



*Controls Over Outside Employment Are
Not Sufficient to Prevent or Detect
Conflicts of Interest*

September 29, 2014

Reference Number: 2014-10-073

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

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HIGHLIGHTS

CONTROLS OVER OUTSIDE EMPLOYMENT ARE NOT SUFFICIENT TO PREVENT OR DETECT CONFLICTS OF INTEREST

Highlights

Final Report issued on September 29, 2014

Highlights of Reference Number: 2014-10-073 to the Internal Revenue Service Human Capital Officer.

IMPACT ON TAXPAYERS

Generally, IRS employees are allowed to engage in outside employment or business activities after obtaining written approval. Effective controls over outside employment can reduce the risk of conflicts of interest that could result in decisions that are not in the best interest of American taxpayers.

WHY TIGTA DID THE AUDIT

The overall objective of this audit was to determine whether the IRS has controls in place to provide reasonable assurance that outside employment requests are documented and reviewed for conflicts with employees' official duties.

WHAT TIGTA FOUND

IRS records indicate that, in Calendar Year 2011, nearly 3,000 of the more than 6,000 active, full-time IRS employees who held jobs or participated in business activities outside the IRS did not obtain documented approval, as required by Department of the Treasury regulations and IRS policies. IRS Human Capital Office management was generally not aware of the number of employees with unapproved outside employment because responsibility has not been assigned for overseeing the overall outside employment process. In addition, the IRS stated that it does not have authorization to use taxpayer information (*e.g.*, Form W-2, *Wage and Tax Statement*) to identify employees with unapproved outside income because Internal Revenue Code Section 6103 does not clearly

provide that tax data can be used for this purpose.

It will be difficult for the IRS to monitor outside employment because 93 percent of the existing records in the database used to compile outside employment requests are out of date. Moreover, approval of outside employment requests is not always documented on the database or in Official Personnel Folders, in part because of confusing and incomplete guidance.

Improving controls will be important because TIGTA identified current and former IRS employees with both actual and potential conflicts of interest. One employee pled guilty to engaging in a criminal conflict of interest for accessing taxpayer information for the purpose of conducting a private tax and accounting business, 44 IRS employees prepared tax returns for compensation (a prohibited practice), and TIGTA's analysis identified 20 employees with a high risk of potential conflicts of interest who received outside income without documented approval. For example, four employees operated businesses with annual gross receipts ranging from more than \$500,000 to more than \$7 million, and six employees had wages of more than \$50,000 from outside of the IRS. Significant outside income could impact the employee's effectiveness on the job.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS Human Capital Officer update outside employment guidance, appoint management responsibility for overseeing the outside employment process, evaluate whether legislation would be needed to authorize the IRS to perform analyses of employee income information to identify employees with unapproved outside employment, and perform a one-time cleanup of the outside employment database.

In their response, IRS management agreed with three of our recommendations. However, they did not agree that income information should be used to detect IRS employees engaging in potential conflicts of interest. TIGTA continues to believe the IRS should evaluate whether legislation would be needed to allow it to detect employees with outside employment.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 29, 2014

MEMORANDUM FOR INTERNAL REVENUE SERVICE HUMAN CAPITAL OFFICER

FROM:

Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT:

Final Audit Report – Controls Over Outside Employment Are
Not Sufficient to Prevent or Detect Conflicts of Interest
(Audit # 201310009)

This report presents the results of our review to determine whether the Internal Revenue Service (IRS) has controls in place to provide reasonable assurance that outside employment requests are documented and reviewed for potential conflicts with employees' official duties. This review is included in the Treasury Inspector General for Tax Administration's Fiscal Year 2014 Annual Audit Plan and addresses the major management challenge of Human Capital.

Management's complete response to the draft report is included as Appendix VII. We have concerns about certain statements in the IRS's response to our report. We have noted these concerns in Appendix VIII.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. If you have any questions, please contact me or Gregory D. Kutz, Assistant Inspector General for Audit (Management Services and Exempt Organizations).



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Prevent or Detect Conflicts of Interest*

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Abbreviations

| | |
|-------|---|
| IRS | Internal Revenue Service |
| OES | Outside Employment System |
| OPF | Official Personnel Folder |
| TIGTA | Treasury Inspector General for Tax Administration |



Controls Over Outside Employment Are Not Sufficient to Prevent or Detect Conflicts of Interest

Background

Internal Revenue Service (IRS) records indicate that, in Calendar Year 2011, more than 6,000¹ of the IRS's total of 78,000 employees² who were active and full time also held jobs or participated in business activities outside the IRS. To avoid conflicts of interest and to maintain the highest degree of ethical conduct, Department of the Treasury regulations and IRS policies require employees to obtain written, supervisory approval before engaging in any outside employment.³ The outside employment must not conflict with the employee's official IRS duties or impact the employee's effectiveness on the job, and must conform to the general ethical requirements in the Office of Government Ethics *Standards of Ethical Conduct for Employees of the Executive Branch* and to specific requirements in the *Department of the Treasury Supplemental Standards of Ethical Conduct*.⁴ With certain exceptions, activities that involve preparing tax returns for compensation and bookkeeping or accounting related to any tax matter are prohibited.⁵ Additional information about the general rules for outside employment and business activities is included in Appendix V.

IRS employees can request approval for outside employment by preparing Form 7995, *Outside Employment or Business Activity Request*,⁶ or by inputting the information into the IRS's Outside Employment System (OES). The OES was implemented in Fiscal Year 1999 and serves as a single repository for information from Forms 7995, rather than having paper copies maintained in various offices. It also allows supervisors to review the requests online, which is important because not all supervisors are located in the same office with their employees, and IRS management must approve or disapprove the request on the OES within 10 business days of

¹ This figure excludes IRS Office of Chief Counsel employees because they follow a different outside employment process.

² See Appendix I for our methodology for determining these figures.

³ IRS employees are allowed to engage in certain outside activities that are not considered employment or business-related without approval. See Appendix V for a list of these activities.

⁴ IRS employees sign an acknowledgement of their receipt and understanding of these standards when they are hired by the IRS.

⁵ Employees may engage in bookkeeping and accounting that is directly related to a tax determination in the following situations: keeping the books for a firm owned or run by immediate family and prospects for a conflict of interest are remote; engaging in the activity for a civic, religious, educational, or charitable non-profit organization, where the employee is not paid for the work; or engaging in business with your spouse with permission.

⁶ IRS Office of Chief Counsel employees use Form 7995-A, *Chief Counsel Outside Employment or Business Activity Request*, to request outside employment. However, the information from this form is not maintained on the Outside Employment System module of the Totally Automated Personnel System, which houses a database comprised of IRS employee requests for outside employment.



