TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Trends in Compliance Activities Through Fiscal Year 2007

April 18, 2008

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TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

April 18, 2008

MEMORANDUM FOR DEPUTY COMMISSIONER FOR SERVICES AND ENFORCEMENT

Michael R. Phillips

FROM: Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Trends in Compliance Activities Through Fiscal Year 2007 (Audit # 200830016)

This report presents the results of our review of statistical information reflecting collection and examination activities within the Internal Revenue Service (IRS). The overall objective of this review was to provide statistical information and trend analyses of the data, as requested by the IRS Oversight Board.[1]

Impact on the Taxpayer

This report is a compilation of statistical information reported by the IRS. We did not verify or validate the authenticity or reliability of the data and, therefore, did not identify any specific impact on the taxpayer. However, continued effort to improve compliance is important to reducing the tax gap and maintaining the integrity of the voluntary tax compliance system.

Synopsis

Since Fiscal Year (FY) 2000, the IRS has reversed many of the downward trends in compliance activities that had occurred in prior years. In FY 2007, many of these activities continued to increase, even though Collection and Examination function field staffing decreased slightly. Both the Collection and Examination functions plan to hire enforcement personnel during FY 2008.

[1] See Appendix IV for a glossary of terms used in this report.

Some of the positive changes noted in this report might be attributable to management emphasis on the Collection and Examination functions' programs. Over the last few years, the Small Business/Self-Employed Division has implemented reengineering and organizational changes that could have had a positive impact on enforcement efforts. In addition, both functions continue to study ways to improve workload selection.

As our report points out, the IRS has reversed many of the enforcement declines in both the Collection and Examination functions. Although the IRS has taken significant actions to improve its enforcement efforts, the Government Accountability Office continued to include enforcement of tax laws (collection of unpaid taxes and Earned Income Tax Credit noncompliance) as one of the high-risk areas in the Federal Government in its most recent (January 2007) update.[2]

In FY 2007, the level of compliance activities and the results obtained in many Collection function areas showed a continued increase. The uses of liens and levies (collection enforcement tools) continued to increase and reached the 10-year highs. The use of seizures also increased but is unlikely to return to pre-1998 levels in the foreseeable future. Enforcement revenue collected also continued to increase (to $59.2 billion), but the total dollar amount of uncollected liabilities increased to the 10-year high of $290 billion. In addition, the gap between new delinquent account receipts and closures had widened by almost 63 percent by the end of FY 2007.

The Collection function collected almost 3 percent more than in FY 2006, but the number of taxpayers (866,777) and the amount owed ($34.9 billion) on accounts in the Queue were each at a 10-year high. One reason for the increase in the Queue this year is a rise in the number of compliance assessments. While the Queue is a source of work for Collection function employees, a significant number of accounts in the Queue might never be worked. In addition, in FYs 2001 through 2007, the IRS removed almost 7.6 million accounts with balance-due amounts totaling almost $31.2 billion from Collection function inventory. These accounts might never be worked.

In September 2006, the IRS started assigning balance-due cases that otherwise would not have been worked to private collection agencies. Through FY 2007, the IRS had received a total of $26.6 million after expected commissions on cases assigned to the collection agencies, and program costs totaled $69.8 million. More than 96 percent of the total revenue collected by the agencies was received during FY 2007 alone. The program netted $11.3 million after subtraction of expected commissions and program costs for the year. However, continued use of private collection agencies is uncertain because some members of Congress want the IRS to discontinue their use.

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[2] *HIGH-RISK SERIES – An Update* (GAO-07-310, dated January 2007).

During FY 2007, the overall percentage of tax returns examined increased by almost 9 percent, even though the number of field Examination function personnel decreased by just over 4 percent. In addition, the overall percentage of tax returns examined was 2 percent higher than in FY 1998.

Overall, the number of individual tax returns examined increased during FY 2007.[3] Correspondence examinations accounted for 83 percent of the examinations of individuals.[4] Because correspondence examinations are usually not as comprehensive as face-to-face examinations, the impact on compliance might be limited. In addition, the dollar yield per hour increased for individual income tax return examinations conducted by revenue agents and tax compliance officers.

In FY 2007, the number of corporate tax returns examined increased by just over 4 percent, after decreasing 1 percent in FY 2006. However, the number of corporate returns examined has decreased almost 45 percent since FY 1998. The total number examined decreased from 1 of 48 returns filed in FY 1998 to 1 of 75 returns filed in FY 2007. The number of tax returns examined for small corporations (those with assets of less than $10 million) increased by slightly more than 12 percent, while the number of returns examined for large corporations (those with assets of $10 million and greater) decreased by almost 9 percent. The dollar yield per hour decreased by 36 percent in FY 2007.

Continued effort to improve compliance is important to reducing the tax gap and maintaining the integrity of the voluntary tax compliance system. According to a tax gap strategy document dated September 2006, the tax gap for Tax Year 2001 was $345 billion.[5] The strategy document provides a broad base on which to build future efforts to address the tax gap but depends on future budgets to provide detailed strategy elements. In August 2007, the IRS released a report that builds on the strategy by providing details about actions planned to reduce the tax gap.[6] However, many of the actions will require the assistance of Congress.

Recommendation

We made no recommendations in this report. However, key IRS management officials reviewed the report prior to issuance and agreed with the facts and conclusions.

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[3] This includes examinations conducted by employees located in field offices and campuses.
[4] We computed this percentage using the audit technique to identify whether there was actual face-to-face contact during the examination. This number differs from publicized reports that rely solely on the organizational code.
[5] *A Comprehensive Strategy for Reducing the Tax Gap* (Department of the Treasury, Office of Tax Policy, dated September 26, 2006).
[6] *Reducing the Federal Tax Gap – A Report on Improving Voluntary Compliance* (IRS, dated August 2, 2007).

Copies of this report are also being sent to the IRS managers affected by the report information. Please contact me at (202) 622-6510 if you have questions or Margaret E. Begg, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-8510.

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Abbreviations

ACS	Automated Collection System
CFf	Collection Field function
FY	Fiscal Year
IRS	Internal Revenue Service
SCCB	Service Center Collection Branch
TDA	Taxpayer Delinquent Account
TDI	Taxpayer Delinquency Investigation
TIGTA	Treasury Inspector General for Tax Administration

Background

We initiated this review of nationwide compliance statistics for examination and collection activities due to an ongoing request of the Internal Revenue Service (IRS) Oversight Board. Our data analyses were performed in the Treasury Inspector General for Tax Administration (TIGTA) Chicago, Illinois, office during the period January through March 2008. We used nationwide data from IRS management information system reports during our review. Due to time and resource constraints, we did not audit IRS systems to validate the accuracy and reliability of their information. Also, we did not assess internal controls because doing so was not applicable within the context of our objective. Our analyses were limited to identifying changes and trends in data prepared and reported by the IRS.

Detailed information on our objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II. A Glossary of Terms is included in Appendix IV. Detailed charts and tables referred to in the body of this report are included in Appendix V. We eliminated some charts for examinations of individual taxpayers this year because the IRS Examination function changed the way in which it categorizes individual tax returns. We added charts showing statistics for efforts to secure delinquent tax returns from taxpayers.

Most of the calculations throughout the report and Appendix V are affected by rounding. All initial calculations were performed using the actual numbers rather than the rounded numbers that appear in the report. Much of the data included in this report update prior TIGTA reports on compliance trends. Appendix VI presents a list of those reports.

Results of Review

Overall, many compliance activities increased and results improved during Fiscal Year (FY) 2007. Since FY 2000, the IRS has reversed numerous downward trends in compliance activities that occurred in prior years. In FY 2007, many of these activities continued to increase, while others fell slightly from the prior year.

Although the IRS has reversed many of the downward trends in compliance activities, the enforcement staff levels in the Collection and Examination functions are not significantly higher than the 10-year lows experienced in FY 2003. The combined number of Collection function and Examination function enforcement personnel[1] declined by 23 percent, from approximately 19,500 at the beginning of FY 1998 to 15,000 at the end of FY 2007. After increasing by 8 percent during FY 2006, staffing decreased by 4 percent this year. The Small Business/Self-Employed Division FY 2008 Hiring Plan includes authorized hiring of nearly 1,000 revenue agents, tax compliance officers, and revenue officers. The Collection and Examination Enforcement budget was flat for FYs 2006 through 2008. However, the President's Budget Proposal for FY 2009 includes an 8 percent increase for that budget account.

Overall, Compliance Activities Increased and Results Improved

For some time, the total number of tax returns filed and the total dollars the IRS received (gross collections) have increased. In the past 10 years, the total number of tax returns filed grew by almost 12 percent, from about 161 million in Calendar Year 1997 to more than 179 million in Calendar Year 2006. IRS gross collections grew from $1.77 trillion in FY 1998 to $2.13 trillion in FY 2001, then fell a total of slightly more than 8 percent during FYs 2002 and 2003 to $1.95 trillion. These were the first decreases in total revenue since FY 1983. However, since FY 2003, gross collections have increased by almost 38 percent and reached a new record high of $2.69 trillion in FY 2007.[2]

After remaining relatively constant for FYs 1999 through 2002, the amount of enforcement revenue collected increased by almost 74 percent in the last 5 years. During FY 2007, enforcement revenue collected increased by 22 percent to $59.2 billion.[3] This amount (not adjusted for inflation) is 68 percent higher than the FY 1998 amount.[4]

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[1] Collection function and Examination function staff located in field offices, excluding management and overhead staff.
[2] See Appendix V, Figure 1.
[3] See Appendix V, Figure 3.
[4] See Appendix V, Figure 2.

As our report points out, the IRS has reversed many of the enforcement declines in both the Collection and Examination functions. However, despite work the IRS is doing to improve its enforcement efforts, the Government Accountability Office continued to include enforcement of tax laws (collection of unpaid taxes and Earned Income Tax Credit noncompliance) as 1 of the 26 high-risk areas in the Federal Government in its most recent (January 2007) update.[5] The Government Accountability Office states that improvements in compliance with tax laws will require efforts by the IRS and Congress.

Continued effort to improve compliance is important to reducing the tax gap and maintaining the integrity of the voluntary tax compliance system. According to a tax gap strategy document dated September 2006, the tax gap for Tax Year 2001 was $345 billion, representing a compliance rate of about 84 percent.[6] The purpose of the strategy document was to provide a broad base on which to build future efforts to address the tax gap. In August 2007, the IRS released a report that builds on the strategy by providing details about actions planned to reduce the tax gap.[7]

The IRS' current strategy for reducing the tax gap is largely dependent on receipt of funding for additional compliance resources and legislative changes. Therefore, long-term success will in large part be dependent on reducing risk factors, some of which are beyond the control of the IRS. One proposal–to add information reporting requirements–is a proven method for increasing compliance. However, outside stakeholder groups have expressed concern about the increased burden of additional information reporting requirements. However, 61 percent of taxpayers surveyed cited information reporting as a factor for reporting and paying taxes honestly.[8]

Collection Function Compliance Activities Increased and Results Improved

The number of Collection Field function (CFf) revenue officer personnel working assigned delinquent cases decreased 4 percent (to 3,724) by the end of FY 2007.[9] However, since the start of FY 1998, revenue officer staffing has decreased by almost 32 percent.

Although revenue officer staffing is down, many compliance activities continued to increase and results improved during FY 2007. Some of the improvements in Collection function activities that have occurred over the last few years could be the result of an FY 2005 organizational change in the Small Business/Self-Employed Division and efforts to improve business processes. However, the results of some activities were not positive.

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[5] *HIGH-RISK SERIES – An Update* (GAO-07-310, dated January 2007).
[6] *A Comprehensive Strategy for Reducing the Tax Gap* (Department of the Treasury, Office of Tax Policy, dated September 26, 2006).
[7] *Reducing the Federal Tax Gap – A Report on Improving Voluntary Compliance* (IRS, dated August 2, 2007).
[8] *IRS Oversight Board 2007 Taxpayer Attitude Survey* (dated February 2008).
[9] See Appendix V, Figure 5.

Many Collection function operations showed improvement

The following activities showed positive results for the Collection function during FY 2007:

- Dollars collected on Taxpayer Delinquent Accounts (TDA) by Automated Collection System (ACS) and CFf employees totaled just over $6.3 billion, an increase of almost 3 percent from FY 2006.[10] This year's amount is almost 76 percent greater than the 10-year low that occurred in FY 2000.
- The average amount collected per CFf staff year on TDAs increased by just over 2 percent from FY 2006. The amount increased by just over 109 percent (to $567,733) from a low of $271,110 in FY 1999.[11] However, the average amount collected is about 2 percent less than that in FY 2005, the 10-year high.
- The number of TDAs closed (excluding shelved accounts) and the number closed by full payment increased by almost 7 percent and by almost 6 percent, respectively, from FY 2006.[12] This year's volumes are the 10-year highs.
- The number of taxpayers with Taxpayer Delinquency Investigations (TDI) closed by the ACS and the CFf because delinquent tax returns were received by the IRS increased by almost 2 percent from FY 2006. This was due to the large increase in closures by the CFf; ACS closures decreased by almost 6 percent during the year. Overall, there has been a 74 percent increase since the 10-year low that occurred in FY 2002.
- As shown in Figure 1, the use of liens (a collection enforcement tool) has increased by 307 percent since the low experienced in FY 1999. During FY 2007, the number of liens issued by the CFf increased by almost 17 percent, while liens issued by the ACS decreased by almost 2 percent.[13] The CFf and total volumes represented 10-year highs. As mentioned

Figure 1: Use of Collection Enforcement Tools

	Liens	Levies	Seizures
FY 1998	382,755	2,503,409	2,259
FY 1999	167,867	504,403	161
FY 2000	287,517	219,778	74
FY 2001	426,165	674,080	234
FY 2002	482,509	1,283,742	296
FY 2003	544,316	1,680,844	399
FY 2004	534,392	2,029,613	440
FY 2005	522,887	2,743,577	512
FY 2006	629,813	3,742,276	590
FY 2007	683,659	3,757,190	676

Source: Small Business/Self-Employed Division Collection Planning and Analysis, Collection National Reports, and IRS Data Book.

