began. As IRS addresses these concerns, the challenges still to be addressed include:

- Research Leadership--Key leadership positions within the research units were filled in January and February 2001, or remained unfilled, and a vision for research had yet to be fully developed. In addition, transitional issues, such as overcoming past perceptions that the research organization is ineffective, had not been fully addressed.
- Human Capital--The research units had numerous staff shortages compared to authorized positions. For example, in one operating division, the officials told us that about one-third of the research positions were vacant. Furthermore, the operating divisions reported inconsistencies between the mix of skills of the current staff and the skills needed to perform research; however, inventories to determine the extent of skill deficiencies had not been conducted.
- Organizational Infrastructure--The research units relied on old work processes and procedures as an interim guide for their day-to-day activities, largely because the research leaders were too new or were not available to develop new guidance. Additionally, few tools were available to assist in managing the geographically dispersed research units. For example, the Compliance Research Intranet, created

 $<sup>^{\</sup>scriptscriptstyle b}$  We excluded two research units from our review-the Tax Exempt/Government Entities Division and the Criminal Investigation unit-because these units are start-up operations that did not receive an allocation of the research staff (and projects) that existed when they started.

to record information on research projects, was less effective than it should be, according to IRS officials.

- Systems and Data Management—IRS officials told us that the data on compliance in reporting items on tax returns were outdated and that IRS did not use alternative data as fully as it could. For example, IRS officials told us about IRS data sources, such as reports of telephone services provided to taxpayers, and about external data sources, such as census data, that could be used to a greater extent as alternative sources.
- Customer Focus--While the research units have identified their internal customers, one research unit that has external customers had not completed its work to identify them. Furthermore, the research units had not determined how to involve and communicate with their customers within the new research structure.
- Performance Measures—The IRS was in the early stages of developing appropriate measures to determine the effectiveness of its research results. Some measures existed for customer satisfaction, but they were not fully developed.

During our briefing, the Deputy Commissioner and other IRS officials told us that the information we presented was accurate and timely. They suggested minor changes to improve the clarity of our information, which we made as appropriate. In addition, they provided information on additional efforts to modernize the new research units that had occurred since we completed our review. For example, the officials said that the Director of Research for the Wage and Investment Division assumed his position during March 2001.

We are sending copies of this letter to interested congressional committees. The letter is also available on GAO's home page at <u>http://www.gao.gov</u>. This letter was prepared under the direction of Tom Short. Other major contributors were Kerry Dunn, Libby Mixon, and Anthony Foster. If you have any questions about this letter, please contact Tom Short or me on (202) 512-9110.