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receipt of a fully completed Form 7995.⁷ If an employee does not have access to the OES, a paper Form 7995 may be submitted and the supervisor is required to input the completed form on the OES. Additionally, it is the employee's responsibility to submit a new Form 7995 or input a new request into the OES and void any previously approved requests whenever his or her outside employment or IRS employment changes, such as if the employee moves to another location or changes position or job duties. Seasonal employees in non-duty status may engage in outside employment or business activities without prior written approval, but they cannot engage in prohibited activities, and they must submit an outside employment request upon their return to duty status to continue the outside employment.

The employee's immediate supervisor is responsible for reviewing the request to determine if there is a conflict of interest or if the request conflicts with applicable ethics rules, as well as entering the approval or disapproval date on the OES. Any additional reviewers must also input their approval date to the OES, including second-level managers and the IRS Labor Relations⁸ office when assistance is requested at any level of review. Approved requests should be printed from the OES and placed in the supervisors' employee "drop file," and mailed to the Official Personnel Folder (OPF) Consolidated Site to be placed in the employee's official personnel file.

Annually, supervisors are required to review all their employees' OES records to determine if there are any changes in the employees' outside employment or business activities. If there are no changes, the supervisor must enter the review date on the OES. If the information is incorrect, the supervisor should enter the date the employment or business activity changed or ended, and the record will be moved to the OES historical file. A screen snapshot of the request should be marked "VOID" and mailed to the IRS OPF Consolidated Site to be filed in the employee's official personnel file.

This review was performed with information obtained from the IRS Human Capital Office located in Washington, D.C., and from the OPF Consolidated Site in Lee's Summit, Missouri, during the period July 2013 through March 2014. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We limited the scope of our analysis to IRS employees who were full time and active during every pay period in 2011, excluding IRS Office of Chief Counsel and seasonal employees. Chief Counsel employees follow a different outside employment process that we did not review. Seasonal employees were

⁷ Supervisors may return incomplete Forms 7995 or request that additional information be included with the employee's request. For example, our review noted some Forms 7995 that included attached memorandums detailing duties that would be performed as part of outside employment and statements that prohibited activities would not be performed.

⁸ The Labor Relations/Employee Relations Field Operations Office provides guidance and representation to IRS management in areas such as contract and agency grievances; discipline, adverse, and performance cases; interaction and contractual obligations with National Treasury Employees Union; and outside employment requests.



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excluded because they generally work at the IRS for only several months of the year. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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Results of Review

A Significant Number of Employees Conduct Outside Business Activities Without Properly Documented Approval

IRS records indicate that nearly 3,000⁹ (approximately 50 percent) of the more than 6,000 full-time, active IRS employees who received income or participated in business activities outside the IRS during Calendar Year 2011¹⁰ did not have approval for outside employment or the activities were not documented on the OES as required. Prior to January 2012, employees were required to manually submit Form 7995 to their supervisor to request approval for outside employment and IRS Labor Relations assistants input the Forms 7995 to the OES. Beginning in January 2012, this process was automated and employees had the option to use the OES or submit a Form 7995. If an employee chose to submit a Form 7995, the supervisor was responsible for adding the data from Form 7995 to the OES. A memorandum was issued explaining the new process but guidance that has been provided is confusing and incomplete. For example:

- The Internal Revenue Manual has not been updated to include the new requirement to submit outside employment requests through the OES.
- Outside employment guidance is provided to new employees¹¹ during the onboarding¹² process, but periodic or annual reminders are not provided.
- Current and up-to-date guidance is available on the IRS intranet, but employees may not be aware of or find the location of the guidance unless they know to search for it. In

⁹ This is 3.8 percent of the nearly 78,000 full-time, active IRS employees (excluding Office of Chief Counsel employees). We originally identified more than 3,500 employees who potentially held jobs or participated in business activities outside the IRS during Calendar Year 2011 and did not have approval for outside employment on the OES current file. However, we estimate that more than 500 had either requested approval for outside employment, but the outside employment was no longer active and the approval had been moved to the OES historical records as of the time of our review, or we determined that the name on the Form W-2, *Wage and Tax Statement*, did not match the employee's name on the Treasury Integrated Management Information System.

¹⁰ These employees had one or more Forms W-2 or filed a Form 1040, *U.S. Individual Income Tax Return*, Schedule C, *Profit or Loss From Business*, associated with their Social Security Number, in addition to their IRS income.

¹¹ Employees are required to sign the *Plain Talk About Ethics* document during the onboarding process, which details the outside employment restrictions.

¹² Onboarding is a year-long process which integrates new employees into the workforce. It includes manager preparation for their arrival, a comprehensive first day orientation, and programs throughout the first year of employment to build engagement.



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addition, not all IRS employees are assigned computers. Those IRS employees who are not assigned computers have access to computer kiosks and must leave their workspace to search the intranet or submit the OES requests.

- One IRS division¹³ may have caused confusion by issuing guidance that employees should submit Forms 7995 and also input their requests into the OES.

Supervisors should especially be concerned about employees with a higher risk for conflicts of interest¹⁴ because of the nature of their positions. For example, employees who spend much of their workday outside the office could work on outside employment activities without being detected. In addition, employees who can access taxpayer account information on IRS computers and employees who can make changes to taxpayers' account information have a higher risk for a conflict of interest.

We determined that many of the more than 3,500¹⁵ employees who potentially held jobs or participated in business activities outside the IRS during Calendar Year 2011 without documented approval in the OES current file were in positions with a higher risk for conflicts of interest. For example, more revenue agents have unauthorized outside employment than any other position. Revenue agent positions have a higher risk for being involved in outside activities that could conflict with their official duties without being detected because they often work off-site. Revenue agents also examine tax returns and have access to taxpayer information available on IRS computer systems. Figure 1 highlights employee positions with the highest occurrences of potential unapproved outside income.¹⁶

¹³ The IRS is organized into business and functional operating divisions. The IRS's four business operating divisions serve groups of taxpayers, including the Large Business and International, Small Business/Self-Employed, Tax Exempt and Government Entities, and Wage and Investment Divisions. The IRS's functional operating divisions, including the Agency-Wide Shared Services organization, the IRS Human Capital Office, and the Information Technology organization, provide support services to the entire IRS organization.

¹⁴ Consistent with the general ethical requirements of the Office of Government Ethics Standards and IRS Policies and Procedures, outside employment should be approved in advance and must not conflict with the employee's official duties or have an impact on the employee's effectiveness on the job.