10 See Appendix V, Figure 9.
11 See Appendix V, Figure 8.
12 See Appendix V, Figures 17 and 18.
13 See Appendix V, Figure 19.

in last year's report, part of the increase in the number of liens filed on accounts with large balance-due amounts might be attributable to procedural changes made by the Collection function.[14]

As also shown in Figure 1, the uses of levies and seizures (additional collection enforcement tools) increased substantially from lows experienced in FY 2000. Levies increased by 1,610 percent, and seizures increased by 814 percent.[15] While use of levies has surpassed the FY 1998 level, the current seizure level represents only a small fraction of the FY 1998 level. The use of seizures is unlikely to return to a pre-1998 level in the foreseeable future.

Some Collection function operations showed mixed results

Some indicators were not positive for Collection function compliance activity during FY 2007.

- The amount of gross accounts receivable increased by almost 7 percent (to $290 billion) after increasing almost 5 percent during FY 2006.[16] The FY 2007 amount represents the 10-year high. The increase in gross accounts receivable occurred even though there were increases in gross collections and enforcement revenue collected.
- More TDAs were received than closed, and the gap between TDA receipts and TDA closures had widened by almost 63 percent (to 1,914,508 accounts) as of the end of the fiscal year.[17] This is the largest year-end gap in the 10-year period.

An inventory of unassigned collection cases is maintained in the Queue. The number of taxpayers with TDAs in the Queue and the amount owed on these accounts increased to 10-year highs during FY 2007.[18] The number of taxpayer accounts increased by just over 11 percent to 866,777. At the same time, the amount owed increased by just over 28 percent to $34.9 billion. One reason for the increase in the Queue is a rise in the number of compliance assessments.[19] In addition, the number of taxpayers with TDIs increased by just over 21 percent to 998,287, even though there was a just over 173 percent increase in the number of these accounts that were shelved or surveyed (removed from inventory) during the year.[20] Although many of the cases in the Queue might be assigned to be worked, a significant number might never be worked.

As noted above, the Queue inventory increased during FY 2007. However, those inventory figures do not include the millions of TDA and TDI tax periods shelved or surveyed (removed)

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[14] *High-Risk Work Is Selected From the Unassigned Delinquent Account Inventory, but Some Unassigned Accounts Need Management's Attention* (Reference Number 2006-30-030, dated February 2006).
[15] See Appendix V, Figures 20 and 21.
[16] See Appendix V, Figure 3.
[17] See Appendix V, Figure 15.
[18] See Appendix V, Figure 16.
[19] See Appendix V, Figures 22, 24, and 45.
[20] See Appendix V, Figures 10 and 11.

from Collection function inventory during the last few years. In FYs 2001 through 2007, the IRS removed almost 7.6 million TDAs[21] (with balance-due amounts totaling almost $31.2 billion) and 18.1 million TDI tax periods from Collection function inventory. These cases were removed because they were potentially less productive than other available inventory and might never be worked.

The Collection function is unable to work all of the existing accounts in the Queue with current staffing, and the number of TDA receipts is outpacing closures. If changes do not occur, a significant number of cases will continue to not be worked. This reinforces the need for additional resources to work the cases. As previously noted, the number of revenue officers decreased during FY 2007, but there are plans to hire for this position during FY 2008. In addition, in September 2006, the IRS started assigning balance-due cases that otherwise would not have been worked to private collection agencies. Through FY 2007, the IRS had received a total of $26.6 million after expected commissions on cases assigned to the collection agencies, and program costs totaled $69.8 million. More than 96 percent of the total revenue collected by the agencies was received in FY 2007 alone. The program netted $11.3 million after subtraction of expected commissions and program costs for the year. However, continued use of private collection agencies is uncertain because some members of Congress want the IRS to discontinue their use.

Examination Function Compliance Activities Increased and Results Improved

Overall, the number of field Examination function personnel that conduct examinations of tax returns decreased by just over 4 percent between FYs 2006 and 2007. The number of revenue agents decreased to 10,121, while the number of tax compliance officers decreased to 1,060 as of the end of the fiscal year.[22] The number of examiners in field offices[23] has decreased by almost 20 percent since the start of FY 1998.

Despite the decrease in the number of examiners during FY 2007, Examination function compliance activities increased in some areas, as noted below. Some of this increase could have been the result of changes implemented by the Small Business/Self-Employed Division, which over the last few years has implemented reengineering and organizational changes that could have had a positive impact on compliance activities within the Examination function. In addition, the Examination function continues to study methods that will result in identifying for examination those tax returns that contain greater potential for noncompliance.

[21] See Appendix V, Figure 11.
[22] See Appendix V, Figure 4.
[23] Examiners in field offices include revenue agents, tax compliance officers, tax examiners, and revenue officer examiners.

Compared to FY 2006, the percentage of tax returns examined increased for most types of returns during FY 2007. At the same time, the dollar yield per hour on examinations increased for individual tax returns, but revenue agent results decreased for corporate and other types of tax returns.[24]

The number of tax returns examined increased, but many examinations were conducted via correspondence

When analyzing examination coverage rates, one must recognize differences in the types of contacts that are counted in Examination function statistics. Examinations range from issuance of an IRS notice asking for clarification of a single tax return item that appears to be incorrect (correspondence examination) to a full, face-to-face interview and review of the taxpayer's records. Face-to-face examinations are generally more comprehensive and time consuming for the IRS and the taxpayers, and they typically result in higher dollar adjustments to the tax amounts. Thus, caution should be used when combining statistics from the various Examination function programs into overall examination rates. During FY 2007, slightly more than 71 percent of all examinations were conducted via correspondence.

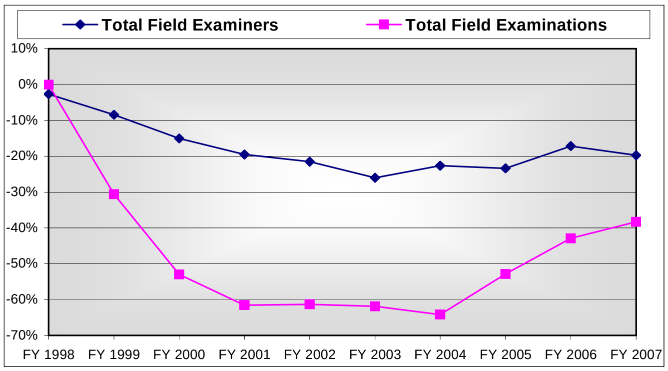
In addition, the IRS uses several computer-matching and automated error-checking routines in the Computing Centers to check the accuracy of tax returns. These routines often identify adjustments to tax liabilities. However, these adjustments are not included in the traditional "audit rates" and are not generally reported separately as enforcement efforts.

The overall percentage of tax returns examined (including face-to-face and correspondence examinations) increased by almost 9 percent[25] from FY 2006 and has doubled since FY 2000. In addition, the overall percentage of tax returns examined was almost 2 percent higher than in FY 1998. The largest increase in the examination rate from FY 2000 was due to examinations of individual, employment, and excise tax returns. Examinations of other types of tax returns did not increase as significantly or decreased.

[24] See Appendix V, Figures 23 through 26.

[25] The IRS has traditionally calculated the percentage of examination coverage by dividing the number of returns examined in the current fiscal year by the number of returns filed in the preceding calendar year.

Figure 2: Percentage Change in the Number of Field Examiners and Examinations



Source: IRS Data Book and Examination Table 37.

Figure 2 compares the change in field Examination function staffing to the change in the number of examinations by field employees, for all types of tax returns, from the beginning of FY 1998 through FY 2007. The chart line for the number of field examiners does not start at zero because the number of examiners conducting examinations during FY 1998 decreased by almost 3 percent during the year. While Examination function staffing decreased during FY 2007, the IRS plans to hire additional examiners in FY 2008.

A continued effort to increase examination coverage is important to maintaining the effectiveness of the voluntary tax compliance system. The study of taxpayer attitudes about the acceptability of cheating on taxes showed a decline in each of the last 2 years, after showing improvements each year since 2003. In 2007, 13 percent of taxpayers believed it was acceptable to cheat on their tax returns. This is up from 10 percent in 2005. Fear of examination as a major factor influencing taxpayers to report taxes honestly also decreased in the last 2 years. In 2007, 54 percent of taxpayers surveyed cited fear of examination as a factor that influenced their voluntary compliance. This is down from 62 percent in 2005.

The following paragraphs summarize examination coverage for various types of tax returns:

- *Individual Income Tax Examinations* – Overall, the number of individual income tax returns examined decreased from FY 1998 through FY 2000. During FY 2000, only 617,765 (1 of every 202) individual income tax returns were examined. Since then, the number examined has continuously increased: 1,384,563 (1 of every 97) returns were examined in FY 2007.[26] Almost 83 percent of the examinations of individuals were done by correspondence during FY 2007.[27] Only 1 of every 561 individual income tax returns filed received a face-to-face examination, while 1 of every 118 received a correspondence examination.
- *Corporate Income Tax Examinations* – The number of corporate income tax returns examined (excluding returns for foreign corporations and S Corporations) increased by

[26] This includes examinations conducted by employees located in field offices and campuses. See Appendix V, Figure 29.
[27] We computed this percentage using the audit technique to identify whether there was actual face-to-face contact during the examination. This number differs from publicized reports that rely solely on the organizational code.

just over 4 percent in FY 2007, after decreasing by 1 percent in FY 2006. However, the number of examinations has decreased by almost 45 percent since FY 1998. In FYs 1998 to 2007, the total number of corporate tax returns examined decreased from 53,648 (1 of every 48 returns filed) to 29,664 (1 of every 75 returns filed).[28] The number of corporate income tax returns filed decreased by 13 percent during the 10-year period. The decrease in the number of returns filed reduced the impact on the examination coverage rate.

The number of corporate tax returns examined with assets of less than $10 million increased by slightly over 12 percent in FY 2007. During the same period, the number of corporate tax returns examined with assets of $10 million and greater decreased by almost 9 percent, and examinations of those with assets of $250 million and greater decreased by almost 20 percent. However, a much higher percentage of the large corporations than those with assets of less than $10 million is examined.

- *S Corporation Return Examinations* – After declining by 75 percent from FYs 1998 to 2004, the number of S Corporation tax returns examined increased by almost 176 percent from FYs 2004 to 2007. The increase in FY 2007 alone was slightly over 26 percent. Since FY 2004, the number of S Corporation returns filed has increased by 16 percent. During that period, the number of tax returns examined increased from 1 of every 526 returns filed to 1 of every 221 returns filed.[29] The increase in examination coverage can be partly attributed to the IRS research project studying the compliance of S Corporation entities. However, almost all of these examinations are completed, which could result in a decrease in the number of examinations in future years. The results of this project could lead to future changes in the examination selection methodology for this type of tax return.
- *Partnership Return Examinations* – The number of partnership returns examined increased by 25 percent in FY 2007 and has increased by almost 141 percent since the 10-year low experienced in FY 2001. The number of returns filed increased by about 42 percent between FYs 2001 and 2007.[30] About 1 of every 408 returns filed was examined in FY 2001. This increased to 1 of every 241 for this year.
- *Other Tax Types Examinations (Fiduciary, Employment, Excise, Estate, and Gift Taxes)* – The overall number of examinations in these 5 classes increased by just over 49 percent during FY 2007 and was up just over 156 percent from the 10-year low experienced in FY 2003. A major portion of this year's increase was due to rises in the number of examinations of employment and excise tax returns. The number of fiduciary

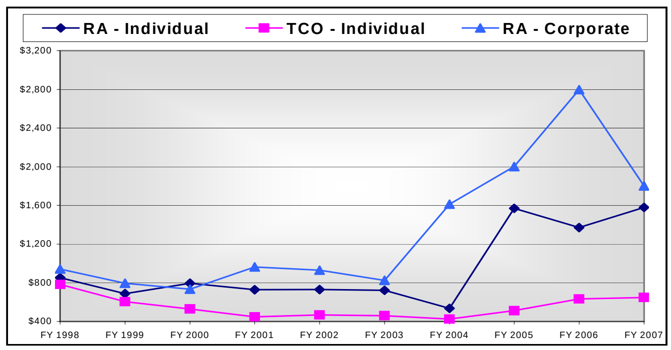
[28] See Appendix V, Figures 34, 35, and 46 for coverage by size of corporation.
[29] See Appendix V, Figures 37 and 46.
[30] See Appendix V, Figures 38 and 46.

returns examined increased slightly, but the number of estate and gift tax returns examined decreased.[31]

Examination function dollar yield per hour has mixed results

Figure 3 shows the dollar yield per hour for FYs 1998 through 2007 for revenue agents and tax compliance officers. The dollar yield per hour improved for examinations of individual tax returns during FY 2007–by almost 3 percent for tax compliance officers and by just over 15 percent for revenue agents. However, the yield decreased by almost 36 percent for revenue agent examinations of corporate tax returns during FY 2007.

