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Report to Designated Congressional
Committees

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**TAX POLICY AND
ADMINISTRATION**

**1986 Annual Report
on GAO's Tax-Related
Work**





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The Honorable Dan Rostenkowski
Chairman, Committee on
Ways and Means
House of Representatives

The Honorable Lloyd W. Bentsen
Chairman, Committee on
Finance
United States Senate

The Honorable Dan Rostenkowski
Chairman, Joint Committee
on Taxation
Congress of the United States

The Honorable Jack Brooks
Chairman, Committee on
Government Operations
House of Representatives

The Honorable John Glenn
Chairman, Committee on
Governmental Affairs
United States Senate

This is our annual report for calendar year 1986 on our work on tax policy and administration matters. The report, which is submitted in compliance with 31 U.S.C. 719(d), consists of the following appendices.

I. Open recommendations to Congress from reports issued during calendar year 1986. Actions taken and/or pending as of September 30, 1987, are included.

II. Open recommendations to Congress from reports issued before calendar year 1986. Actions taken and/or pending as of September 30, 1987, are included.

III. Legislative actions taken on recommendations made during calendar year 1986.

IV. Tax-related recommendations made during calendar year 1986 to the Secretary of the Treasury; the Commissioner of Internal Revenue; and

to other interested congressional committees and will make copies available to others upon request.

Jennie S. Stathis

Jennie S. Stathis
Associate Director

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The Internal Revenue Code Should Be Amended to Give IRS an Interest-Free Period to Process Certain Non-Income-Based Returns

(GAO/GGD-86-72, 7/28/86)

Sections 6611(e), (f), and (h) of the Internal Revenue Code provide an interest-free period for processing income tax refunds, carryback applications, and windfall profit tax refunds. On the other hand, the code does not provide an interest-free processing period for refunds of such non-income-based taxes as employment taxes, excise taxes, estate taxes, and gift taxes. Interest on these refunds is generally paid for the entire period between the overpayment date and the date of the refund.

In 1983 and 1984, IRS proposed to the Department of the Treasury legislative changes that would have created an interest-free period for processing refunds of such non-income-based taxes as employment taxes, excise taxes, estate and gift taxes, and railroad retirement taxes. In preparing its proposal to create an interest-free processing period for non-income-based tax returns, IRS determined that for an 11-month period ending October 1, 1982, \$72 million in interest was paid on employment tax refunds alone. Of that amount, IRS estimated that \$36.6 million could have been saved if a 45-day interest-free period had been in effect.

We did not verify IRS estimates. It should be noted, however, that IRS has been able to process over 90 percent of income-based refunds within 45 days even though the volume of these refunds is much higher.

Matter for Consideration by Congress

We suggested that Congress consider amending Section 6611 of the Internal Revenue Code to provide an interest-free processing period for non-income-based tax returns. We did not attempt to determine how long such a period should be. However, a 45-day processing period would make the treatment of non-income-based returns consistent with most income-based returns.

Action Taken And/or Pending

No action was taken or planned as of September 30, 1987.

**Appendix II
Open Recommendations to Congress From
Reports Issued Before Calendar Year 1986**

Action Taken And/or
Pending

No action was taken or planned as of September 30, 1987.

Legislative Actions Taken on Recommendations Made During Calendar Year 1986

Congress Should Consider Whether to Amend the Tax Code to Require Discounting of Property/Casualty Insurance Companies' Loss Reserves for Tax Purposes

(GAO/GGD-85-10, 3/25/85)

About half the business of the property/casualty insurance industry is constituted by insurance contracts involving claims that are paid out over a considerable period of time. For example, 50 percent of the amount of medical malpractice claims and 30 percent of general liability claims incurred during 1977 remained unsettled 5 years later. Loss reserves are needed to ensure that a company has adequate funds to make future payments on claims.

While the concept of tax deductions for such reserves seems appropriate, the former practice used by the industry overstated the amounts needed to satisfy future claims. The amounts being reserved were not reduced by the investment income being earned on the reserves from the time they are established to the time they are paid out, thus resulting in the understatement of taxable income. Furthermore, for those property/casualty companies whose reserves for loss payments were growing, this practice would increasingly understate taxable income. One way to remedy this problem would be to discount reserves at a rate based on each company's investment return.

Recommendation

We recommended that if Congress wished to assure that the property/casualty insurance industry's revenues and expenses were more closely matched for purposes of measuring taxable income, it should consider amending the tax code to provide that in calculating the loss reserve deduction for tax purposes, loss reserves are discounted.

Action Taken And/or Pending

Section 1023 of the Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) provided for the discounting of reserves, as we recommended with some modification.

Congress Should Consider Whether to Retain the Special Tax Preference for Mutual Property/Casualty Insurance Companies in Its Present Form

(GAO/GGD-85-10, 3/25/85)

The Revenue Act of 1962 established a protection against loss (PAL) account to confer a tax preference to mutual property/casualty insurance companies. The reason for the PAL account was concern about mutual companies' lack of access to capital markets in the event that they sustained catastrophic losses.

The PAL account operated to defer taxes on a portion of a mutual company's income. For tax purposes, a mutual company could set aside funds based on the size of its incurred losses and underwriting income. These funds, subject to certain statutory limitations, were deductions against current period underwriting gains. We reported that the rationale for the PAL account may have been based on questionable economic assumptions. If catastrophic losses were to occur, the PAL account would not necessarily ensure the company's ability to satisfy its contract obligations. Moreover, it was questionable whether stock companies faced with a catastrophic loss could successfully access capital markets.

Recommendation

We recommended that Congress consider whether the special tax preference for mutual property/casualty insurance companies should be retained in its then present form.

Action Taken And/or Pending

Section 1024 of the Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) repealed the PAL account.

Congress Should Further Restrict Use of the Completed Contract Method of Accounting

(GAO/GGD-86-34, 1/17/86)

The completed contract method of accounting allows contractors to defer reporting all revenues and expenses attributable to a long-term contract until the contract is completed. We reviewed the 1980 through 1984 annual reports of 135 contractors who used the completed contract method of accounting for tax purposes, and found that the cumulative amount of taxes deferred was \$5.2 billion.

The Treasury first authorized construction contractors to use the completed contract method of accounting for tax purposes in 1918. When Treasury regulations were revised in 1976, manufacturers with long-term contracts were also allowed to use it. The Treasury subsequently reported that some contractors were realizing extensive and unintended tax benefits by using the completed contract method and recommended its elimination. In 1982, rather than bar its use, Congress directed Treasury to modify the completed contract method to restrict its unintended benefits. Treasury issued its modifications on December 30, 1985.

The completed contract method is an exception to the basic concept that federal income tax liability should be determined and reported on the basis of annual (tax year) revenues and expenses, since contractors using the completed contract method wait until the year in which the contract is completed to report revenues and/or expenses. Over the years, contractors in certain trades have justified using the completed contract method to alleviate the uncertain profitability of individual projects. They argued that this uncertainty precluded them from making the reasonably dependable estimates required for tax purposes.

Based on our review, most contractors already estimate contract costs and the percentage of the project's completion for financial reporting purposes. These same estimates could be used for tax-reporting purposes. We believe that most manufacturing and construction contractors either have or should be able to acquire the expertise needed to make reasonably dependable estimates of project cost and/or progress for tax purposes. Therefore, we believe that the completed contract method should not be allowed for tax-reporting purposes except for those few contractors who can satisfactorily demonstrate that they cannot estimate the cost of completing specific contracts.

Recommendation

We recommended that Congress not allow the use of the completed contract method for income tax purposes except in those instances where

**Qualifying Income for
Renters of Tax-
Exempt Bond-
Financed Housing
Should Be Adjusted
for Household Size**

(GAO/RCED-86-2, 2/10/86)

Tax-exempt bonds are designed to stimulate multifamily rental housing production and achieve a greater public purpose by requiring that at least 20 percent (or 15 percent in targeted areas) of units be occupied by low- or moderate-income individuals. Such individuals are defined as those earning no more than 80 percent of an area's median income.

Housing projects we reviewed that were financed with tax-exempt bonds generally had the required 20 percent of low- and moderate-income households. However, ambiguity surrounded the issue of whether incomes should be adjusted for family size when qualifying households as low or moderate income. Neither the law or implementing Treasury regulations were clear as to whether such an adjustment should be made. In the absence of clear guidance, most housing agencies had not made an adjustment. In 12 of 19 agencies we visited, the low- or moderate-income eligibility criterion was the same for one-, two-, and three-person households as for a family of four. The lack of an adjustment considerably increased the number of projects able to qualify as having at least 20 percent of their units occupied by low and moderate income households. In our survey, 56 percent of the households met the definition of low- and moderate-income, whereas only 35 percent would have met the definition if family-size adjustments had been required. If Treasury amended its regulations to require an adjustment for family size, it would eliminate confusion and further the interests of low- and moderate-income households.

Recommendation

We recommended that the Secretary of the Treasury amend the implementing regulations to the Internal Revenue Code to require that income used in qualifying households as low or moderate income be adjusted to take household size into account.

**Action Taken And/or
Pending**

The Department of Treasury issued proposed regulations (50 Fed. Reg. 4603, Nov. 7, 1985) to amend the income tax regulations to require that, with respect to obligations issued after December 31, 1985, a family size adjustment be made when qualifying households as low or moderate income. The Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) adopted the requirement proposed in the Treasury regulations.

Congress May Need to Reevaluate Tax-Free Weapons Transfers

(GAO/GGD-86-49, 6/5/86)

Some individuals may have paid the \$200 yearly occupational tax to achieve National Firearms Act (NFA) dealer status in order to avoid the tax which would otherwise apply to individual transactions. An economic incentive existed for individuals who expected to engage in more than one weapon transaction in a year. By paying the \$200 dealer tax, they avoided the \$200 per weapon tax on transfers between individuals or between a dealer and an individual. Tax-exempt transfers between NFA occupational taxpayers were, by far, the most common method of acquiring NFA weapons accounting for about 78 percent of the weapons transactions between fiscal years 1978 and 1984. Also, our random sample of 114 current and former dealers in two states showed that 58 purchased, but never sold, the 279 weapons they acquired between October 1976 and July 1978.

Matter for Consideration by Congress

We suggested that Congress consider whether, and if so, how the incentive that exists for individuals to obtain NFA dealer status to avoid the per weapon transfer tax should be reduced or eliminated. We identified and assessed four alternatives for congressional consideration. The report also included three legislative proposals that the Bureau of Alcohol, Tobacco and Firearms (BATF) developed to eliminate the problem.

Action Taken And/or Pending

On May 19, 1986, Congress enacted Public Law 99-308 that placed restrictions on the possession of machine guns. Machine guns manufactured on or after May 19, 1986, may be possessed only for government agency use or export. Although dealers may be able to acquire samples for generating sales to agencies, the number of samples that can be acquired will be limited and the samples cannot be retained when the dealer ceases NFA operations. According to BATF, this law may lessen the incentive for individuals to obtain NFA dealer status to avoid the per weapon transfer tax because machine guns have constituted the majority of the weapons transfers.

**Appendix III
Legislative Actions Taken on
Recommendations Made During Calendar
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affordability of health insurance to high-risk individuals and small groups. However, we did conclude that making such plans taxable should not affect the availability of health insurance for most Americans, who are insured as members of large, employer-paid groups.

**Matter for Consideration
by Congress**

We suggested that Congress decide whether the exemptions for Blue Cross and Blue Shield plans under section 501(c)(4) were warranted. We said that if Congress decides not to continue the current exemptions, but to offer special tax treatment for insurers who provide coverage to high-risk individuals by amending the tax code, it should establish specific criteria for granting such treatment. The criteria could include such factors as whether an insurer (1) offers continuous open enrollment, (2) fully covers medical services for high-risk conditions, (3) offers coverage to high-risk individuals at the same rates charged to other individual policyholders, and (4) offers coverage without regard to age or employment status.

**Action Taken And/or
Pending**

The Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) amended 501(c)(3) and (4) of the Internal Revenue Code so that an organization is exempt under those sections only if no substantial part of its activities consists of providing commercial-type insurance. The act provides special treatment for Blue Cross and Blue Shield organizations which meet certain requirements and substantially all of whose activities are providing health insurance. However, the act also provides that such organizations eligible for special treatment are subject to tax as property and casualty insurance companies under Part II of Subchapter L of the Code, as amended under the act.

IRS Needs to More Effectively Monitor Businesses That Have Filed for Bankruptcy

(GAO/GGD-86-20, 2/21/86)

We performed work in three bankruptcy court districts, and found that 254 of 583 businesses that filed for reorganization in these districts in 1981 accumulated about \$6.6 million in delinquent taxes after bankruptcy proceedings began. Of the \$6.6 million, about \$5.5 million was still outstanding at the time of our fieldwork in early 1984. We believe that IRS could reduce such delinquencies by more closely monitoring those businesses that had the greatest potential for accumulating additional taxes, that is businesses with past delinquencies or large payrolls. Also, once IRS detects a problem, it could require businesses to file monthly instead of quarterly tax returns.

Recommendations

We recommended that the Commissioner of Internal Revenue (1) develop and include in the bankruptcy manual additional indicators for IRS personnel to use in deciding how frequently cases should be monitored, such as a firm's prior delinquency history; and (2) make greater use of IRS' authority to require businesses with employment tax liabilities to file monthly rather than quarterly returns.

Actions Taken And/or Pending

On December 5, 1986 IRS revised its Internal Revenue Manual to

- require its employees to consider past delinquency history in determining how frequently to monitor a business, and
- provide that monthly filing of tax returns be considered for those businesses whose payment history warrants such action.

IRS Needs to Assess the Effect of Recent Revisions to the Bankruptcy Court Rules

(GAO/GGD-86-20, 2/21/86)

Under revised bankruptcy court rules that became effective in August 1983, the courts are required to notify IRS of liquidation bankruptcies only when it is listed as a creditor on the bankruptcy petition. Work we did in one district office before the new rule became effective showed that some of the businesses that owed taxes had not listed IRS as a creditor. Under the new procedures, IRS would not have been notified of these bankruptcies.

IRS sought the new rule, hoping that it would eliminate the task of processing cases when the businesses did not owe taxes. IRS officials told us that they believed the money IRS saves by not working all bankruptcy cases far outweighs any revenue it might lose by not filing claims, but the officials said that IRS had no factual data to support this conclusion.

We attempted to evaluate the effect of this change in notification requirements by reviewing all 260 business liquidations filed in the three bankruptcy court districts during August and September 1983. Although our analysis did not show that the new rule was causing any major problems, we were concerned that due to the timing of our analysis, it might not fully reflect the effects of this change on the notification process. Our analysis covered the first 2 months that the rules were in effect, and many court districts continued to notify IRS of all bankruptcies after the August implementation date. At the time we completed our field work in one IRS district in June 1984, IRS officials told us that they were beginning to experience greater problems with businesses incorrectly failing to list IRS as a creditor.

Recommendation

We recommended that the Commissioner of Internal Revenue periodically test the effects of the revised bankruptcy court rules' notification requirements to (1) determine the extent to which liquidating businesses are not listing IRS as a creditor on bankruptcy petitions and (2) provide the basis for developing corrective action if needed.

Action Taken And/or Pending

IRS conducted a study to determine the effect of the revised bankruptcy court rule that requires the courts to notify IRS of liquidation bankruptcies only when IRS is listed as a creditor on the bankruptcy petition. Based on the results of its study, IRS will not seek a change to the current bankruptcy rule regarding notice to IRS of liquidating bankruptcies.

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Specifically:

- The National Computer Center has no designated backup processing site.
- IRS' Computer Services Office said that computer capacity problems may make infeasible IRS' currently proposed arrangement for one service center to back up another.
- IRS has not identified the most critical work load functions, that is, those that must be performed first in the event of a prolonged disruption to a center's operations.
- Backup tape files containing data and programs necessary to continue operations were not always maintained as required by IRS.
- Testing to ensure the workability of ADP contingency plans has ranged from nonexistent to limited

As a result, existing ADP contingency plans do not meet IRS' requirements to deal with the basic stages of emergency reaction—emergency response, backup operations, and recovery operations. Regarding backup operations, IRS has not analyzed and ranked the feasibility, costs, risks, and benefits of alternative backup strategies.

Recommendations

We recommended that IRS expedite its efforts to develop, certify, and test ADP contingency plans, and perform periodic risk analyses. In addition, we recommended IRS continue to report the lack of contingency plans and periodic risk analyses as material control weaknesses under the Federal Managers Financial Integrity Act until such plans are developed, certified, and tested, and risk analyses are completed for all computer centers.

**Actions Taken And/or
Pending**

IRS agreed with our findings and recommendations. IRS' Automation Policy Board (now the Information Systems Policy Board) directed the Assistant Commissioner for Computer Services to proceed with developing contingency plans. The Assistant Commissioner established an Office of Disaster Recovery, which is currently estimating the costs and resources needed to develop and implement such plans. Its recommendations are expected to be made in early 1990.

IRS also said it plans to complete risk analyses at all computer centers in 1987. It added that although such analyses are costly, it is committed to this effort, and it will continue to report the lack of risk analyses and contingency plans as a material control weakness under the Federal Managers Financial Integrity Act until they are resolved.

BATF Should Increase Compliance With Retail Alcohol Occupational Excise Taxes

(GAO/GGD-86-49, 6/5/86)

Occupational tax revenue is being lost due to noncompliance with the retail alcohol taxes. Our four-state sample showed that 4 out of every 10 liable retail establishments were noncompliant. Noncompliance with the retail alcohol taxes resulted in a projected fiscal year 1983 revenue loss of between \$1.8 million and \$3.7 million in the four states reviewed.

Income tax returns filed with IRS by businesses provide for entering the taxpayer's main or principal business activity. Two of the codes specifically pertain to retail alcohol establishments and other codes potentially involve businesses that sell alcoholic beverages. Matching taxpayer identification numbers of businesses classified under two or more of these codes with occupational tax information would identify businesses which may be liable for, but did not pay, the occupational tax. Also, every retail establishment that sells beverages in the United States are required to obtain some type of state or local license. BATF could increase taxpayer awareness and, in turn, compliance by obtaining the names of newly licensed establishments and informing them of their tax liabilities.

Recommendations

We recommended that the Director, BATF:

- Identify for follow-up potentially noncompliant retail alcohol establishments by arranging for IRS to match occupational tax payment data with businesses classified under selected principal industry activity codes.
- Arrange for state and local alcoholic beverage licensing agencies to provide BATF with the names of new licensees and advise the licensees by telephone or correspondence of their federal tax liabilities.

Actions Taken And/or Pending

BATF said that since it has recently assumed the collection function from IRS it is developing its own data base of special occupational taxpayers for use in following up on potentially noncompliant retail alcohol establishments. BATF also said that it is working with the states to obtain names of new state licensees and to advise them of their reporting responsibilities.

IRS' Monthly Filing Requirement for the Tax on Gross Wagers Needs to Be Revised

(GAO/GGD-86-49, 6/5/86)

IRS regulations require that the tax return on gross wagers be filed monthly, even if no tax is due. A majority of other excise taxes are filed quarterly unless the amount of tax due for a month exceeds \$100 or IRS requires more frequent filing for a noncompliant taxpayer.

At one IRS service center, we examined 2,345 gross wagering returns for March and December 1983 and found that if this tax had the same dollar threshold requirement as other excise taxes, 2,167, or 92 percent, of the returns reviewed would not have been required to be filed during these 2 months. Thus, because of the monthly filing requirement, IRS incurs costs to process returns that include little or no tax remittances. Taxpayers also incur unnecessary costs and inconvenience.

Recommendation

We recommended that the Commissioner of Internal Revenue revise the monthly filing requirement for the tax on gross wagers so that monthly returns would not be required unless an established dollar threshold is met.

Action Taken And/or Pending

IRS disagreed with our recommendation because it believed the savings would be negligible and the change might adversely affect compliance. As we pointed out in the report, some savings, although perhaps not substantial, would be realized through a change in the filing requirement. Also, we were unable to identify any compliance activities associated with the monthly filing requirement, or any adverse impact that would result from a change to quarterly filing.

IRS Needs to Improve Its Reporting Procedures for Commodity Credit Loan and Crop Insurance Income

(GAO/GGD-86-69, 7/22/86)

Millions of dollars of liquidated commodity credit loan and crop insurance income either were not reported, or were improperly reported, during tax years 1982 and 1983. Our analysis of sampled liquidated commodity credit loans and federal crop insurance payments showed that most of the income that went unreported was attributable to individuals and businesses that did not file their tax returns, as required. For those portions of the loan and insurance payment universes to which we could project our sample data, we estimated that recipients of more than 5,250 crop loans and insurance indemnity payments representing about \$53 million of income did not file 1982 and/or 1983 tax returns.

Proper reporting of crop loan and insurance income should increase soon, as well as IRS' ability to detect unreported income from crop loans and insurance payments. As required by the Internal Revenue Code, agricultural agencies are taking steps to send taxpayers and IRS information returns for these types of income. Generally, information returns detail the type and the amount of income received and should act as a reminder to taxpayers to report the income.

If matched against tax returns, moreover, information returns should help IRS to determine whether the income was properly reported and the applicable taxes were assessed. We found that the costs of operating computer matching programs for crop loan and insurance income should be small compared to the additional taxes that would be assessed. However, to make the most of commodity credit loan and crop insurance information returns, IRS needs to improve information return forms, filing instructions, and computer programs and to develop procedures for handling optional year reporting.

Recommendations

We recommended that the Commissioner of Internal Revenue (1) clarify instructions and forms concerning commodity credit loan and crop insurance income so that taxpayers and IRS can more efficiently and effectively use information returns, and (2) incorporate commodity credit loan and crop insurance income into IRS' document matching program.

Additional Interest Savings Could Result From Issuing Some Refunds Before Examination

(GAO/GGD-86-72, 7/28/86)

Refunds on amended returns are sometimes delayed due to audits or requests for additional information. Under current IRS procedures, these must be completed before the refund can be issued. We estimated that IRS paid \$37.6 million in interest during fiscal year 1983 to process refunds that it delayed for examination purposes. We also estimated that, on average, these refunds were delayed about 55 days more than those refunds which were not examined.

Currently, when taxpayers submit their initial tax returns and claim a refund, IRS performs various math and validity checks before issuing the refund. In most instances refunds of this type are issued within 45 days of the due date of the return. Subsequently, certain returns are examined to verify the correctness of reported revenues, credits, or deductions. Should IRS determine that a taxpayer owes additional taxes, IRS sends the taxpayer a bill. Taxpayers may appeal the results of an examination through the IRS appeals system or the courts.