¹⁵ This number includes more than 500 employees who had requested approval for outside employment, but the outside employment was no longer active and the approval had been moved to the OES historical records as of the time of our review, or we determined that the name on the Form W-2 did not match the employee's name on the Treasury Integrated Management Information System. The Treasury Integrated Management Information System supports payroll and personnel processing and reporting requirements for the IRS.

¹⁶ The term unapproved outside income is used throughout this report to refer to those employees with multiple sources of income with no record of approval for outside employment. There are some activities that do not require written approval. See Appendix V for a list of these activities. We determined that only one of these activities, work performed for a credit union, would most likely result in the issuance of a Form W-2 to the employee. In our review of a sample of 136 of the more than 3,500 employees who held jobs or participated in business activities outside the IRS during Tax Year 2011 without documented approval in the OES current file, we did not identify that the income was related to work performed for a credit union.



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Figure 1: Top 10 Positions of Employees With Multiple Sources of Income and No Record of Approval on the OES Current File

| Position | Number of Employees |
|------------------------------------|----------------------------|
| Revenue Agents | 660 |
| Contact Representatives | 397 |
| Information Technology Specialists | 363 |
| Tax Examining Technicians | 343 |
| Revenue Officers | 242 |
| General Analysts | 175 |
| Management/Program Analysts | 150 |
| Criminal Investigators | 140 |
| Secretaries | 140 |
| Correspondence Examiners | 84 |

Source: Treasury Inspector General for Tax Administration's (TIGTA) analysis of the IRS Returns Transaction File Individual Master File¹⁷ and Forms W-2 file, the OES, and the Treasury Integrated Management Information System.

Although IRS policy requires that approval for outside employment be recorded on the OES, we found significant occurrences of employees receiving outside income without approval on the OES for outside employment. This indicates that IRS employees engaged in unapproved outside employment. IRS Human Capital Office management was generally not aware of the extent of unapproved outside employment by employees because responsibility for overseeing the overall outside employment process has not been assigned, including ensuring the records on the OES are kept up-to-date and accurate. In addition, IRS Human Capital Office management informed us that they do not conduct analyses to identify employees with secondary income because Internal Revenue Code Section (§) 6103¹⁸ does not clearly provide that IRS management can use tax data for this purpose. However, such an analysis would greatly improve the IRS's ability to reasonably assure that IRS employees who administer the tax laws comply with outside employment requirements. In addition, IRS Human Capital Office management stated that some employees may have submitted requests for outside employment using paper Forms 7995 that were approved by their supervisor but were never input to the OES. Without performing analyses to identify employees who have unapproved outside employment and assuring that

¹⁷ The Returns Transaction File Individual Master File is a database of individual tax return information, including tax return schedules, reformatted and posted to the Returns Transaction File On-Line.

¹⁸ Internal Revenue Code § 6103, *Confidentiality and Disclosure of Returns and Return Information*, requires that tax returns and return information shall be confidential, with certain exceptions. One exception is that returns and return information shall, without written request, be open to inspection by or disclosure to officers and employees of the Department of the Treasury whose official duties require such inspection or disclosure for tax administration purposes.



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employees and supervisors input all requests to the OES, the IRS is at increased risk that outside employment activities may be in conflict with employees' IRS responsibilities.

Recommendations

The IRS Human Capital Officer should:

Recommendation 1: Update the Internal Revenue Manual and associated outside employment guidance available to IRS employees and supervisors to include the requirements for using the OES to request and approve outside employment requests.

Management's Response: The IRS agreed with this recommendation. The IRS Human Capital Officer will update the Internal Revenue Manual and other related outside employment guidance to include the revised outside employment policy guidance and procedures.

Recommendation 2: Appoint management responsibility for overseeing the outside employment process, including providing reasonable assurance that OES records are kept up-to-date and accurate.

Management's Response: The IRS agreed with this recommendation. The Director, Workforce Relations Division, will provide clarification that the Associate Director, Labor Relations Strategy and Negotiations Policy, has program responsibility for the outside employment process.

Recommendation 3: Work with the IRS's Office of Chief Counsel to evaluate whether a legislative proposal is needed to amend Internal Revenue Code § 6103 to enable the IRS to use tax data to perform analyses and identify employees who have multiple sources of income without an approved request for outside employment.

Management's Response: The IRS disagreed with this recommendation. IRS management does not believe that sensitive taxpayer information should be used to oversee the IRS's outside employment program. Further, IRS management does not agree the IRS should be singled out to utilize such a method for oversight simply because it is the repository for, and custodians of, such information.

Office of Audit Comment: IRS employees have access to sensitive taxpayer information, which we believe creates an inherent risk for a conflict of interest as a result of any misuse of this information. IRS management agreed to three other recommendations in this report that will improve their ability to prevent employees from engaging in outside employment that may present a conflict with their IRS position. However, the greater risk lies in unapproved outside employment that this report indicates likely exists and will continue to go undetected without proactive analyses. Given the number of employees we identified without approval for their outside



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employment, we continue to believe the IRS should determine whether changes to Internal Revenue Code § 6103 are necessary to address this problem.

The Outside Employment Database Is Ineffective for Identifying Potential Conflicts of Interest

IRS management should monitor outside employment activities for conflicts of interest; however, this will be difficult to do because we determined that 93 percent of the records on the OES current file are out of date and the OES is incomplete. The *Department of the Treasury Supplemental Standards of Ethical Conduct* requires IRS employees to obtain approval for outside employment and IRS guidance requires supervisors to annually certify their employees' outside employment, also known as recertification. The OES is out of date because IRS supervisors generally do not annually recertify or document recertification of their employees' outside employment activities on the OES, and the database is incomplete because it does not contain records for nearly 3,000¹⁹ employees who had unapproved outside income. IRS Human Capital Office management was generally not aware of these conditions because guidance was not clear on how supervisors should document the annual recertification in the OES database; controls were not effective to identify supervisors who did not recertify and update existing outside employment records; and, as previously mentioned, analysis is not performed to identify employees with outside income who do not have approved outside employment requests on the OES.

OES records are not always recertified and records are out of date

To determine if OES records are up to date, we completed the following analysis:

- We analyzed the population of 21,979 records in the OES current file as of February 12, 2013, and found that 20,470 (93 percent) were out of date because supervisors had not recertified outside employment activities on the OES for more than one year.²⁰ This includes nearly 7,000 records where the outside employment had never been recertified, and two records that had not been recertified since 1983.
- We reviewed a random sample of 138²¹ of the 21,809 records in the OES current file and found that 13 (9 percent) employees received unapproved outside income in

¹⁹ These employees had one or more Forms W-2 or filed a Form 1040, Schedule C, associated with their Social Security Number, in addition to their IRS income.

