



*The Remediation Plan Still Does Not Contain  
All the Necessary Actions to Address the  
Unpaid Assessments Material Weakness*

**July 19, 2012**

**Reference Number: 2012-10-069**

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

### **THE REMEDIATION PLAN STILL DOES NOT CONTAIN ALL THE NECESSARY ACTIONS TO ADDRESS THE UNPAID ASSESSMENTS MATERIAL WEAKNESS**

## Highlights

**Final Report issued on July 19, 2012**

Highlights of Reference Number: 2012-10-069 to the Internal Revenue Service Chief Financial Officer.

### **IMPACT ON TAXPAYERS**

The Federal Financial Management Improvement Act (FFMIA) remediation plan is a critical part of the IRS's efforts to bring its financial management systems into compliance with the FFMIA and to provide reliable and timely financial data. Overall, the IRS still faces challenges in its efforts to comply with the FFMIA. Complete and reliable financial information is critical to the IRS's ability to accurately report on the results of its operations to both internal and external stakeholders, including taxpayers.

### **WHY TIGTA DID THE AUDIT**

The overall objectives of this review were to report to Congress, as required by the FFMIA, any instances of and reasons for missed intermediate target dates established in the IRS's September 30, 2011, FFMIA remediation plan, and to determine whether the IRS has taken adequate corrective actions on prior audit findings related to the plan.

### **WHAT TIGTA FOUND**

The IRS continues to face challenges in becoming compliant with the FFMIA. Our review of the IRS's September 30, 2011, FFMIA remediation plan identified that the plan continues to provide specific remediation actions to address the material weakness relating to information security. However, as previously reported, the IRS continues to not fully include costs and remediation actions relating to addressing the unpaid assessments material weakness.

TIGTA also found that this year's remediation plan does not include any specific detail related to the Customer Account Data Engine 2 (CADE 2). Since the CADE 2 is the key piece of the IRS's strategy to address its material weakness related to unpaid assessments, TIGTA continues to believe this information should be included in the remediation plan. Until the IRS updates its FFMIA remediation plan with additional information and actions related to addressing the unpaid assessments material weakness, TIGTA will be unable to fully assess the IRS's overall progress in resolving its noncompliance with the FFMIA.

Additionally, our review of the remediation plan found that the IRS did not complete two of the remedial actions that the plan indicated were closed. Because the actions were not taken, additional actions will be necessary to resolve the underlying material weakness. As such, TIGTA believes the IRS should have developed new action items to address the issue rather than close these two actions.

### **WHAT TIGTA RECOMMENDED**

TIGTA recommended that the IRS's Chief Financial Officer: 1) determine whether the November 2014 implementation of the CADE 2 that fully addresses the unpaid tax assessments material weakness is still achievable and update future remediation plans with a more accurate date, if necessary, and 2) develop alternative actions and target implementation dates for the two issues TIGTA identified.

In their response, IRS management agreed with our recommendations. Management agreed to determine whether the November 2014 implementation date for CADE 2 is still achievable and to develop alternative actions and target implementation dates for the two issues TIGTA identified.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

July 19, 2012

**MEMORANDUM FOR CHIEF FINANCIAL OFFICER**

A handwritten signature in black ink, appearing to read "Michael E. McKenney".

**FROM:** Michael E. McKenney  
Acting Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – The Remediation Plan Still Does Not Contain  
All the Necessary Actions to Address the Unpaid Assessments  
Material Weakness (Audit # 201210012)

This report presents the results of our review of the Internal Revenue Service's (IRS) Federal Financial Management Improvement Act<sup>1</sup> (FFMIA) remediation plan for Fiscal Year 2011. The overall objectives of this review were to report to Congress, as required by the FFMIA, any instances of and reasons for missed intermediate target dates established in the IRS's September 30, 2011, FFMIA remediation plan, and to determine whether the IRS has taken adequate corrective actions on prior audit findings related to the plan. This review is included in our Fiscal Year 2012 Annual Audit Plan and addresses the major management challenge area of Achieving Program Efficiencies and Costs Savings.

Management's complete response to the draft report is included as Appendix IV.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Russell P. Martin, Acting Assistant Inspector General for Audit (Management Services and Exempt Organizations), at (202) 622-8500.

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<sup>1</sup> Pub. L. No. 104-208, 110 Stat. 3009.