Figure 3: Examination Function Dollar Yield per Hour



Source: TIGTA analysis of Examination Table 37. RA = revenue agent. TCO = tax compliance officer.

The Examination function dollar yield per hour for individual income tax return examinations was lower in FY 2004 than in FY 1998.[32] Since FY 2004, the yield has increased each year for tax compliance officers. The dollar yield per hour increased significantly for revenue agents during FY 2005, decreased slightly during FY 2006, then increased slightly during FY 2007. The dollar yield per hour for revenue agents is above the FY 1998 level, but the yield for tax compliance officers is not. The dollar results per individual income tax return examined fluctuated during the 10-year period, especially for revenue agents. The number of hours used to examine each tax return increased substantially through FY 2004, then decreased through FY 2007 except for a small increase during FY 2007 for tax compliance officers.

The dollar yield per hour spent examining corporate tax returns increased by 239 percent from FYs 2003 to 2006 and then decreased almost $1,000 per hour (36 percent) in FY 2007.[33] During the same time period, the average hours spent examining each tax return and the average dollar amounts assessed per return fluctuated significantly. The net effect was an increase in the dollar yield per hour for FYs 2003 through 2006 and a decrease in FY 2007.

Conclusion

Since FY 2000, the IRS has reversed numerous downward trends in compliance activities that occurred in both the Collection and Examination functions. The IRS should continue its efforts to improve the business processes and workload selection methods because they appear to be

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[31] See Appendix V, Figures 39 through 43 and 46.
[32] See Appendix V, Figures 23 and 26.
[33] See Appendix V, Figure 24.

having a positive impact on compliance efforts. In addition, the hiring and training of new enforcement personnel should continue to be a top priority because many experienced employees in those positions are already eligible for retirement or will become eligible in the next few years.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to provide statistical information and trend analyses of examination and collection activities, as requested by the IRS Oversight Board.[1]

To accomplish our objective, we analyzed information obtained from IRS management information system reports to determine trends and changes in the major areas of compliance. Due to time and resource constraints, we did not audit IRS systems to validate the accuracy and reliability of their information. Also, we did not assess internal controls because doing so was not applicable within the context of our objective. The major issues we focused on included:

- Enforcement revenue and gross accounts receivable.
- Collection and Examination function staffing.
- Collection and Examination function direct time.
- Collection function delinquent account inventories and unfiled return investigations.
- Collection function enforcement actions (liens, levies, and seizures).
- Examination function coverage of individual and business tax returns compared to the number of returns filed in each category.
- Examination function productivity results for individual and business tax returns.
- Other activities resulting in improvements in the accuracy of filed tax returns and the filing of delinquent returns.

[1] See Appendix IV for a glossary of terms used in this report.

Appendix II

Major Contributors to This Report

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Appendix III

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Appendix IV

Glossary of Terms

6020(b) Program – A provision of the Internal Revenue Code that allows the IRS to prepare returns for businesses when they appear to be liable for a return, have not filed the return, and attempts to secure the return have failed.

Automated Collection System – A telephone contact system through which telephone assistors collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.

Automated Substitute for Return system – A system designed to assess taxes on wage earners who fail to file tax returns. It analyzes information submitted to the IRS and historical tax return information.

Balance Sheet – A statement of the financial assets and liabilities of a business at a given date filed with a corporate income tax return. It is used by the IRS to group businesses by the size of their assets.

Campus – The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

Collection Field function – The unit in the field offices consisting of revenue officers who handle personal contacts with taxpayers to collect delinquent accounts or secure unfiled tax returns.

Compliance Assessments – Those assessments generated by the Examination function, the Underreporter Program, the Automated Substitute for Return Program, and the 6020(b) Program.

Computing Centers – IRS facilities that support tax processing and information management through a data processing and telecommunications infrastructure.

Corporate Income Tax Return – U.S. Corporation Income Tax Return (Form 1120). It is used by corporations to report the corporate income tax.

Dollar Yield Per Hour – The amount of tax adjustments on tax returns divided by the number of hours spent examining those returns.

Earned Income Tax Credit – A tax credit for certain people who work and have income under established limits.

Employment Tax Returns – Various Form 940 return series (primarily Employer's Annual Federal Unemployment (FUTA) Tax Return (Form 940) and Employer's QUARTERLY Federal Tax Return (Form 941)) filed by businesses to report things such as employer's Federal unemployment taxes and Federal taxes withheld.

Enforcement Revenue – Any tax, penalty, or interest received from a taxpayer as a result of an IRS enforcement action (usually an examination or a collection action).

Estate Tax Return – United States Estate (and Generation-Skipping Transfer) Tax Return (Form 706). It is filed for estates of certain deceased persons.

Examination (Face-to-Face) – A field examination of an individual, a partnership, or a corporation that occurs either at the taxpayer's place of business or through an interview(s) at an IRS office.

Excise Tax Return – Quarterly Federal Excise Tax Return (Form 720). It is used to report and pay certain taxes, such as those on transportation and fuel.

Fiduciary Income Tax Returns – Income tax returns filed for estates and trusts.

Gift Tax Return – United States Gift (and Generation-Skipping Transfer) Tax Return (Form 709). It is used to report transfers subject to the Federal gift taxes and to calculate the taxes due on those transfers.

Gross Accounts Receivable – Includes all unpaid tax, with accrued penalties and interest, on taxpayers' delinquent accounts.

Individual Income Tax Returns – U.S. Individual Income Tax Returns (Form 1040 series). They are annual income tax returns filed by citizens or residents of the United States.

IRS Data Book – An IRS annual report providing information on returns filed and taxes collected, enforcement, taxpayer assistance, the IRS budget and workforce, and other selected activities for the fiscal year.

IRS Oversight Board – An independent body charged with overseeing the IRS in its administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws.

Levy – A method used by the IRS to collect outstanding taxes from sources such as bank accounts and wages.

Lien – An encumbrance on property or rights to property as security for outstanding taxes.

Math Error Program – A process in which the IRS contacts taxpayers through the mail or by telephone when it identifies mathematical errors or mismatches of taxpayer information that would result in tax changes.

National Research Project – Research conducted by the IRS to determine filing, payment, and reporting compliance by taxpayers for different types of taxes.

Overhead Staff – Support staff performing indirect duties within the function such as automation support, technical support, and quality review.

Partnership Return – U.S. Return of Partnership Income (Form 1065). It is used to report the income and expenses of domestic partnerships and the share distributed to each partner.

Queue – An automated holding file for unassigned inventory of delinquent cases for which the Collection function does not have enough resources to immediately assign for contact.

Revenue Agent – An employee in the Examination function who conducts face-to-face examinations of more complex tax returns such as businesses, partnerships, corporations, and specialty taxes (e.g., excise tax returns).

Revenue Officer – An employee in the CFf who attempts to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses (formerly known as service centers) or the ACS.

Revenue Officer Examiner – A revenue officer who has been trained to conduct examinations of employment tax returns.

S Corporation Tax Return – U.S. Income Tax Return for an S Corporation (Form 1120S). It is filed by qualifying small business corporations and includes amounts distributed to shareholders.

Seizure – The taking of a taxpayer's property to satisfy his or her outstanding tax liability.

Service Center Collection Branch – An IRS function that mails the balance-due and return-delinquency notices to taxpayers and analyzes and responds to taxpayer correspondence.

Shelved or Surveyed Cases – Delinquent unpaid accounts or investigations of unfiled tax returns that have been taken out of the Collection function inventory because they are of lower priority than other available inventory.

Tax Compliance Officer/Tax Auditor – An employee in the Examination function that primarily conducts examinations of individual taxpayers through interviews at IRS field offices. The position title was changed in 2002 from tax auditor to tax compliance officer.

Tax Examiner – In the context of this report, an employee located in a field office who conducts examinations through correspondence. However, the tax examiner position is also used for many other types of positions located in various IRS offices.

Taxpayer Delinquent Account – A balance-due account of a taxpayer. A separate TDA exists for each delinquent tax period.

Taxpayer Delinquency Investigation – An unfiled tax return(s) for a taxpayer. One TDI exists for all delinquent tax periods for a taxpayer.

Tax Gap – The difference between what taxpayers should have paid and what they actually paid on time.

Tax Period – Refers to each tax return filed by the taxpayer for a specific period (year or quarter) during a calendar year for each type of tax.

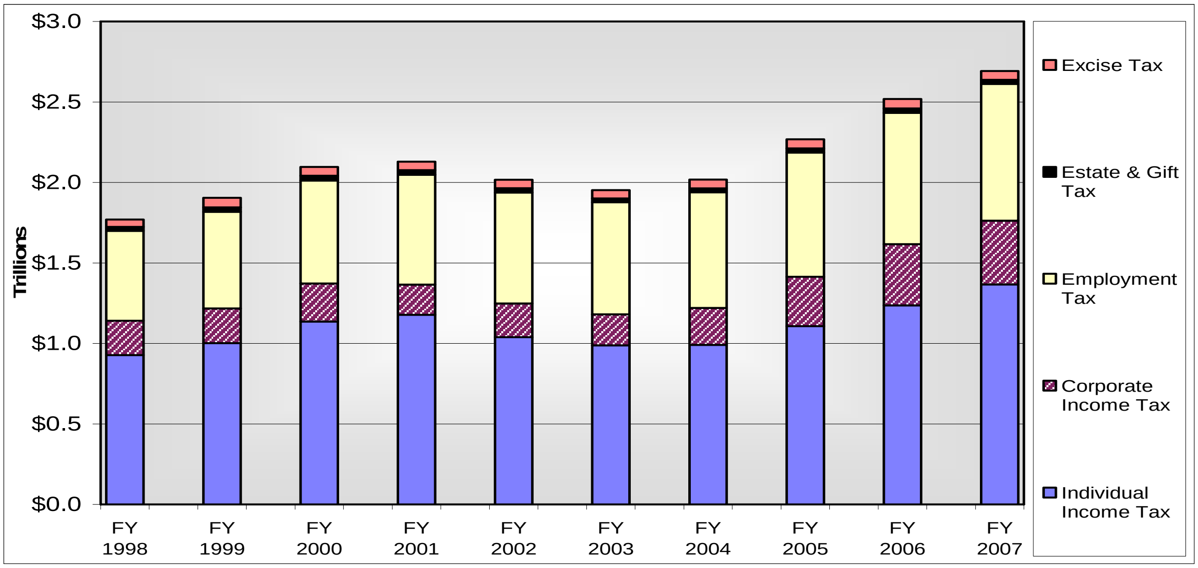
Underreporter Program – A process where items reported on an individual's income tax return are matched to information supplied to the IRS from outside sources (such as employers, banks, and credit unions) to determine if the taxpayer's tax return reflected the correct amounts and if the tax amount is correct.

Appendix V

Detailed Charts of Statistical Information

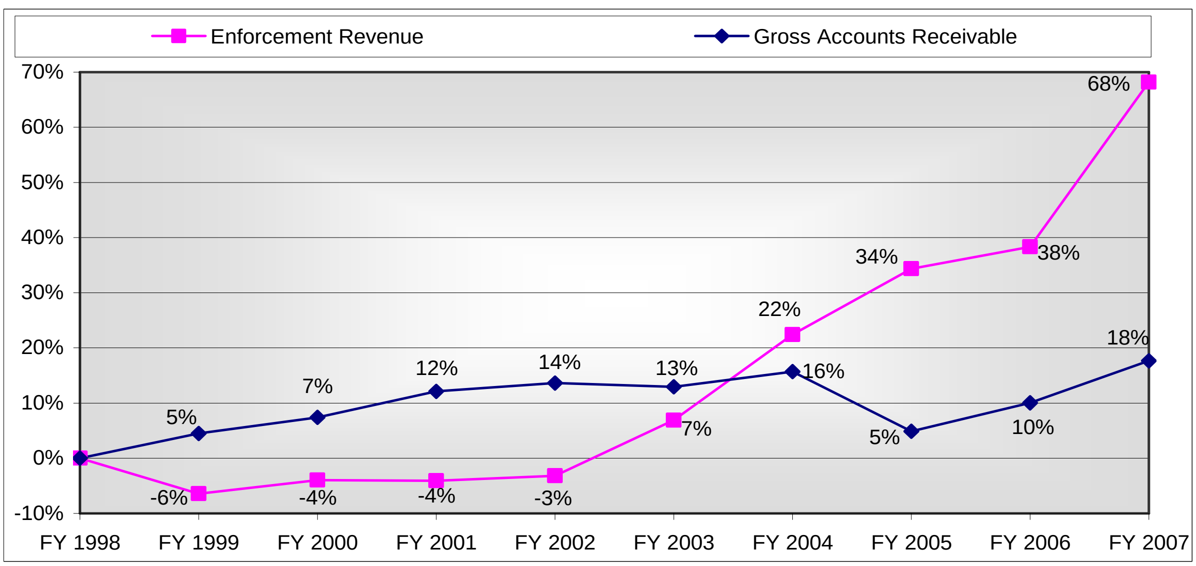
***Note**: We eliminated some charts for examinations of individual taxpayers this year because the IRS Examination function changed the way in which it categorizes individual tax returns. We added charts showing statistics for efforts to secure delinquent tax returns from taxpayers.*

Figure 1. Gross Collections by Type of Tax Since FY 1998. Overall, gross tax collections rose in FY 2007 to the highest level of the 10-year analysis. Since the low experienced in FY 2003, tax collections have increased by 104 percent (corporate income tax), 38 percent (individual income tax), and 22 percent (employment tax).



