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ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20005

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MEMORANDUM FOR SECRETARY YELLEN

FROM: J. Russell George
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SUBJECT: Management and Performance Challenges Facing the Internal Revenue Service for Fiscal Year 2022

The Reports Consolidation Act of 2000[1] requires that the Treasury Inspector General for Tax Administration (TIGTA) summarize, for inclusion in the annual *Department of the Treasury Agency Financial Report*, its perspective on the most serious management and performance challenges confronting the Internal Revenue Service (IRS).

Each year, TIGTA evaluates IRS programs, operations, and management functions to identify the most vulnerable areas in the Nation's tax system. For Fiscal Year (FY) 2022, the IRS's top management and performance challenges, in order of priority, are:

1. Administration of Tax Law Changes and Pandemic Relief Benefits;
2. Enhancing Security of Taxpayer Data and Protection of IRS Resources;
3. Improving Tax Reporting and Payment Compliance to Reduce the Tax Gap;
4. Modernizing IRS Operations;
5. Improving Customer Service and the Taxpayer Experience;
6. Addressing Emerging Threats to Tax Administration;
7. Reducing Fraudulent Claims and Improper Payments;
8. Increasing International Tax Compliance;
9. Protecting Taxpayer Rights; and
10. Human Capital.

The following information detailing the management and performance challenges is being provided to promote the economy, efficiency, and effectiveness of the IRS's administration of the Nation's tax laws.

[1] 31 U.S.C. § 3516(d) (2006).

ADMINISTRATION OF TAX LAW CHANGES AND PANDEMIC RELIEF BENEFITS

The IRS's operations were significantly impacted by the Coronavirus Disease 2019 (COVID-19) pandemic. Although the Tax Processing Centers were open for the 2021 Filing Season, the IRS was not always able to operate at full capacity due to social distancing requirements. As such, the IRS was unable to perform many of its essential functions. The backlog of individual tax returns and other types of taxpayer account work nearly doubled when compared to the 2020 Filing Season. For example, as of August 16, 2021, the IRS reported having approximately 11 million paper tax returns waiting to be processed and approximately 9.6 million cases in other key tax processing functions that still needed to be addressed. At about the same time in 2020, the IRS reported having more than 4.8 million tax returns waiting to be processed and about 5.4 million cases in other key tax processing functions that still needed to be addressed. The backlog of returns, correspondence, and other types of work has, and will continue to have, a significant impact on the associated taxpayers.

The pandemic also resulted in numerous legislative changes that impacted tax administration. Most recently, the American Rescue Plan Act of 2021 (ARP),[2] enacted on March 11, 2021, includes approximately $1.9 trillion in economic relief and stimulus to address the continuing impact of the COVID-19 pandemic on the economy, public health, State and local governments, individuals, and businesses. It also contains numerous tax-related provisions intended to provide relief to individuals and businesses. This legislation creates a third Recovery Rebate Credit (RRC) of up to $1,400 per eligible individual to be applied toward income earned during Tax Year (TY) 2021. The legislation directs the IRS to make advance payments of the RRC as soon as possible, but not later than December 31, 2021. The IRS began issuing the RRC payments on March 11, 2021, the same day the ARP Act was enacted. As of June 3, 2021, the IRS reports issuing more than 163 million advance payments totaling nearly $390 billion for the third round of the RRC.

Another key provision in the ARP Act is the expanded Child Tax Credit. Determining eligibility for, and the amount of, the Child Tax Credit is a complex process. Available tax data may reflect children who qualify for the credit in prior tax years but do not qualify in the current tax year. The IRS will have to continually adjust the Child Tax Credit advance payments as updated information is obtained from taxpayers.

A number of the provisions contained in pandemic legislation required the IRS to take steps to implement such legislation while in the midst of its 2020 and 2021 annual tax filing seasons. The tax filing season is a critical time for the IRS because this is when most individuals file their income tax returns and contact the IRS if they have questions about specific tax laws or filing procedures. The extensive actions the IRS must undertake to implement tax legislation will continue to be challenging when tax law changes are enacted close to, or after, the start of the annual filing season. Additional legislative developments related to tax reform and tax policy will continue to present challenges for the IRS.

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[2] Pub. L. No. 117-2, 135 Stat. 4.