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*Abbreviations*

CADE 2	Customer Account Data Engine 2
CFO	Chief Financial Officer
FFMIA	Federal Financial Management Improvement Act
GAO	Government Accountability Office



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## *Background*

The Federal Financial Management Improvement Act of 1996 (FFMIA)<sup>1</sup> was established to advance Federal financial management by ensuring that Federal financial management systems provide accurate, reliable, and timely financial management information to the Government's managers. Further, this disclosure should be done on a basis that is uniform across the Federal Government from year to year by consistently using professionally accepted accounting standards. Specifically, FFMIA Section 803 (a) requires each agency to implement and maintain systems that comply substantially with:

***As of November 2011, the Government Accountability Office continued to report that the IRS's financial management systems do not comply with FFMIA requirements.***

- Federal Government financial management systems requirements.
- Applicable Federal Government accounting standards.
- The United States Government Standard General Ledger<sup>2</sup> at the transaction level.

If the agency's financial systems do not comply, the agency is required to develop a remediation plan that describes the resources, remedies, and intermediate target dates for achieving compliance and to file the plan with the Office of Management and Budget. In addition, Section 804 (b) requires that agency Inspectors General report to Congress instances when and reasons why an agency has not met the intermediate target dates established in its remediation plan.

As of November 2011, the Government Accountability Office (GAO) continues to report<sup>3</sup> that the Internal Revenue Service's (IRS) financial management systems do not substantially comply with FFMIA requirements. Because the GAO has reported noncompliance with the requirements of the FFMIA, the IRS has been required to prepare and maintain a remediation plan. Noncompliance includes material weaknesses in internal controls over both information security and unpaid assessments.<sup>4</sup> The information security material weakness affects the reliability of the IRS's financial management information and increases the risk that confidential IRS and taxpayer information is compromised. The unpaid assessments material weakness affects the IRS's ability to quantify the amount of unpaid assessments owed to the IRS.

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<sup>1</sup> Pub. L. No. 104-208, 110 Stat. 3009.

<sup>2</sup> Provides a uniform Chart of Accounts and technical guidance to be used in standardizing Federal agency accounting.

<sup>3</sup> Government Accountability Office, GAO-12-165, *Financial Audit: IRS's Fiscal Years 2011 and 2010 Financial Statements* (Nov. 2011).

<sup>4</sup> An unpaid assessment is a legally enforceable claim against a taxpayer and consists of taxes, penalties, and interest that have not been collected or abated (a reduction in a tax assessment).



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Chief Financial Officer (CFO) management stated that the IRS implemented a new accounting system in January 2010, the Redesign Revenue Accounting Control System, which allows it to post transactions in compliance with Federal Government requirements, supports traceability for revenue transactions, and further assists it in becoming compliant with the FFMIA. However, the IRS informed us that it does not believe it will become fully compliant with the FFMIA and address the material weakness relating to unpaid assessments until approximately November 2014, pending successful implementation of Transition State 2 of the Customer Account Data Engine 2 (CADE 2).

The CADE 2 will result in a single relational database to house all individual taxpayer accounts in a central data source that will make reporting and retrieval faster and more efficient. The IRS indicates that the CADE 2 system will result in timelier taxpayer data, increased analytical data stores, improved/increased tools to more effectively use data for compliance and customer service, and enhanced data security. The IRS also indicated that this will improve its ability to quantify the amount of unpaid assessments.

The IRS began implementation of the CADE 2 in January 2012. The initial phase modified the Individual Master File<sup>5</sup> from a weekly cycle to daily processing, established a new relational database to store all individual taxpayer account information, and provided management tools to more effectively use data for compliance and customer service. The next phase launches a single processing system whereby applications directly access and update the taxpayer account database. The single processing system is designed to provide expanded traceability of taxpayer account activity and identify duplicate tax assessments across multiple accounts. The IRS plans to implement this phase in January 2014. The IRS has previously reported that closure of the material weakness on unpaid assessments is dependent upon implementation of this phase of the CADE 2 to provide the capability to properly categorize unpaid assessment data and provide an audit trail to detailed taxpayer transactions.

This review was performed at the IRS National Headquarters in Washington, D.C., in the office of the CFO during the period October 2011 through March 2012. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Detailed information on our audit objectives, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

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<sup>5</sup> The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.