Sincerely yours,

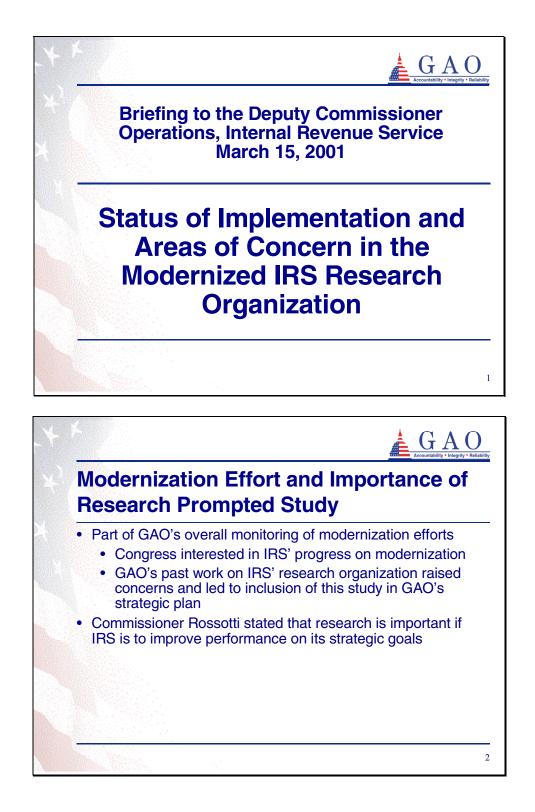
Muchael Broth

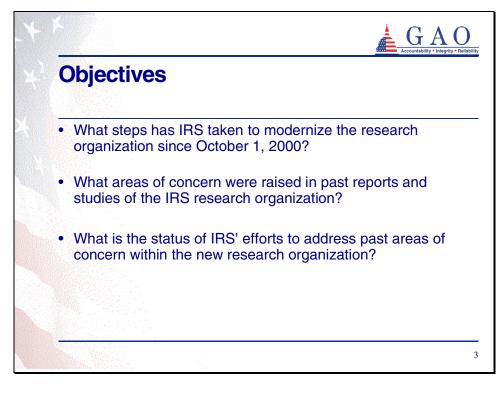
Michael Brostek Director, Tax Issues

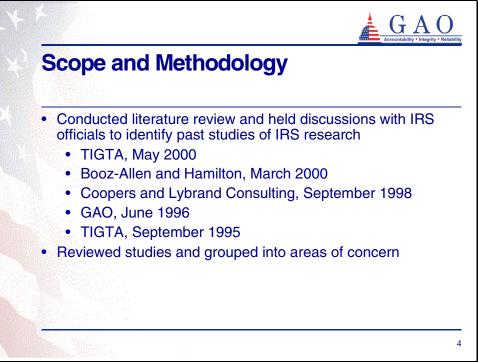
Enclosures

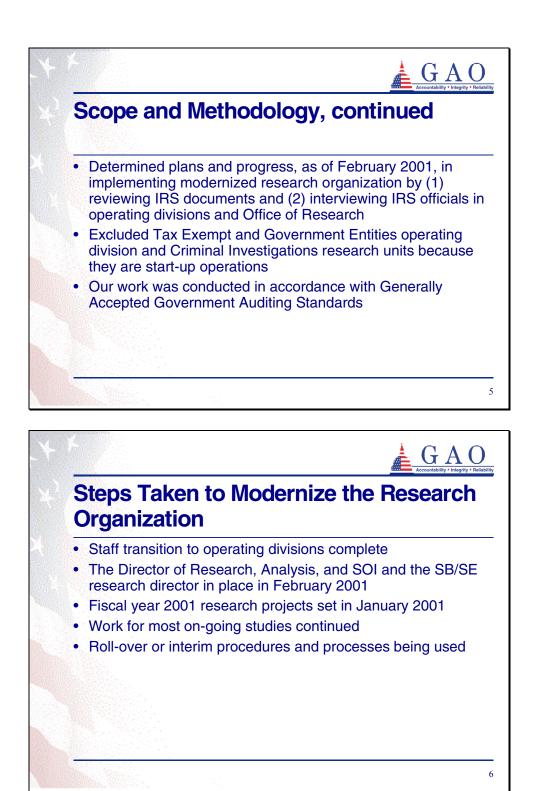
## Abbreviations Used in GAO's Briefing

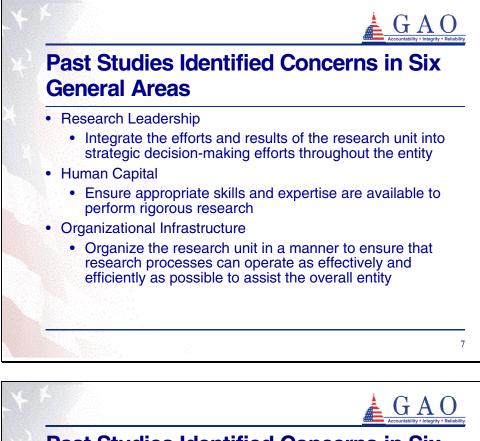
General Accounting Office Internal Revenue Service Treasury Inspector General for Tax Administration Statistics of Income Wage and Investment Operating Division Small Business/Self-Employed Operating Division
Small Business/Self-Employed Operating Division Large and Mid-Size Business Operating Division