²⁰ For purposes of our analysis, we reviewed the records to determine if they had been reviewed prior to February 12, 2012, which was one year prior to the date of the OES we reviewed.

²¹ The random sample was selected from 21,809 records instead of the total population of 21,979 records because 170 individuals who were not currently employed with the IRS as of the date of our review were eliminated. The personnel files for four employees were unavailable at the time of our review; therefore, we selected and reviewed four additional personnel files.



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Tax Year 2012 as reported on Forms W-2 and/or Form 1040, Schedule C, that did not match the approved outside employment. Based on these results, we estimate that 2,054²² of 21,809 outside employment requests are out of date because employees may have changed their outside employment and the OES has not been updated to reflect approval of the new outside employment activities.

In addition, questionnaires were sent to 101 supervisors of employees who received outside income in Calendar Year 2011 but had no approved outside employment request on the OES. Nearly one-half of the 97 supervisors²³ who responded to our questionnaire stated that they review outside employment forms annually. However, only three supervisors responded that the annual review is documented on the OES, which is a requirement of the 2012 IRS Outside Employment Policy and Procedures. Most supervisors responded that they either perform an informal review or maintain documentation locally.

The OES is incomplete

To determine if supervisors approved outside employment and forwarded Forms 7995 for placement in the employees' OPFs instead of documenting the approval on the OES, we completed the following analysis.

We reviewed the OPFs for a random sample of 136²⁴ employees with outside income that was not approved on the OES current file²⁵ during Calendar Year 2011. We found that:

- 8 employees had an approved Form 7995 in their OPF that matched the outside employment activities, as required. Based on these results, we estimate that there are 208²⁶ approved outside employment requests in OPFs that are not on the OES.

²² We are 95 percent confident that the number of outside employment requests that are out of date because employees may have changed their outside employment and the OES has not been updated to reflect approval of new outside employment activities is between 991 and 3,118.

²³ We selected a random sample of 136 of the more than 3,500 employees who received outside income in Calendar Year 2011, but had no approved outside employment request on the OES current file. The personnel file for one employee in our sample was unavailable at the time of our review; therefore, we replaced this employee with another employee. Questionnaires were sent to 101 of the employees' supervisors and responses were received from 97 of the supervisors. We did not send a questionnaire to the supervisors of 35 employees in the sample because: (1) the employees had previously requested approval for the outside employment, but it had been moved to the OES historical file at the time of our review; (2) the supervisors of the employees were no longer employed by the IRS at the time of our review; or (3) the employees had been referred to TIGTA's Office of Investigations. See Appendix VI for additional results.

²⁴ We selected a random sample of 136 of the more than 3,500 employees who received outside income in Calendar Year 2011, but had no approved outside employment request on the OES current file.

²⁵ These employees had one or more Forms W-2 or filed a Form 1040, Schedule C, associated with their Social Security Number, in addition to their IRS income.

²⁶ We are 95 percent confident that the number of approved outside employment requests that are in the OPFs and not on the OES is between 70 and 346.



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- 102 employees did not have approved Forms 7995 in their OPF that matched the outside employment activities. Based on these results, we estimate that there are 2,656²⁷ employees who are working outside the IRS without documented approval in either the OES or the OPF.
- 26 employees in our sample had either requested approval for the outside employment, but the record had moved to the OES historical file,²⁸ or we determined that the name on the Form W-2 did not match the employee's name.²⁹ These employees were therefore determined to be non-exceptions and were eliminated from further analysis.

More than one-half of the supervisors who responded to our questionnaire stated that the employees did not request approval for outside employment. Although some supervisors provided us with copies of an approved Form 7995 that was maintained locally, the outside employment process was not followed as these forms were missing from the OES, the OPF, or both.

We believe these conditions occurred in part because of confusing and incomplete guidance. For example, the Internal Revenue Manual, as previously mentioned, has not been updated to include the new requirement to submit outside employment requests through the OES and for supervisors to record the annual management recertification on the OES. When we informed IRS management of our concerns, they stated that they had already started updating guidance for all IRS managers and employees reminding them of the outside employment requirements. These actions had not been completed as of the end of our review in March 2014.

IRS management needs to be vigilant to provide reasonable assurance that employees and managers properly understand how to use the OES for outside employment. If employees do not request approval for outside employment, IRS supervisors do not have the opportunity to review the outside employment activities for conflicts of interest. In addition, if OES information is not accurate or if supervisors do not annually recertify outside employment, there is a risk that the employee's outside position could be different from what was originally approved and may result in a conflict of interest.

²⁷ We are 95 percent confident that the number of employees working outside the IRS without documented approval in either the OES or the OPF is between 2,402 and 2,909.

²⁸ Examples of when a record could move to the historical file include if the manager never approved the request or if the employee or supervisor removes the record when the employee is no longer engaged in the outside employment.

²⁹ One reason a mismatch can occur is because of employment-related identity theft.



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Recommendation

Recommendation 4: The IRS Human Capital Officer should, after establishing effective controls to use the OES to request and approve outside employment, require all supervisors to perform a one-time cleanup of the OES to correct outside employment data.

Management's Response: The IRS agreed with this recommendation. The Associate Director, Labor Relations Strategy and Negotiations Policy, will collaborate with Labor Relations/Employee Relations Field Operations to conduct a one-time cleanup of the OES.

Control Weaknesses Allowed Conflicts of Interest to Occur Without Detection and Current Potential Conflicts of Interest Exist

Because of weak controls over approving and documenting outside employment, there is a greater likelihood that employees who engage in outside employment that results in a conflict of interest will go undetected. Prior TIGTA investigations identified that actual conflicts of interest have occurred and TIGTA analysis identified that current IRS employees have potential conflicts of interest.

IRS employees have engaged in activities that conflict with their duties

In April 2013, one former employee pled guilty to engaging in a criminal conflict of interest for accessing taxpayer information for the purpose of conducting a private tax and accounting business. From Calendar Year 2005 through 2008, the employee accessed and obtained taxpayer information on an IRS computer system more than 2,000 times for the purpose of conducting a private tax and accounting business. The employee also directed unsuspecting, subordinate IRS employees to obtain information for him or her. These employees believed the information was being requested for official purposes.