ENHANCING SECURITY OF TAXPAYER DATA AND PROTECTION OF IRS RESOURCES

The IRS is responsible for safeguarding a vast amount of sensitive financial and personal data. IRS systems withstand approximately 1.4 billion cyberattacks annually (including denial-of-service attacks, unsuccessful intrusion attempts, probes or scans, and other unauthorized connectivity attempts). Many of these attempts are sophisticated in nature or represent advanced, persistent threats.[3]

On July 1, 2019, Congress enacted the Taxpayer First Act[4] and amended the Internal Revenue Code to give the IRS the authority to disclose certain return information for the purpose of cybersecurity and the prevention of identity theft tax refund fraud. The IRS decided to leverage the Security Summit[5] to disclose return information related to refund fraud schemes to State tax agencies and industry partners. However, TIGTA reported that additional policies, procedures, and actions are needed to improve the effectiveness of security over the sharing and storing of the data.[6] In addition, opportunities exist to enhance controls and ensure consistency in applying policies for accessing the shared data.

Further, the Taxpayer First Act contained provisions to modernize the IRS's Income Verification Express Service (IVES) program[7] and increase taxpayer protections. However, TIGTA found that some key processes are not operating as intended to ensure that taxpayers authorize the release of their tax transcripts.[8] IVES program management did not conduct compliance reviews in FY 2019 to ensure that participants completed the required client certifications. These certifications are important because they validate the identity of clients that ultimately receive the transcripts. The IRS also did not conduct sufficient suitability checks on 577 IVES participants that were "grandfathered" into the program in February 2016 when management implemented the suitability checks.

Additionally, the IRS continues to digitize many of the previously paper processes, which generates targets of opportunity for malicious actors around the globe. Each new system created, while potentially improving the experience of the taxpayer, also enables new ways to subvert, misuse, manipulate, and disrupt the IRS's ability to administer the Federal tax system. Numerous Government agencies also rely on tax information to

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[3] Written testimony of Charles Rettig, Commissioner, Internal Revenue Service, *On the IRS Budget and Current Operations,* Senate Appropriations Committee, Subcommittee on Financial Services and General Government (May 15, 2019).
[4] Pub. L. No. 116-25, 133 Stat. 981 (2019).
[5] The IRS formed the Security Summit with representatives from State Departments of Revenue, the Chief Executive Officers of leading tax preparation firms, software developers, and payroll and tax financial product processors. The Security Summit's primary mission is to assist in the fight against the filing of fraudulent tax returns and protect taxpayers from identity theft tax refund fraud.
[6] TIGTA, Report No. 2021-25-025, *Taxpayer First Act: Data Security in the Identity Theft Tax Refund Fraud Information Sharing and Analysis Center* (May 2021).
[7] Once accepted in the IVES Program, participants such as banks and financial institutions can submit requests, on behalf of their clients, to obtain tax transcripts for individuals and businesses.
[8] TIGTA, Report No. 2021-45-017, *Additional Security Processes Are Needed to Prevent Unauthorized Release of Tax Information Through the Income Verification Express Service Program* (Feb. 2021).

administer public benefits, which sets the stage for downstream effects on other Government benefit programs when IRS systems are successfully exploited.

In June 2021, Pro Publica released data it claimed to be from the tax returns of thousands of individuals, covering more than 15 years. The protection of taxpayer data will continue to be a top priority for the IRS as it tries to leverage technology to be responsive to taxpayers' needs for its services, while minimizing the risks from cyberattacks and insider threats.

IMPROVING TAX REPORTING AND PAYMENT COMPLIANCE TO REDUCE THE TAX GAP

One of the IRS's key responsibilities is to ensure that taxpayers comply with the tax law. Sustaining and improving taxpayer compliance is important because small declines in compliance cost the Nation billions of dollars in lost revenue and shift the tax burden away from those who do not pay their taxes onto those who pay their taxes on time every year.

According to the IRS, high-income nonfilers, although fewer in number, contribute to the majority of the nonfiler Tax Gap. High-income taxpayers generally have more opportunities to engage in planning to avoid taxes. In March 2021, TIGTA reported that the IRS could more effectively prioritize high-income taxpayers who owe delinquent taxes.[9] Specifically, TIGTA identified approximately 685,000 taxpayers with adjusted gross income of $200,000 or more that owed a combined total of $38.5 billion as of May 14, 2019. TIGTA also found that revenue officer staffing does not always align with locations where the greatest number of high-income cases are located. While TIGTA recognizes that resources are limited, hiring or reallocating resources to work high-income cases in these areas could lead to higher collection potential and increased revenue.

