AUTOMATION AND TAX ADMINISTRATION

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Commissioner Cohen points out the effects of the increasing use of computers by the Internal Revenue Service. He states that it should result in more efficient processing of returns, increase the amount of revenue collected, promote uniformity in treatment of taxpayers and create more accurate statistical data related to fiscal planning. Automatic data processing will in many instances result in simplified tax return forms and enable the Service to develop a more effective information program.

In this technological age some people predict that computers will de-emphasize humanity. The Internal Reveune Service does not share this pessimistic point of view. On the contrary, we believe that the computer, by removing the need for routine clerical decisions and the mass of paperwork details, will free personnel for more important work.

Computers are, after all, only sophisticated machinery. No computer has yet been invented that can create *anything*. Creativity is still man's perogative. Yet, the growth of our complex society has been such that business and government have had to turn to the computer for assistance. As long ago as 1948 the Internal Revenue Service began research on the feasibility of handling tax returns by automatic data processing (ADP). It had already become apparent that IRS would need faster and more efficient ways to cope with its ever-increasing workload.

In 1930 the number of taxpayer totaled only six million. By the end of World War II, this figure had jumped to 20 million. Last year, the number had skyrocketed to over 102 million. By 1970, it is estimated it will increase to 111 million; by 1980, to 135 million. ADP will provide a means of keeping pace with this enormous and growing processing workload.

The Service began its ADP program in the Southeast Region (Georgia, Alabama, North Carolina, South Carolina, Mississippi, Tennessee and Florida). In 1962 all business returns there were handled under the computer system. By January 1965, all business returns throughout the country were being processed by ADP. Processing of individual income tax returns with computers began in 1963 in the same region. Through a year-by-year phasing-in schedule, the entire country is being brought into the system, and January, 1967,

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will mark the beginning of nationwide processing of tax returns by computers.

Since Internal Revenue began to use ADP, the processing of tax returns by computer has accounted for millions of additional dollars in revenue. Since January 1962, a total of six million dollars can be *directly* attributed to ADP.

Computers have also saved IRS a tremendous amount of time on collection procedures. In years gone by, in an attempt to provide fast, efficient service, refunds were often made to taxpayers who owed money for one or more prior years. Previously, too, millions of dollars were reported in estimated credits that could not be verified. Under ADP, a computer automatically searches its memory to find out whether or not a given taxpayer owes money before a refund check is written. In addition, computers also mathematically verify every return.

But IRS is not concerned solely with using its compters for the processing of returns. Automation is also being used for research to obtain statistical data which will provide the President and the Secretary of the Treasury with more complete and current information on taxes than is now available. In a rapidly changing economy figures from three years, two years, or even one year ago, are obsolete. Through the speed of electronic computers it will be possible to keep up-to-date on reporting patterns, revenue receipt variations and income changes.

IRS will have—effective with the 1967 income tax filing season— a Master File containing pertinent information on every taxpayer in the nation. This file will significantly reduce administrative costs. Before such a file was in existence, checking on whether or not a taxpayer had filed a return was a lengthy, arduous job. Under the Master File System, it is a relatively simple task to determine a taxpayer's status; this is, whether or not he filed and whether or not he owes money.

Once the ADP system is operative nationwide, the machines will insure that the returns from each and every taxpayer are checked in a uniform manner. Under manual procedures, IRS made every effort to treat each taxpayer alike, but, since human judgment was involved, a lack of uniformity sometimes occurred.

One of the areas in which IRS previously did not have the best or most uniform administrative procedures was that of tax-exempt organization listings. The listings were incomplete because some exempt organizations were not required to file returns. Others were required to file only information returns or returns on only one or more aspects of their activities. Lists of names of some tax-exempt organizations

were kept in the National Office, while others were maintained in district offices.

The lack of a master list and the fact that requirements for filing returns vary made it difficult for IRS to know whether or not an organization which was granted tax-exempt status in a given year was, in fact, still in existence, whether it had merged with another organization, or even whether it had changed its purposes and activities. Further complicating the picture was the tremendous growth in the number of tax-exempt organizations over the past twenty years.

To solve the recordkeeping problem, IRS turned to the same sophisticated automatic machinery it had used to compile the Master File. The characteristics of each exempt organization were placed on punch cards, then transferred to magnetic tape. Included in the data now recorded on the Master File for tax-exempt organizations are the name, address, the identification number, the sub-section of the law under which tax-exempt status was granted, the date of the exemption rulings, and the stated purposes and activities of each organization. Data relative to returns filed and audit information will also be on the ADP tape file.