Current IRS procedures for issuing refunds on amended returns, however, require that returns be completely reviewed and the information proven correct before a refund is made. Some refunds require minimal review and are paid quickly, but others require additional information or examination before the refund is made. IRS procedures require more in-depth examination of returns that (1) claim refunds over a set dollar amount, (2) claim certain types of deductions, (3) make changes to certain items, or (4) involve particular tax issues.

The results of our sample showed that significantly more time was used to process returns that needed more detailed examination. This resulted in additional interest costs and delayed issuance of the refund. If IRS were to issue refunds before examining these returns, as it normally does in processing refunds claimed on original returns, interest costs would be reduced and some taxpayers would receive their refunds sooner. By issuing a refund before examination, IRS could avoid paying interest for the time spent verifying and investigating the return.

Recommendation

We recommended that the Commissioner of Internal Revenue amend IRS procedures to provide for issuing certain refunds before making a detailed examination of the refund claim. The criteria for making these refunds should recognize the need for IRS to continue to hold certain refunds having a high potential for disallowance.

Administrative Changes Could Lead to Earlier Resolution of Tax Disputes

(GAO/GGD-86-75, 7/30/86)

Most taxpayers who disagree with the results of an IRS examination of their income tax returns either request that their cases be referred to IRS' Appeals Division or bypass Appeals and file directly with the Tax Court. Our study of how taxpayers resolved their disputes with IRS showed that many taxpayers who initially bypassed IRS' internal appeals process and filed with the court eventually settled their cases out of court with the IRS' Appeals Division.

In the seven IRS districts we visited, we estimated that (1) about \$1.2 million in added IRS and court processing costs and (2) about \$268,200 in taxpayer filing fees were spent in fiscal year 1984 on cases that were initially bypassed, but were ultimately settled by the Appeals Division. We believe that some of these costs could have been eliminated had the Appeals Division had an opportunity to deal with these cases before they were filed with the court. Our analysis of appeals officers' opinions in a sample of cases we reviewed indicated that more than one-third of the taxpayers may not have fully understood the dispute resolution process, including the potential benefits of seeking administrative resolutions before filing with the Tax Court. We believe IRS could do more to facilitate the early involvement of the Appeals Division in the case resolution process by better informing taxpayers about the dispute resolution process and encouraging them to go to IRS' Appeals Division before filing with the Tax Court.

Recommendation

We recommended that the Commissioner of Internal Revenue revise the language of IRS' 30-day letter to taxpayers, various IRS publications, and the information on the appeal procedures given to taxpayers by IRS auditors and revenue agents. These changes should (1) emphasize the advantages of going to the Appeals Division before filing with the Tax Court; and (2) point out that, even if taxpayers bypass Appeals, the cases will still be assigned to it for attempted settlement.

Action Taken And/or Pending

IRS agreed with the thrust of our recommendation to further inform taxpayers about the advantages of exhausting appeals before petitioning the Tax Court. IRS revised its publication entitled "Examination of Returns, Appeal Rights, and Claims for Refunds" to include language that explains the appeals process to the taxpayer in a more detailed manner.

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Pending**

IRS said that while it would issue instructions on how the information contained in a rate reduction request is to be evaluated, this is a subjective area that does not lend itself to uniform criteria. IRS also said that it would require the regions to more closely monitor the process to ensure consistent treatment of applicants. In February 1987, IRS issued Internal Revenue Manual Transmittal 4600-58, which provides broad guidelines for district office personnel to follow in evaluating tip rate reduction reports from employees and in monitoring the process.

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**Actions Taken And/or
Pending**

IRS generally agreed with our recommendations and has initiatives underway that can be useful in developing and implementing an overall strategy for reducing tip income nonreporting. For example, IRS provided its regions a list of establishments with potentially noncompliant tipped employees and established a tip document matching program to better identify tip income nonreporting. IRS is also conducting a study designed to provide information on compliance levels and the nature of noncompliance and identify the establishments and geographical areas that are most noncompliant. Results of the study will be analyzed and corrective action will be considered when the study is complete.

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that prohibit the timely installation of replacement processors or cause the existing processors to experience capacity or reliability problems.

- Update existing and future work load projections and monitor the performance of the communications processors and supporting mainframes to ensure that these computing resources can fulfill the IRS mission. Such updates and performance monitoring should be conducted regularly throughout the life of the systems.

**Actions Taken And/or
Pending**

IRS has taken, or plans to take, the following actions in response to our recommendations:

- IRS met with the House Committee on Ways and Means on several occasions since the report was issued, and will continue to report significant installation schedule changes to the Committee as recommended.
- IRS has developed contingency plans for the Data Communications Processing Systems for each service center for the 1987 processing season.
- IRS has begun to implement procedures to review all computer services work requests for system capacity impact. This analysis, along with performance monitoring data, will be used to continuously update work load projections and identify potential capacity problems.

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- Monitor the performance of the installed mainframe computers to provide a baseline for determining whether the initiatives actually extend the useful life of the existing mainframes and for evaluating alternatives for meeting future ADP requirements.
- Analyze the impact of the various work loads on the utilization of the mainframe computers to effectively estimate and plan for future IRS ADP requirements.
- Report to the Subcommittee on Oversight, House Committee on Ways and Means, any significant deviations or delays in the achievement of the initiatives or any other factors that may jeopardize IRS' ability to extend the useful life of its mainframes through 1991.

**Actions Taken And/or
Pending**

In December 1986, IRS established a multifunctional task force to develop a plan for providing adequate service center computer capacity until 1992 and beyond

IRS has also implemented an IRS Capacity Management Methodology intended to (1) provide a baseline model that establishes and characterizes existing systems work loads, and (2) project the impact of anticipated work load growth on current systems capacity.

IRS intends to continue to report to the House Committee on Ways and Means on its progress in extending the useful life of the service center computer systems until implementation of the Tax System Redesign.

**Appendix IV
Tax-Related Recommendations Made During
Calendar Year 1986 to the Treasury, IRS, and
BATF and Their Responses to Those
Recommendations**

**Actions Taken And/or
Pending**

IRS said that it was taking action to study the feasibility of implementing our recommendations. IRS intends to complete its study by January 1988.

**Effect of Using the
Completed Contract
Method of Accounting**

(B-221074, 1/31/86)

This letter to the Honorable Lawton Chiles, U. S. Senate, was a supplement to our report, entitled Congress Should Further Restrict Use Of The Completed Contract Method (GAO/GGD-86-34, Jan. 17, 1986). The letter contained seven tables of information on the effect that the use of the completed contract method of accounting has had on the taxes paid by large federal contractors during fiscal years 1980 through 1984. These tables include information on the income and tax liability of the top 20 defense contractors, illustrating how use of the completed contract method has affected the dollar amount of taxes deferred.

**Summary of Related
Action(s)**

The information in this letter was useful to Senator Chiles and his staff in their analysis of the tax implications of the continued use of completed contract method by major defense contractors. The use of the completed contract method for tax-reporting purposes was severely curtailed by the Tax Reform Act of 1986 (Public law 99-514, dated October 22, 1986). (See pp. 19 and 20.)

Nonbusiness Interest Deductions

(GAO/GGD-86-53BR, 3/13/86)

The House-passed tax reform bill (H.R. 3838) included provisions that generally were designed to restrict the amount of nonbusiness interest deductions other than mortgage interest. The data we presented in this briefing report to the Honorable Bill Frenzel, House of Representatives, shows that the potential existed for some homeowners to avoid these proposed restrictions because they could use their home equity as collateral to finance purchases of consumer items and nonbusiness investments, then deduct the related interest as home mortgage interest.

Summary of Related Action(s)

The information in this briefing report was useful particularly to the Senate as it conducted deliberations on the House-passed tax bill. The House version of the bill contained a provision which was revised by the Senate to reduce the potential that nonbusiness interest other than qualified residence interest could be deducted. The Tax Reform Act of 1986 (Public Law 514, dated October 22, 1986) specifies that the amount deductible as qualified residence interest consist of interest on debt that does not exceed the taxpayer's cost for the residence, plus the cost of any improvements. If the debt exceeds the qualified amount, interest still can be deducted to the extent that the borrowed amounts incurred after August 16, 1986, are used for educational or medical purposes.

**Financial Cycles in the
Property/Casualty
Insurance Industry**

(GAO/GGD-86-56FS, 4/9/86)

This fact sheet to the Chairman of the House Committee on Ways and Means contains four graphs that illustrate the property/casualty insurance industry's underwriting cycles. The graphs illustrate the industry's underwriting profit and loss cycle since 1967 (since 1945 for stock companies) and show that the current loss cycle has been more protracted than previous loss cycles.

**Summary of Related
Action(s)**

The information in this fact sheet was useful to the Committee in its consideration of and revision to the tax laws as they affect the property/casualty insurance industry. The taxation of the property/casualty insurance industry was substantially changed by the Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986). (See pp. 15 to 17.)

**GAO's Views on a
Proposed Tax
Administration Trust
Fund**

(B-223617, 7/16/86)

In its version of the tax reform bill (H.R. 3838, as amended), the Senate included a provision for funding IRS through a temporary trust fund called the Tax Administration Trust Fund. In our identical letters to the Chairman of the Senate Committee on Finance and the Chairman of the House Committee on Ways and Means, we noted that GAO has generally not favored earmarking government revenues for special purposes because doing so can lessen accountability for and control over such funds. We also suggested that if Congress decided that earmarking was necessary in IRS' case, it should provide for maintaining control over the trust fund through the congressional appropriations process.

**Summary of Related
Action(s)**

These letters were available to the congressional conferees during tax reform deliberations. The trust fund provision was stricken from the bill by the conferees and was not included in the Tax Reform Act of 1986.

Information on IRS' Automated Collection System

(GAO/GGD-86-120BR, 7/31/86)

This briefing report to the Chairman of the Subcommittee on Oversight, House Committee on Ways and Means, provides an overview of IRS' Automated Collection System (ACS)—a computerized system designed to manage collection cases and to improve communications between IRS and taxpayers. Specifically, the report presents (1) a description of IRS' collection system for obtaining delinquent returns and collecting delinquent taxes, (2) a description of how ACS fits into IRS' overall collection system, and (3) the results of ACS calls that we monitored and our case analysis of how the system disposed the collection cases related to these calls.

Our analysis of the monitored calls showed that IRS generally treated these taxpayers fairly when processing their cases on ACS. If a taxpayer said IRS was in error, IRS attempted to reconcile the problem before taking additional actions. IRS' actions to resolve the cases were generally reasonable based on information available to ACS personnel.

Summary of Related Action(s)

This briefing report provided the House Ways and Means Subcommittee on Oversight with insight into the operations of ACS and its responsiveness to taxpayer questions. In addition, the report was one in a series of products that assisted the subcommittee in meeting its oversight responsibilities.

**Use of Book Income in
the Proposed
Corporate Alternative
Minimum Tax**

(B-223878, 8/11/86)

This letter to the Chairmen of the House Committee on Ways and Means and Senate Committee on Finance synthesizes various analyses of the Senate's proposal to link the corporate alternative minimum tax to book income and evaluates the validity of arguments raised by those analyses.

**Summary of Related
Action(s)**

This letter was available to the congressional conferees during tax reform deliberations. The Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) adopted a revised procedure for determining a corporate alternative minimum tax.

Excise Taxes on Sporting Arms, Ammunition, and Archery Equipment

(GAO/GGD-86-114FS, 8/12/86)

This fact sheet to the Chairman and Ranking Minority Member of the Subcommittee on Fisheries and Wildlife Conservation and the Environment, House Committee on Merchant Marine and Fisheries, contains information on the administration of federal excise taxes in four categories of sporting goods—pistols and revolvers, other firearms, shells and cartridges, and bows and arrows. Our primary focus was on (1) IRS' compliance programs for excise taxes on sporting goods; (2) IRS' and the Department of the Treasury's accounting procedures for sporting goods excise tax receipts; (3) the accuracy of the Department of the Interior's U.S. Fish and Wildlife's estimates of future tax receipts; and (4) the size of annual fluctuations in actual receipts.

IRS' statistical data showed that its Examination Division had established an audit presence for excise taxes on sporting goods tax returns. IRS officials in 14 district offices said that they had not identified any particular noncompliance trends or concerns. Additionally, IRS' Collection Division pursued a compliance project in fiscal year 1987 because of a disparity between the number of sporting goods excise taxpayers on IRS' Business Master File (about 793 per quarter in fiscal year 1985) and the number of licensees as shown by BATF data (approximately 13,477 as of September 30, 1985).

IRS processes quarterly excise tax returns filed by taxpayers and transfers these receipts to the Federal Aid in Wildlife Restoration Fund. The fund is transferred to the Department of the Interior for subsequent apportionment to states and territories.

Estimates by Interior have varied from actual receipts. To improve forecasting accuracy, Interior is considering using more data on the sporting arms and ammunition industry.

For the 5-year period 1981-1985, there were more annual declines in the receipts than in previous 5-year periods. Industry and government officials attributed these fluctuations to the depressed economic condition of the sporting arms and ammunition industry.

Summary of Related Action(s)

The information in this fact sheet was useful to the House Subcommittee on Fisheries and Wildlife Conservation and the Environment in its oversight of the funds earmarked for state wildlife conservation and hunter education programs.

Choosing Among Consumption Taxes

(GAO/GGD-86-91, 8/20/86)

This GAO staff study provides information on consumption taxes, which are sometimes considered alternatives to income taxes in helping to reduce the federal budget deficit. A consumption tax is levied on a taxpayer's expenditures for goods and services rather than on that person's income. Commonly known examples of consumption taxes are the retail sales tax at the state and local level and excise taxes on alcohol, tobacco, and gasoline at the federal level.

We prepared this study to provide the layman with a general overview of consumption taxes and related issues. The study was intended to acquaint the general public, Congress, and other interested parties with the principal features of various consumption taxes, their relative advantages and disadvantages, and some key questions and issues associated with consumption taxes. The study contained no conclusions or recommendations.

Summary of Related Action(s)

None.

**Information on IRS'
Backlog of Tax
Returns With Tax
Shelter Issues
Awaiting Settlement**

(GAO/GGD-86-140BR, 9/12/86)

This briefing report to the Joint Committee on Taxation discusses IRS' increasing backlog of tax returns with tax shelter issues and the additional taxes and penalty adjustments that have been proposed for these cases. Although IRS has devoted considerable resources to identifying and settling tax shelter cases, our data show that the overall backlog of cases continued to increase. Furthermore, our data show that most taxpayers disagreed with tax adjustments proposed by the Examination Division. For example, taxpayers disagreed with the proposed adjustments in 86,218, or 61 percent of the total 141,423 tax shelter returns closed by the Examination Division in fiscal year 1985. These returns involving disagreements accounted for \$2.3 billion in proposed taxes and penalties and contributed to the backlog of cases in IRS' Appeals and Tax Litigation Divisions.

**Summary of Related
Action(s)**

This briefing report was useful to the Joint Committee on Taxation in its assessment of IRS' backlog of tax returns with tax shelter issues.

Benefits and Costs of ESOP Tax Incentives for Broadening Stock Ownership

(GAO/PEMD-87-8, 12/29/86)

This report, the third in a series to the Honorable Russell B. Long, U. S. Senate, provided information on four issues dealing with ESOPs: (1) the number of ESOPs, the number of participants covered by ESOPs, and the value of assets in ESOP trusts; (2) the factors associated with a company's decision to establish and continue in ESOP; (3) the costs of ESOPs in terms of federal revenues forgone; and (4) the degree to which ESOPs are broadening the ownership of capital assets in the United States. From our analyses, we estimated that as of March 1986, there were about 4,800 ESOPs active in the United States, and an additional 2,400 similar stock bonus plans. As of 1983, ESOPs covered more than 7 million workers, and held nearly \$19 billion in assets. Employers established ESOPs for a number of reasons, but by far the most commonly cited purposes were to provide a benefit to employees, utilize the ESOP tax incentives, and improve productivity. Employers maintained their plans largely because they experienced specific advantages (especially improved employee morale and tax savings), but usually no disadvantages. The tax incentives for ESOPs cost an estimated \$1.7 billion to \$1.9 billion per year, or \$12.1 billion to \$13.3 billion over the period 1977-83. These costs are high relative to the \$19 billion in assets participants have accumulated to date, apparently reflecting the dollar-for-dollar tax credits permitted for contributions to some ESOPs. Finally, ESOPs do appear to broaden the degree of capital ownership within sponsoring firms, but the small number of employees covered and the small percentage of all stock held by ESOP trusts put an upper limit on the extent of overall expansion of capital ownership in the United States associated with ESOPs.

Summary of Related Action(s)

The information in this briefing report was useful to Senator Long and his staff in monitoring ESOP issues.

Appendix VI
Listing of GAO Products on Tax Matters
Issued During Calendar Year 1986

Title	Date
Choosing Among Consumption Taxes (GAO/GGD-86-91)	08/20/86
No Improper Actions Found on IRS' Contract for Data Retrieval System (GAO/IMTEC-86-33BR)	08/26/86
Information on IRS' Backlog of Tax Returns With Tax Shelter Issues Awaiting Settlement (GAO/GGD-86-140BR)	09/12/86
Tip Income Reporting Can Be Increased (GAO/GGD-86-119)	09/30/86
Selection Procedures Same for Foreign- Owned and Other U.S Corporations (GAO/GGD-87-2)	10/12/86
Thorough Testing and Work load Analyses Needed for IRS Processors (GAO/IMTEC-87-3BR)	10/14/86
IRS Must Better Estimate its Computer Resource Needs (GAO/IMTEC-87-5BR)	11/03/86
How IRS Ensures That Others Adequately Safeguard Tax Data (GAO/GGD-87-13)	11/14/86
IRS Can Improve Its Collection Procedures for Taxpayers Living Overseas (GAO/GGD-87-14)	12/12/86
Benefits and Costs of ESOP Tax Incentives for Broadening Stock Ownership (GAO/PEMD-87-8)	12/29/86

Tax-Related Assignments Authorized Pursuant to 31 U.S.C. 713 During Calendar Year 1986

Subject matter	Objectives	Month authorized
Alien Nonfilers	<p>To develop information on the extent of tax revenue losses resulting from nonfiling and income underreporting by resident and nonresident aliens in the United States</p> <p>To evaluate the effectiveness of IRS' efforts to identify and collect taxes due on income earned by such aliens</p> <p>To evaluate the usefulness of information documents IRS receives from U S tax withholding agents concerning alien income</p> <p>To evaluate the level and effectiveness of coordination among IRS, State Department, Immigration and Naturalization Service, and Social Security Administration concerning aliens in the United States</p>	February
Federal Excise Taxes on Sporting Arms, Ammunition, and Archery Equipment	To determine the effectiveness of collection and accounting procedures for these taxes	February
Asset Reversions to Employers Who Terminate Overfunded Pension Plans.	<p>To determine reasons defined benefit plans had excess assets at termination</p> <p>To determine why plans were terminated and what types of replacement plans were provided</p> <p>To determine the effect of guidelines on employers' termination and replacement decisions</p>	March
Pension Plan Underfunding and Its Impact on the Federal Policy for Insuring Private Pension Benefits	To determine extent of pension plan underfunding	March
IRS' Efforts to Detect and Follow Up on Business Nonfilers	<p>To determine major factors contributing to such underfunding</p> <p>To identify ways for IRS to cost effectively and systematically detect business nonfilers through matching information returns and other IRS data sources</p> <p>To evaluate the effectiveness of IRS' procedures for following up on identified business nonfilers</p>	April
Properly Accounting for Taxes Earmarked for Specific Trust Funds	<p>To determine how IRS insures proper accounting and reporting of tax receipts earmarked for various trust funds</p> <p>To determine how IRS treats penalty and interest income associated with trust fund collections</p> <p>To determine how IRS monitors Treasury tax and loan accounts</p> <p>To determine methods IRS uses to collect trust fund data</p>	April
Unreported Business Income	To evaluate IRS' efforts to detect unreported business income and business nonfilers by implementing a business document matching process	June
IRS' Efforts to Process Federal Tax Deposits Using Optical Character Recognition Equipment	To determine whether processing of Federal Tax Deposit coupons is enhanced by encoding and, if so, whether opportunities exist to increase the incidence of encoding	July
IRS' Correspondence/ Adjustment Program	<p>To determine what causes taxpayers to correspond with IRS</p> <p>To determine how responsive IRS is to taxpayer inquiries</p> <p>To determine to what extent improper, incomplete, or unclear responses cause repeated correspondence with the taxpayer</p>	September

(continued)

GAO Order Relating to Audit Assignments Involving Access to Tax Information

GAO FORM - 379 (Aug. 72)
United States
General Accounting Office
Operations Manual



Order

0135.1

AUDIT ASSIGNMENTS INVOLVING
ACCESS TO TAX INFORMATION

September 24, 1985

Distribution C, N, R, and S

Initiated by: General Government Division

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- d. GAO Order 2752.1, Adverse Actions.
- e. GAO General Policy Manual, Chapter 6, Access to Records.

f. IRS Publication 1075, Tax Information Security Guidelines, (Rev. 7-83). Publication 1075 may be obtained from the General Government Division's (GGD), Issue Area Coordinator for Tax Policy and Administration.

4. FORMS.

- a. GGD Form 4, Tax Administration Disclosure Control Document
- b. GGD Form 8, Record of Receipt
- c. GAO Form 100A, Assignment Authorization/Continuation Sheet
- d. GAO Form 319, Action Routing Slip
- e. GAO Form 393, Routing and Control Record

5. DEFINITIONS.

a. The term "tax information" means returns, return information, and taxpayer return information as defined in 26 U.S.C. 6103(b), including information provided to IRS by foreign governments under the exchange of information articles of tax treaties. (See appendix 1 for statutory definition of "return," "return information," and "taxpayer return information.")

b. The term "program division" refers to any headquarters division that initiates an assignment involving access to tax information.

6. DELEGATION OF AUTHORITY. In accordance with 31 U.S.C. 713(b)(2), the Comptroller General designates in writing every 6 months the GAO employees who are to have access to tax information. Authority is hereby delegated to the Director, GGD, to make interim designations in writing, as necessary in connection with any assignment. The authority to make interim designations is re delegated to the Associate Director for Tax Policy and Administration, GGD.

7. GAO'S ACCESS TO TAX INFORMATION. Whether and how GAO has access to tax information on a given audit assignment is dictated by the source or initiator of the work being done. In this regard, audit assignments are divided into two broad categories: (a) assignments initiated at the request of tax writing committees or other congressional committees with access authority and performed with GAO employees as their designated agents and (b) self-initiated assignments and request assignments not covered by (a). Furthermore, under either (a) or (b), GAO may have access to information provided to IRS by foreign governments under tax treaties, if those treaties specifically allow GAO such access. GAO's access authority under each category is subject to certain limitations and procedures that are set forth in the succeeding paragraphs. Refer questions concerning GAO's accessibility to tax information for a particular assignment to GGD's Issue Area Coordinator for Tax Policy and Administration.