Prior to FY 2018, the IRS had a High Income High Wealth strategy focusing on high-income taxpayers whose total positive income was at least $200,000 on Form 1040, *U.S. Individual Income Tax Return*.[10] However, TIGTA reported that the majority (73 percent) of the individual returns closed using the strategy for FYs 2015 through 2017 had total positive income of less than $200,000.[11] After disbanding the High Income High Wealth strategy, the IRS focused instead on using the less productive Discriminant Function strategy[12] resulting in $121.5 million in potential lost assessments for FYs 2018 and 2019.

TIGTA also reported that for TY 2017 numerous business and individual nonfiler taxpayers with Form 1099-K, *Payment Card and Third Party Network Transactions*,

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[9] TIGTA, Report No. 2021-30-015, *High-Income Taxpayers Who Owe Delinquent Taxes Could Be More Effectively Prioritized* (Mar. 2021).
[10] Total positive income is the sum of all positive incomes shown for the various sources of income reported on the individual income tax return and, therefore, excludes losses.
[11] TIGTA, Report No. 2021-30-041, *The IRS Continued Compliance Efforts for High-Income Taxpayers After Disbanding the High Income High Wealth Strategy, but With Less Effective Outcomes* (July 2021).
[12] The Discriminant Function examination strategy contains returns selected based on algorithms. The results of the IRS's National Research Program strategy examinations are used to update the algorithms.

income were not identified and cases were not created by the IRS's nonfiler programs, and in other cases, they were identified but not worked by the IRS.[13] Specifically, TIGTA identified 314,586 business taxpayers with $335.5 billion in Form 1099-K income that appeared to have a filing obligation, but were not identified as nonfilers by the IRS.

Further, the growth of peer-to-peer payment applications has greatly enhanced the flow and transfer of funds between users on virtual platforms, making it easier and cheaper to send payments from one person to another. However, the technology presents additional tax compliance challenges in that the payments are not always reported to the IRS and can be hard to detect during an IRS examination.[14]

MODERNIZING IRS OPERATIONS

The IRS relies extensively on computerized systems to support its financial and mission-related operations. The IRS requested $305 million for the modernization effort in its FY 2022 budget request, an increase of $82 million or approximately 37 percent from the FY 2021 enacted budget. Successful modernization of systems and the development and implementation of new information technology applications are critical to meeting the IRS's evolving business needs and enhancing services provided to taxpayers. The reliance on legacy systems and its use of outdated programming languages pose significant risks to the IRS's ability to deliver its mission. Modernizing the IRS's computer systems has been a persistent challenge for many years and will likely remain a challenge for the foreseeable future.[15]

For example, the IRS uses more than 60 different legacy case management systems that widely vary in complexity, size, and customization to support tax administration. In January 2015, the IRS formally established the Enterprise Case Management (ECM) program to provide an enterprise solution to perform case management functions utilizing a Department of the Treasury Cloud platform, thus reducing long-term costs and increasing operational efficiency, innovation, and security. However, TIGTA reported that the ECM program has not finalized its agile development methodology.[16] The program is implementing a mixture of two different agile configurations and trying to strike a balance between implementing the recommended roles while minimizing unnecessary overhead. In addition, the benefits of the ECM program are defined in broad terms and will make it difficult for leadership to manage continuous implementation of processes over a long period of time, identify tradeoffs in competing priorities, and evaluate success.[17]

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[13] TIGTA, Report No. 2021-30-002, *Billions in Potential Taxes Went Unaddressed From Unfiled Returns and Underreported Income by Taxpayers That Received Form 1099-K Income* (Dec. 2020).
[14] TIGTA, Report No. 2021-30-022, *The Internal Revenue Service Faces Challenges in Addressing the Growth of Peer-to-Peer Payment Application Use* (Apr. 2021).
[15] TIGTA, Report No. 2021-20-001, *Annual Assessment of the Internal Revenue Service's Information Technology Program for Fiscal Year 2020* (Oct. 2020).
[16] IRS guidance characterizes agile development as having iterative product development and delivery. Regular testing intervals, customer involvement, and continuous product delivery allow for feedback throughout the development process.
[17] TIGTA, Report No. 2021-20-059, *Enterprise Case Management Deployed Its Initial Release, but Process Improvements Are Needed for Future Releases* (Sept. 2021).