In addition, TIGTA investigations that were closed between October 1, 2009, and July 31, 2013, showed that 44 IRS employees prepared tax returns for compensation (a prohibited practice), six employees' outside employment interfered with their IRS position, and four employees had outside employment that involved illegal or potentially unethical behavior. Case notes specified that five of these 54 employees did not obtain approval for the outside employment, and the case notes for the remaining employees did not specify whether approval was requested.



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Current employees have significant income from outside sources, which increases the risk of the outside employment interfering with their official duties

Through analysis of IRS records, we identified 20 employees with significant outside income; however, approval for outside employment was not documented on the OES or found in the OPF as required by IRS guidance.³⁰ Tax return information showed that four current employees (two of which are revenue agents) operated businesses with annual gross receipts ranging from more than \$500,000 to more than \$7 million. Additionally, 16 other employees earned unapproved outside income ranging from more than \$18,000 to nearly \$340,000, or 38 percent to more than 300 percent of their IRS wages. Six of these employees had wages of more than \$50,000 from outside of the IRS. According to the general ethical requirements of the Office of Government Ethics Standards and IRS Policies and Procedures, outside employment activities should not conflict with an employee's official duties or impact an employee's effectiveness on the job. IRS employees with the job responsibilities of these employees, including examining tax returns, collecting taxes, and maintaining IRS information systems, typically have access to taxpayer accounts on IRS computers. Significant outside income as an employee or business owner could conflict with the employee's official duties or impact the employee's effectiveness on the job.

³⁰ IRS management suggested that the approval could have been included in the employees' drop files.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to determine whether the IRS has controls in place to provide reasonable assurance that outside employment requests are documented and reviewed for potential conflicts with employees' official duties. To accomplish this objective, we:

- I. Evaluated the controls for requesting and approving outside employment requests to determine if reasonable assurance is provided that outside employment activities do not conflict with employees' official duties.
 - A. Determined IRS requirements for requesting and approving outside employment requests.
 - B. Determined if IRS employees with multiple sources of income request and managers approve the outside employment.
 1. Queried the Treasury Integrated Management Information System¹ and identified 77,872 IRS employees who were full time and active during every pay period of Calendar Year 2011. The 77,872 IRS employees were compared to Tax Year 2011 Form W-2, *Wage and Tax Statement*,² records and 4,171 employees were identified with income from the IRS and at least one additional source of income. The 77,872 IRS employees were also compared to the Tax Year 2011 Returns Transaction File Individual Master File³ and 3,275 employees were identified that filed a Form 1040, *U.S. Individual Income Tax Return, Schedule C, Profit or Loss From Business*, reporting outside income from business activities. The total number of full-time, active IRS employees who held jobs or participated in business activities outside the IRS in Calendar Year 2011 was adjusted to: 1) prevent double counting 327 employees with both Form W-2 and Form 1040, Schedule C, outside income; 2) eliminate those no longer employed by the IRS as of the date we performed our analysis; 3) exclude Office of Chief Counsel employees; and 4) exclude Forms W-2 issued from the Beckley Computing Center because these amounts are generally not for employment but for moving expenses, incentive payments, *etc.* This resulted in a total of 6,331 current IRS employees who were full time and active during every

¹ The Treasury Integrated Management Information System supports payroll and personnel processing and reporting requirements for the IRS.

² Forms W-2 are part of the IRS's Information Returns Master File that is housed at the Martinsburg Computing Center. Forms W-2 are filed by employers to report wages and other compensation paid to employees and to report other tax-related items like tax withholdings, 401(k) contributions, Social Security/Medicare taxes paid, *etc.*

³ The Returns Transaction File Individual Master File is a database of individual tax return information, including tax return schedules, reformatted and posted to the Returns Transaction File On-Line.



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pay period in Calendar Year 2011 with outside income. By comparing the 6,331 IRS employees to the OES current file, we found that 3,541 did not have properly documented approval for outside employment. We then estimated that 651 of these employees had either requested approval for outside employment, but the outside employment was no longer active and the approval had been moved to the OES historical records as of the time of our review, or the name on the Form W-2 did not match the employee's name on the Treasury Integrated Management Information System. This resulted in 2,890 employees who had unapproved outside employment. Validation testing of Form W-2; Form 1040, Schedule C; and Treasury Integrated Management Information System data were completed by comparing data from a sample of cases for all three files. Fields tested include Social Security Numbers, names, and tax year. Form 1040, Schedule C, information was compared to the Integrated Data Retrieval System⁴ for a sample of cases. In addition, data fields were reviewed to determine if fields were complete. These data were determined to be reliable for the purposes of this report.

2. Obtained OPFs for a random sample of 136 of the 3,541 IRS employees from Step I.B.1, based on a 95 percent confidence level, 10 percent error rate, and ± 5 percent precision rate. The OPFs were reviewed for copies of approved outside employment requests matching the income sources. Questionnaires were sent to 101⁵ supervisors of employees still employed by the IRS at the time of our review to determine whether the employees had requested approval for outside employment by a means other than the OES, and why the requests were not input to the OES. Our sampling plan and projections were reviewed by our contracted statistician.
- C. Identified cases involving substantiated conflicts of interest on the Performance and Results Information System⁶ for the period of Fiscal Year 2010 to July 31, 2013.
- II. Evaluated the controls for review and input of outside employment requests to determine if they are sufficient to maintain up-to-date and accurate information on the OES.
- A. Determined the requirements for input and review of existing outside employment requests on the OES database.

⁴ IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.

⁵ Questionnaires were not sent to the supervisors of 35 employees in the sample because (1) the employees had previously requested approval for the outside employment, but it had been moved to the OES historical file at the time of our review, (2) the supervisors of the employees were no longer employed by the IRS at the time of our review, or (3) the employees had been referred to TIGTA's Office of Investigations.

⁶ The Performance and Results Information System is the primary management information system for TIGTA's Office of Investigations. The Performance and Results Information System provides TIGTA the managerial ability to account for and track all leads developed by TIGTA, all complaints received from external sources, and all investigations initiated as a result of internal and external allegations.



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- B. Determined if supervisors are identifying changes in their employees' outside employment during the annual recertification by selecting and reviewing a random sample of 138 outside employment request records from the population of 21,809 records for current IRS employees on the OES as of February 12, 2013, using a 95 percent confidence level, 10 percent error rate, and ± 5 percent precision rate. We reviewed any Tax Year 2012 income information for the employees associated with the 138 sampled OES records and determined whether the 2012 payer information matched a record on the OES current file. Our sampling plan and projections were reviewed and agreed upon by our contracted statistician.
- C. Determined if the review date in the OES module had been updated to reflect the latest management recertification date through analysis of the 21,979 records in the OES current file as of February 12, 2013.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: Department of the Treasury regulations and IRS policies, procedures, and practices for reviewing, approving, and monitoring employee requests for outside employment and business activities. We evaluated these controls by reviewing applicable documentation; interviewing management about the process for reviewing, approving, and maintaining records of outside employment requests; testing the accuracy of the system for maintaining records of outside employment requests; and analyzing data for selected employees with multiple sources of income.