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8. INITIATING ASSIGNMENTS REQUIRING ACCESS TO TAX INFORMATION. There are varying notification procedures that must be carried out before GAO can obtain access to tax information. The procedures differ for (1) assignments conducted as duly designated agents of tax writing committees or other congressional committees authorized access to tax information by a congressional resolution and (2) self-initiated assignments and request assignments not covered by (1). The procedures also differ depending on the agencies involved in the assignment. The Associate Director for Tax Policy and Administration, GGD, is responsible for coordinating the initiation of all assignments for which access to tax information is required. The notification letters required to initiate an audit must be processed through the Associate Director or his/her designee. The general policies and procedures pertaining to notification letters follow. Before preparing any written material, however, the initiating division discusses the proposed assignment with the Associate Director for Tax Policy and Administration. (See appendix 3 for detailed information on the notification procedures.)

a. Self-Initiated Assignments and Requests from Members of Congress and from Committees Not Authorized Access to Tax Information.

(1) Joint Committee Letter. The Joint Committee on Taxation must be notified by the Comptroller General of each such assignment and given 30 days to evaluate GAO's need for access to tax information. The joint committee can disapprove that access by a vote of two-thirds of its members within the 30-day period. 26 U.S.C. 6103(1)(7)(c).

(a) At least 90 days before access to tax information is required, the program division prepares (1) a draft letter notifying the Joint Committee on Taxation of the assignment and (2) a tentative assignment justification (GAO Form 100A). Cite in the notification letter GAO's audit and access authority, describe the assignment's objective and scope, state GAO's need for access to tax information, and illustrate that need by briefly describing how tax information will be used in meeting the assignment objectives. If the assignment is of the nature described in paragraphs 7a(2) or (3), also state in the letter that in using tax information and in formulating recommendations, GAO will consider any potential impact on tax administration and taxpayer confidentiality. If the assignment is of the nature described in paragraph 7a(3), state in the letter that in evaluating its need for access to tax information, GAO has considered the burdens that such access would impose on IRS. (A sample letter appears in appendix 4.)

(b) The program division forwards the draft notification letter and tentative GAO Form 100A to GGD's Issue Area Coordinator for Tax Policy and Administration. Within 2 weeks, the issue area coordinator reviews those documents and notifies the program division of any suggested changes. Once revised, if necessary, the notification letter, still in draft, is returned to the issue area coordinator for delivery to the staff of the joint committee. It is our practice to send the draft letter to the committee staff before sending it officially to the committee so as to take advantage of the staff's expertise and to identify any aspects of our notification letter that should be clarified. After the letter has been reviewed by the committee staff and revised, if appropriate, the program division forwards it, in final form, to the Associate Director for Tax Policy and Administration along with the draft GAO

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(b) The program division forwards the draft letter to GGD's Issue Area Coordinator for Tax Policy and Administration for processing. The issue area coordinator notifies the program division of any suggested changes. The program division forwards the letter, in final form, to the Associate Director for Tax Policy and Administration for signature. The letter includes, as enclosures, copies of the joint committee letter, the GGD Form 8, and the agency head letter, and is dated one day after the date of the agency head letter. The signed letter and copies are delivered to the recipients identified in appendix 3. An additional letter is needed each time a new location is included in an assignment.

b. Assignments Conducted as Duly Designated Agents of Committees Authorized Access to Tax Information. For these assignments only one letter is required, a letter to the agency from which tax information is to be obtained.

(1) As soon as a request letter is received, the program division must prepare a letter notifying agency officials of the assignment and the need for access to tax information. The letter cites the job code and the anticipated work sites and includes the request letter as an enclosure. Letters to IRS or BATF should refer to the assignment as a study, analysis, or evaluation (rather than a survey or review); state the date that GAO plans to begin the assignment (which must be at least 2 weeks after the date of the letter); and request that appropriate officials be notified of GAO's assignment plans. (A sample letter appears in appendix 8.)

(2) The program division forwards the draft letter to GGD's Issue Area Coordinator for Tax Policy and Administration. The issue area coordinator notifies the program division of any suggested changes.

(3) If the letter is addressed to IRS or BATF, the program division forwards the letter in final form to GGD's Associate Director for Tax Policy and Administration for signature. Otherwise, the program division is responsible for getting the letter signed. The signed letter and copies are delivered to the recipients identified in appendix 3.

9. DESIGNATION OF GAO EMPLOYEES HAVING ACCESS TO TAX INFORMATION. GAO employees are not entitled to possession of, knowledge of, or access to tax information solely by virtue of the office or position held. Rather, access to tax information within GAO is limited to those GAO employees who need to obtain and/or review such information in conjunction with an assignment described under paragraph 7 and have been designated in writing by the Comptroller General or his designee as having access to such information. These written designations are made before the start of assignments and at certain specified intervals and are not effective until they have been distributed to the appropriate congressional committees and agencies. The designations must include any GAO employee who will need access to the tax information, including administrative staff, attorneys, and other office personnel. In this regard, consultants can be included on designation lists and thus authorized access to tax information only if they are classified as special government employees under title 5 of the U.S. Code; they can not be included if they are classified as independent contractors. GAO's policies and procedures for preparing and distributing written designations follow.

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(2) The associate director delivers certified copies of the initial and updated lists to (a) the committee for which GAO is acting as an agent, (b) IRS or BATF, if appropriate, and (c) the program division responsible for the assignment. The program division delivers copies of the lists to agencies other than IRS and BATF who will provide tax information as part of the assignment.

d. Program Division Responsibilities.

(1) For self-initiated assignments and assignments undertaken as agents of the Joint Committee on Taxation, program division directors must advise GGD's Issue Area Coordinator for Tax Policy and Administration, by the 15th of each month, of the employees who are to be added to or deleted from the prior month's designation list. For assignments undertaken as an agent of the House Committee on Ways and Means or the Senate Committee on Finance, program division directors must advise the issue area coordinator, as soon as possible, of changes that are needed to the designation list. For all assignments, directors should provide the full name and title of the employee, the assignment code, and, if applicable, the name of the committee for which the employee is to act as an agent. This information is needed for all headquarters, region, and staff office professional and administrative employees who are to be assigned to or released from assignments requiring access to tax information.

(2) Program divisions are responsible for assuring delivery of certified copies of the lists to agencies, other than IRS and BATF, that are to provide tax information.

(3) Program divisions are responsible also for assuring that tax information is obtained and/or reviewed by only those employees who have been designated by the Comptroller General or his designee as having access to such information.

10. RESTRICTIONS ON DISCLOSING TAX INFORMATION. The confidentiality of tax information is closely protected by U.S. statutes. Unless specifically authorized, government employees, including those of GAO, are expressly prohibited from disclosing tax information. There are severe criminal and civil penalties for making unauthorized disclosures. GAO employees are responsible for protecting the confidentiality of tax information and for preventing unauthorized disclosures.

a. Authorized Disclosures. GAO employees are expressly prohibited by statute from disclosing tax information in a form that can be associated with, or otherwise identify, either directly or indirectly, a particular taxpayer except as provided below. 26 U.S.C. 6103(i)(7)(A); 31 U.S.C. 713(b)(3).

(1) Within GAO, tax information may only be disclosed to employees who (a) by virtue of their involvement in an assignment, have a need to examine such information and (b) have been designated as having access to the information under the procedures set forth under paragraph 9.

(2) Outside of GAO, tax information may be disclosed only to the Joint Committee on Taxation, the Senate Committee on Finance, or the House Committee on Ways and Means, but only when GAO is acting as a duly designated agent of one of those committees and when the committee for which GAO is an agent is sitting

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(c) On the last day of every month, the GAO staff at each work location must forward a copy of the GGD Form 4 showing the month's postings to the Associate Director for Tax Policy and Administration, GGD, or to his designee. If no disclosures were made during the month, a GGD Form 4 must be forwarded reflecting that fact. If the agency disclosure officer at a particular location requests a copy of the month's postings, it should be provided.

(d) The GAO staff at each work location maintains the original GGD Form 4s and copies of the agency's disclosure forms or other supporting records in a separate folder at each work location until the audit work is completed. At that time, the folder is sent to the Associate Director for Tax Policy and Administration, GGD, or to his designee.

(2) Tax Information Disclosed by GAO. As discussed under paragraph 10a(2), any requests for access to tax information made to GAO must be referred to the Associate Director for Tax Policy and Administration, GGD, who is responsible for responding to and accounting for such requests.

b. Controlling Access to Tax Information. GAO employees are responsible for controlling access to tax information in their possession. Program division directors are responsible for ensuring that all GAO employees on assignments within their areas of responsibility are familiar with the appropriate agency standards regarding the safeguarding of tax information and the policies and procedures set forth in this order. Any employee who has knowledge of the loss or possible compromise of any tax information must promptly report the circumstances to the Associate Director for Tax Policy and Administration, GGD, who will take appropriate action.

c. Physical Control Over Tax Information. GAO employees are responsible for maintaining physical control over the tax information in their possession. The tax information must be controlled in a manner that is consistent with the security standards set forth in IRS' Publication 1075, Tax Information Security Guidelines, any additional standards established by the agency that provided the information to GAO, and the policies and procedures set forth in this order. Program division directors are responsible for ensuring that all GAO employees on assignments within their areas of responsibility are familiar with all appropriate physical security standards. For example:

(1) All workpapers and workpaper bundles containing tax information must be marked "access limited to GAO personnel designated for this assignment."

(2) Computer files containing tax return information must be protected against disclosure to unauthorized personnel when being processed at non-IRS computer facilities. The following safeguards must be adhered to:

(a) All magnetic media, files, reports, and related items must remain under the direct control of an authorized GAO employee before, during, and after processing.

(b) Tax information must not be left in the computer memory at the end of processing. While tax data is resident in memory, access must be limited to authorized applications.

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and reporting the results to the head of the division or office involved and to the Associate Director for Tax Policy and Administration, GGD. The inspection records are available for IRS' review upon request.

(3) The Associate Director for Tax Policy and Administration, GGD, is responsible for summarizing the inspection results for inclusion in the annual Safeguard Activity Report to IRS as required by 26 U.S.C. 6103(p)(4)(E). That report is also to include (a) information on significant changes in safeguard procedures or authorized access to tax information during the year and any changes or enhancements to physical and computer security measures used to safeguard tax information and (b) the identity of tax information disposed of during the year and the date and manner of destruction. By December 31 of each year, program divisions should forward any information concerning the above to the Associate Director for Tax Policy and Administration for inclusion in the annual report.

e. General.

(1) The Comptroller General and all GAO employees will cooperate with the Commissioner of Internal Revenue and the heads of other federal agencies in implementing any additional controls or safeguards deemed necessary by the Secretary of the Treasury to safeguard the confidentiality of tax information in GAO's possession. 26 U.S.C. 6103(p)(4)(D).

(2) Program division directors refer any additional safeguard procedures recommended by the Commissioner of Internal Revenue or the heads of other federal agencies for use within GAO to the Associate Director for Tax Policy and Administration, GGD, for review and approval.

12. BACKGROUND INVESTIGATIONS AND OUTSIDE EMPLOYMENT. To be consistent with IRS' requirements for its own internal auditors, it is GAO's policy that any employee having access to tax information be subject to the favorable completion of a background investigation. It is GAO's policy also that employees assigned to jobs involving access to tax information not engage in outside employment involving the preparation of tax returns.

13. ACCEPTANCE OF SPECIFIC TAXPAYERS' NAMES FROM CONGRESS. In accordance with GAO's policy, GAO audits of IRS' administration of the tax laws is normally based on a random sampling from appropriate universes of tax information rather than on a review of information for preselected taxpayers. The circumstances and procedures under which GAO will accept from the Congress names of specific taxpayers are set forth in appendix 10.

14. NOTIFICATION OF COMPLETION OF CERTAIN ASSIGNMENTS. When GAO completes an assignment of the nature described in paragraphs 7a(2) or (3), the Joint Committee on Taxation must be notified within 90 days. 26 U.S.C. 6103(i)(7)(B)(iii). In that regard, the program division, within 30 days after completion of an assignment, prepares a letter to describe (a) the federal agency's use of the tax information, (b) GAO's recommendations with respect to the federal agency's use of tax information, and (c) the impact of GAO's recommendations on the confidentiality of tax information and on the administration of the tax laws. The division forwards the notification letter, in final form with an action routing slip, through the Associate Director for Tax Policy and

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APPENDIX 1. DEFINITIONS OF "RETURN," "RETURN INFORMATION," AND "TAXPAYER RETURN INFORMATION" LOCATED IN 26 U.S.C. 6103(b)

1. **RETURN.** The term "return" means any tax or information return, declaration of estimated tax, or claim for refund required by, or provided for or permitted under, the provisions of this title which is filed with the Secretary by, on behalf of, or with respect to any person, and any amendment or supplement thereto, including supporting schedules, attachments, or lists which are supplemental to, or part of, the return so filed.

2. **RETURN INFORMATION.** The term "return information" means

a. a taxpayer's identity, the nature, source, or amount of his income, payments, receipts, deductions, exemptions, credits, assets, liabilities, net worth, tax liability, tax withheld, deficiencies, overassessments, or tax payments, whether the taxpayer's return was, is being, or will be examined or subject to other investigation or processing, or any other data, received by, recorded by, prepared by, furnished to, or collected by the Secretary with respect to a return or with respect to the determination of the existence, or possible existence, of liability (or the amount thereof) of any person under this title for any tax, penalty, interest, fine, forfeiture, or other imposition, or offense, and

b. any part of any written determination or any background file document relating to such written determination (as such terms are defined in section 6110(b)) which is not open to public inspection under section 6110.

But such term does not include data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer. Nothing in the preceding sentence, or in any other provision of law, shall be construed to require the disclosure of standards used or to be used for the selection of returns for examination, or data used or to be used for determining such standards, if the Secretary determines that such disclosure will seriously impair assessment, collection, or enforcement under the internal revenue laws.

3. **TAXPAYER RETURN INFORMATION.** The term "taxpayer return information" means return information as defined in paragraph (2) which is filed with, or furnished to, the Secretary by or on behalf of the taxpayer to whom such return information relates.

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<u>AGENCY</u>	<u>PROGRAM OR ACTIVITY</u>	<u>TYPE OF TAX INFORMATION</u>
Federal, state, and local child support enforcement agencies	Establishment and collection of child support obligations	Information from returns related to income and dependents
Federal, state, and local agencies that administer the Food Stamp Program	Determination of eligibility for, or the correct amount of, benefits under the Food Stamp Program	Information from returns with respect to wages, retirement and self-employment income, and Information from returns with respect to unearned income
Federal, state, and local agencies which administer the Aid to Families with Dependent Children Program	Determination of eligibility for, or the correct amount of, benefits under the Aid to Families with Dependent Children Program	Information from returns with respect to wages, retirement and self-employment income, and Information from returns with respect to unearned income
Federal, state, and local agencies that administer the Medicaid Program	Determination of eligibility for, or the correct amount of, benefits under the Medicaid Program	Information from returns with respect to wages, retirement and self-employment income, and Information from returns with respect to unearned income
Federal, state and local agencies that administer the Supplemental Security Income Program	Determination of eligibility for, or the correct amount of, benefits under the Supplemental Security Income Program	Information from returns with respect to wages, retirement and self-employment income, and Information from returns with respect to unearned income
Federal, state, and local agencies that administer assistance programs in the territories	Determination of eligibility for, or the correct amount of, benefits under assistance programs in the territories	Information from returns with respect to wages, retirement and self-employment income, and Information from returns with respect to unearned income

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26 U.S.C. 6103(1) and (u)

(1) Disclosure of Returns and Return Information for Purposes Other Than Tax Administration.—

(1) Disclosure of certain returns and return information to Social Security Administration and Railroad Retirement Board.—The Secretary may, upon written request, disclose returns and return information with respect to—

(A) taxes imposed by chapters 2, 21, and 24, to the Social Security Administration for purposes of its administration of the Social Security Act;

(B) a plan to which part I of subchapter D of chapter 1 applies, to the Social Security Administration for purposes of carrying out its responsibility under section 1131 of the Social Security Act, limited, however to return information described in section 6057(d); and

(C) taxes imposed by chapter 22, to the Railroad Retirement Board for purposes of its administration of the Railroad Retirement Act.

(2) Disclosure of returns and return information to the Department of Labor and Pension Benefit Guaranty Corporation.—The Secretary may, upon written request, furnish returns and return information to the proper officers and employees of the Department of Labor and the Pension Benefit Guaranty Corporation for purposes of, but only to the extent necessary in, the administration of titles I and IV of the Employee Retirement Income Security Act of 1974.

(3) Disclosure that applicant for federal loan has tax delinquent account.—

(A) In general.—Upon written request, the Secretary may disclose to the head of the Federal agency administering any included Federal loan program whether or not an applicant for a loan under such program has a tax delinquent account.

(B) Restriction on disclosure.—Any disclosure under subparagraph (A) shall be made only for the purpose of, and to the extent necessary in, determining the creditworthiness of the applicant for the loan in question.

(C) Included federal loan program defined.—For purposes of this paragraph, the term "included Federal loan program" means any program—

(i) under which the United States or a Federal agency makes, guarantees, or insures loans, and

(ii) with respect to which there is in effect a determination by the Director of the Office of Management and Budget (which has been published in the Federal Register) that the application of this paragraph to such program will substantially prevent or reduce future delinquencies under such program.

(4) Disclosure of returns and return information for use in personnel or claimant representative matters.—The Secretary may disclose returns and return information—

(A) upon written request—

(i) to an employee or former employee of the Department of the Treasury, or to the duly authorized legal representative of such employee or former employee, who is or may be a party to any administrative action or proceeding affecting the personnel rights of such employee or former employee; or

(ii) to any person, or to the duly authorized legal representative of such person, whose rights are or may be affected by an administrative action or proceeding under section 330 of title 31, United States Code, solely for use in the action or proceeding, or in preparation for the action or proceeding, but only to the extent that the Secretary determines that such returns or return information is or may be relevant and material to the action or proceeding; or

(B) to officers and employees of the Department of the Treasury for use in any action or proceeding described in subparagraph (A), or in preparation for such action or proceeding, to the extent necessary to advance or protect the interests of the United States.

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- (i) aid to families with dependent children provided under a State plan approved under part A of title IV of the Social Security Act;
- (ii) medical assistance provided under a State plan approved under title XIX of the Social Security Act;
- (iii) supplemental security income benefits provided under title XVI of the Social Security Act, and federally administered supplementary payments of the type described in section 1616(a) of such Act (including payments pursuant to an agreement entered into under section 212(a) of Public Law 93-66);
- (iv) any benefits provided under a State plan approved under title I, X, XIV, or XVI of the Social Security Act (as those titles apply to Puerto Rico, Guam, and the Virgin Islands);
- (v) unemployment compensation provided under a State law described in section 3304 of this Code;
- (vi) assistance provided under the Food Stamp Act of 1977, and
- (vii) State-administered supplementary payments of the type described in section 1616(a) of the Social Security Act (including payments pursuant to an agreement entered into under section 212(a) of Public Law 93-66)

(8) Disclosure of certain return information by social security administration to state and local child support enforcement agencies.—

(A) In general.—Upon written request, the Commissioner of Social Security shall disclose directly to officers and employees of a State or local child support enforcement agency return information from returns with respect to social security account numbers, net earnings from self-employment (as defined in section 1402), wages (as defined in section 3121(a) or 3401(a)), and payments of retirement income which have been disclosed to the Social Security Administration as provided by paragraph (1) or (5) of this subsection.

(B) Restriction on disclosure.—The Commissioner of Social Security shall disclose return information under subparagraph (A) only for purposes of, and to the extent necessary in, establishing and collecting child support obligations from, and locating, individuals owing such obligations. For purposes of the preceding sentence, the term "child support obligations" only includes obligations which are being enforced pursuant to a plan described in section 454 of the Social Security Act which has been approved by the Secretary of Health and Human Services under part D of title IV of such Act.

(C) State or local child support enforcement agency.—For purposes of this paragraph, the term "State or local child support enforcement agency" means any agency of a State or political subdivision thereof operating pursuant to a plan described in subparagraph (b).

(9) Disclosure of alcohol fuel producers to administrators of state alcohol laws.— Notwithstanding any other provision of this section, the Secretary may disclose—

(A) the name and address of any person who is qualified to produce alcohol for fuel use under section 5181 and

(B) the location of any premises to be used by such person in producing alcohol for fuel,

to any State agency, body, or commission, or its legal representative, which is charged under the laws of such State with responsibility for administration of State alcohol laws solely for use in the administration of such laws.

(10) Disclosure of certain information to agencies requesting a reduction under Section 6402(c) or 6402(d).—

(A) Return information from Internal Revenue Service.—The Secretary may, upon receiving a written request, disclose to officers and employees of an agency seeking a reduction under section 6402(c) or 6402(d)—

- (i) the fact that a reduction has been made or has not been made under such subsection with respect to any person;
- (ii) the amount of such reduction, and
- (iii) taxpayer identifying information of the person against whom a reduction was made or not made

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(4) Individuals who have defaulted on student loans.—

(A) In general—Upon written request by the Secretary of Education, the Secretary may disclose the mailing address of any taxpayer who has defaulted on a loan—

(i) made under part B or E of title IV of the Higher Education Act of 1965.

or

(ii) made pursuant to section 3(a)(1) of the Migration and Refugee Assistance Act of 1962 to a student at an institution of higher education.

for use only by officers, employees, or agents of the Department of Education for purposes of locating such taxpayer for purposes of collecting such loan

(B) Disclosure to educational institutions, etc.—

Any mailing address disclosed under subparagraph (A)(i) may be disclosed by the Secretary of Education to—

(i) any lender, or any State or nonprofit guarantee agency, which is participating under part B of title IV of the Higher Education Act of 1965, or

(ii) any educational institution with which the Secretary of Education has an agreement under part E of title IV of such Act.

for use only by officers, employees or agents of such lender, guarantee agency, or institution whose duties relate to the collection of student loans for purposes of locating individuals who have defaulted on student loans made under such loan programs for purposes of collecting such loans

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REQUIRED
 NOTIFICATION
 LETTERS

ADDRESSEE

SIGNER

PROCEDURES

2. Agency memo Assignments for which tax information is to be obtained from IRS letter.

Commissioner of
 Internal Revenue.

Comptroller
 General.

Program division prepares draft letter and sends it to GGD's Issue Area Coordinator for Tax Policy and Administration within 15 days of the date of the Joint Committee on Taxation letter.

Issue area coordinator discusses suggested changes with the program division.

Program division finalizes letter and forwards it with an action routing slip through the Associate Director for Tax Policy and Administration, GGD, to the Comptroller General for signature.