Ineffective security controls to protect IRS systems and data could have a significant effect on a broad array of Government operations and assets. Without effective security controls, computer systems are vulnerable to human errors or actions committed with malicious intent. Server virtualization[18] is now an established standard for enterprise information technology infrastructure in data centers and cloud services as it provides better utilization of hardware resources, reduces physical space required, and reduces power consumption and administrative overhead. As a result, the IRS concluded that its diverse and widely deployed server infrastructure would benefit from a consolidation and virtualization project. TIGTA reported that the IRS is performing security scans of the virtual host infrastructure platform.[19] However, the IRS inventory system does not accurately reflect all of the virtual host infrastructure platform servers. For example, virtual host servers were uncategorized and incorrectly recorded. Protecting critical assets and infrastructure helps reduce the risk of internal and external attacks on IRS assets that could potentially expose taxpayer data and information.

IMPROVING CUSTOMER SERVICE AND THE TAXPAYER EXPERIENCE

The 2021 Filing Season began later than normal, on February 12, 2021. The later start was needed to update the IRS's processing systems. On March 17, 2021, the Department of the Treasury extended the income tax filing due date to May 17, 2021. Backlogs of unprocessed tax returns and other types of tax account work that affected the previous filing season now continue into the 2021 Filing Season. The inability to timely address these backlogs will continue to have a significant impact on the associated taxpayers.

Contributing to the IRS's inability to address backlogs is the significant shortfall in its hiring of personnel needed for their Submission Processing functions as well as the closure of its Tax Processing Site in Fresno, California. The IRS also continues to take steps to protect the health and safety of its employees working in its Tax Processing Centers; as a result, it was not always able to operate at full capacity due to social distancing requirements. These requirements include limiting close contact with other employees and maintaining a physical distance of at least six feet in an effort to reduce the spread of COVID-19. Finally, while much of the IRS's workforce continues to telework, the work performed at the IRS's Tax Processing Centers is not conducive to a remote telework environment. This work includes receiving, sorting, and distributing of mail and processing of paper tax returns, which requires manually inputting information from tax returns into IRS systems, correcting errors, and corresponding with the taxpayer, when needed.

In an effort to restore customer service options to taxpayers the IRS accelerated the implementation of several new initiatives it had been testing and expanded the use of

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[18] Virtualization is the simulation of the software and hardware upon which other software runs. This simulated environment is called a virtual machine.

[19] TIGTA, Report No. 2021-20-024, *Improvements Are Needed for the Virtual Host Infrastructure Platform* (June 2021).

existing technologies and capabilities.[20] However, while the majority of customer service assistance options are now available to taxpayers, the previous closures are a contributing factor to increased demand on the IRS and its inability to provide quality customer service. For example, the IRS reported 321.4 million visits to IRS.gov for the 2020 Filing Season as of March 6, 2020. In comparison, as of March 5, 2021, the IRS reported 555.7 million visits to IRS.gov this filing season, which is an increase of 72.9 percent. However, as of March 5, 2021, the IRS only provided a 27.3 percent Level of Service on its toll-free customer service lines. In comparison to the same timeframe in March 2020, the IRS reported a 68 percent Level of Service.

The Taxpayer First Act included provisions for the IRS to develop a comprehensive customer service strategy to better serve taxpayers. In response, the IRS developed the taxpayer experience strategy. According to the Commissioner of Internal Revenue, the taxpayer experience strategy is designed to improve a taxpayer's experience with the IRS through expanded digital services, increased multilingual services, and an increased presence in hard-to-reach, historically underserved communities.[21] This law also requires the IRS to develop an organizational redesign strategy that prioritizes the taxpayer experience to ensure that taxpayers can easily and readily receive the help they need.