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Prevent or Detect Conflicts of Interest*

Appendix II

Major Contributors to This Report

Gregory D. Kutz, Assistant Inspector General for Audit (Management Services and Exempt Organizations)
Troy D. Paterson, Director
Gerald T. Hawkins, Audit Manager
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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Operations Support OS
Deputy Commissioner for Services and Enforcement SE
Director, Workforce Relations Division OS:HC:R
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: IRS Human Capital Officer: OS:HC



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Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to Congress.

Type and Value of Outcome Measure:

- Reliability of Information – Potential; 20,470 out-of-date OES records (see page 8).

Methodology Used to Measure the Reported Benefit:

Our review of all the records in the current OES as of February 12, 2013, showed that 20,470 (93 percent) of the 21,979 existing records did not have a review date on or before February 12, 2012. IRS supervisors are required to review all their employees' OES records to determine if there are any changes in the employee's outside employment or business activities. If there are no changes, the supervisor must enter the review date on the OES. If the information is incorrect, the supervisor should enter the date the employment or business activity changed or ended, and the record will be moved to the OES historical file.

Type and Value of Outcome Measure:

- Reliability of Information – Potential; 208 outside employment requests located in OPFs that were not included on the OES (see page 8).

Methodology Used to Measure the Reported Benefit:

We identified 3,541 IRS employees who were active and full time for every pay period in Calendar Year 2011 and were issued a Tax Year 2011 Form W-2, *Wage and Tax Statement*, from an employer other than the IRS or who filed a Schedule C, *Profit or Loss From Business*, with their Tax Year 2011 Form 1040, *U.S. Individual Income Tax Return*, and did not have a record of any outside employment request on the OES current file. Employees were eliminated who were employed by the IRS's Office of Chief Counsel or who were separated from the IRS at the time of our audit work.

A random sample of 136 of the 3,541 IRS employees with Tax Year 2011 Forms W-2 or Form 1040, Schedule C, from outside employment or business activities was selected for



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review.¹ We reviewed the employees' OPFs to determine whether there was a copy of a request for outside employment or a business activity that matched all the Forms W-2 payer information or sole proprietorships reported under the employees' Social Security Numbers.

We found eight employees who had approved Forms 7995 in their OPFs that matched the Forms W-2 payer information or sole proprietorships reported on Schedule C. Based on these results, we estimate that 208² of the 3,541 employees have approved Forms 7995 in their OPFs that are not documented on the OES, as required.³ This is based on the ratio of eight (6 percent) to 136 applied to the total population of 3,541 employees, which resulted in 208 employees who could be affected.

Type and Value of Outcome Measure:

- Reliability of Information – Potential; 2,656 IRS employees with outside employment or business activities without documented approval on the OES or in the OPF (see page 8).

Methodology Used to Measure the Reported Benefit:

We identified 3,541 IRS employees who were active and full time for every pay period in Calendar Year 2011 and were issued a Tax Year 2011 Form W-2 from an employer other than the IRS, or who filed a Schedule C with their Tax Year 2011 Form 1040, and did not have a record of any outside employment request on the OES current file. Employees were eliminated who were employed by the IRS's Office of Chief Counsel or who were separated from the IRS at the time of our audit work.

A random sample of 136 of the 3,541 IRS employees with Tax Year 2011 Forms W-2 or Form 1040, Schedule C, from outside employment or business activities was selected for review.⁴ We reviewed the employees' OPFs to determine whether there was a copy of a request for outside employment or a business activity that matched all the Forms W-2 payer information or sole proprietorships reported under the employees' Social Security Numbers on Form 1040, Schedule C.

¹ We selected the random sample using a 95 percent confidence level, a 10 percent error rate, and a ± 5 percent precision rate.

² We are 95 percent confident that the number of employees who have approved Forms 7995 in their OPFs that are not documented on the OES is between 70 and 346.

³ We selected the random sample using a 95 percent confidence level, a 10 percent error rate, and a ± 5 percent precision rate.

⁴ We selected the random sample using a 95 percent confidence level, a 10 percent error rate, and a ± 5 percent precision rate.



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We found 102 employees did not have approved Forms 7995 in their OPF.⁵ Based on these results, we estimate that 2,656⁶ of the 3,541 employees had no approved Form 7995 in their OPF or on the OES, as required. This is based on the ratio of 102 (75 percent) to 136 applied to the total population of 3,541 employees, which resulted in 2,656 employees who could be working outside the IRS without documented approval.

⁵ We also confirmed that Form W-2 payee name information matched the employee name and Social Security Number for these cases.

⁶ We are 95 percent confident that the number of employees who could be working outside the IRS without documented approval in either the OES or the OPF is between 2,402 and 2,909.



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Appendix V

General Rules for Outside Employment Requests and Approvals

| <i>Prohibited Activities¹</i> |
|--|
| Legal services involving Federal, State, or local tax matters. |
| Appearing on behalf of any taxpayer before any Federal, State, or local governmental agency in an action involving a tax matter, except with the written authorization of the Commissioner of the IRS. |
| Outside activity (unless otherwise permitted) that deals directly with any tax-related matter. However, employees may engage in bookkeeping and accounting that is directly related to a tax determination in the following situations: keeping the books for a firm owned or run by immediate family and prospects for a conflict of interest are remote; engaging in the activity for a civic, religious, educational, or charitable non-profit organization, where the employee is not paid for the work; or engaging in business with your spouse with permission. |
| <i>Allowed Activities Must:</i> |
| Conform to the general ethical requirements in the Office of Government Ethics Standards. |
| Not conflict with the employee's official duties. |
| Not be prohibited by statute or an agency supplemental regulation. |
| Not require that the employee disqualify themselves from matters so central and critical to the performance of their IRS duties as to materially impair their ability to perform those duties. |
| Not result in improper use of Government property. |
| Not result in the use or disclosure of nonpublic official information obtained in connection with the employee's Government duties or position. |
| Not impact the employee's effectiveness on the job. |

¹ If the activity is prohibited, the employee may not do it indirectly, that is in the name of, or through family members. In addition, an employee may not advertise their employment with the IRS to generate business.