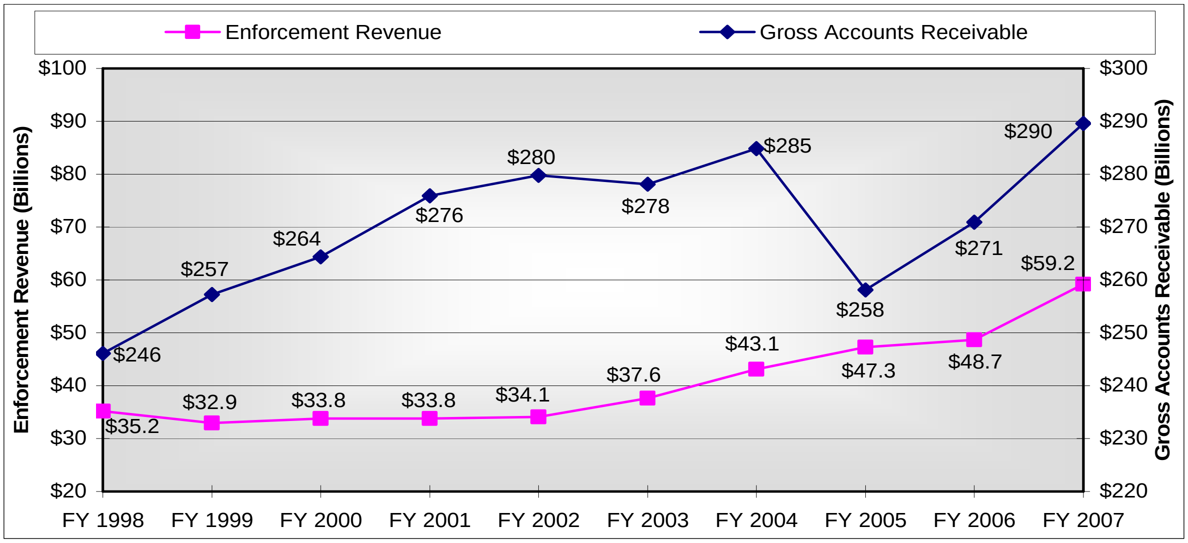
Source: TIGTA analysis of IRS Data Book.

Figure 2. Changes in Enforcement Revenue and Gross Accounts Receivable – Percentage Change From FY 1998. Enforcement revenue has been increasing sharply since FY 2002. In FY 2007, it was 68 percent higher than in FY 1998. After decreasing sharply during FY 2005, gross accounts receivable was 18 percent higher in FY 2007 than in FY 1998.



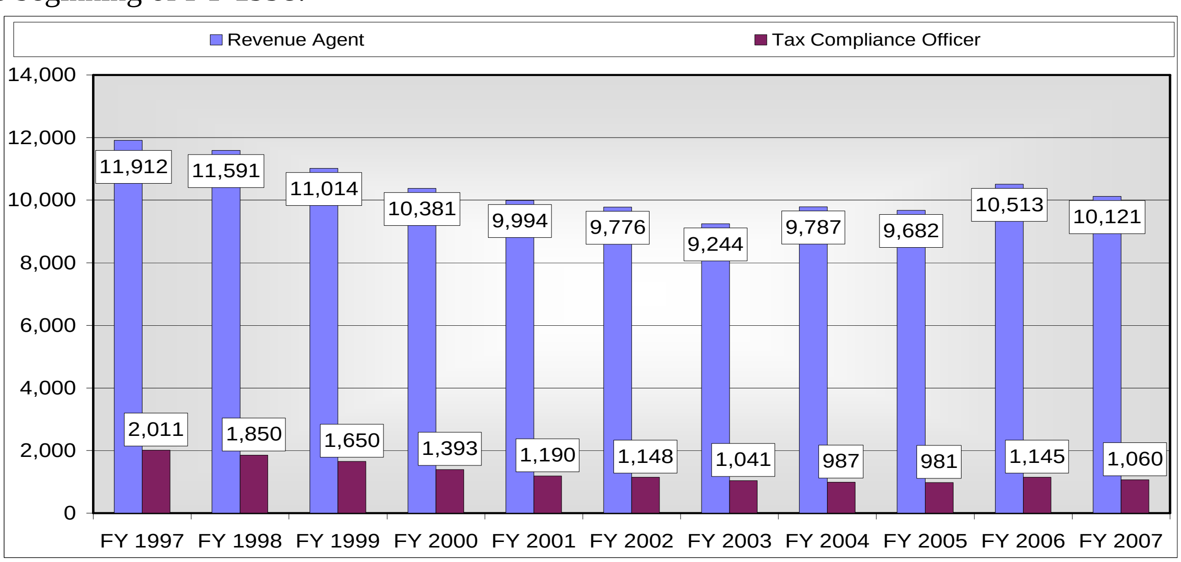
Source: Office of Research, Analysis, and Statistics and Chief Financial Officer information.

Figure 3. Amounts of Enforcement Revenue Collected Compared to Growth in Gross Accounts Receivable. After dropping off significantly during FY 2005, gross accounts receivable has increased by almost $31.5 billion since then. During the same time period, enforcement revenue increased by $11.9 billion.



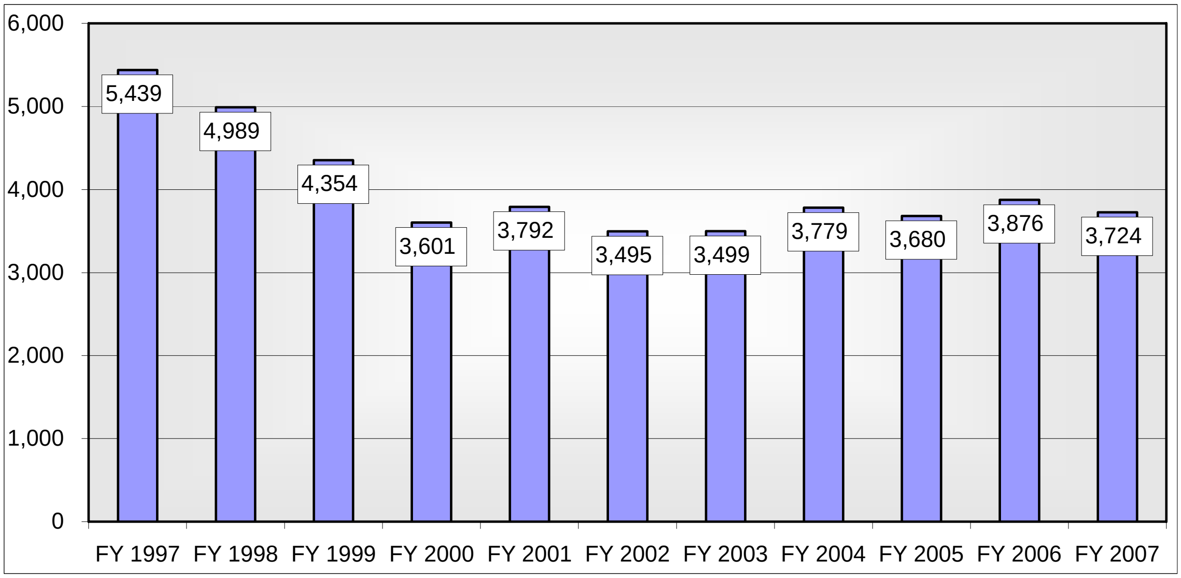
Source: Office of Research, Analysis, and Statistics and Chief Financial Officer information.

Figure 4. Examination Function Staffing at the End of Each Fiscal Year. The numbers in Figure 4 represent the Examination function staff conducting examinations of tax returns (excludes management and overhead staff). During FY 2007, revenue agent and tax compliance officer staffing decreased slightly. The combined total is almost 20 percent lower than it was at the beginning of FY 1998.



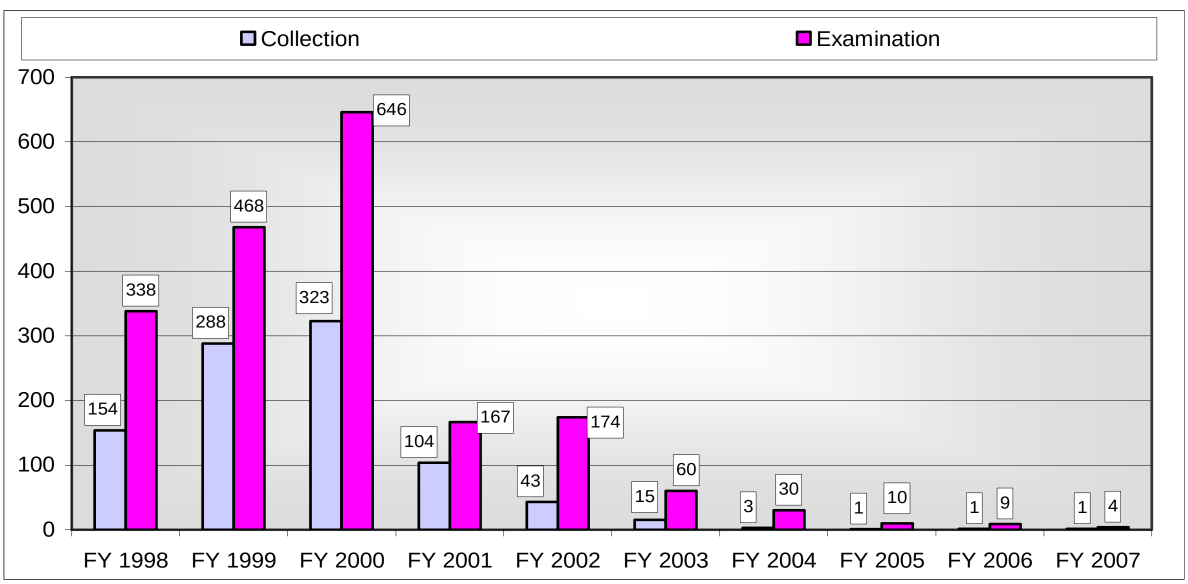
Source: TIGTA analysis of Examination Table 37.

Figure 5. CFf Staffing at the End of Each Fiscal Year. The number of revenue officers working assigned delinquent cases (excludes management and overhead staff) decreased slightly during the year and was almost 32 percent lower than at the start of FY 1998.



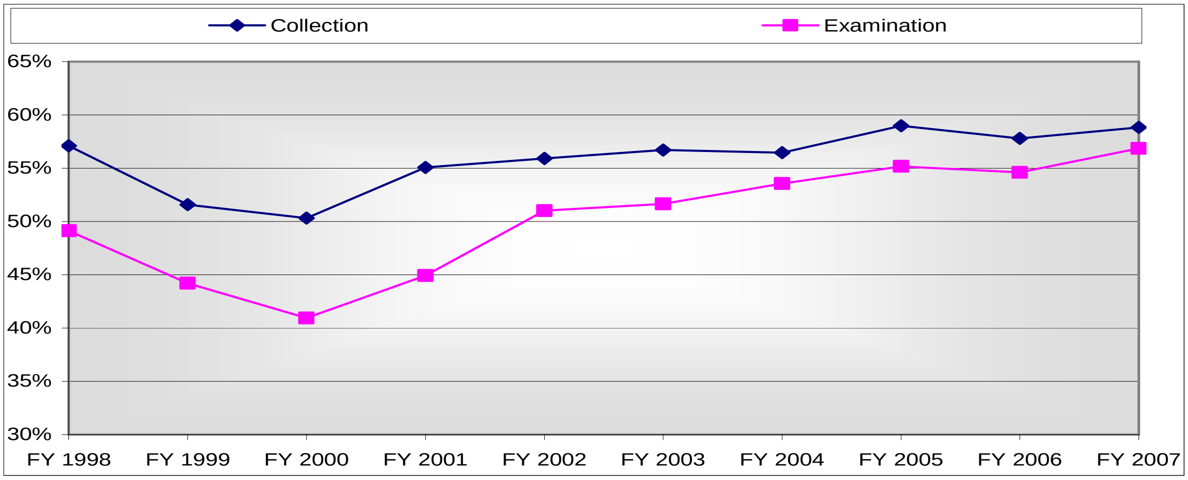
Source: Collection Report 5000-23.

Figure 6. Staff Years Detailed to Assist Walk-In Taxpayers. The number of staff years detailed to assist walk-in taxpayers decreased again in FY 2007 and remained lower than the number detailed during FY 1998.



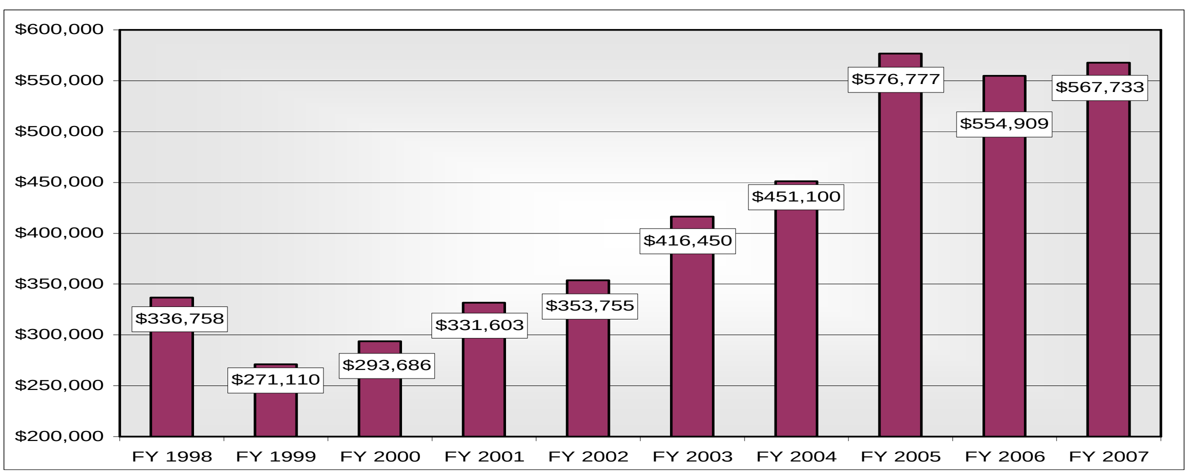
Source: TIGTA analysis of Collection Report 5000-23 and Examination Table 37.