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## *Results of Review*

The IRS continues to face challenges in becoming compliant with the FFMIA. Our review of the IRS's September 30, 2011, FFMIA remediation plan identified that the plan continues to provide specific remediation actions to address the material weakness relating to information security. However, as we previously reported, the IRS continues to not fully include costs and remediation actions relating to addressing the unpaid assessments material weakness. We found that this year's remediation plan does not include any specific details relating to the CADE 2. Since the IRS indicates that the CADE 2 is the key piece of its strategy to address its material weakness related to unpaid assessments, we continue to believe this information should be included in the remediation plan. Until the IRS updates its FFMIA remediation plan with additional information and actions related to addressing the unpaid assessments material weakness, we will be unable to fully assess its overall progress in resolving its noncompliance with the FFMIA.

### ***The Remediation Plan Still Does Not Contain All the Necessary Actions to Address the Unpaid Assessments Material Weakness***

In response to the unpaid assessments material weakness, the IRS is required by FFMIA Section 803 (a) to include in its remediation plan the resources, remedies, and intermediate target dates for achieving compliance. Our review identified that this required information continues to not be included in the plan. Specifically, the IRS continues to not fully report on the costs and specific actions it plans to take to address the unpaid assessments material weakness.

In a previous TIGTA report,<sup>6</sup> we recommended that the IRS include in future remediation plans action items and costs related to the implementation of the CADE 2. IRS management disagreed with this recommendation. As a result, this year's remediation plan does not contain any specific action items or costs associated with the CADE 2 system. However, the IRS does mention the CADE 2 in the remediation plan's executive summary, citing its importance in addressing the unpaid assessments material weakness. The plan does not include detail on how the CADE 2 will assist in mitigating the unpaid assessments material weakness or additional actions related to this weakness. Specifically, the FFMIA remediation plan indicates that the IRS expects to implement the CADE 2 by November 2014 and, therefore, fully address its material weakness over unpaid tax assessments.

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<sup>6</sup> Treasury Inspector General for Tax Administration, Ref. No. 2011-10-041, *Challenges Continue With Reporting Complete and Accurate Information in the Federal Financial Management Improvement Act Remediation Plan* (May 2011).



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In its Fiscal Year 2013 budget request, the IRS requested an additional \$148 million related to the continued development of the CADE 2. However, we recently reported<sup>7</sup> that management indicated funding concerns may impact the implementation of the CADE 2 (Transition State 2) by January 2014. Since the remediation plan does not include any intermediate action items and dates for the CADE 2, we do not know the IRS's progress related to the CADE 2 in resolving its material weakness for unpaid assessments. As a result, we are unsure whether the November 2014 implementation date for the CADE 2 contained in the remediation plan is still accurate.

Management stated that the FFMIA remediation plan was created to address the actions required for IRS financial systems and believes that the CADE 2 is not a financial system; rather, it is a Business System Modernization project used to modernize the IRS tax system for individual taxpayer account data. We continue to believe that including additional information in the remediation plan will increase the likelihood of the IRS addressing the material weakness relating to unpaid assessments. This will also enable external stakeholders to better understand how the CADE 2 will address the material weakness and monitor the IRS's progress in becoming compliant with the FFMIA.

## ***Recommendation***

***Recommendation 1:*** The IRS CFO should determine whether the November 2014 implementation of the CADE 2 that fully addresses the unpaid tax assessments material weakness is still achievable and update future remediation plans with a more accurate date, if necessary.

***Management's Response:*** IRS management agreed with this recommendation. The CFO will reassess the November 2014 closing date for this material weakness once the scope for CADE 2 Transition State 2 has been determined. The CFO continues to work with the Wage and Investment Division, as the business owner, and with Modernization and Information Technology Services organization to determine the financial requirements that will be in the scope for the CADE 2 Transition State 2 build. The CFO will update the remediation plan with additional milestones and costs to address the material weakness on unpaid tax assessments to leverage the information from the CADE 2, as appropriate.

## ***Two Remediation Action Items Were Misclassified As Completed***

Remediation actions are the steps the IRS plans to take to resolve issues contributing to its noncompliance with the FFMIA. Many of the actions detailed in the plan have an estimated

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<sup>7</sup> Treasury Inspector General for Tax Administration, Ref. No. 2011-20-109, *The Customer Account Data Engine 2 Is Making Progress Toward Achieving Daily Processing, but Improvements Are Warranted to Ensure Full Functionality* (Sept. 2011).