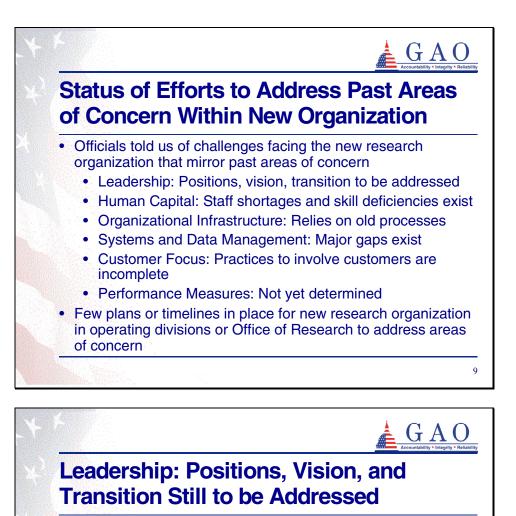




# Past Studies Identified Concerns in Six General Areas, continued

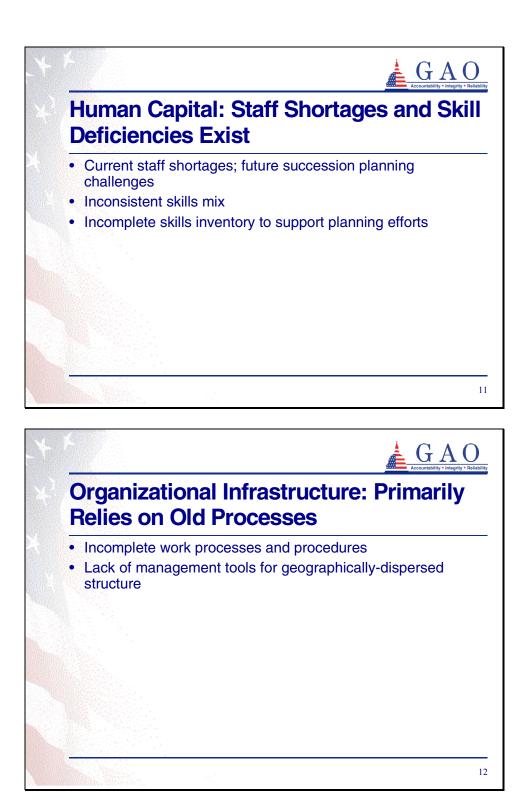
- Systems and Data Management
  - Maintain objective data that are readily accessible for research
- Customer Focus
  - Involve and consult with research customers during all phases of a project
- Performance Measures
  - Establish and institutionalize methods to monitor project progress and determine the overall impact of research

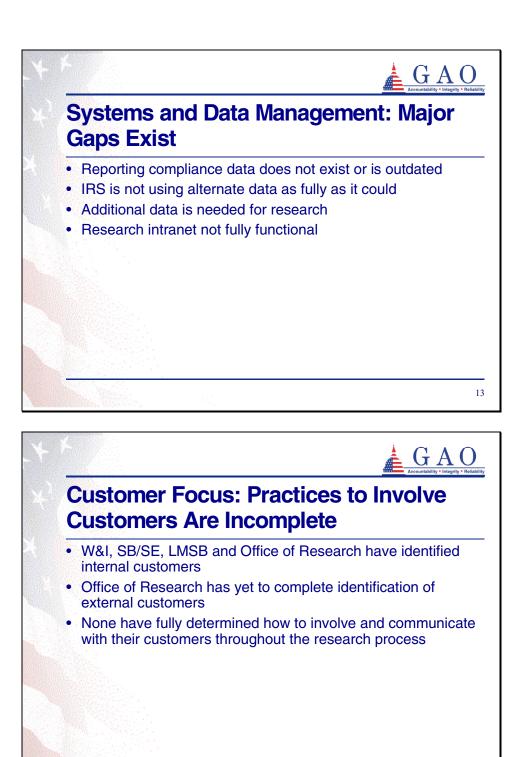
8



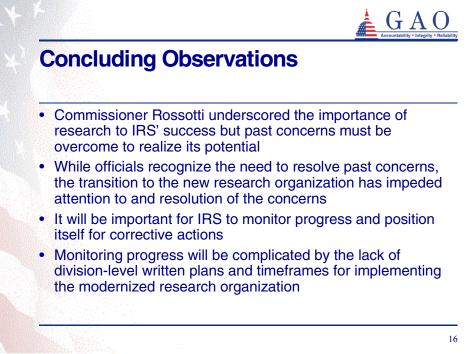
- Key positions not filled
- Vision for research organization not yet fully developed
- Transition issues not fully addressed
  - Research historically viewed as somewhat ineffective
  - · Research staff have and continue to face major changes

10









### **Enclosure II**

### **Studies GAO Reviewed**

Booz-Allen and Hamilton. Research. Discussion Document (draft), March 9, 2000.

Coopers and Lybrand Consulting. *IRS Office of Research and District Offices of Research and Analysis--Training and Organizational Assessment Project Report.* June 26,1998.

U.S. Department of the Treasury Inspector General for Tax Administration (TIGTA). *The Internal Revenue Service Needs to Improve Control of Its Compliance Research Program.* Reference No. 2000-40-068, May 12, 2000.

U.S. Department of the Treasury Inspector General for Tax Administration (TIGTA). *Review of the National Office Research Analysis/District Office Research Analysis and Compliance Research Information System Implementation*. Reference No. 056406, September 7, 1995.

U.S. General Accounting Office. *Tax Research: IRS Has Made Progress but Major Challenges Remain.* GAO/GGD-96-109, June 5, 1996.

(268922)