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Allowed Activities Not Requiring Written Approval

Outside activities that are not considered employment or business.

Membership and services in civic, scout, religious, educational, fraternal, social, community, veteran, and charitable organizations, where such office or services do not entail the management of a business-type activity (*e.g.*, direct operation of commercial-type clubhouse).

Membership and services (including holding office) in the local office of a credit union, which may include paid bookkeeping work performed by the treasurer, or part-time clerical or teller services.

Services as a notary public.

Minor services and odd jobs for friends, relatives, or neighbors that is not for compensation as an employee or for a business.

Furnishing advice and assistance in the preparation of tax returns where no fee or other consideration is accepted.

Unpaid bookkeeping, preparation of tax returns and other forms required by the IRS, and maintenance of other records for civic, religious, educational, and charitable non-profit organizations that are exempt from Federal income tax.

Source: TIGTA summary of The Office of Government Ethics Standards of Ethical Conduct for Employees of the Executive Branch, 5 CFR Part 2635; and the Additional Rules for IRS Employees, 5 CFR 3101.106, and various IRS policies and procedures.



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Appendix VI

Supervisor Questionnaire Responses

The following table summarizes the responses to a questionnaire sent to supervisors of 101 of the 136 employees in our random sample of employees with outside income, but no approved outside employment request on the OES. Responses were received from 97 of these supervisors. Several of the responses to the questions included in the questionnaire were open-ended. Therefore, we reviewed the supervisor's responses, and categorized them as no, yes, or other based on the facts provided by the supervisor.

| Question | No | Yes | Other ¹ |
|--|----|-----|--------------------|
| Did the employee request approval via Form 7995? | 51 | 33 | 13 |
| Did the employee request approval using another means? | 85 | 0 | 12 |
| Was the request for outside employment approved? | 0 | 33 | 64 |
| Was the approved request forwarded to the OPF? | 7 | 18 | 72 |
| Was approval for outside employment recorded on the OES? | 26 | 5 | 66 |
| Do you review the OES forms annually? | 12 | 43 | 42 |

Source: Summary of responses to a questionnaire TIGTA sent to supervisors of IRS employees with outside income reported under their Social Security Number.

¹ Several supervisors were not currently supervising the employee and no longer had access to the employee's personnel file; therefore, they responded "n/a" or specified that they were unsure for a majority of our questions.



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Appendix VII

Management's Response to the Draft Report



HUMAN CAPITAL OFFICE

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

September 4, 2014

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

Daniel T. Riordan *DT Riordan*
IRS Human Capital Officer

SUBJECT:

Draft Audit Report – Controls Over Outside Employment Are Not Sufficient To Prevent And Detect Conflicts Of Interest (Audit # 201310009)

Thank you for the opportunity to respond to the subject draft audit report. We are committed to ensuring outside employment requests are documented and reviewed for conflicts with employees' official duties.

We agree we did not routinely follow internal IRS processes in documenting outside employment requests, including documenting requests in the Outside Employment System (OES), because of confusing or incomplete guidance. To address this issue we have already implemented a number of major improvements during fiscal year 2014 to include: usability enhancements to the OES; multiple communications to managers and employees clarifying their roles and responsibilities; and, improved Frequently Asked Questions on the Employee Resource Center. We agree with three of your recommendations, as described in the corrective actions, which will be developed and implemented. We disagree with one of your recommendations, as described in our attached response.

As noted in the report, only 0.3% of active, full-time employees who earned outside income did not have an outside employment agreement and earned significant outside income that "could conflict with the employee's official duties or impact the employee's effectiveness on the job." However, we would like to bring to your attention some aspects of the report that we feel are misleading or inaccurate.

First, we disagree with your methodology for identifying employees who were required to request approval to engage in an outside activity. To determine if reasonable assurance is provided that outside employment activities do not conflict with employees' official duties, you identified employees with Form W-2, *Wage and Tax Statement* or Form 1040 Schedule C, *Profit or Loss from Business* income filings for Tax Year 2011. The receipt of income reported on Form W-2 or Form 1040 Schedule C is not determinative of whether an employee is required to request approval.



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2

We also disagree with your estimate that 2,656 employees are engaged in outside employment without documented approval. In your review of a random sample of 136 employees with outside income, 25% had either an approved OES request or approved Form 7995 in the Official Personnel File. For 75% of the identified cases, TIGTA did not complete a check of the employee's drop file where an outside employment document may have been stored, nor did they ask management if the form may have been stored there. For 99.7% of IRS employees, TIGTA did not find a high risk of potential conflict of interest; additionally, the cases identified by TIGTA as a conflict of interest or prohibited outside activities, had all been previously identified and referred for appropriate action.

Finally, we disagree with the statement that employees who "spend much of their workday outside the office" or "can access taxpayer account information" are at higher risk for a conflict of interest. As stated in the *Plain Talk About Ethics and Conduct* handbook, a conflict of interest occurs when the employee's outside employment violates a regulation or causes an employee to have to be recused from official matters to such an extent that it impedes the employee's ability to perform his job. Management regularly monitors employees' performance and conduct regardless of their work location. Engaging in an outside activity while on-duty is an example of employee misconduct (e.g., misuse of official time), not a conflict of interest. Additionally, IRS maintains a robust system to monitor all access to taxpayer data and ensure employees only access information as required to perform their official duties. As noted in the report, from October 1, 2009, through July 31, 2013, 54 employees engaging in prohibited outside employment or with a conflict of interest were referred to TIGTA for investigation. We believe this reflects the strength of the controls in place to identify these issues.

We appreciate the continued support and assistance provided by your office. If you have any questions, please contact me at (202) 317-7600, or a member of your staff may contact Terry Guidt at (202) 317-3286.

Attachment



Controls Over Outside Employment Are Not Sufficient to Prevent or Detect Conflicts of Interest

Attachment

RECOMMENDATION 1:

Update the Internal Revenue Manual and associated outside employment guidance available to IRS employees and supervisors to include the requirements for using the Outside Employment System (OES) to request and approve outside employment requests.

- **CORRECTIVE ACTION:**
We agree with this recommendation. The IRS Human Capital Officer will update Internal Revenue Manual 6.735, and other related outside employment guidance, to include the revised Outside Employment Policy guidance and procedures.
- **ESTIMATED IMPLEMENTATION DATE:**
September 30, 2015
- **RESPONSIBLE OFFICIAL:**
Director, Workforce Relations Division
- **CORRECTIVE ACTION MONITORING PLAN:**
We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it on a monthly basis until completed.

RECOMMENDATION 2:

Appoint management responsibility for overseeing the outside employment process, including providing reasonable assurance that OES records are kept up to date and accurate.