GGD's Issue Area Coordinator for Tax Policy and Administration delivers the letter, with copies of the joint committee letter and the GGD Form 8 enclosed, to the addressee.

Copies of the letter and enclosures are provided to
 --the program division;
 --the Associate Director for Tax Policy and Administration, GGD; and
 --GGD's Issue Area Coordinator for Tax Policy and Administration (2 copies).

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SIGNER

PROCEDURES

Assignments conducted as duly designated agents of
committees authorized access to tax information

1. Agency letter. Assignments for which tax information is to be obtained from IRS

Assistant Commis-
sioner (Inspec-
tion)
Internal Revenue
Service.

GGD's Associate
Director for Tax
Policy and
Administration.

Program division prepares draft letter and
forwards to GGD's Issue Area Coordinator
for Tax Policy and Administration for review.

Issue area coordinator discusses suggested
changes with the program division.

Program division finalizes letter and forwards
it to the Associate Director for Tax Policy
and Administration, GGD, for signature.

GGD's Issue Area Coordinator for Tax Policy and
Administration delivers the letter to the
addressee.

Copies of the letter are provided to

- the program division;
- the Associate Director for Tax Policy and
Administration, GGD; and
- GGD's Issue Area Coordinator for Tax Policy
and Administration (2 copies).

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SIGNER

PROCEDURES

Assignments for which tax information is to be obtained from an agency other than IRS or BATF

As appropriate.

To be determined
 by the responsible
 program division.

Program division prepares draft letter and forwards to GAO's Issue Area Coordinator for Tax Policy and Administration for review.

Issue area coordinator discusses suggested changes with the program division.

Program division finalizes letter, signs it, and delivers it to addressee.

Copies of the letter are provided to
 --the Associate Director for Tax Policy and Administration, GAO, and
 --GAO's Issue Area Coordinator for Tax Policy and Administration (2 copies).

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APPENDIX 5. SAMPLE GAO FORM 319, ACTION ROUTING SLIP

U. S. GENERAL ACCOUNTING OFFICE
 ACTION ROUTING SLIP

B-

NAME	DATE
Associate Director, GGD	
1. (name of Associate Director for Tax Policy and Admin.) Director, GGD	
2. (name)	
3. OCR	
4. Comptroller General Associate Director GGD	
5. (same name as in block 1)	
6.	
7.	
8.	
9.	
10.	

REMARKS

Please call (Associate Director's name) on (telephone number) when letter is signed. He will date it.

GAO FORM 319 (New Apr 64)

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APPENDIX 7. SAMPLES OF AGENCY HEAD LETTERS

The Honorable Roscoe L. Egger, Jr.
Commissioner of Internal Revenue
Department of the Treasury

Dear Mr. Egger:

Pursuant to the authority granted us in 31 U.S.C. 713 and Section 6103 of the Internal Revenue Code, we are conducting a study of the Internal Revenue Service's Office of Chief Counsel. To effectively carry out our work, we will need access to tax returns and return information.

Pursuant to the procedures noted in Section 6103 of the Code, we notified the Joint Committee on Taxation on May 24, 1983 of our intent to initiate this audit. Copies of our letter and the receipt signed by the joint committee are enclosed.

Accordingly, this letter is to formally notify you of our audit and request access to appropriate tax returns and return information. Mr. Norman Stubehofer will be in contact with IRS to work out the arrangements for obtaining the necessary information.

Sincerely yours,

Comptroller General
of the United States

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APPENDIX 8. SAMPLES OF LIAISON LETTERS

Use this letter when assignment is self-initiated or being done at request of a member of Congress or a committee not authorized access to tax information.

Mr. Robert L. Rebein
Assistant Commissioner (Inspection)
Internal Revenue Service

Dear Mr. Rebein:

This letter is to notify you that the Information Management and Technology Division of the General Accounting Office plans to initiate an audit (Job Code 510015) of the computer-based systems supporting IRS' information returns program (IRP). The objectives in this regard are to determine (1) whether the IRP computer-based systems contain sufficient internal controls to ensure accurate and reliable data processing; (2) whether the current IRP computer-based systems and document matching methodology are as efficient and effective as possible or whether alternative computerized methodologies would be more efficient and effective; and (3) the potential impact that the Tax Equity and Fiscal Responsibility Act of 1982 will have on the existing IRP computer-based systems regarding capacity to process additional information returns.

On September 12, 1983, we notified the Chairman, Joint Committee on Taxation, of this audit and stated that to carry out the objectives, it would be necessary for us to obtain tax returns and return information from the Internal Revenue Service. Copies of that letter and the joint committee's signed receipt are enclosed. A copy of the Comptroller General's subsequent notification letter to the Commissioner is also enclosed.

We would like to begin work during the week of October 31, 1983. We plan to visit the National Office; National Computer Center, Martinsburg; North Atlantic Region, Andover Service Center; and Western Region, Fresno Service Center. If we need to expand to additional locations, we will identify those for you at a later date.

We would appreciate your advising appropriate officials of our plans. If you have any questions concerning this job please contact me on 275-6407 or Ted Conter of our Information Management and Technology Division on 275-4797.

Sincerely yours,

Johany C. Finch
Senior Associate Director

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**APPENDIX 10. CONDITIONS UNDER WHICH GAO WILL ACCEPT FROM THE CONGRESS NAMES
OF TAXPAYERS WHEN AUDITING IRS' ADMINISTRATION OF THE TAX LAWS**

1. STATEMENT OF PRINCIPLE.

a. GAO's policy is not to investigate and report on the tax status of specific taxpayers identified for GAO by others. GAO officials articulated this policy in testimony given before a congressional committee considering passage of the bill which became Public Law 95-125 (now codified at 31 U.S.C. 713):

"In performing an audit of IRS, [GAO] would not be concerned with the identity of individual taxpayers, nor . . . would [GAO] impose [its] judgment upon that of IRS in individual tax cases. [GAO] would examine the individual transactions on a sample basis and only for the purpose of evaluating the effectiveness of IRS' operations and activities."

In addition, the legislative history of Public Law 95-125 indicated that

"The purpose of the legislation is to resolve . . . the right of GAO to gain access to records necessary to perform regular audits of the Service. . . .

"[The legislation] scrupulously safeguards the privacy and integrity of income tax returns and information from unauthorized disclosure."
(H.R. Rep. No. 95-480)

b. In accordance with this policy, GAO audits of IRS' administration of the tax laws will normally be based on a random sampling from appropriate universes of tax information rather than on a preselection of individual returns. The circumstances and procedures under which GAO will accept from committees and Members of Congress the names of taxpayers suspected of incorrectly reporting income, expenses, or deductions on their returns are set forth in the guidelines stated in the paragraphs below.

2. WORK DONE UNDER GAO AUTHORITY. When GAO initiates a review pursuant to 31 U.S.C. 713 and section 6103(i)(7) of the Internal Revenue Code, tax information will be obtained by sampling from appropriate universes.

a. Receipt of Names from Tax Writing Committees and Appropriate Oversight Committees or Subcommittees.

(1) If the House Ways and Means Committee, Senate Finance Committee, Joint Committee on Taxation, or committees or subcommittees having a jurisdictional interest in the administration of the tax laws have knowledge of possible incorrect reporting of income, expenses, or deductions on returns by specific taxpayers and want to provide the names of such taxpayers to GAO for audit purposes, GAO will first suggest that they give the information directly to the Internal Revenue Service. If these committees still want to give the taxpayers'

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APPENDIX 11. SAMPLE FORMATS FOR ANNUAL REPORT

1. Sample format for open recommendations to the Congress.

SELF-EMPLOYMENT INCOME REPORTED
FOR CREDIT TOWARD SOCIAL SECURITY
BENEFITS ALTHOUGH TAX NOT PAID

B-137762
8-9-73
and
GGD-77-78
8-8-77

Summary of finding

IRS reports to the Social Security Administration the amount self-employed persons designate on their income tax returns as self-employment income even though such persons may not have paid the applicable self-employment social security tax. The self-employed person thus receives credit toward social security benefits even if that person has not made the required contribution.

Recommendation

We recommended that the Congress amend section 205(c) of the Social Security Act (42 U.S.C. 405(c)) to prohibit a person from receiving credits toward social security benefits if that person has not paid the required tax on self-employed income.

Action taken and/or pending

During the 95th Congress, the Chairman of the Ways and Means Oversight Subcommittee introduced H.R. 12565, the "Self-Employment Tax Payments Act of 1978," which contained the substance of our recommendation. However, no action was taken on the bill.

In 1979 the Chairman of the Ways and Means Oversight Subcommittee reintroduced the bill which was renumbered as H.R. 5465 and was referred to the Subcommittee on Social Security. The subcommittee did not take action on the bill during the 96th Congress. No further action has been taken.

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3. Sample format for recommendations made to the heads of federal agencies concerning the administration of taxes and/or the use of tax information.

IRS HAS NOT REVIEWED THE FINANCIAL
SOUNDNESS OF THE TEAMSTERS' CENTRAL
STATES PENSION FUND

HRD-82-13
8-199238
4-28-82

Summary of finding

ERISA requires that employee pension plans satisfy minimum funding standards each year and that each plan submit an annual report and actuarial data to enforce ERISA's minimum funding standards.

Since 1975, the trustees of the Teamsters' Central States Southeast and Southwest Areas Pension Fund have had five actuarial valuations of the fund's financial soundness. The last report, issued on April 3, 1981, stated that the current funding should satisfy ERISA's requirements and that the fund is operating on a sound financial basis. However, the actuary's report described some problems and situations that could have serious financial implications for the fund. Consequently, the actuary recommended that until the effects of deregulation on the trucking industry and the Multi-Employer Amendments Act of 1980 can be evaluated, the fund should adopt a conservative posture with respect to any liberalizing of benefits. Moreover, the actuary's April 1981 report showed that the fund's unfunded accrued liability for current and future pension benefits was about \$6.05 billion at January 1, 1980. In this regard, IRS needs to closely monitor the financial status of the fund to assure that it, in fact, meets ERISA's funding standards.

Recommendation

We recommended that the Commissioner of Internal Revenue direct IRS officials to closely monitor the fund's financial operations to ascertain that the fund meets the minimum funding standards of ERISA and, if not, take whatever action is needed to assure that the fund meets the act's requirements.

Action taken and/or pending

IRS stated that the fund's July 1982 annual report would be thoroughly examined to ensure compliance with the minimum funding standards.

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5. Sample format for testimony on tax matters given by GAO officials during the year.

TESTIMONY ON TAX MATTERS
GIVEN BY GAO OFFICIALS DURING 1982

<u>GAO Official</u>	<u>Congressional Committee</u>	<u>Subject Matter</u>	<u>Date</u>
William J. Anderson, Director, General Government Division	Subcommittee on Commerce, Consumer and Monetary Affairs, House Committee on Government Operations	Adequacy of IRS' Resources	3/17/82
Morton A. Myers, Director, Program Analysis Division	Senate Finance Committee	Taxation of In- surance Companies	3/18/82
William J. Anderson, Director, General Government Division	Subcommittee on Oversight of the Internal Revenue Service, Senate Finance Committee	Senate Bill 2198, Taxpayer Compliance Improvement Act of 1982	3/22/82
William J. Anderson, Director, General Government Division	Subcommittee on Oversight of Government Management, Senate Committee on Governmental Affairs	Status of IRS' Taxpayer Service Program	3/24/82
Daniel F. Stanton, Deputy Director, General Government Division	Subcommittee on Oversight of the Internal Revenue Service, Senate Committee on Finance	Senate Bill 2369, Independent Contractor Tax Classification and Compliance Act of 1982	4/26/82
William J. Anderson, Director, General Government Division	Subcommittee on Oversight, House Committee on Ways and Means	IRS Policies and Procedures to Safeguard Taxpayer Rights and the Effects of Certain Provisions of the 1976 Tax Reform Act	4/26/82

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APPENDIX 12. 31 U.S.C. 713, 719(d)

AUTHORITY TO AUDIT IRS (31 U.S.C. 713)

(a) Under regulations of the Comptroller General, the Comptroller General shall audit the Internal Revenue Service and the Bureau of Alcohol, Tobacco, and Firearms, of the Department of the Treasury. An audit under this section does not affect a final decision of the Secretary of the Treasury under section 6406 of the Internal Revenue Code of 1954 (26 U.S.C. 6406).

(b)(1) To carry out this section and to the extent provided by and only subject to section 6103 of the Internal Revenue Code of 1954 (26 U.S.C. 6103)—

(A) returns and return information (as defined in section 6103(b) of the Internal Revenue Code of 1954 (26 U.S.C. 6103(b))) shall be made available to the Comptroller General; and

(B) records and property of, or used by, the Service or the Bureau, shall be made available to the Comptroller General.

(2) At least once every 6 months, the Comptroller General shall designate each officer and employee of the General Accounting Office by name and title to whom returns, return information, or records or property of the Service or the Bureau that can identify a particular taxpayer may be made available. Each designation or a certified copy of the designation shall be sent to the Committee on Finance of the Senate, the Committee on Ways and Means of the House of Representatives, the Committee on Governmental Affairs of the Senate, the Committee on Government Operations of the House, the Joint Committee on Taxation, the Commissioner of Internal Revenue, and the Director of the Bureau.

(3) Except as expressly provided by law, an officer or employee of the Office may make known information derived from a record or property of, or in use by, the Service or the Bureau that can identify a particular taxpayer only to another officer or employee of the Office whose duties or powers require that the record or property be made known.

ANNUAL REPORT TO CONGRESSIONAL COMMITTEES (31 U.S.C. 719(d))

(d) The Comptroller General shall report each year to the Committees on Finance and Governmental Affairs of the Senate, the Committees on Ways and Means and Government Operations of the House of Representatives, and the Joint Committee on Taxation. Each report shall include—

(1) procedures and requirements the Comptroller General, the Commissioner of Internal Revenue, and the Director of the Bureau of Alcohol, Tobacco, and Firearms, prescribe to protect the confidentiality of returns and return information made available to the Comptroller General under section 713(b)(1) of this title;

(2) the scope and subject matter of audits under section 713 of this title; and

(3) findings, conclusions, or recommendations the Comptroller General develops as a result of an audit under section 713 of this title, including significant evidence of inefficiency or mismanagement.

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APPENDIX 14. PROCEDURES AND RECORDKEEPING TO SAFEGUARD
TAX INFORMATION IN 26 U.S.C. 6103(p)(1)
THROUGH (p)(6)

(p) Procedure and Recordkeeping.—

(1) Manner, time, and place of inspections.—Requests for the inspection or disclosure of a return or return information and such inspection or disclosure shall be made in such manner and at such time and place as shall be prescribed by the Secretary

(2) Procedure.—

(A) Reproduction of returns.—A reproduction or certified reproduction of a return shall, upon written request, be furnished to any person to whom disclosure or inspection of such return is authorized under this section. A reasonable fee may be prescribed for furnishing such reproduction or certified reproduction.

(B) Disclosure of return information.—Return information disclosed to any person under the provisions of this title may be provided in the form of written documents, reproductions of such documents, films or photoimpressions, or electronically produced tapes, disks, or records, or by any other mode or means which the Secretary determines necessary or appropriate. A reasonable fee may be prescribed for furnishing such return information.

(C) Use of reproductions.—Any reproduction of any return, document, or other matter made in accordance with this paragraph shall have the same legal status as the original, and any such reproduction shall, if properly authenticated, be admissible in evidence in any judicial or administrative proceeding as if it were the original, whether or not the original is in existence.

(3) Records of inspection and disclosure.—

(A) System of recordkeeping.—Except as otherwise provided by this paragraph, the Secretary shall maintain a permanent system of standardized records or accountings of all requests for inspection or disclosure of returns and return information (including the reasons for and dates of such requests) and of returns and return information inspected or disclosed under this section. Notwithstanding the provisions of section 552a(c) of title 5, United States Code, the Secretary shall not be required to maintain a record or accounting of requests for inspection or disclosure of returns and return information, or of returns and return information inspected or disclosed, under the authority of subsections (c), (e), (h)(1), (3)(A), or (4), (i)(4) or (7)(A)(ii), (k)(1), (2), or (6), (1)(1), (4)(B), (5), (7), (8), (9), (10), or (11), (m) or (n). The records or accountings required to be maintained under this paragraph shall be available for examination by the Joint Committee on Taxation or the Chief of Staff of such joint committee. Such record or accounting shall also be available for examination by such person or persons as may be, but only to the extent, authorized to make such examination under section 552a(c)(3) of title 5, United States Code.

(B) Report by the Secretary.—The Secretary shall, within 90 days after the close of each calendar year, furnish to the Joint Committee on Taxation a report with respect to, or summary of, the records or accountings described in subparagraph (A) in such form and containing such information as such joint committee or the Chief of Staff of such joint committee may designate. Such report or summary shall not, however, include a record or accounting of any request by the President under subsection (g) for, or the disclosure in response to such request of, any return or return information with respect to any individual who, at the time of such request, was an officer or employee of the executive branch of the Federal Government. Such report or summary, or any part thereof, may be disclosed by such joint committee to such persons and for such purposes as the joint committee may, by record vote of a majority of the members of the joint committee, determine.

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(5) **Report on procedures and safeguards.**—After the close of each calendar quarter, the Secretary shall furnish to each committee described in subsection (f)(1) a report which describes the procedures and safeguards established and utilized by such agencies, bodies, or commissions and the General Accounting Office for ensuring the confidentiality of returns and return information as required by this subsection. Such report shall also describe instances of deficiencies in, and failure to establish or utilize, such procedures.

(6) **Audit of procedures and safeguards.**—

(A) **Audit by Comptroller General.**—The Comptroller General may audit the procedures and safeguards established by such agencies, bodies, or commissions pursuant to this subsection to determine whether such safeguards and procedures meet the requirements of this subsection and ensure the confidentiality of returns and return information. The Comptroller General shall notify the Secretary before any such audit is conducted.

(B) **Records of inspection and reports by the Comptroller General.**—The Comptroller General shall—

(i) maintain a permanent system of standardized records and accounting of returns and return information inspected by officers and employees of the General Accounting Office under subsection (i)(7)(A)(ii) and shall, within 90 days after the close of each calendar year, furnish to the Secretary a report with respect to, or summary of, such records or accountings in such form and containing such information as the Secretary may prescribe; and

(ii) furnish an annual report to each committee described in subsection (f) and to the Secretary setting forth his findings with respect to any audit conducted pursuant to subparagraph (A).

The Secretary may disclose to the Joint Committee any report furnished to him under clause (i).

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(C) Public report on disclosures.—The Secretary shall, within 90 days after the close of each calendar year, furnish to the Joint Committee on Taxation for disclosure to the public a report with respect to the records or accountings described in subparagraph (A) which—

(i) provides with respect to each Federal agency, each agency, body, or commission described in subsection (d), (j)(3)(B)(i), or (l)(6), and the General Accounting Office the number of—

(I) requests for disclosure of returns and return information,

(II) instances in which returns and return information were disclosed pursuant to such requests or otherwise,

(III) taxpayers whose returns, or return information with respect to whom, were disclosed pursuant to such requests, and

(ii) describes the general purposes for which such requests were made.

(4) Safeguards.—Any Federal agency described in subsection (h)(2), (h)(6), (j)(1), (2), (3), or (5), (j)(1) or (2), (l)(1), (2), (3), (5), (10), or (11) or (a)(1), the General Accounting Office, or any agency, body, or commission described in subsection (d), (j)(3)(B)(i), or (l)(6), (7), (8), or (9) shall, as a condition for receiving returns or return information—

(A) establish and maintain, to the satisfaction of the Secretary, a permanent system of standardized records with respect to any request, the reason for such request, and the date of such request made by or of it and any disclosure of return or return information made by or to it,

(B) establish and maintain, to the satisfaction of the Secretary, a secure area or place in which such returns or return information shall be stored;

(C) restrict, to the satisfaction of the Secretary, access to the returns or return information only to persons whose duties or responsibilities require access and to whom disclosure may be made under the provisions of this title;

(D) provide such other safeguards which the Secretary determines (and which he prescribes in regulations) to be necessary or appropriate to protect the confidentiality of the returns or return information;

(E) furnish a report to the Secretary, at such time and containing such information as the Secretary may prescribe, which describes the procedures established and utilized by such agency, body, or commission or the General Accounting Office for ensuring the confidentiality of returns and return information required by this paragraph; and

(F) upon completion of use of such returns or return information—

(i) in the case of an agency, body, or commission described in subsection (d), (j)(3)(B)(i), or (l)(6), (7), (8), or (9) return to the Secretary such returns or return information (along with any copies made therefrom) or make such returns or return information undisclosable in any manner and furnish a written report to the Secretary describing such manner; and

(ii) in the case of an agency described in subsections (h)(2), (h)(6), (j)(1), (2), (3), or (5), (j)(1) or (2), (l)(1), (2), (3), (5), (10), or (11) or (a)(1), or the General Accounting Office, either—

(I) return to the Secretary such returns or return information (along with any copies made therefrom),

(II) otherwise made such returns or return information undisclosable, or

(III) to the extent not so returned or made undisclosable, ensure that the conditions of subparagraphs (A), (B), (C), (D), and (E) of this paragraph continue to be met with respect to such returns or return information.

except that the conditions of subparagraphs (A), (B), (C), (D), and (E) shall cease to apply with respect to any return or return information if, and to the extent that, such return or return information is disclosed in the course of any judicial or administrative proceeding and made a part of the public record thereof. If the Secretary determines that any such agency, body, or commission or the General Accounting Office has failed to, or does not, meet the requirements of this paragraph, he may, after any proceedings for review established under paragraph (7), take such actions as are necessary to ensure such requirements are met, including refusing to disclose returns or return information to such agency, body, or commission or the General Accounting Office until he determines that such requirements have been or will be met. In the case of any agency which receives any mailing address under subsection (m)(2) or (4) and which discloses any such mailing address to any agent, this paragraph shall apply to such agency and each such agent (except that, in the case of an agent, any report to the Secretary or other action with respect to the Secretary shall be made or taken through such agent).

5(1)

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APPENDIX 13. GAO ACCESS TO TAX INFORMATION AUTHORIZED
IN 26 U.S.C. 6103(1)(7)

(A) Comptroller General.--

(A) Returns available for inspection --Except as provided in subparagraph (C), upon written request by the Comptroller General of the United States, returns and return information shall be open to inspection by, or disclosure to, officers and employees of the General Accounting Office for the purpose of, and to the extent necessary in, making--

- (i) an audit of the Internal Revenue Service or the Bureau of Alcohol, Tobacco and Firearms which may be required by section 713 of title 31, United States Code, or
- (ii) any audit authorized by subsection (p)(6),

except that no such officer or employee shall, except to the extent authorized by subsection (f) or (p)(6), disclose to any person, other than another officer or employee of such office whose official duties require such disclosure, any return or return information described in section 4424(a) in a form which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer, nor shall such officer or employee disclose any other return or return information, except as otherwise expressly provided by law, to any person other than such officer or employee of such office in a form which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.