ADDRESSING EMERGING THREATS TO TAX ADMINISTRATION

Identity theft tax refund fraud involves the use of another person's name and Taxpayer Identification Number[22] to file a fraudulent tax return reporting false income and withholding in an effort to receive a fraudulent tax refund. The IRS recognized that the Economic Impact Payments (EIP) created a new risk for tax-related identity theft. In response, the IRS developed specific filters to identify potentially fraudulent filings. Once a return was identified as potentially fraudulent, it was sent to an IRS team for review. As of December 31, 2020, the IRS identified 528,388 questionable tax returns associated with the EIP for review and determined that 46,111 tax returns were fraudulent.

Illicit actors may also file false individual international tax returns in order to obtain refunds. TIGTA evaluated IRS processes to identify and prevent potentially fraudulent individual international tax returns and identified areas for improvement.[23] Specifically, the IRS does not have sufficient processes in place to identify potentially fraudulent individual international tax returns at the time these returns are filed. TIGTA's review of

[20] TIGTA, Report No. 2021-46-029, *Assessment of the Effects of the Coronavirus Pandemic on Customer Service Operations* (Apr. 2021).
[21] Written testimony of Charles Rettig, Commissioner, Internal Revenue Service, *The IRS's Fiscal Year 2022 Budget,* Senate Finance Committee (June 8, 2021).
[22] A nine-digit number assigned to taxpayers for identification purposes. Depending upon the nature of the taxpayer, it can be an Employer Identification Number, a Social Security Number, or an Individual Taxpayer Identification Number.
[23] TIGTA, Report No. 2021-40-057, *Improvements Are Needed to Identify Potentially Fraudulent Individual International Tax Returns During Processing* (Sept. 2021).

TY 2018 tax returns identified 8,332 international tax returns with potentially erroneous or fraudulent refunds totaling nearly $20.6 million that were not identified by the IRS.

Identity theft not only affects individuals, it can also affect businesses. The IRS defines business identity theft as creating, using, or attempting to use businesses' information without authority to obtain tax benefits. The IRS continues to take actions to improve its detection of business identity theft, including expanding the number of identity theft filters from 35 in Processing Year 2018 to 84 in Processing Year 2020. However, continued expansion of detection capabilities, to include other business return types, is needed. For example, TIGTA found that 36 business return types with refunds issued totaling $10.5 billion in Processing Year 2019 were not evaluated for potential identity theft.[24]

Preventing refund fraud associated with prisoners' Social Security Numbers is also a challenge for tax administration. The IRS implemented corrective actions in response to concerns raised in a TIGTA report issued in July 2017.[25] However, in April 2021, TIGTA reported that the IRS could take additional actions to expand its participation in the Blue Bag Program, a program in which the IRS partners with the Federal Bureau of Prisons and State Departments of Corrections to identify potentially fraudulent tax returns and refunds.[26]

TIGTA works closely with the IRS to identify, investigate, and combat threats to tax administration. After passage of the Coronavirus Aid, Relief, and Economic Security Act (CARES),[27] TIGTA observed an increase in related illicit scams and schemes with various objectives, such as manipulation of IRS online applications, theft of EIPs, and efforts to steal sensitive taxpayer information. Because the IRS used the same distribution methodology for ARP Act payments as it did for CARES Act payments, TIGTA estimates that a similar amount of theft will occur.

TIGTA plays a key role in protecting IRS employees. Threats and assaults directed at IRS employees, facilities, and infrastructure impede the effective and safe administration of the Federal tax system and the IRS's ability to collect tax revenue. In the last several years, threats directed at the IRS have remained the second largest component of TIGTA's Office of Investigations' work. Recent incidents involving taxpayers who threatened or assaulted IRS employees underscore the dangers that these employees face.