Figure 7. Changes in Direct Time Percentages. The Collection and Examination functions both increased the percentage of overall time charged to their direct tax-related responsibilities (collecting taxes, securing tax returns not timely filed, and examining tax returns) during FY 2007. This can be partially attributed to a decrease in training time because there were fewer new hires. The Collection and Examination functions changed the types of time they capture as direct and indirect in recent years, including capturing some of the previous indirect time as direct time. Figure 7 depicts our recalculation of direct time based on direct time categories from prior years, to present consistent data for the 10 years included in the graph.



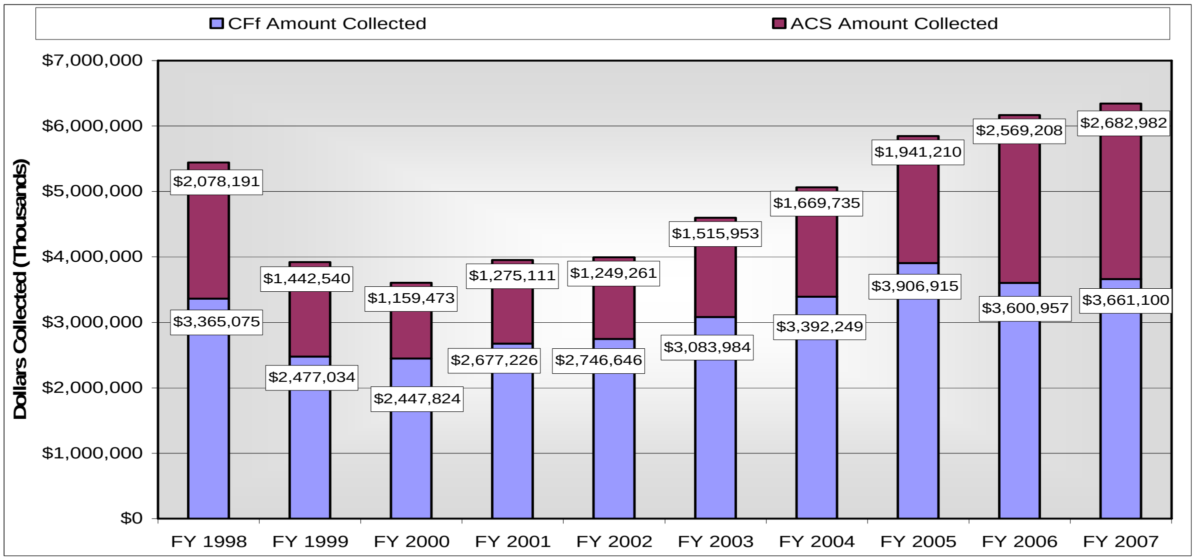
Source: TIGTA analysis of Collection Report 5000-23 and Examination Table 37.

Figure 8. Average Dollars Collected per Staff Year on TDAs by the CFf. The average amount collected by the CFf for each staff year has increased by just over 109 percent since FY 1999. It increased by just over 2 percent in FY 2007, after decreasing by almost 4 percent in FY 2006.



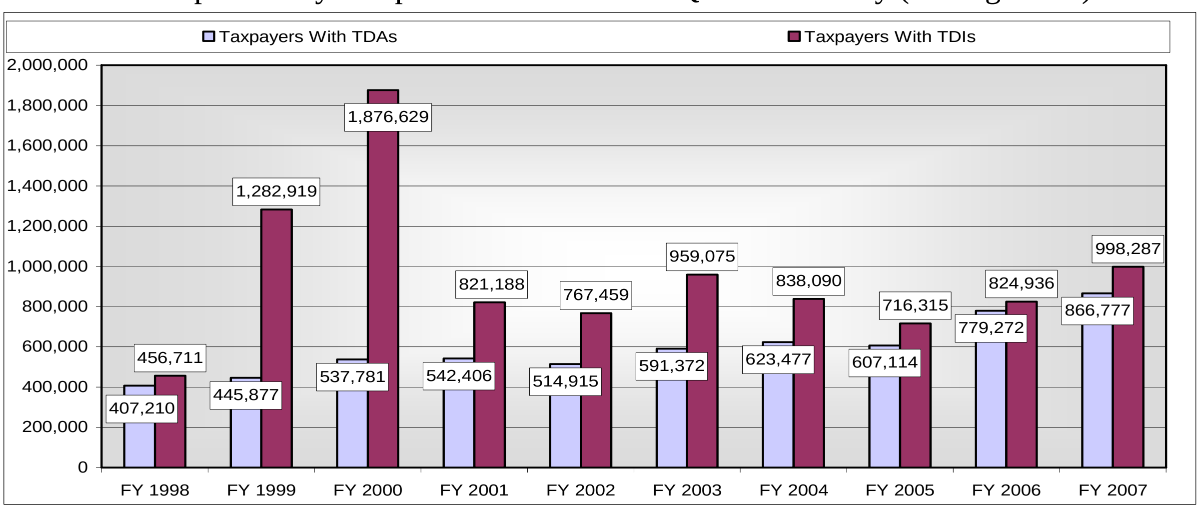
Source: TIGTA analysis of Collection Reports 5000-2 and 5000-23.

Figure 9. Total Dollars Collected on TDAs by the CFf and ACS. The combined amount collected by the CFf and ACS has increased each year since FY 2000. The CFf and ACS both had increases in the amounts collected during FY 2007.



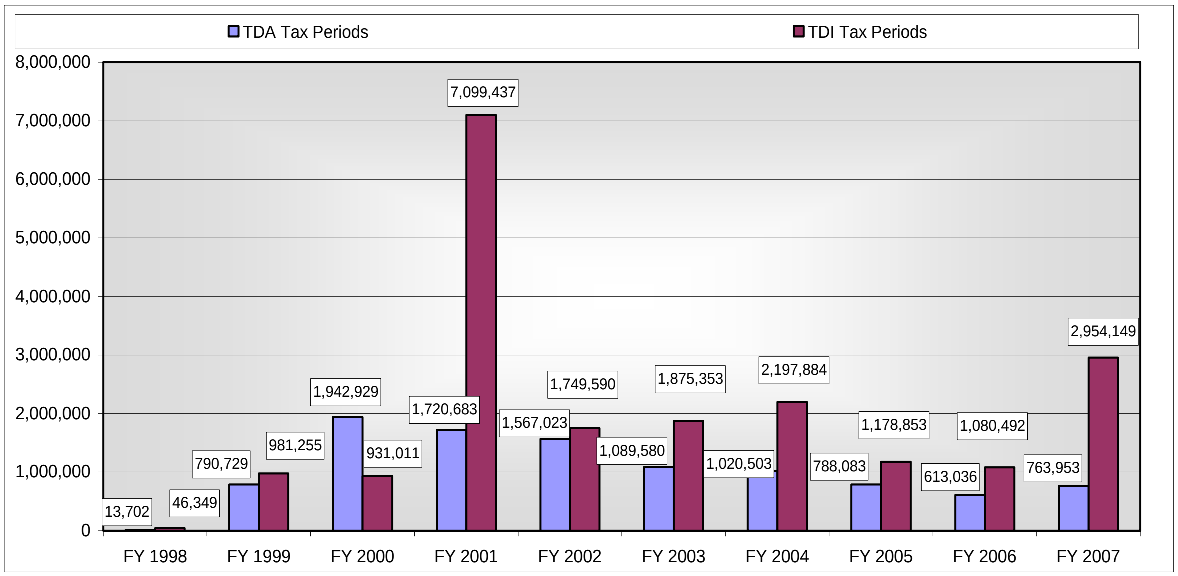
Source: Collection Report 5000-2.

Figure 10. TDAs and TDIs in the Queue. The number of taxpayers with TDIs in the Queue increased from FYs 1998 to 2000–with significant spikes during FYs 1999 and 2000–then decreased to remain at lower levels. However, the overall trend showed an increase in the number of taxpayers with TDAs in the Queue during FYs 1998 through 2007. This occurred even though, in recent years, the IRS removed from the Queue a large number of cases that were considered to be potentially less productive than other Queue inventory (see Figure 11).



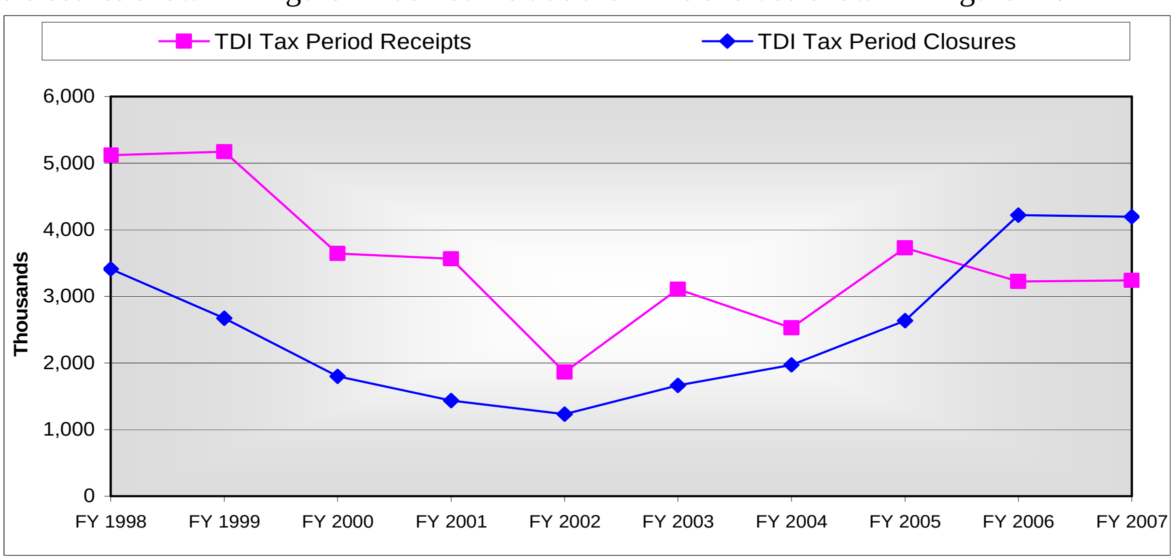
Source: Collection Reports 5000-2 and 5000-4.

Figure 11. TDA and TDI Tax Periods Shelved or Surveyed Each Year. While the total volume of TDA and TDI tax periods shelved or surveyed decreased by just over 47 percent from FY 2004 to FY 2006, it increased by almost 120 percent during FY 2007. The IRS has removed millions of TDA and TDI tax periods from the Queue inventory in recent years.



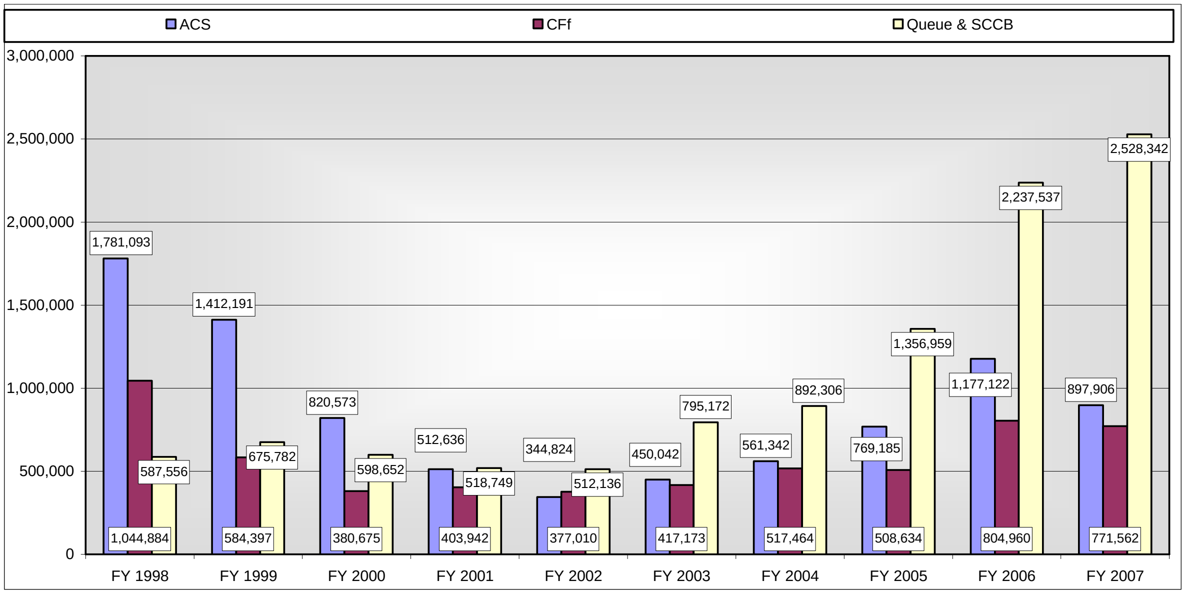
Source: TIGTA analysis of Collection Reports 5000-2 and 5000-4.