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completion date and are long-term in nature. In its September 30, 2011, remediation plan, the IRS reported that it:

- Added two remediation actions to the 30 open remediation actions.
- Completed 21 remediation actions, leaving 11 remaining open remediation actions.
- Extended two intermediate target dates for open remediation actions. Although the IRS had a reasonable explanation for the extended intermediate target date, delays could further hinder the IRS's ability to timely resolve the reported issues that cause its noncompliance with the FFMIA.

Each of the 11 open remedial actions had an intermediate target date that extended more than three years from the initial determination that IRS financial management systems were not in substantial compliance with the FFMIA. As required, the IRS obtained concurrence from the Office of Management and Budget to extend corrective actions beyond the three-year limitation.

However, of the 21 remediation actions completed, the IRS erroneously showed two of these action items as being completed. For these two action items, we determined that the steps needed to fully complete the actions were not taken. IRS management stated that the decision to report these two actions as completed was based on a cost-benefit analysis indicating the cost of implementation for the actions would exceed the benefits of implementation. Both action items related to programming changes concerning its accounting systems. The IRS advised us that it considers these two actions to be closed even though future actions will be necessary to fully resolve the underlying issue of resolving the unpaid assessments material weakness. Because the necessary actions specified in the remediation plan were not taken and additional actions will be necessary to resolve the unpaid assessments material weakness, we believe the IRS should have developed new action items rather than close these two action items.

## ***Recommendation***

***Recommendation 2:*** The IRS CFO should develop alternative actions and target implementation dates for the two issues we identified. These actions should be included in future remediation plans.

***Management's Response:*** The IRS agreed with this recommendation. The CFO closed the two corrective actions identified because they were not cost effective. Instead, the CFO added 15 new corrective actions to the internal unpaid assessments material weakness action plan and will add these corrective actions to the third quarter Fiscal Year 2012 remediation plan.



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## **Appendix I**

### *Detailed Objectives, Scope, and Methodology*

The overall objectives of this review were to report to Congress, as required by the FFMIA,<sup>1</sup> any instances of and reasons for missed intermediate target dates established in the IRS's September 30, 2011, FFMIA remediation plan, and to determine whether the IRS has taken adequate corrective actions on prior audit findings related to the plan. To accomplish our objective, we:

- I. Researched the requirements of the FFMIA, including Office of Management and Budget and Department of the Treasury guidance for compliance with it.
- II. Determined whether the IRS's remediation plan was consistent with GAO recommendations from prior IRS financial audits and related financial management reports.
- III. Determined whether 1) the IRS missed any intermediate target dates established in its remediation plan, 2) intermediate target dates were extended without sufficient documentation to support the revised dates, and 3) proper approval was obtained for remedial actions extending more than three years.
  - A. Verified that all remedial actions have intermediate target dates established.
  - B. Identified instances when the IRS had not met the intermediate target dates.
  - C. If instances of missed dates were identified, interviewed IRS officials about the reason the IRS did not meet the intermediate target date.
  - D. Compared the September 30, 2011, FFMIA remediation plan to the Fiscal Year 2010 plan to identify intermediate target dates that have changed since the previous Treasury Inspector General for Tax Administration review.<sup>2</sup> We also obtained and analyzed documentation in support of any changes.

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<sup>1</sup> Pub. L. No. 104-208, 110 Stat. 3009.

<sup>2</sup> Treasury Inspector General for Tax Administration, Ref. No. 2011-10-041, *Challenges Continue With Reporting Complete and Accurate Information in the Federal Financial Management Improvement Act Remediation Plan* (May 2011).



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- IV. Determined whether 1) the IRS remediation plan had established resource needs for remedial actions and 2) the resources presented were consistent with supporting documentation.
  - A. Verified that resource requirements were identified for all remedial actions.
  - B. Obtained budget information.
  - C. Traced remediation plan resources to budget information.
  - D. Interviewed the functional financial plan managers associated with all significant cost estimates.
- V. Determined whether the IRS had taken adequate corrective actions on prior reported audit findings related to the FFMIA remediation plan.
  - A. Identified the prior year's Treasury Inspector General for Tax Administration audit findings and corresponding management responses concerning corrective actions that should have been completed by the time of our audit.
  - B. Confirmed through discussions and observations that actions had been completed.

**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 the following internal controls were relevant to our audit objectives: the IRS's policies, procedures, and practices for tracking remediation actions implemented due to identified material weaknesses. We evaluated these controls by interviewing management and reviewing applicable documentation.