REDUCING FRAUDULENT CLAIMS AND IMPROPER PAYMENTS

The Office of Management and Budget describes an improper payment as any payment that should not have been made, was made in an incorrect amount, or was made to an

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[24] TIGTA, Report No. 2021-40-004, *Refinement and Expansion of Filters to Include Additional Business Returns Will Continue to Improve Business Identity Theft Detection Efforts* (Oct. 2020).
[25] TIGTA, Report No. 2017-40-041, *Actions Need to Be Taken to Ensure Compliance With Prisoner Reporting Requirements and Improve Identification of Prisoner Returns* (July 2017).
[26] TIGTA, Report No. 2021-40-027, *Actions Were Taken to Improve the Identification of Prisoner Tax Returns* (Apr. 2021).
[27] Pub. L. No. 116-136, 134 Stat. 281 (2020).

ineligible recipient. The Improper Payments Information Act of 2002[28] requires Federal agencies, including the IRS, to estimate the amount of improper payments and report to Congress annually on the causes of, and the steps taken to, reduce improper payments. The Earned Income Tax Credit (EITC) has been identified as a high-risk program; therefore, the IRS must include the rate and amount of improper payments for the EITC program in the Department of the Treasury's annual Agency Financial Report.

In FY 2020, the Office of Management and Budget determined that the EITC, Additional Child Tax Credit (ACTC), and American Opportunity Tax Credit are also high-priority programs that are susceptible to significant improper payments.[29] The IRS estimates it issued approximately $22.8 billion in potentially improper EITC, ACTC, and American Opportunity Tax Credit in FY 2020. This represents a significant loss to both the Federal Government and taxpayers.

The IRS did not calculate the dollar amount and percentage rate of improper payments for another high-risk program – the Net Premium Tax Credit.[30] IRS management stopped working on this calculation, citing delays stemming from significant demands placed on the Department of the Treasury and the IRS in connection with the COVID-19 pandemic as well as delays working with the Department of Health and Human Services and the Centers for Medicare and Medicaid Services to develop a joint methodology for assessing improper payment risk for the Premium Tax Credit.

Further, the passage of the ARP Act temporarily expands the Child and Dependent Care Credit. Beginning on January 1, 2021, the credit is fully refundable and the amount of the credit and the income phase-out limits have significantly increased. The unintended consequence of refundable credits is that they can result in the issuance of improper payments and can be the targets of unscrupulous individuals. TIGTA is planning to conduct several audits evaluating the IRS's implementation of this credit.

INCREASING INTERNATIONAL TAX COMPLIANCE

Complexity and change in the international tax environment require that the IRS collaborate with tax administrations of foreign countries to enforce compliance. The IRS has not developed a reliable estimate of the international tax gap. The Tax Gap is estimated using statistics from the IRS's National Research Program data that does not measure international noncompliance.[31] The IRS must continue to focus significant efforts on global tax cooperation and tax administration practices that can prevent and resolve disputes among countries to increase certainty for taxpayers. International

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[28] Pub. L. No. 107-300, 116 Stat. 2350 (2018).

[29] TIGTA, Report No. 2021-40-036, *Improper Payment Rates for Refundable Tax Credits Remain High* (May 2021).

[30] Eligible taxpayers can choose to receive the Advanced Premium Tax Credit (APTC), which helps cover the cost of their health insurance premiums. When taxpayers prepare their tax return, they must reconcile the APTC with the amount of the Premium Tax Credit that they are allowed to claim. Taxpayers whose Premium Tax Credit exceeds their APTC have a Net Premium Tax Credit, which reduces their tax liability and, if more than the tax liability, results in a refundable tax credit.

[31] TIGTA, Report No. 2009-IE-R001, *A Combination of Legislative Actions and Increased IRS Capability and Capacity Are Required to Reduce the Multi-Billion Dollar U.S. International Tax Gap* (Jan. 2009).

agreements and tax law changes are important, but the Department of the Treasury and the IRS should follow through to ensure that these efforts achieve their intended results.

The Foreign Account Tax Compliance Act (FATCA) was designed to establish reporting requirements for U.S. citizens with foreign accounts, with significant penalties if foreign accounts were not reported.[32] It was estimated that revenue from the FATCA would be $8.7 billion from FYs 2010 to 2020. While initial enforcement-related complications involved data reliability issues, more recent problems are related to the fact that the Department of the Treasury and the IRS have delayed the requirement for Foreign Financial Intermediaries (FFI) to require that U.S. citizens provide Social Security Numbers when establishing accounts and the FFIs to provide that information to the United States so the IRS can match compliance information it has with information that the FFIs have.