Figure 12. Gap Between TDI Tax Period Receipts and Closures. The volume of TDI receipts and closures during FY 2007 remained basically unchanged from the prior year. However, the number of cases closed increased from the 10-year low experienced in FY 2002. The closures shown in Figure 12 do not include the TDIs shelved shown in Figure 11.



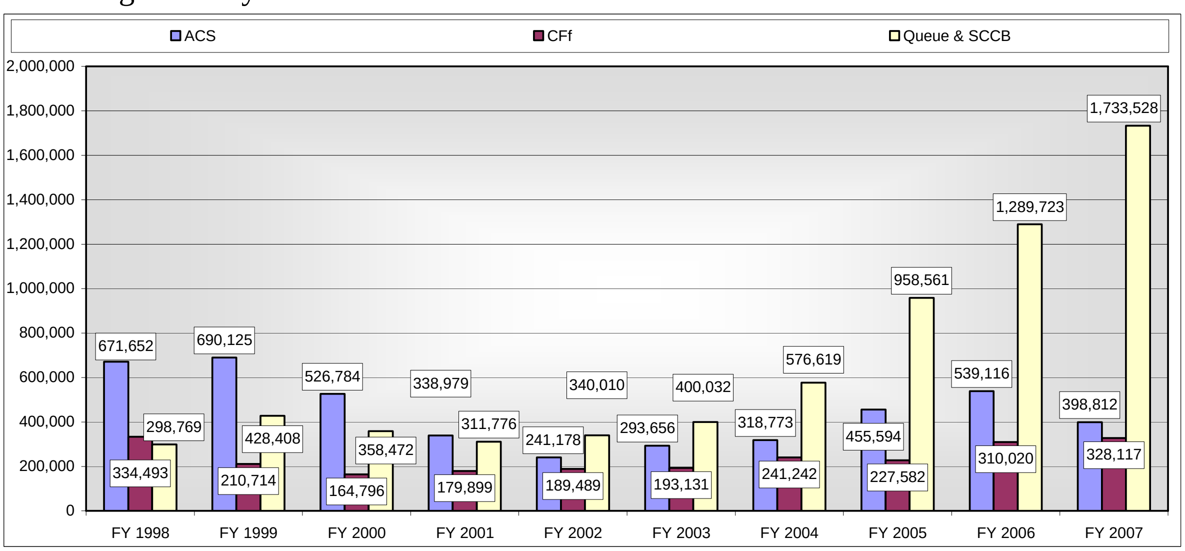
Source: TIGTA analysis of Collection Report 5000-4.

Figure 13. Number of TDI Tax Periods Closed, Excluding Shelved Accounts. The number of TDI tax periods closed by both the ACS and the CFf decreased during FY 2007, after showing an overall pattern of increasing since FY 2002. However, the number closed from the Queue and by the Service Center Collection Branch (SCCB) has increased substantially since FY 2002.



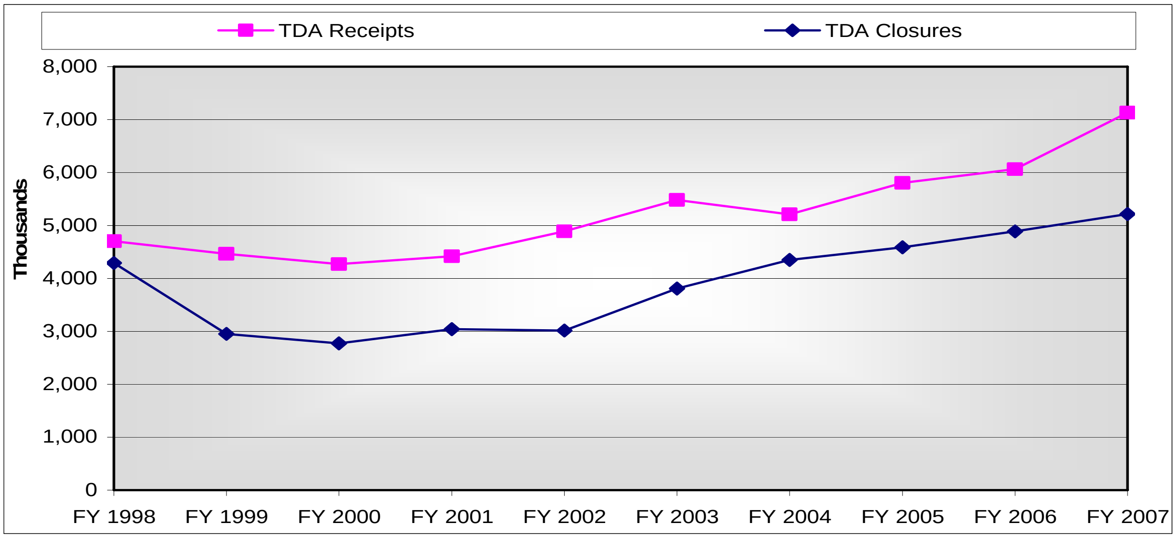
Source: TIGTA analysis of Collection Report 5000-4.

Figure 14. Number of TDI Tax Periods Closed With Receipt of a Delinquent Tax Return. The number of delinquent tax returns received increased for the CFf, while the number decreased for the ACS during FY 2007. The number closed from the Queue and by the SCCB has increased significantly since FY 2004.



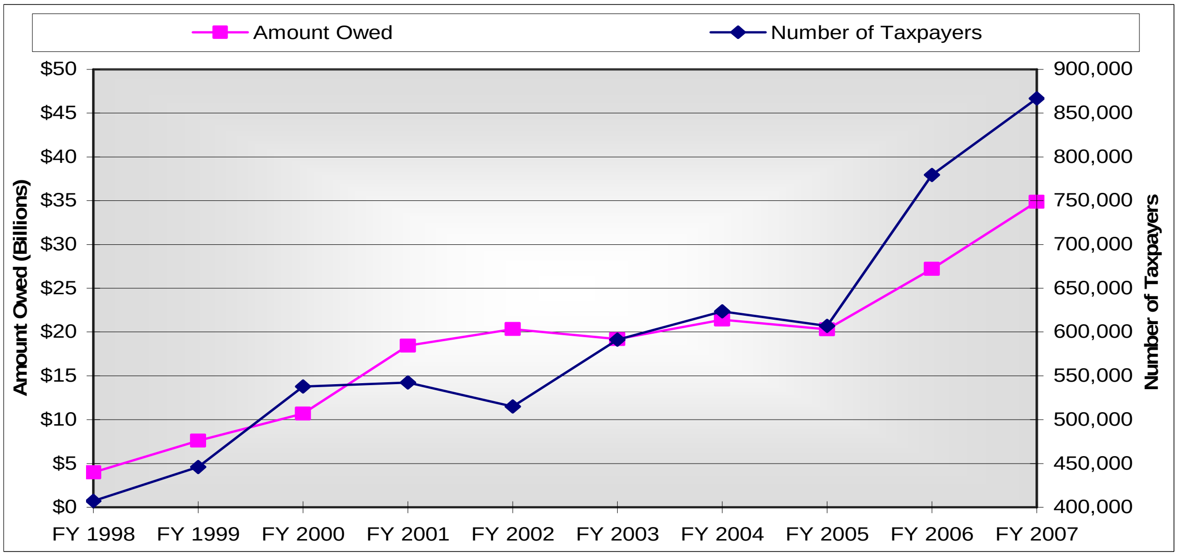
Source: TIGTA analysis of Collection Report 5000-4.

Figure 15. Gap Between TDA Receipts and Closures. The gap between TDA receipts and closures widened substantially in FY 2007 after narrowing slightly in FY 2006. However, the number of receipts has been greater than the number of closures each year since FY 1998. The closures shown in Figure 15 do not include the TDAs shelved shown in Figure 11.



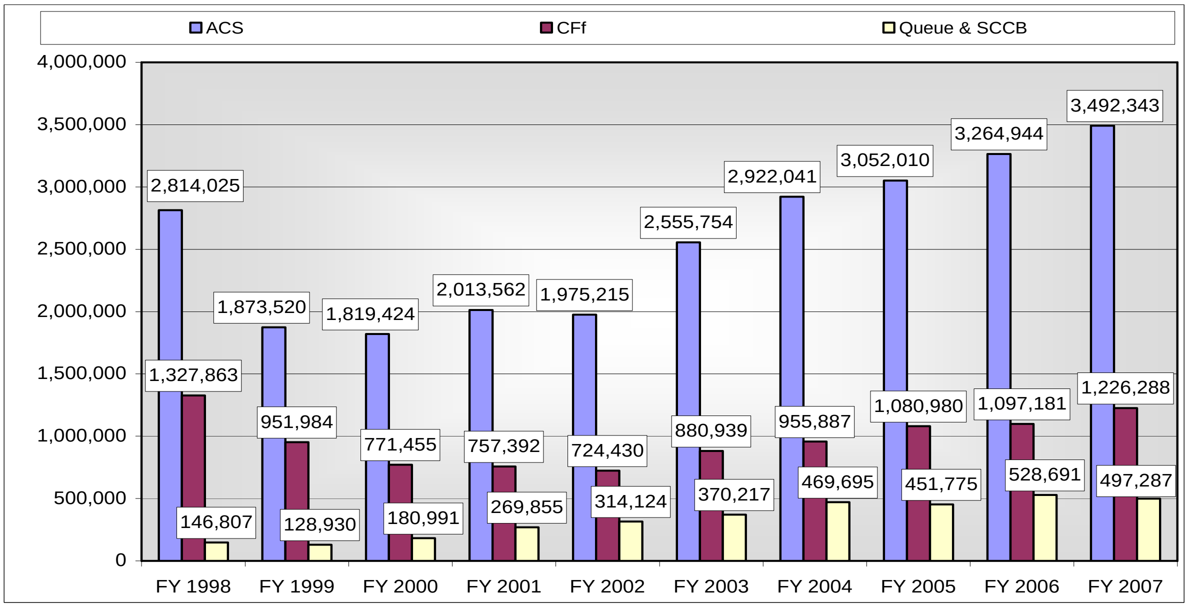
Source: TIGTA analysis of Collection Report 5000-2.

Figure 16. Number of Taxpayers and Amount Owed in the Queue. Between FYs 2005 and 2007, the number of taxpayers with TDAs in the Queue inventory increased by almost 43 percent, and the amount owed on those accounts increased by almost 72 percent.



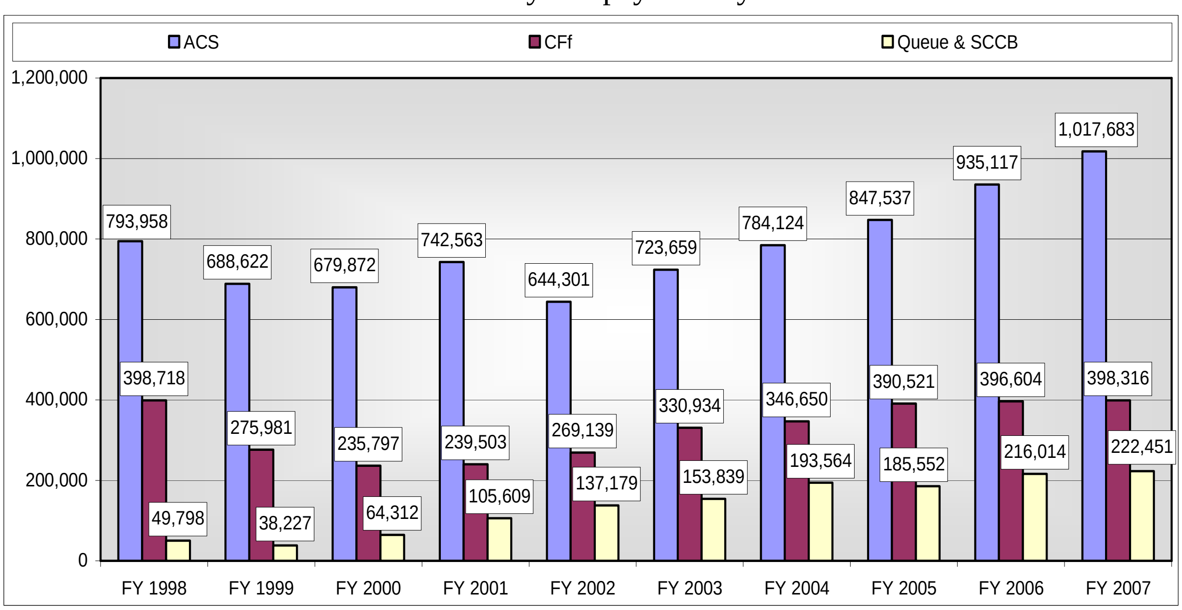
Source: Collection Report 5000-2.

Figure 17. Number of TDAs Closed, Excluding Shelved Accounts. The numbers of TDAs closed by the ACS and CFf increased in FY 2007. The number in the SCCB increased slightly, but the number in the Queue decreased–resulting in the combined decrease in FY 2007.