- **CORRECTIVE ACTION:**
We agree with this recommendation. The Director, Workforce Relations Division will provide clarification that the Associate Director, Labor Relations Strategy and Negotiations Policy has program responsibility for the Outside Employment process.
- **IMPLEMENTATION DATE:**
September 30, 2014
- **RESPONSIBLE OFFICIAL:**
Director, Workforce Relations Division
- **CORRECTIVE ACTION MONITORING PLAN:**
We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it on a monthly basis until completed.



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RECOMMENDATION 3:

Work with the IRS's Office of Chief Counsel to evaluate whether a legislative proposal is needed to amend Internal Revenue Code § 6103 to enable the IRS to use tax data to perform analyses and identify employees who have multiple sources of income without an approved request for outside employment.

We disagree with this recommendation. We do not believe that sensitive taxpayer information should be used to oversee the IRS' outside employment program. Further, we do not agree the IRS should be singled out to utilize such a method for oversight simply because we are the repository for, and custodians of, such information.

RECOMMENDATION 4:

The IRS Human Capital Officer should, after establishing effective controls to use the OES to request and approve outside employment, require all supervisors to perform a one-time cleanup of the OES to correct outside employment data.

• **CORRECTIVE ACTION:**

We agree with this recommendation. The Associate Director, Labor Relations Strategy and Negotiations Policy will collaborate with Labor Relations/Employee Relations Field Operations to conduct a one-time cleanup of the OES.

• **ESTIMATED IMPLEMENTATION DATE:**

October 30, 2015

• **RESPONSIBLE OFFICIAL:**

Director, Workforce Relations Division

• **CORRECTIVE ACTION MONITORING PLAN:**

We will enter this corrective action into the Joint Management Enterprise System (JAMES) and monitor it on a monthly basis until completed.



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Appendix VIII

Office of Audit Comments on Management's Response

In response to our draft report, the IRS Human Capital Officer included some general comments and assertions that we believe warrant additional comment. The following includes portions of management's response and our related comments:

Management's Statement: *As noted in the report, only 0.3 percent of active, full-time employees who earned outside income did not have an outside employment agreement and earned significant outside income that "could conflict with the employee's official duties or impact the employee's effectiveness on the job."*

Office of Audit Comment: This is an incorrect statement. Review of IRS records indicate that nearly 3,000 full-time, active IRS employees who received income or participated in business activities outside the IRS during Calendar Year 2011 did not have approval for outside employment or the activities were not documented on the OES as required. These employees could be involved in outside employment that could be in conflict with their official duties or impact their effectiveness on the job. The 0.3 percent that the IRS refers to relates to 20 employees mentioned in our report who were referred to TIGTA's Office of Investigations for potential conflicts of interest. We did not perform additional research on the remaining nearly 3,000 employees to determine if they are involved in outside employment activities significant enough to refer for investigation.

Management's Statement: *We disagree with your methodology for identifying employees who were required to request approval to engage in an outside activity. To determine if reasonable assurance is provided that outside employment activities do not conflict with employees' official duties, you identified employees with Form W-2, Wage and Tax Statement or Form 1040 Schedule C, Profit or Loss from Business income filings for Tax Year 2011. The receipt of income reported on Form W-2 or Form 1040 Schedule C is not determinative of whether an employee is required to request approval.*

Office of Audit Comment: TIGTA acknowledged in Footnote 16 of the report that there are some activities that do not require written approval. We determined that only one of these activities, work performed for a credit union, would most likely result in the issuance of Form W-2 to the employee. In our review of a random sample of 136 of the more than 3,500 employees who held jobs or participated in business activities outside



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the IRS during Tax Year 2011 without documented approval in the OES current file, we did not identify any that had income related to work performed for a credit union.

Management's Statement: *We also disagree with your estimate that 2,656 employees are engaged in outside employment without documented approval. In your review of a random sample of 136 employees with outside income, 25% had either an approved OES request or approved Form 7995 in the Official Personnel File. For 75% of the identified cases, TIGTA did not complete a check of the employee's drop file where an outside employment document may have been stored, nor did they ask management if the form may have been stored there.*

Office of Audit Comment: The IRS statement above omits an important aspect of our estimate. We estimate that 2,656 employees are working outside the IRS without documented approval in either the OES or the OPF, which is required by IRS guidelines. In addition, during fieldwork TIGTA worked with the IRS Human Capital Office to contact supervisors for 101 of the 136 employees in our random sample of employees with outside income, but no approved outside employment request on the OES. Information for the results of this work is found on page 9 of this report and in Appendix VI. Supervisors were requested to forward copies of approved Forms 7995 maintained in their drop files. Although several supervisors provided copies of the approved forms, most did not and more than one-half stated that employees did not request approval for outside employment.

Management's Statement: *We disagree with the statement that employees who "spend much of their workday outside the office" or "can access taxpayer account information" are at higher risk for a conflict of interest...and that...engaging in an outside activity while on-duty is an example of employee misconduct (e.g., misuse of official time), not a conflict of interest.*

Office of Audit Comment: TIGTA continues to believe that employees who work outside the office and have access to taxpayer information are at a higher risk for potential conflicts of interest. For example, TIGTA identified 660 revenue agents with evidence of outside employment that did not have authorized outside employment agreements. In addition, actual closed cases of conflicts of interest show that IRS employees with access to taxpayer information have improperly used this data for their outside employment. For example, we noted in our report that one former employee pled guilty to engaging in a criminal conflict of interest for accessing taxpayer information for the purpose of conducting a private tax and accounting business. Moreover, tax return information showed that four current employees (two of whom are revenue agents) operated businesses with annual gross receipts ranging from more than \$500,000 to more than \$7 million. Employees such as revenue agents who often work outside of the office are at increased risk of engaging in undetected outside employment and potential conflicts of interest.



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Management's Statement: *As noted in the report, from October 1, 2009, through July 31, 2013, 54 employees engaging in prohibited outside employment or with a conflict of interest were referred to TIGTA for investigation. We believe this reflects the strength of the controls in place to identify these issues.*

Office of Audit Comment: TIGTA agrees that IRS internal controls contributed to the identification of prohibited outside activities of some IRS employees. However, most of the 54 cases identified by TIGTA as a conflict of interest or prohibited outside activities were identified during investigations initiated by TIGTA, as opposed to resulting from a referral from the IRS. Additionally, we referred 23 employees to TIGTA's Office of Investigations that had significant outside income with no documented approval for outside employment on the OES, as required by IRS guidance.