(B) Audits of other agencies --

(i) In general --Nothing in this section shall prohibit any return or return information obtained under this title by any Federal agency (other than an agency referred to in subparagraph (A)) for use in any program or activity from being open to inspection by, or disclosure to, officers and employees of the General Accounting Office if such inspection or disclosure is--

(I) for purposes of, and to the extent necessary in, making an audit authorized by law of such program or activity, and

(II) pursuant to a written request by the Comptroller General of the United States to the head of such Federal agency

(ii) Information from secretary --If the Comptroller General of the United States determines that the returns or return information available under clause (i) are not sufficient for purposes of making an audit of any program or activity of a Federal agency (other than an agency referred to in subparagraph (A)), upon written request by the Comptroller General to the Secretary, returns and return information (of the type authorized by subsection (l) or (m) to be made available to the Federal agency for use in such program or activity) shall be open to inspection by, or disclosure to, officers and employees of the General Accounting Office for the purpose of, and to the extent necessary in, making such audit.

(iii) Requirement of notification upon completion of audit.--Within 90 days after the completion of an audit with respect to which returns or return information were opened to inspection or disclosed under clause (i) or (ii), the Comptroller General of the United States shall notify in writing the Joint Committee on Taxation of such completion. Such notice shall include--

(I) a description of the use of the returns and return information by the Federal agency involved,

(II) such recommendations with respect to the use of returns and return information by such Federal agency as the Comptroller General deems appropriate, and

(III) a statement on the impact of any such recommendations on confidentiality of returns and return information and the administration of this title.

(iv) Certain restrictions made applicable.--The restrictions contained in subparagraph (A) on the disclosure of any returns or return information open to inspection or disclosed under such subparagraph shall also apply to returns and return information open to inspection or disclosed under this subparagraph.

(C) Disapproval by Joint Committee on Taxation.--Returns and return information shall not be open to inspection or disclosed under subparagraph (A) or (B) with respect to an audit --

(i) unless the Comptroller General of the United States notifies in writing the Joint Committee on Taxation of such audit, and

(ii) if the Joint Committee on Taxation disapproves such audit by a vote of at least two-thirds of its members within the 30-day period beginning on the day the Joint Committee on Taxation receives such notice.

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6. Sample format for scope and subject matter of audits requiring access to tax information initiated during the year.

SCOPE AND SUBJECT MATTER OF
JOBS INITIATED DURING 1982
PURSUANT TO 31 U.S.C. 713

<u>Subject matter</u>	<u>Objective/scope</u>	<u>Month started</u>
IRS Taxpayer Assistance	To obtain information on who uses IRS assistance and what assistance the users or taxpayers in general need. To evaluate the resulting data to determine how IRS could use its limited resources more effectively.	January
Multi-Employer Pension Plan Amendments Act of 1980	<p>To assess the impact of the act and its provisions on (1) participants, beneficiaries, employers, employee organizations, and other affected parties, and (2) the self-sufficiency of the insurance fund established to guarantee payment of basic benefits of insolvent multi-employer plans.</p> <p>To address the usability of multi-employer pension plan data maintained by the government.</p> <p>To monitor efforts of IRS, Labor, and Pension Benefit Guaranty Corporation to administer the act.</p> <p>To assess effects of the basic withdrawal liability provisions of the act.</p>	January

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4. Sample format for reports on tax matters.

REPORTS ON TAX MATTERS ISSUED DURING 1982

<u>Title</u>	<u>Date</u>
Legislative and Administrative Changes to Improve Verification of Welfare Recipients' Income and Assets Could Save Hundreds of Millions (HRD-82-9)	1/4/82
Excessive Specifications Are Limiting Competition for IRS Special Design Tax Return Folders (GGD-82-61)	3/24/82
Investigation to Reform Teamsters' Central States Pension Fund Found Inadequate (HRD-82-13)	4/28/82
The Federal Government Can Save \$1.7 Million Annually by Eliminating Strip Stamps (GAO/GGD-82-60)	5/7/82
Uncertainties about the Definition and Scope of the Property Concept May Reduce Windfall Profit Tax Revenues (GAO/GGD-82-48)	5/13/82
Key Issues Affecting State Taxation of Multi-jurisdictional Corporate Income Need Resolving (GAO/GGD-82-38)	7/1/82
Impact of the Paperwork Reduction Act on the Internal Revenue Service's Ability to Administer the Tax Laws (GAO/GGD-82-90)	7/6/82
Compilation of GAO's Work on Tax Administration Activities During 1981 (GAO/GGD-82-82)	7/22/82
Further Research into Noncompliance is Needed to Reduce Growing Tax Losses (GAO/GGD-82-34)	7/23/82
Changes to Appeals Process Could Improve Settlements and Increase Taxpayers' Satisfaction (GAO/GGD-82-54)	7/28/82

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2. Sample format for legislative action taken during the year on recommendations.

DELINQUENT TAXPAYERS DUE REFUNDS
ARE NOT PENALIZED FOR FILING LATE

GGD-79-69
B-137762
7-11-79

Summary of finding

Section 6651(a) of the Internal Revenue Code does not encourage nonfilers due refunds to file on time because they are not penalized for filing late. Late filing penalties are assessed only on nonfilers who owe taxes.

Recommendation

We recommended that the Congress amend section 6651(a) of the Internal Revenue Code to provide for a similar late filing penalty on nonfilers due refunds.

Action taken and/or pending

The Tax Equity and Fiscal Responsibility Act of 1982 adopted our recommendation by providing for a penalty when an income tax return is not filed within 60 days of the due date, whether or not taxes are owed.

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names to GAO, GAO will accept them upon receipt of a letter signed by the chairman of the committee or subcommittee or by the Chief of Staff of the Joint Committee on Taxation.

(2) GAO will not accept taxpayers' names for audit purposes from any other congressional committee or Member. GAO will advise other committees and Members that they should send the names directly to the Internal Revenue Service.

b. General Operating Procedures.

(1) GAO may analyze the tax information provided to it by the tax writing committees or by committees or subcommittees having a jurisdictional interest in the administration of the tax laws to gain a better understanding of the issues involved in an ongoing or planned review GAO might make of the way IRS administers the tax laws.

(2) GAO will not intentionally incorporate any names or information so provided into any samples it draws to carry out its audits of IRS' administration of the tax laws. However, if such names are selected as part of a random sampling of appropriate universes, GAO will analyze the circumstances of that taxpayer in the same way it would for all taxpayers so selected.

(3) GAO will not report or disclose to anyone outside of IRS or GAO the names of taxpayers included in its samples or any information on sampled taxpayers. Nor will GAO advise anyone who gave it taxpayers' names or any information obtained by GAO about those taxpayers.

(4) The disclosure restrictions cited above are consistent with the December 15, 1977, conclusion of the GAO General Counsel that:

" . . . except when we act as agents of a committee or subcommittee pursuant to section 6103(f)(4), we do not believe that section 6103 authorizes us to disclose to a committee or subcommittee of Congress any tax return or any return information obtained during the course of a self-initiated audit of IRS."

3. WORK DONE UNDER COMMITTEE AUTHORITY.

a. When designated by the House Ways and Means Committee, Senate Finance Committee, or Joint Committee on Taxation pursuant to section 6103(f)(4) of the Internal Revenue Code, GAO can accept the names of taxpayers from such committees and report back information on such taxpayers to those committees. GAO can do the same when designated by other committees acting pursuant to an appropriate congressional resolution under the provisions of section 6103(f)(4) of the Internal Revenue Code.

b. However, even in these cases it is GAO policy to encourage the above-mentioned committees to provide the names of specific taxpayers directly to the Internal Revenue Service if there is any suspicion on the committees' part that the taxpayers have incorrectly reported income, expenses, or deductions.

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INSTRUCTIONS FOR GGD FORM 4

GGD FORM 4 INSTRUCTIONS

General Instructions:

GAO is required by 26 U.S.C. 6103(p) to maintain a permanent system of records to account for all disclosures of tax information made to it. To meet this requirement, GGD Form 4s must be completed by each GAO location participating in a job for which GAO was authorized access to tax information. A location should submit its first Form 4 to cover the month in which it started working on the job or the month in which GAO was authorized access to tax information for that job--whichever comes later. For purposes of Form 4 reporting, the date of GAO's access to tax information will be the date the agency is notified of our need for access pursuant to subsection 8(a)(2) or 8(b) of GAO Order 0135.1. A Form 4 should be submitted each month thereafter, even if there have been no disclosures, until a location's participation in the job ceases. Forms are to be prepared by GAO (not agency) location. For example, if a regional office obtains tax information from several agency locations during the month, all of those disclosures should be recorded on one Form 4. The different locations from which the information was received will be identified in block 7.

Specific Instructions:

Blocks 6 through 9 should be completed using information provided on the agency disclosure form, if available. If you believe that an agency has provided GAO with tax information but you have received no disclosure form, you must still record that disclosure on Form 4. Just note in block 5 that a form was "Not Provided" and complete the rest of Form 4 as required. Depending on the circumstances, you may wish to pursue the matter with the agency. If there were no disclosures during the month, complete blocks 1 through 4, write "NONE" across the middle of the form, and complete box 10.

Block 1 Indicate the month and year covered by the report.

Block 2 Provide the job code. Note: If two or more jobs will rely on the same disclosure (use the same sample of returns, for example), the disclosure should be reported on the Form 4 for each job code with appropriate cross reference to the other job(s) for which the disclosure was reported so that the Disclosure Accounting Coordinator will not double count in developing summary data.

Block 3 Provide the name, location, and telephone number of the person submitting the report.

Block 4 Check either box, if appropriate.

Block 5 The agency disclosure forms and the original Form 4s should be maintained in a separate workpaper bundle. The workpaper index should correspond to the workpaper on which the relevant agency disclosure form is mounted. Because disclosure forms are not provided when disclosures are made via magnetic media, such disclosures should be identified in block 5 by the unique I.D. number associated with the tape reel, etc. At job's end, forward workpaper bundles containing the Form 4s and the agency disclosure documents to the Disclosure Accounting Coordinator at GAO's Tax Policy and Administration audit site.

Block 6 Record the disclosure date provided on the agency disclosure form, which should be the date GAO received the taxpayer information.

Block 7 Provide the agency (e.g., IRS, SSA) and location (e.g., Baltimore District Office), where the tax disclosure was made.

Block 8 Provide a general description of the documents obtained (e.g., tax returns, transcripts, correspondence, audit case files). If the information was provided on magnetic media, such as a computer tape, indicate this fact and provide a magnetic media identification number in block 5.

Block 9 Record the number of taxpayers on the agency disclosure form. Generally, each line on the Form 4 should correspond to one agency disclosure form. However, if an agency gave you similar information on several persons on the same date but chose to prepare a separate disclosure form for each person rather than recording all the disclosures on one form, you can, in the interest of brevity, combine the information from all the agency forms on one line on the Form 4.

Block 10 Total the number of taxpayer disclosures during the month of the report. Record the "Cumulative Total to Date" from the previous month's report. Add these two figures and record the updated Cumulative Total to Date.

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Use this letter when assignment is conducted as duly designated agent.

Mr. Robert L. Rebein
Assistant Commissioner (Inspection)
Internal Revenue Service

Dear Mr. Rebein:

This letter is to notify you of our intent to conduct a study of the use of the research and experimentation tax credit at the request (copy enclosed) of the House Committee on Ways and Means (Job Code 268189). Our work, which will be conducted pursuant to section 6103(f)(4)(A) of the Internal Revenue Code, pertains to section 44F which provides a 25-percent income tax credit for certain incremental research and development expenditures related to a trade or business. The Committee would like GAO to provide information and data on the (1) characteristics of users of the credit and (2) specific purposes for credit-related research and development expenditures. To carry out this work, we will need access to tax returns and return information.

Our work will be done at IRS' National Office, including the Office of Chief Counsel; its Midwest, Southeast, and Central Regional Offices; its Detroit data center; and its service centers in Chamblee, Kansas City, and Cincinnati. We also plan to carry out work at IRS district offices in Atlanta, Birmingham, Chicago, Cincinnati, Cleveland, Columbia, Des Moines, Detroit, Jacksonville, Milwaukee, St. Louis, and Springfield. If we need to do work in other locations, we will identify those locations for you at a later date.

We plan to initiate this study on March 5, 1984. We would appreciate your notifying the appropriate officials of our plans. If you have any questions, please call me at 275-6407. Thank you for your cooperation.

Sincerely yours,

Johnny C. Finch
Senior Associate Director

Enclosure

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The Honorable Martha A. McSteen
Acting Commissioner of Social Security
Department of Health and Human Services

Dear Mrs. McSteen:

Pursuant to the authority granted us by Section 6103 of the Internal Revenue Code, we are initiating a study of the effects of uncredited or erroneously credited earnings on individuals' Social Security eligibility and benefit amounts. To effectively carry out our work, we will need access to tax returns and tax information.

We notified the Joint Committee on Taxation on August 23, 1984, of our intent to initiate this study. Copies of our letter and the receipt signed by the joint committee are enclosed.

Accordingly, this letter is to formally notify you of our study and our requirement for access to appropriate tax returns and return information. Mr. Joseph Delfico or Mr. Joseph Kredatus will contact the agency to work out the arrangements for obtaining the necessary information.

Sincerely yours,

Comptroller General
of the United States

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APPENDIX 6. SAMPLE GAO FORM 8, RECORD OF RECEIPT

GGD Form 8 (2-85)

RECORD OF RECEIPT

Received from the U.S. General Accounting Office a letter, dated _____, notifying the Joint Committee on Taxation of its intent to initiate an audit pursuant to the authority granted the General Accounting Office in P. L. 95-125 and section 6103 of the Internal Revenue Code

Joint Committee on Taxation

Date Received

Time Received

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APPENDIX 4. SAMPLE JOINT COMMITTEE LETTER

The Honorable Dan Rostenkowski
Chairman, Joint Committee on Taxation
Congress of the United States

Dear Mr. Chairman:

This letter is to notify you that, pursuant to the authority granted to us by 31 U.S.C. 713 and Section 6103 of the Internal Revenue Code, we plan to review the extent to which the Internal Revenue Service (IRS) is required to pay interest to taxpayers for overpayments it receives. Our overall objectives are to (1) assess the potential impact of changes made by the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) on interest costs and (2) determine whether IRS could take certain administrative actions to improve its return processing procedures and, thereby, reduce the number and amount of such payments.

Under Section 6611 of the Internal Revenue Code, a taxpayer is entitled to receive interest on an overpayment to IRS if IRS does not issue the refund check within 45 days after the return is due (normally April 15th). In general, the code provides that the interest should be calculated from April 15 until the date the refund check is issued. During fiscal year 1982, IRS paid about \$1.8 billion in interest, up from about \$500 million in fiscal year 1980.

TEFRA gave IRS some measure of relief from paying interest by providing that no interest will be paid until a return is filed in a form suitable for processing. Also, TEFRA changed the means by which interest is to be calculated for delinquent filers. Prior to TEFRA, interest was paid from the due date regardless of whether or not the return was delinquent.

To do this work, it will be necessary for us to have access to returns and return information. For example, we plan to analyze a sample of tax returns on which interest was paid by IRS to identify the circumstances surrounding such payments and to determine whether procedural shortcomings are contributing to the interest payment problem.

Should you or members of your staff have any questions or comments on this proposed assignment, please call Mr. Johnny C. Finch on 275-6407.

Sincerely yours,

Comptroller General
of the United States

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REQUIRED
NOTIFICATION
LETTERS

ADDRESSEE

SIGNER

PROCEDURES

Assignments for which tax information is to be obtained from BATF

<p>Secretary of the Treasury, Attn: Assistant Secretary (Enforcement and Operations), Department of the Treasury.</p> <p>cc: Director, Bureau of Alcohol, Tobacco, and Firearms.</p> <p>Inspector General-Audit Staff, Department of the Treasury.</p> <p>Chief, Internal Audit, Bureau of Alcohol, Tobacco, and Firearms.</p>	<p>GGD's Associate Director for Tax Policy and Administration.</p>	<p>Some procedures as for IRS assignments.</p> <p>Additional copies of letter are provided to the Director, Bureau of Alcohol, Tobacco and Firearms;</p> <p>--Inspector General - Audit Staff, Department of the Treasury; and</p> <p>--Chief, Internal Audit, Bureau of Alcohol, Tobacco, and Firearms.</p>
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Program division finalizes letter and forwards it to the Associate Director for Tax Policy and Administration, GGD, for signature.

GGD's Issue Area Coordinator for Tax Policy and Administration delivers the letter to the addressee.

Copies of letter are provided to

- the program division;
- the Associate Director for Tax Policy and Administration, GGD; and
- GGD's Issue Area Coordinator for Tax Policy and Administration (2 copies).

Assignments for which tax information is to be obtained from BATF

Chief, Internal Audit, GGD's Associate
Bureau of Alcohol, Tobacco, Director for Tax
and Firearms, Policy and
Administration.

Same procedures as for IRS assignments.

Assignments for which tax information is to be obtained from an agency other than IRS or BATF

As appropriate.

To be determined by the responsible program division.

To be determined by the responsible program division.

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ADDRESSEE

Assignments for which tax information is to be obtained from BATF

<p>Secretary of the Treasury, Attn: Assistant Secretary (Enforcement and Operations), Department of the Treasury.</p> <p>cc: Director, Bureau of Alcohol, Tobacco, and Firearms.</p> <p>Inspector General- Audit Staff, Department of the Treasury.</p> <p>Chief, Internal Audit, Bureau of Alcohol, Tobacco, and Firearms.</p>	<p>Comptroller General.</p>	<p>Same procedures as for IRS assignments.</p> <p>Additional copies of letter and enclosures are provided to the</p> <p>--Director, Bureau of Alcohol, Tobacco, and Firearms;</p> <p>-- Inspector General - Audit Staff, Department of the Treasury; and</p> <p>--Chief, Internal Audit, Bureau of Alcohol, Tobacco, and Firearms.</p>
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APPENDIX 3. NOTIFICATION PROCEDURES

REQUIRED
NOTIFICATION
LETTERS

Self-initiated assignments and requests other
than those from committees authorized access to
tax information

PROCEDURES

SIGNER

ADDRESSEE

Program Division prepares draft letter and tentative GAO Form 100A and sends it to GGD's Issue Area Coordinator for Tax Policy and Administration.

Issue Area Coordinator informally discusses letter with joint committee and notifies program division of suggested changes.

Program division finalizes letter and forwards it with the tentative GAO Form 100A and Action Routing Slip, GAO Form 319, through the Associate Director for Tax Policy and Administration, GGD, to the Comptroller General for signature.

After signature, program division delivers letter to Joint Committee on Taxation and obtains signed Record of Receipt, GGD Form 8.

Copies of the letter and signed record of receipt are provided to

- the agency from which tax information is received,
- the Associate Director for Tax Policy and Administration, GGD, and
- GGD's Issue Area Coordinator for Tax Policy and Administration (2 copies).

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(B) Restriction on use of disclosed information.—Any officers and employees of an agency receiving return information under subparagraph (A) shall use such information only for the purposes of, and to the extent necessary in, establishing appropriate agency records or in the defense of any litigation or administrative procedure ensuing from reduction made under section 6402(c) or section 6402(d).

(11) Disclosure of certain information to agencies requesting a reduction under section 6402(c).—

(A) Return information from internal revenue service.—The Secretary shall, upon receiving a written request, disclose to officers and employees of a State agency seeking a reduction under section 6402(c)—

(i) the fact that a reduction has been made or has not been made under such subsection with respect to any taxpayer;

(ii) the amount of such reduction;

(iii) whether such taxpayer filed a joint return;

(iv) taxpayer identity information with respect to the taxpayer against whom a reduction was made or not made and of any other person filing a joint return with such taxpayer; and

(v) the fact that a payment was made (and the amount of the payment) on the basis of a joint return in accordance with section 464(a)(3) of the Social Security Act

(B) Restriction on use of disclosed information.—Any officers and employees of an agency receiving return information under subparagraph (A) shall use such information only for the purposes of, and to the extent necessary in, establishing appropriate agency records or in the defense of any litigation or administrative procedure ensuing from a reduction made under section 6402(c)

(m) Disclosure of Taxpayer Identity Information.—

(1) Tax refunds.—The Secretary may disclose taxpayer identity information to the press and other media for purposes of notifying persons entitled to tax refunds when the Secretary, after reasonable effort and lapse of time, has been unable to locate such persons.

(2) Federal claims.—

(A) In general.—Except as provided in subparagraph (B), the Secretary may, upon written request, disclose the mailing address of a taxpayer for use by officers, employees, or agents of a Federal agency for purposes of locating such taxpayer to collect or compromise a Federal claim against the taxpayer in accordance with section 3 of the Federal Claims Collection Act of 1966 [section 3711 of title 31, United States Code] (31 U.S.C. 952)

(B) Special rule for consumer reporting agency.—In the case of an agent of a Federal agency which is a consumer reporting agency (within the meaning of section 603(f) of the Fair Credit Reporting Act (15 U.S.C. 1681a(f))), the mailing address of a taxpayer may be disclosed to such agent under subparagraph (A) only for the purpose of allowing such agent to prepare a commercial credit report on the taxpayer for use by such Federal agency in accordance with section 3 of the Federal Claims Collection Act of 1966 [section 3711 of title 31, United States Code] (31 U.S.C. 952)

(3) National Institute for Occupational Safety and Health.—Upon written request, the Secretary may disclose the mailing address of taxpayers to officers and employees of the National Institute for Occupational Safety and Health solely for the purpose of locating individuals who are, or may have been, exposed to occupational hazards in order to determine the status of their health or to inform them of the possible need for medical care and treatment.

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(5) **Department of Health and Human Services.**—Upon written request by the Secretary of Health and Human Services, the Secretary may disclose information returns filed pursuant to part III of subchapter A of chapter 61 of this subtitle for the purpose of carrying out, in accordance with an agreement entered into pursuant to section 232 of the Social Security Act, an effective return processing program

(6) **Disclosure of return information to Federal, State, and local child support enforcement agencies.**—

(A) **Return information from Internal Revenue Service.**—The Secretary may, upon written request, disclose to the appropriate Federal, State, or local child support enforcement agency

(i) available return information from the master files of the Internal Revenue Service relating to the social security account number (or numbers, if the individual involved has more than one such number), address, filing status, amounts and nature of income, and the number of dependents reported on any return filed by, or with respect to, any individual with respect to whom child support obligations are sought to be established or enforced pursuant to the provisions of part D of title IV of the Social Security Act and with respect to any individual to whom such support obligations are owing, and

(ii) available return information reflected on any return filed by, or with respect to, any individual described in clause (i) relating to the amount of such individual's gross income (as defined in section 61) or consisting of the names and addresses of payors of such income and the names of any dependents reported on such return, but only if such return information is not reasonably available from any other source.