With the rising number of taxpayers giving up or abandoning their U.S. citizenship or resident status, it is important that the IRS has controls in place to enforce the tax provisions applicable to expatriates. Since enactment of the Heroes Earnings Assistance and Relief Tax Act of 2008,[33] the number of taxpayers expatriating increased significantly from Calendar Year 2008 to Calendar Year 2018 (from a total of 312 in 2008 to 3,974 in 2018). During the same period, TIGTA found that the IRS did not have a centralized compliance effort aimed at enforcing the expatriate rules.[34]

In addition, TIGTA reported that the IRS currently has no processes and procedures in place to ensure the legitimacy of certain international tax returns at the time returns are filed.[35] Specifically, TIGTA identified 130,448 international tax returns in which individuals reduced or eliminated the Federal income tax paid on nearly $2 billion in income.

PROTECTING TAXPAYER RIGHTS

The IRS must balance tax compliance activities to enforce the tax code while at the same time upholding taxpayer rights. The IRS continues to dedicate significant resources and attention to complying with the taxpayer rights provisions of the IRS Restructuring and Reform Act of 1998.[36]

The IRS Restructuring and Reform Act of 1998 requires TIGTA to audit certain taxpayer rights provisions and report whether the IRS complied with those provisions. While overall compliance has improved, TIGTA continues to identify areas in which the IRS can improve. For example, TIGTA evaluated whether the IRS followed the joint return

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[32] Pub. L. No. 111-147, Subtitle A, 124 Stat 97 (codified in scattered sections of 26 U.S.C.). TIGTA, Report No. 2018-30-040, *Despite Spending Nearly $380 Million, the Internal Revenue Service Is Still Not Prepared to Enforce Compliance With the Foreign Account Tax Compliance Act* (July 2018).
[33] Pub. L. No. 110-245 (2008).
[34] TIGTA, Report No. 2020-30-071, *More Enforcement and a Centralized Compliance Effort Are Required for Expatriation Provisions* (Sept. 2020).
[35] TIGTA, Report No. 2021-40-057, *Improvements Are Needed to Identify Potentially Fraudulent Individual International Tax Returns During Processing* (Sept. 2021).
[36] Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2, 5, 16, 19, 22, 23, 26, 31, 38, and 49 U.S.C.).

disclosure requirements on collection information requests and determined that disclosure requirements were not followed in 26 of 124 Accounts Management customer service representatives' history files and three of 20 Field Assistance individual taxpayer advisory specialists' history files in the Wage and Investment Division.[37] Also, during the review of the IRS's compliance with the prohibition against designating taxpayers as Illegal Tax Protesters or similar designations, TIGTA found that IRS employees used these designations on some taxpayer accounts.[38]

TIGTA also evaluated the IRS's compliance with provisions of the law that restrict the direct contact of taxpayers who are represented. TIGTA found that in 18 of the 75 cases reviewed, taxpayer rights were potentially infringed upon because the IRS did not send notices and letters to authorized representatives as required.[39] Of the 75 cases reviewed, a power of attorney was authorized to receive notices in 50 of these cases. When projected to the overall population of 4,349 examinations in which taxpayers had an authorized representative, the IRS potentially negatively impacted taxpayer rights for 1,043 taxpayer accounts in regards to representative notice and letter requirements.

Additionally, Collection Due Process hearing provisions are designed to give taxpayers an opportunity for an independent review to ensure that the levy action that has been proposed or the Notice of Federal Tax Lien that has been filed is warranted and appropriate. Similar to prior audits, TIGTA identified processing errors in 16 of 81 sampled taxpayer cases.[40] Processing errors related to proper classification of hearing requests and incorrect Collection Statute Expiration Dates on the taxpayer's accounts. For example, taxpayer accounts had errors due to incorrectly input Collection Statute Expiration Date suspension start and stop dates. In some cases, the IRS incorrectly extended the time period, allowing the IRS additional time to collect delinquent taxes.

HUMAN CAPITAL

Human capital is the Federal Government's most critical asset. At a time when the IRS is taking on such new challenges as the implementation of pandemic relief for taxpayers, the recruitment of new employees and retention of existing employees are critical to ensuring the maintenance of a quality workforce capable of meeting the needs of the American public.