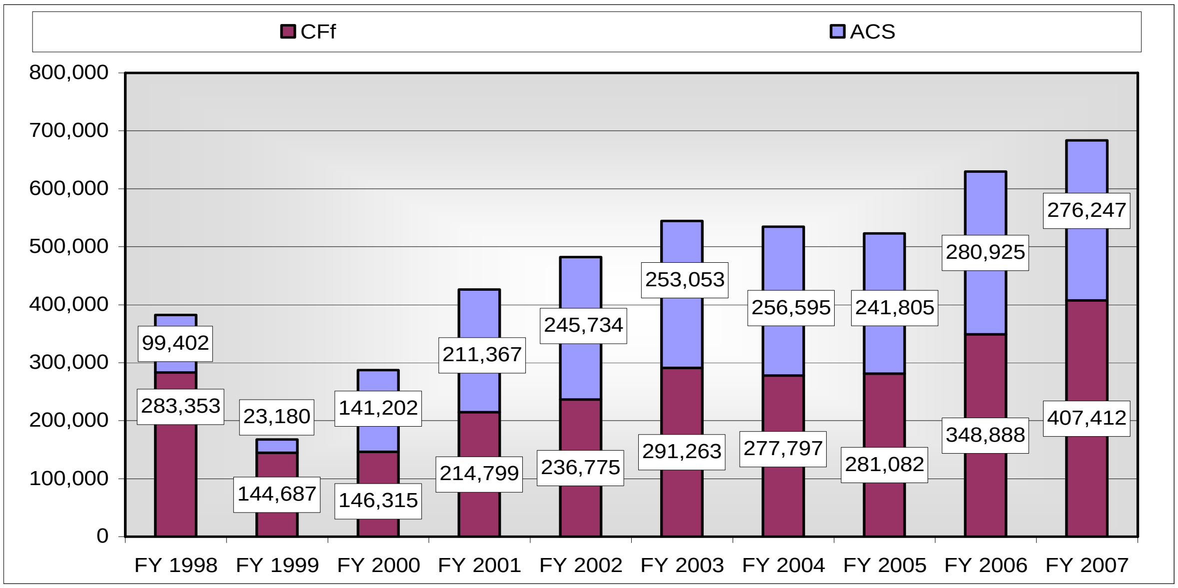
Source: TIGTA analysis of Collection Report 5000-2.

Figure 18. Number of TDAs Closed by Full Payment. The total number of TDAs closed by full payment increased by almost 6 percent in FY 2007. Since FY 2002, there has been a steady increase in the number of accounts closed by full payment by the ACS and CFf.



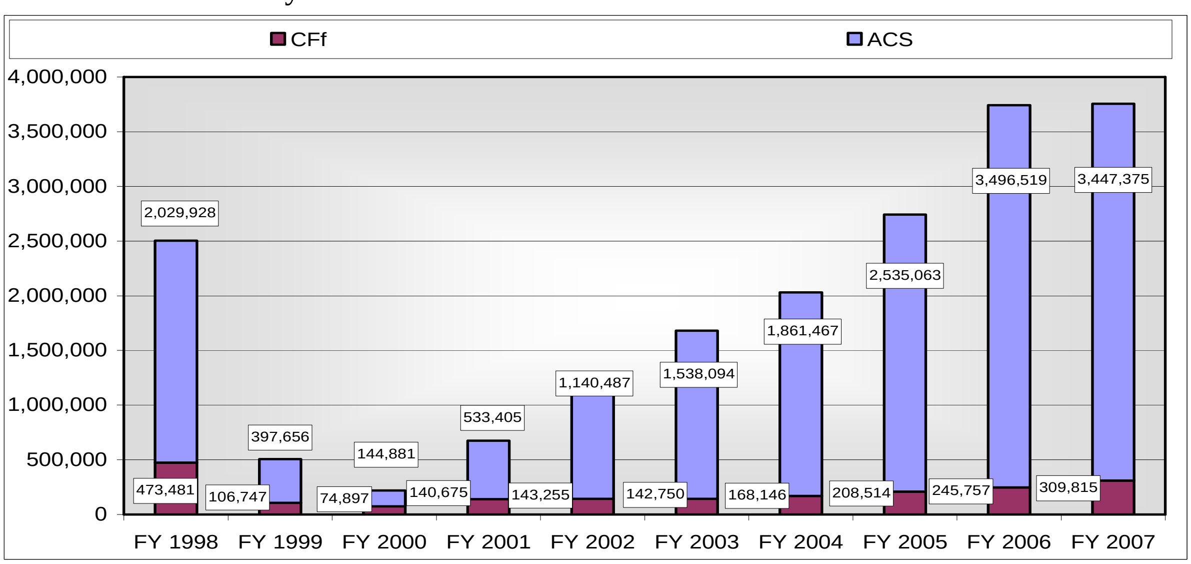
Source: TIGTA analysis of Collection Report 5000-2.

Figure 19. Liens Filed by the CFf and ACS. During the year, the total number of liens filed increased by almost 9 percent. The number of liens filed by the ACS decreased by almost 2 percent, while those filed by the CFf increased by almost 17 percent.



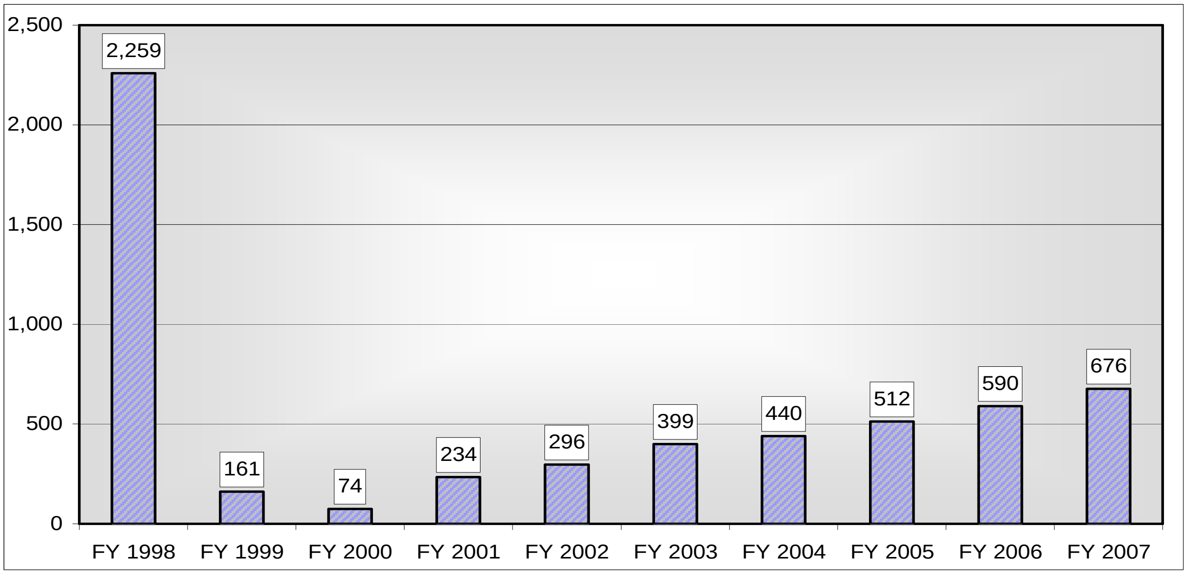
Source: Small Business/Self-Employed Division Collection Planning and Analysis, Collection National Reports.

Figure 20. Levies Issued by the CFf and ACS. The total number of levies issued by the CFf and ACS increased dramatically from FYs 2000 through 2006, then remained at a similar level for FY 2007. The slight decrease in the number of levies issued during FY 2007 by the ACS was offset with an increase by the CFf.



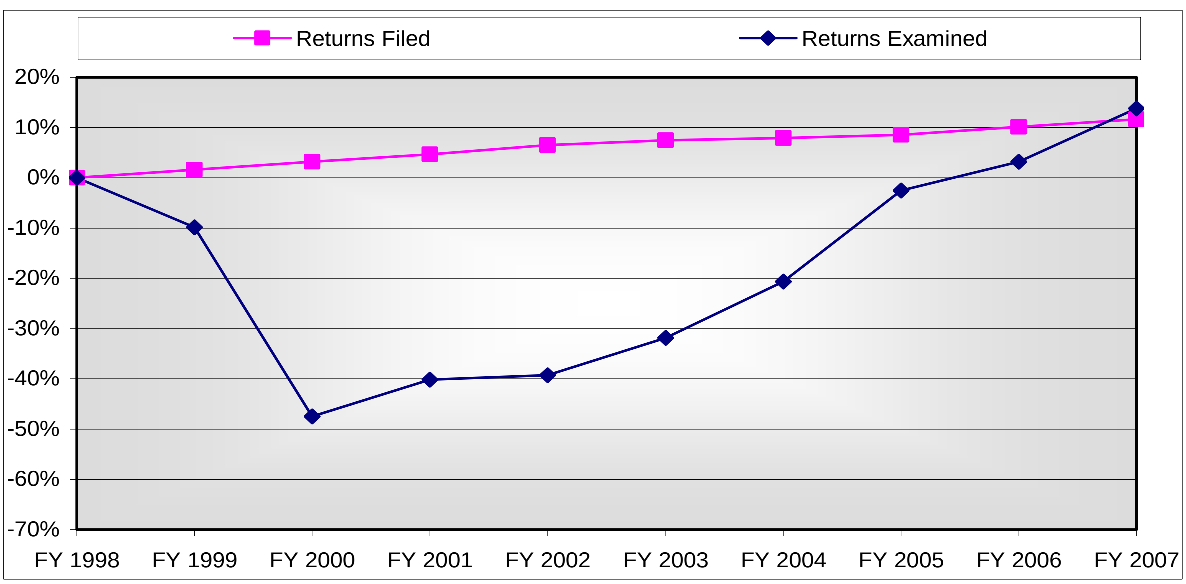
Source: Small Business/Self-Employed Division Collection Planning and Analysis, Collection National Reports.

Figure 21. Number of Seizures Made Each Fiscal Year. The number of seizures made continued the upward trend that has occurred since FY 2000, but it is still only about 30 percent of the number made in FY 1998.



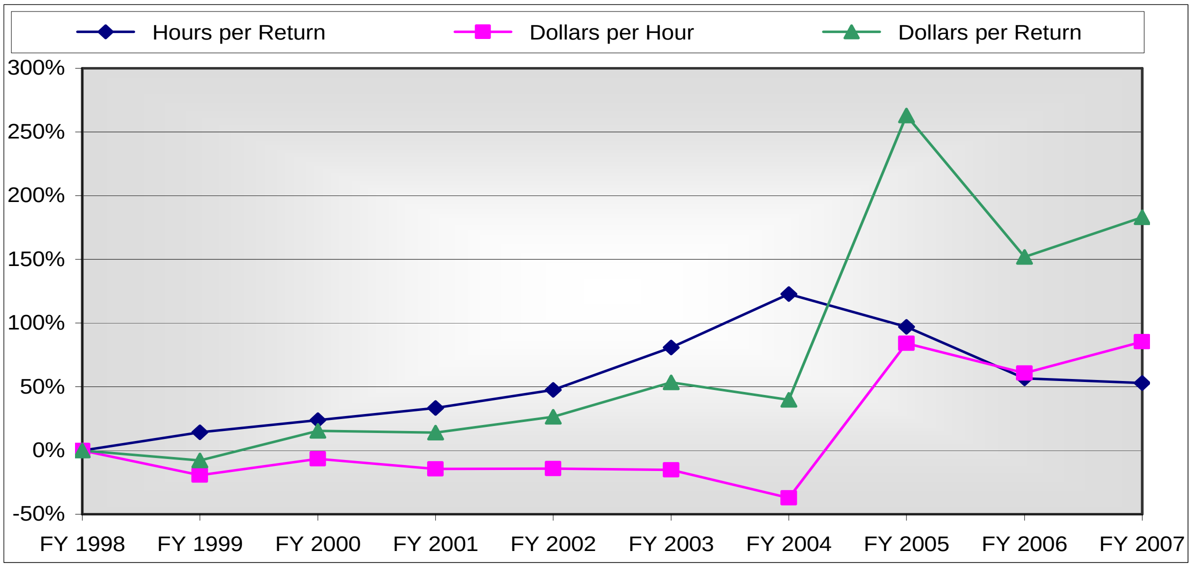
Source: IRS Data Book.

Figure 22. Examination Coverage of All Tax Returns – Percentage Change From FY 1998. Examination coverage of tax returns reached a 10-year low in FY 2000, but the growth in coverage has outpaced the growth in returns filed each year since FY 2002.



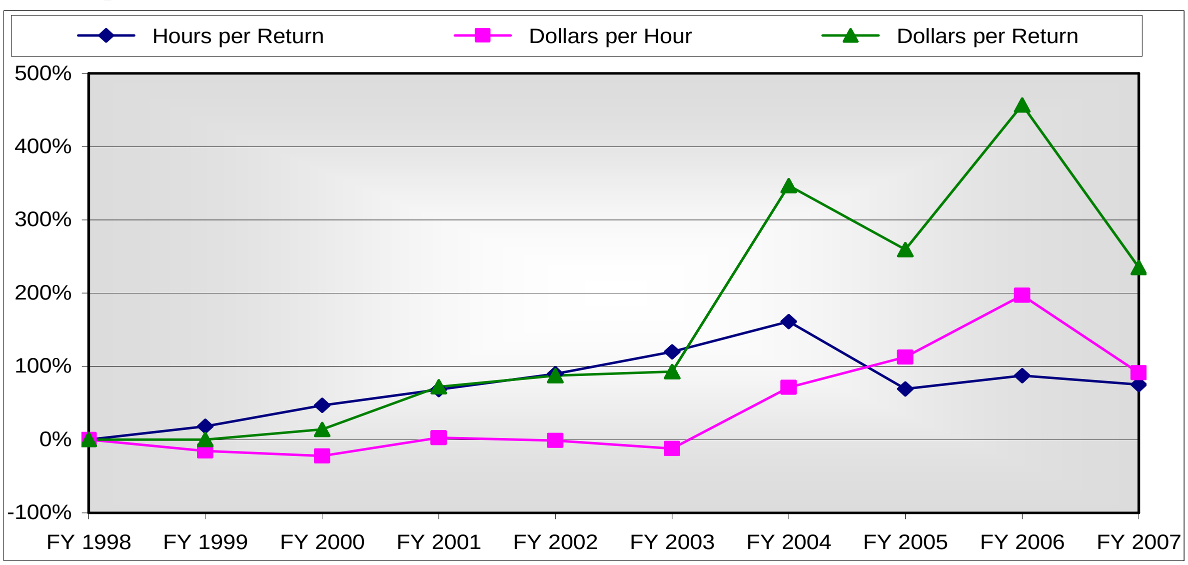
Source: TIGTA analysis of IRS Data Book.