(B) **Restriction on disclosure.**—The Secretary shall disclose return information under subparagraph (A) only for purposes of, and to the extent necessary in, establishing and collecting child support obligations from, and locating, individuals owing such obligations

(7) **Disclosure of return information to federal, state, and local agencies administering certain programs under the Social Security Act or the Food Stamp Act of 1977.**—

(A) **Return information from social security administration.**—The Commissioner of Social Security shall, upon written request, disclose return information from returns with respect to net earnings from self-employment (as defined in section 1402) wages (as defined in section 3121(a) or 3401(a)), and payments of retirement income, which have been disclosed to the Social Security Administration as provided by paragraph (1) or (5) of this subsection, to any Federal, State, or local agency administering a program listed in subparagraph (D)

(B) **Return information from Internal Revenue Service.**—The Secretary shall, upon written request, disclose current return information from returns with respect to unearned income from the Internal Revenue Service files to any Federal, State, or local agency administering a program listed in subparagraph (D)

(C) **Restriction on disclosure.**—The Commissioner of Social Security and the Secretary shall disclose return information under subparagraphs (A) and (B) only for purposes of, and to the extent necessary in, determining eligibility for, or the correct amount of, benefits under a program listed in subparagraph (D)

(D) **Programs to which rule applies.**—The programs to which this paragraph applies are

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<u>AGENCY</u>	<u>PROGRAM OR ACTIVITY</u>	<u>TYPE OF TAX INFORMATION</u>
Federal, state, and local agencies that administer the unemployment compensation benefit program	Determination of eligibility for, or the correct amount of, benefits under the unemployment compensation benefit program	Information from returns with respect to wages, retirement and self-employment income and Information from returns with respect to unearned income
Federal agencies that collect or compromise federal claims	Location of individuals to collect or compromise federal claims	Taxpayer's mailing address
Department of Education	Collection of delinquent student loans	Taxpayer's mailing address
Federal agencies that request IRS offset of debts	Establishment of appropriate agency records or defense of litigation or administrative procedure ensuing from federal debt reduction.	Certain return information related to offset of federal debt

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APPENDIX 2. GAO'S ACCESS TO TAX INFORMATION THAT IRS CAN DISCLOSE TO OTHER AGENCIES UNDER 26 U.S.C. 6103(1) AND (m)

Under certain circumstances, GAO may have access to tax information that a federal agency does not have in its files, but that it could have obtained for non-tax administration purposes. This GAO access authority is limited to (1) audits of the programs and activities for which agencies are authorized access under 26 U.S.C. 6103(1) and (m), a copy of which can be found at the end of this appendix, and (2) the types of tax information that may be disclosed under those sections. Also, before requesting access, GAO must take into account the burden that such access might impose on the Internal Revenue Service.

Some of the programs and activities to which this access authority applies and the kinds of tax information to which GAO may have access are summarized below. The list is not all-inclusive. Because the statutes governing this area are complex, determinations as to whether or not GAO has access to tax information have to be made on a case-by-case basis. These determinations are to be made in consultation with the Associate Director for Tax Policy and Administration, GGD, and the Office of General Counsel.

<u>AGENCY</u>	<u>PROGRAM OR ACTIVITY</u>	<u>TYPE OF TAX INFORMATION</u>
Social Security Administration	Administration of social security benefits	Tax returns and return information with respect to (1) self-employment income, (2) FICA taxes, and (3) income taxes withheld from wages, interest, and dividends
	Administration of vested benefits under employee pension plan	Statements, notifications, reports, or other information related to pension plans
	Administration of the combined annual wage reporting program	Information returns
Railroad Retirement Board	Administration of the Railroad Retirement Act	Tax returns and return information with respect to railroad retirement taxes
Department of Labor and the Pension Benefit Guaranty Corporation	Administration of the employee benefit program	Tax returns and return information
	Administration of the termination insurance program	Tax returns and return information
Federal agencies which make, guarantee, or insure loans	Administration of federal loan programs	Information on whether or not a loan applicant has a delinquent tax account

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Administration, GGD, to the Comptroller General for signature. After the Comptroller General signs the letter, the program division delivers it to the Chief of Staff of the Joint Committee on Taxation and provides a copy to the Associate Director for Tax Policy and Administration.

15. ANNUAL REPORT. The Comptroller General is required by law to submit to the Senate Committees on Finance and Governmental Affairs, the House Committees on Ways and Means and Government Operations, and the Joint Committee on Taxation, a written annual report on GAO assignments involving IRS, BATF, and other federal agencies for which it had access to tax information and the policies and procedures established for protecting the confidentiality of tax information. The program divisions are responsible for providing GGD's Issue Area Coordinator for Tax Policy and Administration with information to be included in the report. The Associate Director for Tax Policy and Administration, GGD, is responsible for preparing the annual report. 31 U.S.C. 719(d).

- a. Contents of Report. The annual report includes information on
- (1) open recommendations to the Congress,
 - (2) legislative action taken during the year on recommendations,
 - (3) recommendations made to the heads of federal agencies concerning the administration of taxes and/or the use of tax information,
 - (4) reports on tax matters issued during the year,
 - (5) testimony on tax matters given by GAO officials during the year,
 - (6) scope and subject matter of assignments requiring access to tax information initiated during the year, and
 - (7) GAO's policies and procedures for safeguarding the confidentiality of tax information.

b. Responsibilities. Program division directors are responsible for providing GGD's Issue Area Coordinator for Tax Policy and Administration with the information listed above for reports and assignments within their areas of responsibility. The information should be provided no later than January 15 of each year and should apply to the prior calendar year. (See appendix 11 for sample formats.) The Associate Director for Tax Policy and Administration, GGD, is responsible for preparing and processing the annual report for the signature of the Director, GGD, as soon as possible after the close of each calendar year.

c. Report Distribution. The report is submitted to the House Committee on Ways and Means, Senate Committee on Finance, Joint Committee on Taxation, House Committee on Government Operations, and Senate Committee on Governmental Affairs. Copies of the report are sent to the heads of the federal agencies discussed in it.

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(c) All undesired computer listings and reports must be properly disposed of by a GAO employee who has been authorized access to tax information.

(3) Tax information, working papers, and magnetic media (such as computer tapes and electronic word processing disks) containing tax information must be stored in authorized metal cabinets with locks maintained in secure areas under the control of employees who have been authorized access to tax information. 26 U.S.C. 6103(p)(4)(B).

(4) Tax information must not be discussed over telephone lines that are not secure and must be transmitted electronically in accordance with GAO-prescribed controls.

(5) When tax information, working papers, and magnetic media containing tax information cannot be hand-carried, they must be sent by registered mail with a return receipt to be signed by an employee authorized access to tax information. Tax information sent in an envelope must be double sealed and the inside envelope marked "to be opened by addressee only." Shipments of tax information must be documented and monitored to ensure that they are promptly received. A GAO Form 393, Routing and Control Record, must be completed in duplicate. The original remains with the sender, the copy accompanies the mailing.

(6) GAO will not retain custody of original returns after an assignment is completed, except by special arrangement made with the Commissioner of Internal Revenue or the Commissioner's designee. GAO will return original returns to IRS.

(7) When copies of returns and working papers containing tax information are no longer needed, they should be transferred to the Federal Records Center. Because special procedures apply to the transfer of tax information, the program division should contact GGD's Issue Area Coordinator for Tax Policy and Administration prior to transferring the records. If the program division has retained custody of the tax information for 3 years after the assignment was terminated, the information must be destroyed in accordance with IRS' Tax Information Security Guidelines, under the supervision of a GAO employee designated as having access to tax information. In accordance with IRS' guidelines, when tax information on magnetic media (e.g., computer tapes and electronic word processing disks) is no longer needed, it must be erased and the tape either released for other use or destroyed. 26 U.S.C. 6103(p)(4)(F).

d. Periodic Inspections of Safeguard Procedures and Annual Safeguard Activity Report.

(1) 26 U.S.C. 6103(p)(4) provides, in effect, that if IRS finds GAO's procedures for safeguarding tax information to be inadequate, it can refuse to disclose tax information to GAO until the inadequacies have been corrected.

(2) In that regard, GGD's Associate Director for Tax Policy and Administration is responsible for assuring that periodic inspections of safeguard procedures are made of GAO divisions and offices and maintaining a record of each inspection in accordance with IRS' Tax Information Security Guidelines. The Office of Security and Safety is responsible for making these inspections

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in closed executive session. The program divisions must coordinate any requests for, or potential disclosures of, tax information with the Associate Director for Tax Policy and Administration, GGD.

b. Penalties For Unauthorized Disclosures.

(1) Disciplinary action, including reprimand and suspension, may be taken against employees who make an unauthorized disclosure of tax information. (See GAO Order 2752.1, Adverse Actions.)

(2) GAO employees who willfully make an unauthorized disclosure are subject to criminal penalties. An unauthorized disclosure is a felony, punishable upon conviction by a fine of up to \$5,000 and/or a jail term of not more than 5 years. Upon conviction, the employee will be discharged from employment. 26 U.S.C. 7213(a)(1), 18 U.S.C. 1905.

(3) Civil penalties are also provided for unauthorized disclosures of tax information. The taxpayer involved can initiate a law suit for civil damages against the United States. 26 U.S.C. 7431.

11. SAFEGUARDING TAX INFORMATION. To protect the confidentiality of tax information and to prevent its unauthorized disclosure, GAO has developed safeguard procedures that have been approved by the Secretary of the Treasury. The Secretary may refuse GAO further access to tax information if these procedures are not fully observed by GAO employees. Also, the Secretary is required to report any safeguard deficiencies to the appropriate congressional committees. GAO employees with access to tax information are responsible for carrying out the following safeguard procedures.

a. Disclosure Accounting. GAO is required to maintain a permanent system of records to account for all disclosures of tax information made to or by it. 26 U.S.C. 6103(p)(4)(A), 26 U.S.C. 6103(p)(6)(B)(i).

(1) **Tax Information Disclosed to GAO.** IRS, BATF, and other federal agencies that disclose tax information to GAO are responsible for determining when such a disclosure has occurred and for documenting each disclosure. GAO generally relies on such determinations and recordings as the basis for its recordkeeping system. Program divisions are responsible for ensuring that their employees obtain and record this information in accordance with the procedures described below.

(a) GAO staff at the location where tax information is received arranges with appropriate agency officials to obtain, on a daily basis, a copy of each agency record of disclosure to GAO. Agency personnel are responsible for preparing these records. Generally, IRS personnel record disclosures to GAO on IRS Forms 5466 and 5466A. Other agencies may have different disclosure forms. GAO staff members are responsible for identifying these forms.

(b) The copies of the agency's disclosure forms or other records are used by the GAO staff for daily posting to GGD Form 4, Tax Administration Disclosure Control Document. A separate form must be kept by each GAO work location for each job code. (A sample GGD Form 4 and instructions for completing the form appear in appendix 9.)

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a. Self-Initiated Assignments and Requests from Non-Ta Writing Committees and Members of Congress.

(1) The Comptroller General, at six-month intervals, designates in writing each GAO employee who is to have access to tax information. These designations are updated monthly by the Associate Director for Tax Policy and Administration, GGD, pursuant to the delegation of authority made under paragraph 6.

(2) The associate director delivers certified copies of the semi-annual lists and monthly updates to (a) the Joint Committee on Taxation, (b) the Senate Committee on Finance, (c) the House Committee on Ways and Means, (d) the Senate Committee on Governmental Affairs, (e) the House Committee on Government Operations, (f) IRS, (g) BATF, and (h) the program divisions responsible for assignments that require access to tax information.

(3) Before the initiation of assignments described under paragraphs 7a(2) and 7a(4), the Associate Director for Tax Policy and Administration, GGD, provides the program divisions with certified copies of lists of those GAO employees from the above lists who are to have access to tax information in the agency's possession. The program divisions are responsible for delivering copies of the lists to the appropriate agencies. The associate director prepares updated listings for these agencies when staffing changes occur.

b. Assignments Conducted as Agents of the Joint Committee on Taxation.

(1) The Comptroller General, at six-month intervals, designates in writing each GAO employee who is authorized access to tax information as an agent for that committee. The Associate Director for Tax Policy and Administration, GGD, updates the designations monthly.

(2) The associate director delivers certified copies of the semi-annual and monthly lists to the Joint Committee on Taxation, IRS, and the program divisions responsible for assignments that require access to tax information.

(3) For an assignment involving an agency other than IRS, the associate director, before initiation of the assignment, provides the responsible program division with a certified copy of a list of GAO employees who are to have access to tax information for the assignment. The program division delivers the list to the agency. The associate director prepares updated listings when staffing changes occur.

c. Assignments Conducted as Agents of the Senate Committee on Finance or the House Committee on Ways and Means.

(1) The Comptroller General, prior to initiation of the assignment, designates in writing each GAO employee who is authorized to have access to tax information. These designations are updated by the Associate Director for Tax Policy and Administration, GGD, as staffing changes occur.

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Form 100A and a GAO Form 319, Action Routing Slip. (A sample GAO Form 319 appears in appendix 5.) The associate director forwards the package to the Comptroller General for signature.

(c) After the notification letter is signed by the Comptroller General, the program division delivers it to the Chief of Staff of the Joint Committee on Taxation along with a GGD Form 8, Record of Receipt. This form is completed by the joint committee at the time of delivery. (A sample GGD Form 8 appears in appendix 6.) Once the letter has been delivered to the Chief of Staff and GGD Form 8 has been completed, copies are provided to the recipients identified in appendix 3.

(2) Agency Head Letter.

(a) After the Joint Committee on Taxation has approved GAO's access to tax information, usually by letting the 30-day period expire, a written notification of the assignment must be provided to the head of the federal agency that is to provide the tax information. The letter cites GAO's audit and access authority, the subject of the assignment, and the date the Joint Committee on Taxation was notified. It should also formally request access to the tax information and include, as enclosures, copies of the joint committee letter and the GGD Form 8. (Sample letters appear in appendix 7.)

(b) The program division drafts the letter and forwards it for processing to GGD's Issue Area Coordinator for Tax Policy and Administration within 15 days of the date of the joint committee letter. The issue area coordinator notifies the program division of any suggested changes. The program division then forwards the letter in final form, along with an action routing slip, to the Associate Director for Tax Policy and Administration, GGD, who forwards it to the Comptroller General for signature. The signed letter is then returned to the associate director for dating. (The date is generally no earlier than 31 days after the date on the GGD Form 8.) The dated letter is given to the agency that is to provide the tax information. Copies are provided to the recipients identified in appendix 3.

(3) Liaison Letter. After the agency head has been notified of an assignment as discussed in paragraph 8a(2), agency liaison officials must be notified in writing of GAO's need to review tax information. The procedure discussed below applies only to assignments for which tax information is to be obtained from IRS or BATF. If the assignment involves access to tax information at an agency other than IRS or BATF, the program division is responsible for identifying and satisfying any liaison requirements.

(a) The program division should draft the liaison letter no later than 15 days after the date of the joint committee letter. The liaison letter states GAO's intent to initiate a study, analysis, or evaluation (rather than a survey or review); cites the job code; states GAO's need for access to tax information; lists the agency organizational units and/or locations involved; states the date that GAO plans to begin the assignment (which must be at least 2 weeks after the date of the letter to give IRS and BATF time to arrange for disclosing the information to GAO); and requests that the appropriate officials be notified of GAO's assignment plans. (A sample letter appears in appendix 8.)

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a. Self-Initiated Assignments and Requests from Members of Congress and from Committees Not Authorized Access to Tax Information.

(1) GAO has access to tax information for the purpose of auditing IRS and BATF. 26 U.S.C. 6103(i)(7)(A).

(2) GAO has access to tax information in the possession of federal agencies, other than IRS and BATF, for the purpose of auditing the programs or activities for which those agencies obtained the tax information. For example, the Social Security Administration (SSA) collects and uses tax information on earnings and withheld taxes for the purpose of administering certain benefit programs. GAO has access to that tax information, but only for the purpose of auditing SSA's administration of those programs and only after certain notification procedures have been completed. 26 U.S.C. 6103(i)(7)(B)(i).

(3) GAO has access to tax information that certain federal agencies are authorized to obtain even if those agencies have not exercised that authority. These agencies must be authorized access to tax information under 26 U.S.C. 6103(l) or (m). GAO's access, however, is limited to audits of those programs or activities for which the agency is authorized access. For example, GAO would have access to the tax information which the Pension Benefit Guaranty Corporation (PBGC) is authorized to obtain from IRS to administer its termination insurance program. GAO has access to that tax information even if PBGC has not obtained the information from IRS. However, GAO cannot gain access to that tax information unless its objective is to evaluate the termination insurance program and then only after certain notification procedures have been completed. That is, GAO would not have access for the purpose of determining whether PBGC could use the tax information to enhance its administration of any other program. 26 U.S.C. 6103(i)(7)(B)(ii). (See appendix 2 for further information regarding GAO's access authority under this paragraph.)

(4) GAO has access to tax information in the custody of federal, state, and local agencies for the purpose of determining if the agencies' procedures and safeguards meet statutory requirements and ensure the confidentiality of tax information. 26 U.S.C. 6103(p)(6)(A).

b. Assignments Undertaken as Agents of Congressional Committees Authorized Access to Tax Information. GAO has access to tax information for auditing any agency or program when it is acting as a duly designated agent of a tax writing committee--the Joint Committee on Taxation (or that Committee's Chief of Staff), the Senate Committee on Finance, or the House Committee on Ways and Means. GAO also has access to tax information when acting as a duly designated agent for other congressional committees authorized access to tax information by a congressional resolution. 26 U.S.C. 6103(f)(4).

c. Assignments Involving Access to Tax Treaty Information. GAO has access to information provided to IRS by foreign governments under the exchange of information articles of certain tax treaties for the purpose of auditing IRS' administration of the taxes covered by the treaty. Such assignments may be self-initiated or conducted as a duly designated agent of a committee authorized access to tax treaty information. Refer questions concerning whether or not GAO has access under a particular treaty to GGD's Issue Area Coordinator for Tax Policy and Administration.

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GAO FORM - 378 (Aug. 72)

United States
General Accounting Office
Operations Manual



Order

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September 24, 1985

Subject: AUDIT ASSIGNMENTS INVOLVING ACCESS TO TAX INFORMATION

1. **PURPOSE, SCOPE, AND APPLICABILITY.** The purpose of this order is to provide guidance for determining whether and how the General Accounting Office (GAO) may obtain access to tax information for a particular assignment and to ensure compliance with laws and regulations for protecting the confidentiality of such information. Specifically, the order

a. cites GAO's statutory authority to obtain and review tax information during audits of the Internal Revenue Service (IRS); the Bureau of Alcohol, Tobacco, and Firearms (BATF); and other federal, state, and local agencies;

b. establishes policies and procedures for initiating, conducting, and completing assignments requiring access to tax information;

c. states policies and procedures for precluding the unauthorized disclosure of tax information in GAO's custody;

d. establishes security standards governing the transmission, custody, and disposition of tax information consistent with statutory provisions;

e. establishes recordkeeping and reporting requirements; and

f. applies to all GAO organizational elements.

NOTE. References throughout this order to the safeguarding of tax information mean the safeguarding of information so as to preclude the unauthorized disclosure of tax information in any form that identifies, either directly or indirectly, a particular taxpayer. Nothing in this order shall be construed as authorizing disclosure, dissemination, release, handling, or transmission of tax information contrary to specific provisions of any law.

2. **SUPERSESION.** This order supersedes GAO Order 0135.1, August 25, 1980. Revision has been so extensive that asterisks have not been used to indicate changes.