Between FY 2010 and FY 2020, the IRS lost more than 33,000 full-time personnel, which included nearly 13,400 key enforcement personnel.[41] In addition, TIGTA reported that the IRS continues to experience challenges hiring and retaining an adequate

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[37] TIGTA, Report No. 2021-30-050, *Fiscal Year 2021 Statutory Review of Disclosure of Collection Activity With Respect to Joint Returns* (Aug. 2021).
[38] TIGTA, Report No. 2021-30-048, *Fiscal Year 2021 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations* (Aug. 2021).
[39] TIGTA, Report No. 2021-30-054, *Fiscal Year 2021 Statutory Review of Restrictions on Directly Contacting Represented Taxpayers* (Aug. 2021).
[40] TIGTA, Report No. 2021-10-049, *Review of the Independent Office of Appeals Collection Due Process Program* (Aug. 2021).
[41] IRS, *Management's Discussion and Analysis*, *Fiscal Year 2020*.

workforce to meet its workload demands at Tax Processing Centers.[42] For example, the IRS's Submission Processing function was only able to reach 59 percent of its hiring goals during the 2021 Filing Season. Although the IRS has several initiatives underway to help address its hiring shortages, these initiatives may not successfully mitigate the hiring challenges as anticipated. We remain concerned about the IRS's continued challenges in hiring sufficient staff needed to work backlog inventory and process tax returns at the same time. The inability of the IRS to hire sufficient staff could further affect taxpayers awaiting refunds and additional Recovery Rebate Credits claimed on TY 2020 returns.

The IRS's FY 2022 budget request includes a net staffing increase of approximately 12 percent, or 8,493 direct Full-Time Equivalents, as compared to FY 2021.[43] Although increased funding would assist the IRS in replacing employees lost through attrition, on-boarding, training, and assimilating large numbers of employees will create its own challenges for the IRS.

In addition, the IRS was faced with unprecedented human capital-related challenges due to the COVID-19 pandemic. In March 2020, the IRS directed all employees, except those performing mission-critical functions that could not be performed remotely, to vacate IRS worksites and work from home or an alternate location. The IRS initially placed nearly 35,000 employees on paid Weather and Safety Leave because the employees could not work in an IRS facility or telework.[44] In response to the pandemic, the IRS steadily increased telework participation, and in July 2020 reopened IRS facilities to some employees. Between March 2020 and September 2020, the IRS distributed nearly 19,000 laptops to employees to allow them to perform their jobs remotely. By September 2020, over 60,000 employees teleworked at least a portion of their work schedule, while approximately 25,000 employees worked at least a portion of their time from an IRS facility.

As the IRS reopened its facilities to mission essential functions and non-portable work, it faced additional challenges.[45] As of June 30, 2021, nearly 4,200 IRS employees reported having tested positive for COVID-19. IRS data show that approximately 47 percent of these employees reported to an IRS facility during the 14 days preceding a positive test result.

In March 2021, TIGTA completed unannounced site visits to eight IRS campuses. Overall, TIGTA found that the IRS had implemented its COVID-19 guidance; however, we observed instances of noncompliance with health and safety guidance at all eight facilities, including guidance pertaining to mask and social distancing requirements.

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[42] TIGTA, Report No. 2021-40-038, *Interim Results of the 2021 Filing Season* (May 2021).
[43] Full-Time Equivalents are a measure of labor hours in which one Full-Time Equivalent is equal to eight hours multiplied by the number of compensable days in a particular fiscal year.
[44] Weather and Safety Leave is a form of administrative leave permitted when an agency determines that safety-related conditions prevent employees from safely traveling to or safely performing work at an approved location or telework site.
[45] TIGTA, Report No. 2021-16-073, *Steps Were Taken to Protect Employee Health and Safety, but Additional Efforts Are Needed to Ensure Compliance With Federal Guidelines During Pandemics* (Sept. 2021).

The IRS will continue to face challenges as it balances the completion of its mission with the health and safety of its employees.

CONCLUSION

This memorandum is provided as our annual summary of the most serious major management and performance challenges confronting the IRS in FY 2022. TIGTA's *Fiscal Year 2022 Annual Audit Plan* and *Fiscal Year 2022 Inspections and Evaluations Program Plan* contain our proposed reviews. If you have any questions or wish to discuss our views on the challenges in greater detail, please contact me at (202) 622-6500.

cc: Deputy Secretary of the Treasury
Acting Assistant Secretary for Management
Deputy Chief Financial Officer
Commissioner of Internal Revenue