ADP is further being used by IRS to compile records of exempt employee trusts that are part of qualified pension or profit-sharing plans.

Initially, a questionnaire is mailed to exempt organizations or others in which IRS is interested. Once the information has been received, the data is keypunched on cards and eventually placed on magnetic tape. So that the District Director and his administrative staff can be aware of the exempt organizations located within a given geographical area, local registers will be maintained in each IRS district office. From information recorded on subsequent information returns, non-tax returns or non-taxable returns, IRS plans to develop techniques to describe and determine norms and standards for audit.

Whereas updating the list of organizations to which contributions are deductible has in the past been a long and costly endeavor, the use of ADP not only will speed up the process, but accomplish a number of other tasks not heretofore possible. By automation, the required information return blanks can be addressed and sent to each organization on schedule. In addition, it will be relatively easy to identify those organizations that fail to file the required forms. We can then prepare and address forms or form letters calling attention to the delinquency. Special inquiries can also be easily made.

An Exempt Organization Master File may make other improvements possible. For example, we may be able to simplify information

returns to relieve many exempt organizations of the burden of providing extensive financial data: a kind of 1040-A for tax-exempt organizations.

Currently, the number of exempt organizations in the IRS Master File totals 250,000. In addition, there are nearly 70,000 employee trusts. These figures alone point up how much tax administration will benefit from the use of high-speed computers. We will have a few feet of tape as compared with endless cabinets of cards—ready accessibility as compared with costly manual look-up procedures.

Another long-range research project in which ADP will play a part is the taxpayer compliance measurement program (TCMP). One measure of compliance may be collection figures. In 1965, IRS collected 114.4 billion dollars. Five years previously, the figure was only 91.7 billion dollars. In fiscal 1966 the figure reached an all-time high of 128.8 billion dollars, a 12.5 percent increase over the 1965 fiscal year.

Does this mean that the Revenue Service is more effective than it was previously? Not necessarily. The growth of the economy has played a highly significant role. Collection figures are not really a scientific device by which to make periodic comparisons on compliance. And before ADP, no measuring rod was available. Information on compliance levels is needed for budgetary purposes and, especially, for manpower needs.

If IRS is to continue to obtain optimum results from the system, studies of compliance must be conducted in the areas of delinquent accounts, delinquent returns, and errors on individual returns filed.

With the help of computer capabilities, IRS hopes to answer such questions as:

1. What is the general reason for delinquent accounts? How long does it take to collect them? What techniques are used? How much does it cost?
2. Why don't people file returns? What kind of people don't file? What further can be done to bring in revenue?
3. What kinds of errors are most prevalent?
4. To what extent is IRS influencing voluntary compliance? To what extent is it not?
5. Is voluntary compliance better this year than last?
6. How much of the total tax is IRS collecting? Through what means?
7. How much of the revenue that should be collected is not?

Collection of information on delinquent accounts as a part of the

TCMP program began in 1963-64 with a tabulation of the number and amount of taxpayer delinquent accounts and a survey of IRS collection efforts. One factor IRS discovered is that a significant number of delinquent accounts could be closed by further correspondence.

The delinquent-returns phase of the TCMP program also was begun in 1963 with pilot interviews of business taxpayers in the Southeast Region.

Probably the most interesting phase of the TCMP study is the "errors in returns filed." A probability sample of 100,000 individual returns has been selected for intensive audit. With the help of computers, it is expected that IRS can determine the following:

1. Characteristics of taxpayers who file erroneous returns.
2. The kinds of errors in relation to income-size, source of income, type of form filed (standard or with itemized deductions), and tax errors by type and size on designated issues.

The results of this study will, of course, materially affect the audit program. They will also have a bearing on the IRS information program. In other words, by knowing which people make what errors and how frequently they make them, Internal Revenue can better know what kinds of materials to disseminate to whom and through what media. An effective information program is far less costly than an intensive enforcement program.

Again, Automatic Data Processing will never replace people. Nor will people become servants of computers. Automated equipment is only as good as man makes it. Already ADP has heightened the need for more imaginative professionals. Throughout all of history, any technological revolution has made the professional more important. What is essential is that man use any new tool as effectively as possible.

After all, it will always be necessary for Revenue agents to discuss with taxpayers information which a computer generates, and for accountants and lawyers to advise clients of their appeal rights. Rather than reducing the need for able tax personnel, the computer has placed a premium on human judgment and ability.