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**Appendix II**

*Major Contributors to This Report*

Russell P. Martin, Acting Assistant Inspector General for Audit (Management Services and Exempt Organizations)  
Nancy A. Nakamura, Assistant Inspector General for Audit (Management Services and Exempt Organizations)  
Jeffrey M. Jones, Director  
Joseph F. Cooney, Audit Manager  
LaToya R. Penn, Lead Auditor  
Mary F. Herberger, Senior Auditor  
Joseph P. Smith, Senior Auditor



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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  
Associate Chief Financial Officer for Corporate Planning and Internal Controls OS:CFO:CPIC  
Chief Counsel CC  
National Tax 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 Liaisons:  
    Chief Financial Officer OS:CFO  
    Chief Technology Officer OS:CTO



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**Appendix IV**

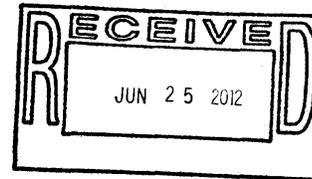
*Management's Response to the Draft Report*



CHIEF FINANCIAL OFFICER

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

June 25, 2012



MEMORANDUM FOR MICHAEL R. PHILLIPS  
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

*Pamela J. LaRue*  
Pamela J. LaRue  
Chief Financial Officer

SUBJECT:

Draft Audit Report – The Remediation Plan Still Does Not  
Contain All the Necessary Actions to Address the Unpaid  
Assessments Material Weakness (Audit # 201210012)

We reviewed the subject draft report and agree with the recommendation to determine whether the November 2014 implementation date for the Customer Account Data Engine 2 (CADE 2) is still achievable, and to develop alternative actions and target implementation dates for the two issues you identified.

As we agreed during our discussions on the draft report, we will revise the executive summary portion of the remediation plan to make it clearer how our financial systems will leverage the improved data in the taxpayer record once CADE 2 Transition State 2 (TS2) is implemented, so external stakeholders can better understand how CADE 2 helps address this material weakness.

Attached are our detailed comments to your recommendations. If you have any questions, please contact Peter Rose, Associate Chief Financial Officer for Corporate Planning and Internal Control, at (202) 622-4508.

Attachment



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**Attachment**

**TIGTA Recommendations and IRS Responses to  
Draft Audit Report # 201210012, "The Remediation Plan  
Still Does Not Contain All the Necessary Actions to  
Address the Unpaid Assessments Material Weakness"**

**RECOMMENDATION 1**

The IRS CFO should determine whether the November 2014 implementation of the CADE 2 that fully addresses the unpaid tax assessment material weakness is still achievable and update future remediation plans with a more accurate date, if necessary.

**CORRECTIVE ACTION**

The IRS agrees with this recommendation. The CFO will reassess the November 2014 closing date for this material weakness once the scope for CADE 2 TS2 has been determined. The CFO continues to work with Wage and Investment, as the business owner, and with Modernization & Information Technology Services to determine the financial requirements that will be in the scope for the CADE 2 TS2 build. The CFO will update the remediation plan with additional milestones and costs to address the material weakness on unpaid tax assessments to leverage the information from CADE 2 TS2, as appropriate. Until that scope is determined, we have no actions, costs, or a new date to report at this time.

**PLANNED IMPLEMENTATION DATE**

December 31, 2013

**RESPONSIBLE OFFICIAL**

Chief Financial Officer

**CORRECTIVE ACTION MONITORING PLAN**

N/A



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The IRS CFO should develop alternative actions and target implementation dates for the two issues we identified. These actions should be included in future remediation plans.

**CORRECTIVE ACTION**

The IRS agrees with this recommendation. The CFO closed the two corrective actions TIGTA identified because they were not cost effective, and they will not be revisited in the plan. Instead, the CFO added 15 new corrective actions to the internal unpaid assessments material weakness action plan, approved by the Financial Management Controls Executive Steering Committee on April 25. The new actions address additional programming changes to improve financial classifications, Trust Fund Recovery Penalty duplication, and ways to improve data input to our systems and the estimation process. The CFO will add these corrective actions to the third quarter FY 2012 remediation plan.

**PLANNED IMPLEMENTATION DATE**

June 30, 2012

**RESPONSIBLE OFFICIAL**

Chief Financial Officer

**CORRECTIVE ACTION MONITORING PLAN**

N/A