3. **REFERENCES.**

a. 26 U.S.C. 6103, 7213, and 7431

b. 31 U.S.C. 713 and 719

c. 18 U.S.C. 1905

Distribution C, N, R, and S

Initiated by General Government Division

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**Appendix VIII
Tax-Related Assignments Authorized
Pursuant to 31 U.S.C. 713 During Calendar
Year 1986**

Subject matter	Objectives	Month authorized
Employer-provided Cash and Deferred Compensation Plans	<p>To evaluate the incidence of 401(k) plans, specific plan features, and relationship of 401(k) plans to other pension plans provided by employers</p> <p>To evaluate participation and contribution levels across firms, especially with regard to withdrawals, employer contributions, and investment options</p> <p>To evaluate the relationships between firm characteristics, plan design and plan experience</p>	October
Effectiveness of ERISA's Minimum Funding Standards	<p>To evaluate the equity of plan participation and contribution levels by earning groups within and between firms</p> <p>To determine what role ERISA's minimum funding standards play in plan underfunding</p> <p>To determine whether certain characteristics may make plans more or less susceptible to underfunding</p>	October
Administration of ERISA's Contribution Requirements	<p>To evaluate IRS' enforcement of single pension plan contribution requirements</p> <p>To evaluate IRS procedures and processes for waiving pension plan contributions</p> <p>To evaluate the effect of waived contributions on the termination insurance program</p>	October

Listing of Testimonies Given on Tax Matters by GAO Officials Before Various Committees of Congress During Calendar Year 1986

GAO Official	Congressional Committee	Subject Matter	Date
Johnny C. Finch Senior Associate Director, General Government Division	Subcommittee on Oversight, House Committee on Ways and Means	IRS' Service Center Operations	3/4/86
William J. Anderson Assistant Comptroller General, General Government Programs	Subcommittee on Oversight, House Committee on Ways and Means	Profitability of the Property/ Casualty Insurance Industry	3/13/86
Johnny C. Finch Senior Associate Director, General Government Division	Subcommittee on Oversight, House Committee on Ways and Means	Profitability of the Property/ Casualty Insurance Industry	4/28/86
Johnny C. Finch Senior Associate Director, General Government Division	Subcommittee on Commerce, Consumer and Monetary Affairs, House Committee on Government Operations	IRS' Information Returns Matching Program	4/29/86
Johnny C. Finch Senior Associate Director, General Government Division	Subcommittee on Oversight, House Committee on Ways and Means	Administration's Fiscal Year 1987 Budget Request for the Internal Revenue Service	5/12/86
Johnny C. Finch Senior Associate Director, General Government Division	Consumer Subcommittee, Senate Committee on Commerce, Science and Transportation	Profitability of the Property/Casualty Insurance Industry	5/20/86
William J. Anderson Assistant Comptroller General, General Government Programs	Subcommittee on Economic Stabilization, House Committee on Banking, Finance and Urban Affairs	Profitability of the Property/Casualty Insurance Industry	7/30/86
William J. Anderson Assistant Comptroller General, General Government Programs	Senate Committee on Finance	Taxation of the Property/Casualty Insurance Industry	10/1/86

Listing of GAO Products on Tax Matters Issued During Calendar Year 1986

Title	Date
Congress Should Further Restrict Use of the Completed Contract Method (GAO/GGD-86-34)	01/17/86
The Property/Casualty Insurance Loss Reserve Accounts (B-209677)	01/24/86
Breakdown of Data Shown in Our Completed Contract Method Report (B-221074)	01/31/86
Interim Report on a Survey of Employee Stock Option Plans and Related Economic Trends (GAO/PEMD-86-4BR)	2/07/86
Costs and Benefits of Financing with Tax-Exempt Bonds (GAO/RCED-86-2)	02/10/86
Protecting Tax Revenue When Businesses File for Bankruptcy (GAO/GGD-86-20)	02/21/86
Nonbusiness Interest Deductions (GAO/GGD-86-53BR)	03/13/86
How IRS' Philadelphia Service Center Is Addressing Processing Problems (GAO/GGD-86-60BR)	03/14/86
Contingency Plans and Risk Analyses Needed for IRS Computer Centers (GAO/IMTEC-86-10)	03/27/86
Financial Cycles in the Property/Casualty Industry (GAO/GGD-86-56FS)	04/09/86
Investment Tax Credit for Offshore Drilling Needs Clarification (GAO/GGD-86-65)	04/10/86
IRS' Actions to Improve the Accuracy of Non-wage Income Data Are Vital (GAO/IMTEC-86-17)	04/21/86
Compliance and Other Issues Associated With Occupational Excise Taxes (GAO/GGD-86-49)	06/05/86
1985 Annual Report on GAO's Tax-Related Work (GAO/GGD-86-81)	06/06/86
Timeliness and Accuracy of IRS' Telephone Assistance on Tax Questions (GGD-86-89FS)	06/18/86
Comparing Blue Cross and Blue Shield Plans with Commercial Insurers (GAO/HRD-86-110)	07/11/86
GAO's Views on the Proposed Tax Administration's Trust Fund (B-223617)	07/16/86
Information Returns Should Increase Proper Reporting of Farm Income (GAO/GGD-86-69)	07/22/86
Use of Tax-Exempt Bonds in Oakland, California (GAO/GGD-86-110BR)	07/24/86
Options for Speeding Tax Refunds and Reducing IRS' Interest Costs (GAO/GGD-86-72)	07/28/86
Administrative Changes Could Lead to Earlier Resolution of Tax Disputes (GAO/GGD-86-75)	07/30/86
IRS' Automated Collection System (GAO/GGD-86-120BR)	07/31/86
Historic Preservation Tax Incentives (GAO/GGD-86-112FS)	08/01/86
Use of Book Income in the Proposed Corporate Alternative Minimum Tax (B-223878)	08/11/86
Economic Effects of Selected Current Tax Provisions on Agriculture (GAO/GGD-86-126BR)	08/11/86
Excise Taxes on Sporting Arms, Ammunition, and Archery Equipment (GAO/GGD-86-114FS)	08/12/86
How Tax Incentives Encourage Soil and Water Conservation Investments (GAO/GGD-86-116FS)	08/13/86

(continued)

**IRS' Audit Selection
Procedures Are the
Same for Foreign-
Owned and Other U.S.
Corporations**

(GAO/GGD-87-2, 10/14/86)

This report to the Joint Committee on Taxation discusses IRS' procedures for classifying and selecting income tax returns of foreign-owned U.S. corporations for audit. The main criterion for selection is the potential for an audit to significantly change the reported tax liability through adjustments in the taxpayer's income or denial of certain deductions or credits. Although some returns having international issues may be selected for audit through special compliance projects, U.S. parent corporations with tax haven subsidiaries are also given special emphasis.

**Summary of Related
Action(s)**

Audit work conducted during this study was the basis for a prior report, entitled Tax Code Amendment: A Change in Foreign-Owned U.S. Corporations' Reporting Requirements (GAO/GGD-86-19, Nov. 1, 1985). (See p. 18.) In that report, we recommended that IRS compliance activities could be improved by amending section 6038A of the Internal Revenue Code to require the reporting to IRS of certain transactions between foreign-owned U.S. corporations and their noncorporate foreign owners. The Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) contains a provision requiring such expanded reporting.

No Improper Actions Found in IRS' Contract for Its Data Retrieval System

(GAO/IMTEC-86-33BR, 8/26/86)

This briefing report to the Chairman of the House Committee on Government Operations provided information on the results of our investigation into IRS' contract award for a major upgrade of its Integrated Data Retrieval System, which is an on-line computer system that supports many IRS functions

IRS' award for a major upgrade to the system was overturned by the General Services Administration's Board of Contract Appeals. We found no evidence of illegal actions on the procurement, but we found other major problems. Specifically, IRS' pricing evaluation was erroneous, and the contract was awarded to an offeror that did not meet IRS' stated technical requirements. However, we found no indication that these errors were intentional.

Summary of Related Action(s)

The information in this briefing report was useful to the House Committee on Government Operations in carrying out its oversight responsibilities in the computer area

How Tax Incentives Encourage Soil and Water Conservation Investments

(GAO/GGD-86-116FS, 8/13/86)

This fact sheet to the Joint Committee on Taxation contains information about the impact of section 175 of the Internal Revenue Code on the promotion of soil and water conservation and on other current and proposed government incentives to encourage such conservation. This information is based primarily on our analysis of two questionnaire surveys—one of farm landowners and the other of United States Department of Agriculture county executive directors—conducted between September 1984 and April 1985.

Sixty-eight percent of the landowners did not invest in conservation measures from 1980 through 1984 primarily because they believed erosion was not a problem on their land. For some landowners who believed their land was eroding, government financial assistance was important in their decisions to make conservation investments. Some landowners believed additional incentives would encourage more conservation and expressed a preference for changing section 175 to allow a choice between a current deduction or a proposed credit over increases in direct governmental assistance.

Approximately one-half of the county executive directors surveyed believed that the impact of section 175 on soil and water conservation investments was limited. They also felt that certain alternatives would be more effective in increasing future conservation investments. The alternative they favored most was increasing direct cash assistance to farmers through current governmental cost-sharing conservation programs.

Summary of Related Action(s)

The information in this fact sheet was available for Congress' use in considering proposed changes to the code section 175 special expensing provisions for soil and water conservation expenditures. The Tax Reform Act of 1986 placed limitations on soil and conservation expenditures that may be treated as current deductions.

Economic Effects of Selected Current Tax Provisions on Agriculture

(GAO/GGD-86-126BR, 8/11/86)

This briefing report to the Honorable Bill Bradley, U. S. Senate, reviews how various tax provisions affect the agricultural sector. The specific points covered include (1) the distribution of farms and income; (2) farm profits and losses claimed by individual taxpayers; (3) the economic effects of various tax provisions in what is now prior law; and (4) the amount and distribution of nonfarm income reported by taxpayers filing a Schedule F (Farm Income and Expenses). We found, based on a consensus among experts, that several provisions in the law prior to the enactment of the Tax Reform Act of 1986 contributed to greater farm output and lower farm prices—generally considered unsatisfactory conditions in the agricultural sector.

Summary of Related Action(s)

The information in this briefing report was available to Congress during its deliberation over the new tax bill. The bill substantially changed many of the provisions that encouraged unsatisfactory conditions in the agricultural sector

Historic Preservation Tax Incentives

(GAO/GGD-86-112FS 8/1/86)

This fact sheet to the Chairman of the Subcommittee on Public Lands, House Committee on Interior and Insular Affairs, provides information on nationwide historic preservation activities and updated an earlier GAO report, entitled Information on Historic Preservation Tax Incentives (GAO/GGD-84-47, Mar. 29, 1984). Our analyses of IRS' Statistics of Income data on 1982 and 1983 qualified rehabilitation expenditures indicated that individual and corporate taxpayers reported about \$6.1 billion in qualified rehabilitation expenditures during those 2 years. About 54 percent of the 2-year total expenditures were for the rehabilitation of 40-year-old buildings and about 36 percent for certified historical structures. Individuals and corporations earned approximately \$1.3 billion in tax credits on the expenditures reported during this 2-year period. We also noted that the Economic Recovery Tax Act impacted greatly on historic preservation activities as evidenced by the increase in the number of applications received, approved plans, estimated expenditures, and certified rehabilitations.

Summary of Related Action(s)

The information in this fact sheet was useful to the House Subcommittee on Public Lands in its evaluation of proposed changes to the tax code relating to historic preservation and should also be useful in future deliberations on historic preservation funding levels.

**Use of Tax-Exempt
Bonds in Oakland,
California**

(GAO/GGD-86-110BR, 7/24/86)

This briefing report to the Honorable Fortney H. (Pete) Stark, House of Representatives, contains information on the City of Oakland's use of tax-exempt bonds during the period January 1, 1983, to May 31, 1986. Various characteristics, such as bond type, purpose, amount, and estimated federal revenues foregone, are presented for each of the 18 bonds issued during the period reviewed. Included in these bond issues are transactions that sold and then leased back city assets, and a transaction that allegedly used bond proceeds to provide a loan to the Oakland Athletics baseball team.

**Summary of Related
Action(s)**

While no specific legislative action was taken with respect to Oakland's various bond issues, the Tax Reform Act of 1986 (Public 99-514, October 22, 1986) tightened restrictions on the annual volume of private activity bonds by establishing the new unified volume cap. This volume cap on most private activity bonds is equal to the greater of \$75 per each state resident or \$250 million. After 1987, the volume cap is further reduced to the greater of \$50 per resident or \$150 million.

**Timeliness and
Accuracy of IRS'
Telephone Assistance
on Tax Questions**

(GAO/GGD-86-89FS. 6/18/86)

This fact sheet to the Chairman of the Subcommittee on Oversight, House Committee on Ways and Means, contains our analysis of the timeliness and accuracy of IRS' Telephone Assistance Program during the 1986 filing season. We conducted a test of this program for 32 days from March 3 through April 15, 1986. During that time we placed 1,280 calls to 31 IRS telephone sites. Our test results showed that, for the majority of calls, taxpayers could expect to be successful in reaching IRS telephone assisters and obtaining accurate answers to their questions. We reached the IRS site on our first call attempt in 68 percent of the cases and IRS responses to our questions were accurate 83 percent of the time.

**Summary of Related
Action(s)**

The information in this fact sheet was useful to the Subcommittee in its oversight of IRS' Taxpayer Service Program.

**How IRS' Philadelphia
Service Center Is
Addressing Processing
Problems**

(GAO/GGD-86-60BR, 3/14/86)

This briefing report to various Senate and House requesters discusses the results of our work at IRS' Philadelphia Service Center during 1985 and the first 2 months of 1986. We found that the Service Center had a better performance record during the first few weeks of 1986 than it did during a comparable period in 1985. However, certain issues which had surfaced in 1985, namely, controls over the processing of computer tapes and backlogs in certain inventories needed continuing management attention.

**Summary of Related
Action(s)**

The information in this briefing report was useful to the requesters in exercising their oversight responsibilities and in responding to constituent inquiries.

Survey of Employee Stock Ownership Plans and Related Economic Trends

(GAO/PEMD-86-4BR. 2/7/86)

This interim briefing report to the Honorable Russell B. Long, U. S. Senate, is the second in a series responding to the Senator's request for information about Employee Stock Ownership Plans (ESOP). The report contained the results of our then continuing analysis of ESOPs.

The major findings discussed in the report relate to our census of ESOPs, the contribution of ESOPs to the goal of broadening the ownership of corporate stock, and the tax revenue losses associated with ESOPs. Based on our analyses, we estimated that in early 1985, 4,174 ESOPs were active, with more than 7 million participants and nearly \$19 billion in assets. We found that tax credit ESOPs have more participants and hold larger amounts of assets than other types of ESOPs but that leveraged ESOPs provide the highest asset value per participant. We also found that the proportion of employees of ESOP-sponsoring firms participating in stock ownership through employer-sponsored ESOPs is more than three times the proportion of all U.S. families owning stock. We estimated that the corporate income tax revenue lost through incentives to promote ESOPs totaled \$9.9 billion between 1977 and 1983, of which \$8.9 billion was attributable to tax credit ESOPs.

The report also covered the (1) distribution of ESOPs among business sectors and geographic regions; (2) relative proportions of ESOPs and ESOP participants and assets in publicly traded and privately held companies; (3) the extent to which ESOPs hold stock that carries voting rights; and (4) trends in the formation of ESOPs, the number of ESOP participants, and contributions to ESOPs over time.

Summary of Related Action(s)

Some of the information contained in this interim briefing report was used by Senator Long and his staff during the tax reform debate to bolster their arguments for the need for changes in ESOP incentives. The Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) included substantial changes to those incentives.

Summary of Information on Tax Matters Reported to Congress During Calendar Year 1986

Comparison of Administration's Proposal for Property/ Casualty Insurance Loss Reserve Account With Reserves for Mining Reclamation

(B-209677, 1/24/86)

This letter to the Chairman of the House Committee on Ways and Means compares the Administration's proposal to create a Qualified Reserve Account for property/casualty insurance company reserves with the treatment of reserves by mining companies for the cost of restoring or reclaiming a mined area. Our analysis showed that the thrust of the Administration's proposal as it dealt with the time value of money was consistent with the treatment of reserves for mine reclamation. Our analysis also compares the differences between the Administration's proposal and its recommendation to discount property/casualty reserves.

Summary of Related Action(s)

The information in this letter was useful to the House Committee on Ways and Means in its consideration of tax reform issues that related to the property/casualty industry. The Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) included a reserve discounting method similar to the one we recommended. (See p. 15.)

IRS Can Improve Its Collection Procedures for Taxpayers Living Overseas

(GAO/GGD-87-14, 12/12/86)

IRS' domestic offices, which are responsible for handling Army Post Office/Fleet Post Office (APO/FPO) collection cases, are not in the best position to deal effectively with overseas taxpayers. Two essential tools for dealing with delinquent taxpayers—the telephone and personal contact—are generally not available to domestic offices when trying to resolve overseas collection cases. Conversely, IRS' Foreign Operations District, which has collection responsibility for overseas taxpayers other than those with an APO/FPO address, has offices overseas and is experienced in dealing, through both telephone and personal contact, with U.S. taxpayers living in foreign countries.

Therefore, we believe that responsibility for APO/FPO collection cases should be assigned to the Office of the Assistant Commissioner (International), which recently assumed the Foreign Operation District's functions. The results of the limited test involving APO/FPO cases transferred from domestic offices to the Foreign Operations District further support our belief.

In conjunction with this transfer of responsibility, we believe that IRS should require APO/FPO taxpayers to file their returns at the Philadelphia Service Center. This action would facilitate immediate access by the Office of the Assistant Commissioner (International) to taxpayer information contained on IRS' Integrated Data Retrieval System when working APO/FPO collection cases. The change also would consolidate tax return filing for overseas taxpayers at one service center because overseas taxpayers who use regular foreign mailing addresses are already required to file at Philadelphia. IRS' handling of APO/FPO cases would be enhanced further if IRS could access locator information maintained by the Defense Manpower Data Center.

Recommendations

We recommended that the Commissioner of Internal Revenue:

- Assign responsibility for APO/FPO collection cases to the Assistant Commissioner (International).
- Require APO/FPO taxpayers to file their tax returns at the Philadelphia Service Center.
- Arrange for access to the Defense Manpower Data Center's information base.

IRS Must Better Estimate Its Computer Resource Needs

(GAO/IMTEC-87-5BR, 11/3/86)

IRS is highly dependent on computers to support its mission. The large mainframe computers at IRS' 10 service centers are the backbone of the tax processing system. Having decided that the mainframe computers would not have the capacity to handle projected tax processing work loads starting in 1989, IRS planned to upgrade or replace these large mainframes by 1989 with a \$186 million computer acquisition known as Capacity Enhancement for the Processing System (CEPS). IRS believed that, with CEPS, its existing mainframe computers would have sufficient capacity to process taxpayer information and update computer files beyond 1989. IRS later decided to postpone upgrading and identified a series of initiatives which it felt would extend the existing mainframe computers' usefulness.

We found that the Department of the Treasury endorsed IRS' decision to abandon CEPS in favor of adopting the initiatives and combining the procurement strategy of CEPS with the planned Tax System Redesign. We believe that (1) the existing mainframes will have the capacity to handle IRS tax processing work loads through at least mid-1991, assuming that no large unexpected increase in work loads occurs and IRS effectively carries out its planned initiatives; (2) IRS' initiative to constrain annual work load growth to 8 or 10 percent could be difficult to achieve because IRS plans to install new equipment and introduce new on-line applications that could increase demand for tax account information; and (3) IRS could experience capacity problems at its larger service centers as early as mid-1988 if it does not implement its initiatives successfully.

We also believe that (1) without a work load analysis and a continuing analysis of current system utilization, IRS will not have adequate assurance that its initiatives are working and could unexpectedly find itself short of computer capacity when it implements the Tax System Redesign, and (2) such an unexpected shortage could have a devastating impact on operations, as was experienced in the 1985 tax filing year.

Recommendations

We recommended that the Commissioner of Internal Revenue:

- Develop and maintain comprehensive work load data for current and planned ADP requirements.

Thorough Testing and Work Load Analyses Are Needed for IRS Processors

(GAO/IMTEC-87-3BR, 10/14/86)

Computers are an essential part of IRS operations. In particular, IRS' communications processors are the computers through which all on-line inquiries via computer terminals must pass to get access to key IRS data bases on the mainframe computers. Our evaluation of the performance of existing communications processors and the soundness of IRS' planned communications replacement system, showed that

- existing communications processors have experienced reliability and capacity problems, but their performance had no significant adverse effect on the 1986 tax filing season;
- a significant delay in the replacement processor installation schedule or an increase in work load will increase the chances that the existing processors will experience reliability and capacity problems;
- replacement processors are both reliable and capable of handling the current IRS work load, but they may not be able to meet long-term IRS needs;
- although the replacement communications software is not fully developed, it already requires more computer capacity than originally estimated;
- original IRS projections of the future work load are outdated and cannot be relied upon; and
- IRS' plan to install the new system at its larger service centers during the 1987 tax filing season increases the risk of serious disruption of processing tax returns and refunds to taxpayers if problems occur with the new equipment or software.

We believe that all of the hardware and software should be thoroughly tested prior to nationwide service center installations.

Recommendations

We recommended that the Commissioner of Internal Revenue:

- Report to the Subcommittee on Oversight, House Committee on Ways and Means, any significant deviations or delays in IRS installation testing plans that could alter the implementation of planned testing safeguards or reduce the chances of all processors being operational by December 1987. The report should also include actions that IRS plans to take to alleviate the situation.
- Establish formal contingency plans at each IRS service center to provide reasonable continuity of data processing support should events occur

IRS Needs an Overall Strategy for Addressing Tip Income Reporting

(GAO/GGD-86-119, 9, 30/86)

Nonreporting of tip income for tax purposes is a major problem for IRS. For example, in calendar year 1981, IRS estimated that the nonreporting of such income was about 84 percent of the amount that should have been reported. This represented the highest nonreporting rate among all legal source income areas and amounted to an estimated \$8.5 billion in unreported tip income with an estimated revenue loss of \$2.3 billion.

IRS efforts to identify and reduce nonreporting of tip income have been limited and fragmented. For example, each IRS region and district independently decides on the amount of resources and types of detection methods to be used in pursuing nonreported tip income. We found that the regions and districts we visited varied significantly in their pursuit of this nonreported income. Some IRS offices were much more active and successful than others in dealing with this issue. While two of the four regions we visited limited their efforts because of various constraints, the other two were more active in pursuing tip income nonreporting because they developed a strategy to offset these constraints.

IRS needs an overall strategy for addressing tip income nonreporting. Without such a strategy, the potential will be greater for the loss of tax revenue and the inequitable treatment of taxpayers.

Recommendations

To enhance IRS' efforts to improve compliance with the requirements for reporting tip income, we recommended that the Commissioner of Internal Revenue formulate and implement an overall strategy for identifying and reducing tip income nonreporting. In formulating this strategy, the Commissioner should, in conjunction with providing tip income information to the regional and district offices,

- identify and evaluate, for IRS-wide applicability, those detection techniques and tools which have been proven effective in conducting tip income reporting projects and communicate this information to all IRS regions and districts; and
- design and implement an overview and evaluation process to monitor the progress of tip enforcement activities, identify potential problem areas, and devise the action(s) needed to deal with them.

IRS Needs to Improve Its Administration of the Rate Reduction Process Involving the Tip Income Reporting Requirement

(GAO/GGD-86-119, 9/30/86)

We reported that IRS needed to improve its administration of the Tax Equity and Fiscal Responsibility Act's (TEFRA) provision which permits employers to petition IRS for a reduction from the reporting of 8 percent of gross receipts as tip income. Our audit work at 18 district offices within four IRS regions showed the various methods used by IRS districts to review the merits of a rate reduction request were different and could result in inequitable treatment of tipped employees working for establishments applying for rate reductions. Although we recognized that total consistency is impossible, we believed that IRS could improve the situation.

When Congress passed TEFRA's tip provisions, certain safeguards were included with the intent that the provisions would not adversely affect employees of food and beverage establishments. One such safeguard permits employers to petition IRS for a reduction from the reporting of 8 percent of gross sales as tip income provided the employer can justify a lower rate. The Commissioner of Internal Revenue delegated the responsibility for granting rate reductions to IRS district directors.

Although the National Office's guidelines for implementing TEFRA's rate reduction provisions outlined the documentation needed to accompany a rate reduction request, they did not contain procedures on how the data should be analyzed. The guidelines, formalized in Revenue Procedure 85-4, stated that a request should include information, such as an establishment's gross receipts, location, and type of clientele. However, the National Office did not provide accompanying instructions to field officials on how to evaluate the data when making decisions on rate reduction requests. In addition, IRS did not establish a monitoring process to identify how each district implemented this review process. As a result, IRS was not in a good position to identify problem areas and the action(s) needed to correct them. We found that various methods of evaluation were being used by the four regions we visited.

Recommendations

To reduce the inconsistencies in the rate reduction process, we recommended that the Commissioner of Internal Revenue (1) establish uniform criteria and standard procedures for reviewing employers' requests for a reduction from the reporting of 8 percent of gross receipts as tip income and (2) monitor the implementation of the review process to assure a reasonably consistent IRS-wide approach.

**Appendix IV
Tax-Related Recommendations Made During
Calendar Year 1986 to the Treasury, IRS, and
BATF and Their Responses to Those
Recommendations**

**Action Taken And/or
Pending**

IRS agreed with our recommendation and, in October 1986, revised its criteria for making certain refunds.

**Appendix IV
Tax-Related Recommendations Made During
Calendar Year 1986 to the Treasury, IRS, and
BATF and Their Responses to Those
Recommendations**

**Actions Taken And/or
Pending**

IRS agreed with our first recommendation and has already taken steps to clarify the information returns forms and instructions on commodity credit loan and crop insurance income. IRS disagreed, however, with our recommendation to incorporate information returns into its document matching program. IRS reasoned that existing statutory rules present serious administrative problems for matching. IRS has since indicated a willingness to explore the use of an alternative matching program for specific crop loan and insurance data to detect nonfilers and under-reporters for this type of income. We plan to monitor IRS' planned alternative approach.

BATF Should Advise Former Firearms Dealers That They May Unknowingly Be Violating State Laws

(GAO/GGD-86-49, 6/5/86)

BATF regulations allow NFA dealers, except for partnerships and corporations, to retain their NFA firearms inventories when they discontinue their status as NFA dealers. However, some former dealers that operated as sole proprietorships and who retained, as individuals, the weapons they acquired as dealers, may unknowingly be violating their state laws. We contacted the District of Columbia and nine states, which have laws that permit dealers, but not individuals, to possess one or all of the NFA-type weapons to determine if individuals in this situation were violating their laws. The seven jurisdictions that responded informed us that former dealers who continue to possess certain NFA weapons as individuals either were or appeared to be violating their jurisdictions' laws.

Recommendations

We recommended that the Director, BATF:

- Inform former NFA dealers who currently possess NFA weapons that such possession may be in violation of the laws of their respective jurisdictions; and
- Develop a way to inform current NFA dealers and those that apply for NFA dealer status that they may be in violation of local laws if they retain private ownership of NFA weapons.

Actions Taken And/or Pending

BATF agreed with our recommendations and is developing notifications to inform former, current, and future NFA dealers of the possible problems they may face due to the retention of certain NFA weapons as private citizens.

IRS Should Increase Compliance With Wagering Occupational Excise Taxes

(GAO/GGD-86-49, 6/5/86)

Compliance with the tax on gross wagers and the wagering occupational tax could be improved if IRS better utilized information already required and obtained information readily available to identify noncompliant taxpayers. Information is readily available from state gambling agencies to identify businesses liable for the annual occupational tax and the tax on gross wagers, but IRS is not using this information to identify delinquent taxpayers.

In addition, IRS already has a means to identify employees/agents liable for the annual occupational tax because the returns filed by businesses (employers) require a listing of employee/agents on behalf of the business. However, IRS does not enforce the requirement or use the information when it is provided to determine whether the employee paid the taxes.

Recommendations

We recommended that the Commissioner of Internal Revenue:

- Obtain gambling license data from states where gambling activities subject to the wagering taxes are authorized and match it with the yearly occupational tax payment records to identify for follow-up potential noncompliant taxpayers.
- Compare tax on gross wagers payment records with the yearly occupational tax payment records for businesses in states which do not license establishments subject to the taxes to identify for follow-up potential noncompliant taxpayers.
- Match the names of employee/agents listed on the employers' occupational tax returns with occupational tax payment records to identify for follow-up potential noncompliant taxpayers. For the match to be effective, the requirement that employers list employee/agents on their occupational tax returns should be enforced.

Actions Taken And/or Pending

IRS responded that our recommendations would not have a significant enough impact on either voluntary compliance or revenues to justify implementation and that its limited resources would be more productively utilized in other areas. We noted in the report the reasons we believed our recommendations should be implemented and pointed out that IRS should advise Congress of its inability to improve compliance because of higher priority work.

**IRS Needs to Improve
the Accuracy of
Nonwage Income Data**

GAO/IMTEC-86-17, 4, 21/86)

In 1962, Congress established the Information Returns Program in IRS to encourage taxpayer compliance with the tax laws and to generate additional revenues. Among other things, the program matches interest and dividend information that banks and other payers submit to IRS with income reported on tax returns. This is intended to identify taxpayers who have underreported their income or have failed to file tax returns.

Because of inadequate controls, IRS did not record or incorrectly recorded over \$3.5 billion in income data for tax year 1983. About 4.1 million unprocessed information returns (from the Atlanta, Cincinnati, and Kansas City Service Centers) on 58 computer tapes were not recorded on the information returns master file and over 700,000 information returns from all 10 of IRS' service centers were miscoded on the master file. As a result, IRS will not identify all taxpayers who are underreporting their income and it will lose millions of dollars in tax revenues.

Recommendations

We made no recommendations because after we informed IRS of our findings, IRS said that it would take several actions in response to the problems we identified

**Actions Taken And/or
Pending**

In response to our findings, IRS added automated edit checks to its computer programs to identify incorrect data, and added a daily log to help assure it processes all computer tapes containing income information. In addition, IRS was able to recover some of the unrecorded information. While it was too late to use this information in its current underreporter program, IRS said it could use the information for other purposes, such as helping it classify cases for potential audit. IRS also instituted follow-up procedures to ensure that corrected data are posted.

Contingency Plans and Risk Analyses Are Needed for IRS Computer Centers

(GAO/IMTEC-86-10, 3/27/86)

IRS relies heavily on computers to process tax returns and receipts and to aid enforcement. Any major loss or damage to its computer equipment, software, or data would limit its ability to collect over \$600 billion in annual revenue and pay about \$85 billion in tax refunds.

IRS' tax return processing system is comprised of two major components—the National Computer Center in Martinsburg, West Virginia, which maintains a master file account on each individual and business taxpayer; and the 10 service centers, which receive and control tax returns and subject them to validity and consistency checks and mathematically verify taxpayers' computations. IRS' Detroit Data Center is responsible for IRS' administrative systems, tax analysis systems, and many of its management information systems.

To reduce disruption caused by events that prevent normal operation at computer centers, the Office of Management and Budget's Circular A-130 requires each agency head to set up an automatic data processing (ADP) security program. Among other things, each agency is required to do the following:

- Develop and maintain contingency plans that will provide reasonable continuity of data processing support should events occur that prevent normal operations. (These plans should be periodically reviewed and tested.)
- Conduct periodic risk analyses at each computer center to determine that center's vulnerabilities and to effectively use security resources to reduce potential loss. These analyses must be performed before a new center is designed, or whenever a significant change to the physical facility, hardware, or software occurs; or at least every 5 years.

IRS' Internal Revenue Manual also requires that ADP contingency plans be developed, maintained, and tested for each of the 12 IRS computer centers. The manual notes that plans must be developed to respond to fire, flood, sabotage, serious equipment damage or failure, loss of electrical power, bomb threats or explosion, and civil and natural disasters.

We found that IRS' draft ADP contingency plans are incomplete. Further, IRS has not taken adequate measures to prepare for an emergency.

**IRS Needs to Improve
the Accuracy of
Claims Filed Against
Businesses Undergoing
Liquidation
Bankruptcy**

(GAO/GGD-86-20, 2, 21/86)

Bankruptcy distribution is based on the amounts and the priority of the delinquencies shown on the claims that are filed; therefore, an inaccurate claim can result in the inequitable distribution of payments that are made. In the three bankruptcy court districts we visited, IRS filed claims for more than 95 percent of the liquidation bankruptcies filed in 1982. However, 77 percent of these cases contained errors totaling an estimated \$1.7 million in overclaims, underclaims, and misclassified priorities. Overclaims and underclaims resulted because IRS incorrectly applied bankruptcy rules for penalties, inadequately followed up on estimated claims, and made mathematical errors in computing claim amounts. Those errors, along with errors in classifying priorities, occurred because IRS district personnel lacked guidance in computing interest and penalties for bankruptcies.

Recommendation

We recommended that the Commissioner of Internal Revenue revise the bankruptcy manual to require that bankruptcy case files contain adequate documentation of claim computations and that supervisory or quality control reviews of these computations be made to ensure that claims are accurately prepared.

**Action Taken And/or
Pending**

On December 5, 1986, IRS revised the Internal Revenue Manual to require that bankruptcy case files contain adequate documentation of claim computations to facilitate more thorough reviews.

Tax-Related Recommendations Made During Calendar Year 1986 to the Treasury, IRS, and BATF and Their Responses to Those Recommendations

IRS Needs to Improve Its Procedures for Referring to Court Businesses That Accumulate Employment Tax Delinquencies During Bankruptcy

(GAO/GGD-86-20, 2/21/86)

IRS must use the bankruptcy courts to pursue action against businesses that accumulate employment tax delinquencies during bankruptcy. IRS should make court referrals quickly to minimize the accumulation of additional tax delinquencies. However, in the three IRS districts we reviewed, there were 10 referrals for delinquent employment taxes and these cases took an average of 15 months to come to court after the first delinquent tax return was due. This was caused partly by the fact that IRS' bankruptcy manual contains limited and inconsistent guidance on when court referrals should be made. The manual also lacked adequate guidance concerning what information should be obtained and provided to counsel for each referral.

Recommendation

We recommended that the Commissioner of Internal Revenue establish minimum criteria in the bankruptcy manual for the referral of delinquent cases to the bankruptcy courts and state in the manual that each referral should include information on the size of its employment tax liability.

Action Taken And/or Pending

On December 5, 1986, IRS revised its Internal Revenue Manual to include minimum criteria for referral of cases for bankruptcy court action.

Congress Should Decide Whether the Current Tax Exemptions for Blue Cross and Blue Shield Health Insurance Plans Are Warranted

(GAO/HRD-86-110, 7/11/86)

IRS has recognized the exemption of the Blue Cross and Blue Shield health insurance plans as social welfare organizations since their inception in the 1930s. These exemptions were initially recognized when the plans pioneered health insurance, offering one community rate to all subscribers. At that time, lack of information on the actuarial soundness of this type of venture deterred commercial companies from underwriting the costs of hospital care. After commercial companies entered the field in the 1940s, a competitive for-profit health insurance industry developed.

On December 16, 1985, the House of Representatives passed H.R. 3838, the Tax Reform Act of 1985. Section 1012 of the bill, which was estimated to raise \$1.7 billion in federal revenues over the next 5 years, would have effectively eliminated the existing tax exemption granted to Blue Cross and Blue Shield plans. However, the bill allowed for special treatment, at the discretion of the Secretary of the Treasury, for that portion of the plans' business related to high-risk individuals and small groups.

The Chairman of the Subcommittee on Health, House Committee on Ways and Means, asked us to provide information to assist the Tax Reform conferees in determining whether the Blue Cross and Blue Shield plans' tax-exempt status was warranted. In response, we compared certain practices of the plans, such as pricing methods, benefits provided, and underwriting, with those of for-profit health insurance companies, particularly as these practices affect the availability of coverage for high-risk persons. We focused on the availability of coverage for high-risk individuals under age 65 because practices of the plans and commercial insurers do not differ significantly in other health insurance markets. Specifically, we compared health insurance offered to 129 high-risk test cases identified by the Blue Cross and Blue Shield in six locations to insurance available from five commercial insurers.

We observed more similarities than differences in the insurance practices of Blue Cross and Blue Shield and commercial insurers with regard to high-risk individuals. Also, IRS officials had found that the significant differences between nonprofit and for-profit insurers that may have justified the initial tax exemptions had been eroded by competitive developments. For various reasons discussed in the report, we were unable to determine the overall effect changes in the tax-exempt status of Blue Cross and Blue Shield plans would have on both the availability and

**Investment Tax Credit
for Offshore Drilling
Rigs Needs
Clarification**

(GAO/GGD-86-65, 4/10/86)

Congressional intent regarding the scope of allowing the investment tax credit for offshore drilling rigs was unclear. The Conference Report for the Tax Reduction Act of 1975 stated that Congress intended to limit the credit to only those offshore rigs used in the northern portion of the Western Hemisphere. However, under section 48(a)(2)(B)(iii) of the Revenue Act of 1962, IRS allowed the investment tax credit for certain offshore rigs used anywhere in the world. This section was not amended by the 1975 act. We estimated that at least \$344 million of investment tax credit had been available since 1975 for offshore drilling rigs used outside the northern portion of the Western Hemisphere. Therefore, significant tax revenue could have been lost, and additional revenue foregone unless Congress clarified the law.

**Matter for Consideration
by Congress**

We suggested that if the investment credit was not repealed, Congress consider clarifying the circumstances under which the investment tax credit is allowed for offshore drilling rigs used outside the northern portion of the Western Hemisphere.

**Action Taken And/or
Pending**

The Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) repealed the investment tax credit.

**Appendix III
Legislative Actions Taken on
Recommendations Made During Calendar
Year 1986**

taxpayers can satisfactorily demonstrate to IRS that they cannot obtain reasonably dependable estimates of the cost to complete or the extent of progress toward completion of a particular contract.

**Action Taken And/or
Pending**

The thrust of our recommendation was included in the Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986). Among other things, Congress revised the tax law as it applied to long-term contracts and limited the use of the completed contract method for all but certain small construction contractors. Long-term contractors are now required to account for their contracts using one of two methods: (1) a modified percentage of completion method; or (2) a "60-40 method" under which 40 percent of contract income is accounted for by using the modified percentage of completion method and 60 percent is accounted for by using some other permissible method (e.g., cash, accrual or completed contract).

**Congress Should
Amend the Internal
Revenue Code
Regarding
Transactions Between
Foreign-Owned U.S.
Corporations and
Their Noncorporate
Foreign Owners**

(GAO/GGD-86-19, 11/1/85)

Under section 6038A of the Internal Revenue Code, certain foreign-owned U.S. corporations are required to submit an information return to IRS if they conduct transactions with a related domestic or foreign corporation. This was intended to enhance the compliance of foreign-owned U.S. corporations with the tax laws.

We expressed concern that the language of section 6038A was not sufficiently broad to ensure maximum compliance. For example, according to IRS, some foreign-owned U.S. corporations may have transactions with related foreign individuals and related noncorporate foreign entities, such as trusts and partnerships, that would not have to be reported to IRS under section 6038A. Although IRS could not quantify the extent of these transactions, its position was that the transactions should be reported even if the number is relatively small. Therefore, an amendment to section 6038A was needed to help IRS enforce the tax laws by identifying transactions between foreign-owned U.S. corporations and their noncorporate foreign owners.

Recommendation

We recommended that Congress amend section 6038A of the Internal Revenue Code to help IRS enforce the tax laws by identifying transactions between foreign-owned U.S. corporations and their noncorporate foreign owners.

**Action Taken And/or
Pending**

Congress included our suggested change in the Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986). Under the act, a corporation subject to the reporting requirements of Section 6038A of the Internal Revenue Code must report to IRS certain information with respect to its transactions with all related persons (as defined in the Code), and not merely its transactions with corporations in its controlled group. In addition, U.S.-controlled foreign corporations, foreign-controlled U.S. corporations and foreign-controlled foreign corporations doing business in the United States must report to IRS certain information regarding their transactions with any related party.

Congress Should Consider Whether to Amend the Tax Code to Require Acquisition Costs to Be Allocated Over the Life of Property/Casualty Insurance Contracts

(GAO/GGD-85-10, 3/25/85)

One income measurement issue in the property/casualty insurance industry is the proper allocation of business expenses related to the sale and renewal of insurance policies. These expenses are considered part of the acquisition costs and include agent and broker commissions, salaries of certain employees involved in underwriting and issuing policies, and medical and inspection fees. The National Association of Insurance Commissioners, whose accounting method was adopted for federal tax computations, currently permits these costs to be deducted immediately regardless of the life of the policy. On the other hand, premium income on insurance contracts is included in revenues only on a pro-rata basis each year. Assuming that a 1-year contract is issued on July 1, for example, only 6 months or one-half of the annual premium would be included as income in the first year, and the balance would not enter into taxable income until the following year.

We believe that, for the proper measurement of taxable income, expenses should be allocated over the same period in which the corresponding income is recognized. Therefore, using the regulatory accounting practices of the National Association of Insurance Commissioner's to measure taxable income is inappropriate because it does not match expenses with associated revenues, thereby resulting in misstated taxable income.

Recommendation

We recommended that if Congress wished to assure that the property/casualty insurance industry's revenues and expenses were more closely matched for purposes of measuring taxable income, it should consider amending the tax code to provide that acquisition costs be allocated over the life of related contracts.

Action Taken And/or Pending

Section 1021 of the Tax Reform Act of 1986 (Public Law 99-514, dated October 22, 1986) provided, in effect, that acquisition costs would be allocated over the life of the contract, as we recommended.

**Legislative Change
Needed to Enable IRS
to Assess Taxes
Voluntarily Reported
by Taxpayers in
Bankruptcy**

(GAO/GGD-83-47, 6/20/83)

The Bankruptcy Reform Act provides qualified debtors with certain protections from creditors including IRS. The act restricts IRS' authority in many cases to assess, collect, or recover a claim against an individual or a business during bankruptcy proceedings. Administratively, this restriction has caused problems for IRS because it requires IRS to stop its automated processing of returns from bankrupt taxpayers and perform many special processing steps. These steps include manual processing procedures at IRS service centers and district offices. During fiscal year 1982, these additional process steps cost IRS an estimated \$500,000.

Recommendation

We recommended that the Bankruptcy Act be amended to allow assessment of the taxes that bankrupt taxpayers report on their returns. Allowing IRS to assess, but not collect, these taxes would still protect bankrupt taxpayers but at less cost to IRS than is presently being incurred.

**Action Taken And/or
Pending**

No action was taken or planned as of September 30, 1987.

Open Recommendations to Congress From Reports Issued Before Calendar Year 1986

Congress Should Adopt a Tax Treatment Which Better Recognizes Changes in Some Electric Cooperatives

(GAO/GGD-83-7, 1/5/83)

Under section 501(c)(12) of the Internal Revenue Code, electric cooperatives are provided tax-exempt status and are permitted to earn substantial untaxed income from nonmember sources, which subsidizes cooperative members' cost of electricity. This exemption was initially granted over 60 years ago when electric cooperatives were generally small, struggling associations that primarily distributed electricity to sparsely populated rural areas. Since that time, however, the operation of many cooperatives and the environment in which they do business have changed substantially.

Today, many electric cooperatives are still small associations that continue to need assistance in order to provide electricity to rural areas at rates comparable to those charged in urban areas. Others, however, have substantially changed in character or have progressed to the point where they closely resemble their taxable counterparts. Yet, unlike other federal assistance programs that can be directed to those organizations having a continuing need for assistance, all electric cooperatives continue to benefit from tax exemption. Under the broad requirements of the law, tax exemption applies across-the-board to all electric cooperatives.

IRS, in administering the tax exemption requirements, has tried to recognize the changes in electric cooperatives. However, it has experienced difficulties because of the broad nature of the law. Therefore, Congress needs to consider alternatives to the present tax treatment of electric cooperatives and adopt a treatment which would better recognize the changes in their operations and the environment in which they operate. As a framework for Congress' consideration, we proposed alternatives to the present law which would (1) modify electric cooperatives' non-member income allowance, or (2) eliminate that allowance, or (3) apply tax rules already applicable to other types of cooperatives. These alternatives, which would have an estimated revenue impact ranging from \$2 million to \$45 million are not all inclusive.

Recommendation

We recommended that Congress, using the alternatives we provided as a guide, establish a tax treatment which better addresses electric cooperatives' present operating environment.

Open Recommendations to Congress From Reports Issued During Calendar Year 1986

The Internal Revenue Code Should Be Amended to Give IRS an Interest-Free Period to Process Refunds Claimed on Most Amended Returns

(GAO/GGD-86-72. 7/28/86)

Section 6611 of the Internal Revenue Code provides that if the Internal Revenue Service (IRS) does not process and issue an income tax refund within 45 days of the overpayment date, it must pay interest. The overpayment date is the due date of the tax return or the date the return is filed, whichever is later. The 45-day processing period does not apply to refunds claimed on most amended returns because the date of overpayment is considered to be either the filing date or due date of the original tax return, whichever is later.

Since taxpayers have up to 3 years to file an amended return and interest must be paid back to the overpayment date of the original tax return, IRS may ultimately pay several years of interest on a refund, regardless of how quickly it processes the amended return. Based on our sample of refund claims paid by IRS in fiscal year 1983, we estimated that IRS processed about 1.5 million amended returns and paid \$419.4 million in interest on the resulting refunds. We further estimated that \$330.3 million of this interest involved returns for which IRS does not have an interest-free processing period. These latter returns were filed an average of 1 year from the time the original returns were filed, and they took an average of about 81 days to process.

Matter for Consideration by Congress

So that IRS can reduce the amount of interest paid on amended returns claiming refunds, we suggested that Congress consider amending section 6611 of the Internal Revenue Code to provide IRS with an interest-free processing period for such returns. We did not attempt to determine how long this interest-free period should be. However, a 45-day processing period would make treatment of amended returns consistent with the treatment of original income tax returns.

Action Taken And/or Pending

No action was taken or planned as of September 30, 1987.

Contents

Abbreviations

APO/FPO	Army Post Office/Fleet Post Office
ACS	Automated Collection System
ADP	Automatic Data Processing
BATF	Bureau of Alcohol, Tobacco and Firearms
CEPS	Capacity Enhancement for the Processing System
ERISA	Employee Retirement Income Security Act
ESOP	Employee Stock Ownership Plan
GAO	General Accounting Office
IRS	Internal Revenue Service
NFA	National Firearms Act
PAL	Protection Against Loss
SSA	Social Security Administration
TEFRA	Tax Equity and Fiscal Responsibility Act

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the Director of the Bureau of Alcohol, Tobacco and Firearms (BATF) and their responses to those recommendations.

V. Summary of information on tax matters reported to Congress during calendar year 1986

VI. Listing of GAO products on tax matters issued during calendar year 1986.

VII. Listing of testimonies given on tax matters by GAO officials before various committees of Congress during calendar year 1986.

VIII. Tax-related assignments authorized pursuant to 31 U.S.C. 713 during calendar year 1986.

IX. GAO Order relating to audit assignments involving access to tax information.

We are pleased to report that the Department of Treasury, Internal Revenue Service, and BATF have taken, or plan to take, action on most of the recommendations we made during calendar year 1986. Also, various congressional members and committees used our products on tax policy and administration matters in overseeing tax administration operations and in considering tax reform. In this regard, the Tax Reform Act of 1986 included the thrust of our various recommendations, including those relating to property/casualty insurance, foreign-owned U.S. corporations, and the completed contract method of accounting.

We look forward to continuing to work closely with Congress in its oversight of tax policy and administration matters and to assist it in considering our legislative recommendations. Also, we would be glad to discuss any of the matters included in the appendixes if you, your colleagues, or staffs believe it would be beneficial.

We are sending copies of this report to the Director of the Office of Management and Budget; the Secretary of the Treasury; the Commissioner of Internal Revenue; and the Director, BATF. We are also sending copies