Figure 23. Revenue Agent Results on U.S. Individual Income Tax Returns (Form 1040), Excluding Training Returns – Percentage Change From FY 1998. The hours per return dropped slightly in FY 2007, while the dollars per return increased. The combined effect resulted in an increase in dollars per hour of slightly over 15 percent.



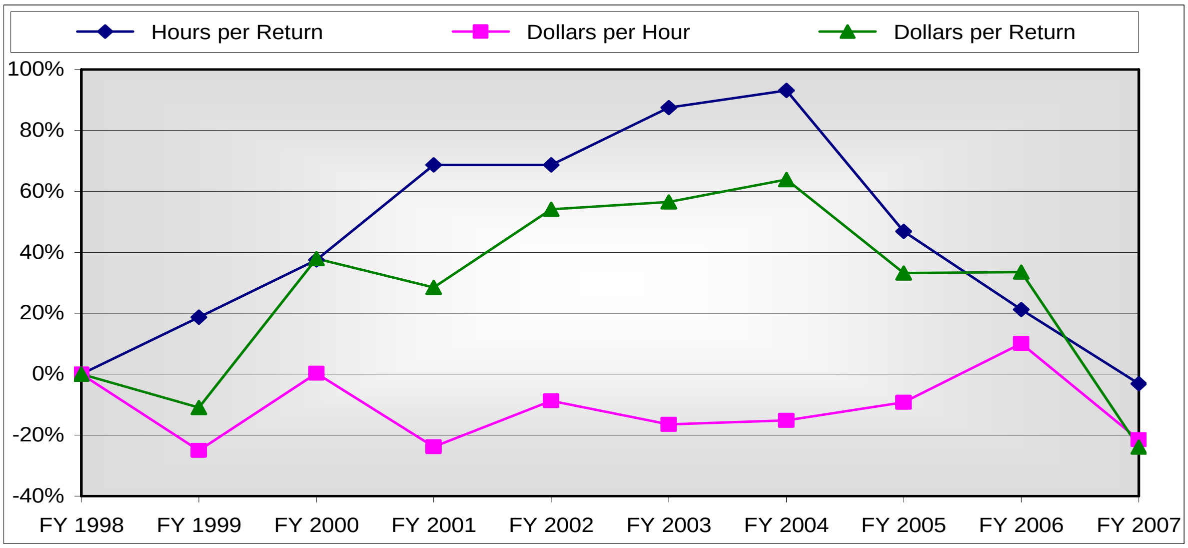
Source: TIGTA analysis of Examination Table 37.

Figure 24. Revenue Agent Results on Corporate Income Tax Returns, Excluding Training Returns – Percentage Change From FY 1998. The hours per return and dollars per return both decreased during the year. The combined effect resulted in a decrease in dollars per hour of almost 36 percent.



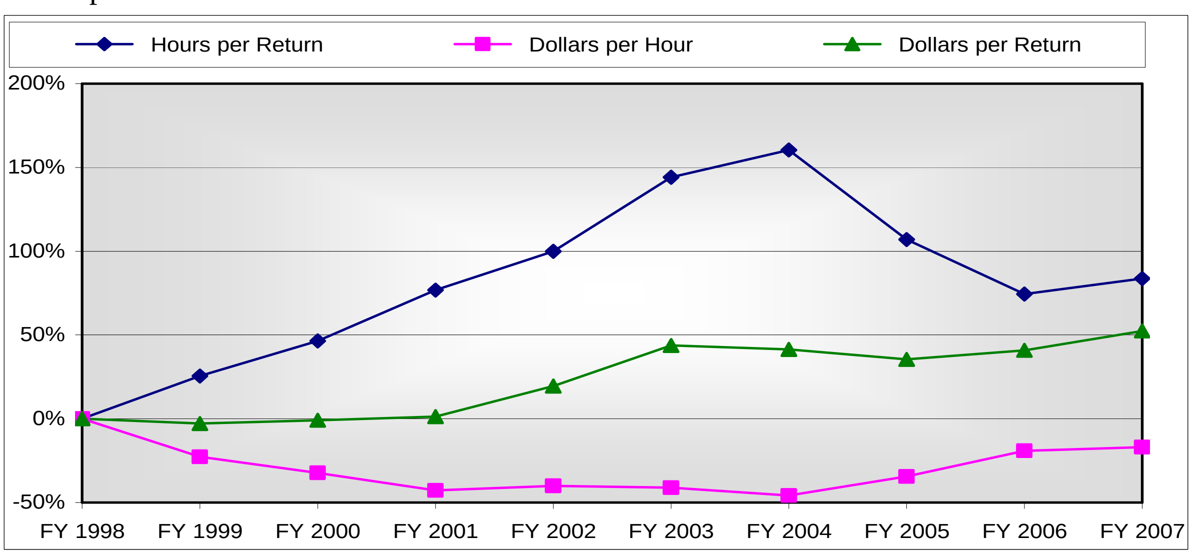
Source: TIGTA analysis of Examination Table 37.

Figure 25. Revenue Agent Results on Other Types of Tax Returns, Excluding Training Returns – Percentage Change From FY 1998. The hours per return and dollars per return both decreased during the year. The combined effect resulted in a decrease in dollars per hour of almost 29 percent.



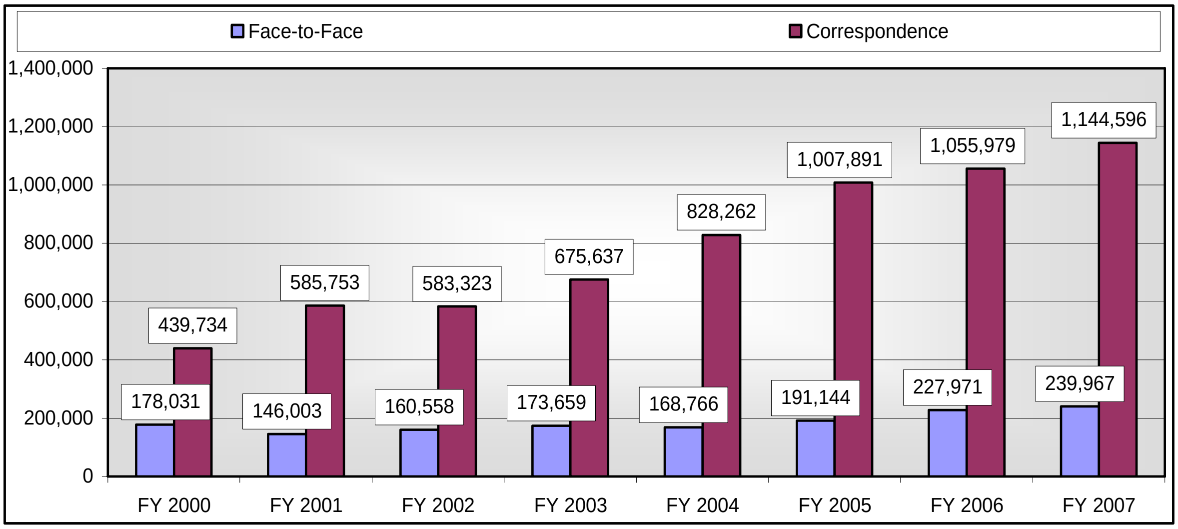
Source: TIGTA analysis of Examination Table 37.

Figure 26. Tax Compliance Officer Results on Forms 1040, Excluding Training Returns – Percentage Change From FY 1998. The hours per return and dollars per return both increased slightly during the year. The combined effect resulted in an increase in dollars per hour of almost 3 percent.



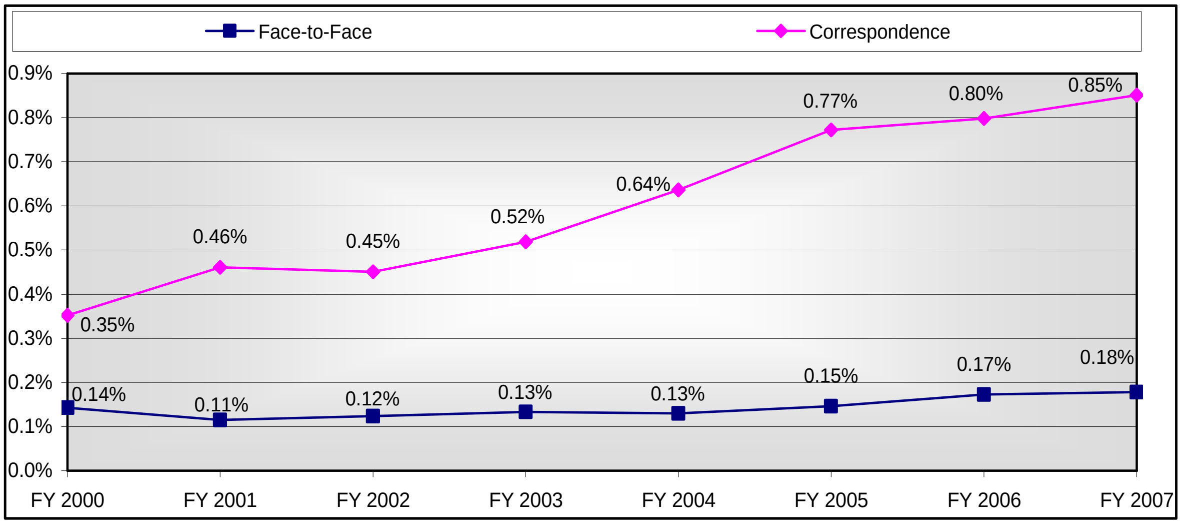
Source: TIGTA analysis of Examination Table 37.

Figure 27. Number of Forms 1040 Examined Face-to-Face or Through Correspondence. The total number of face-to-face examinations of individuals increased by just over 5 percent, and those conducted through correspondence increased by just over 8 percent in FY 2007. Almost 83 percent of Form 1040 examinations were conducted through correspondence. Due to a change in the source of the data, numbers for FYs 1998 and 1999 were not available.



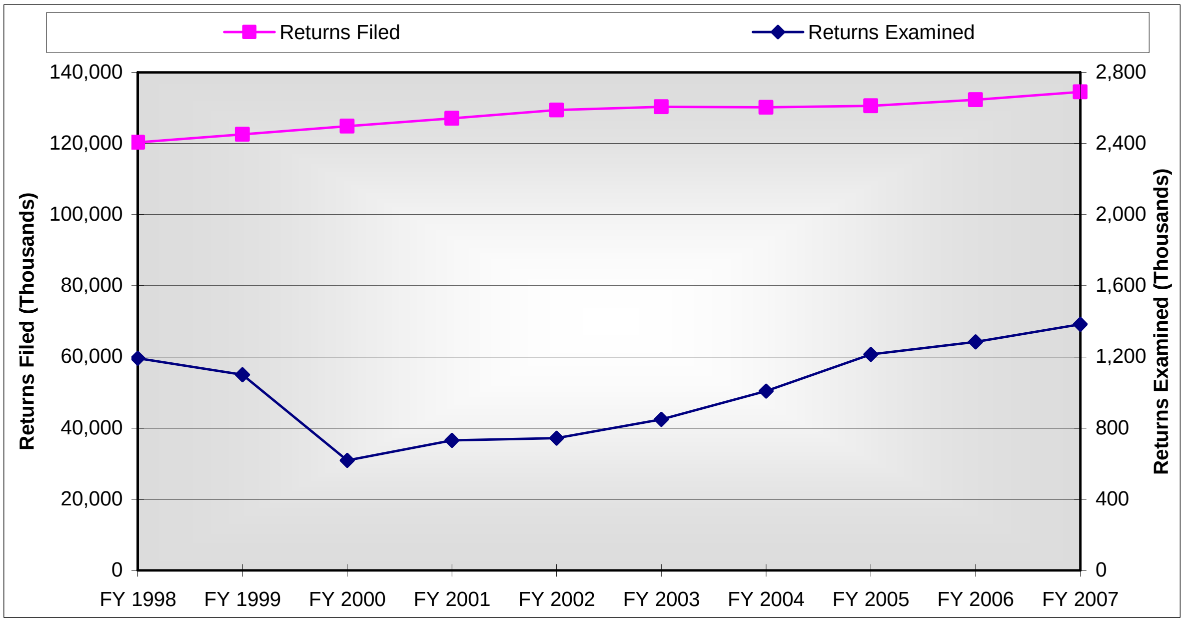
Source: Analysis of Examination Closed Case Database and IRS Data Book.

Figure 28. Percentage of Forms 1040 Examined Face-to-Face or Through Correspondence. During FY 2007, the coverage rates for face-to-face and correspondence examinations of individual income tax returns increased. The coverage rate for examinations conducted by correspondence has nearly doubled since FY 2002. Due to a change in the source of the data, numbers for FYs 1998 and 1999 were not available.



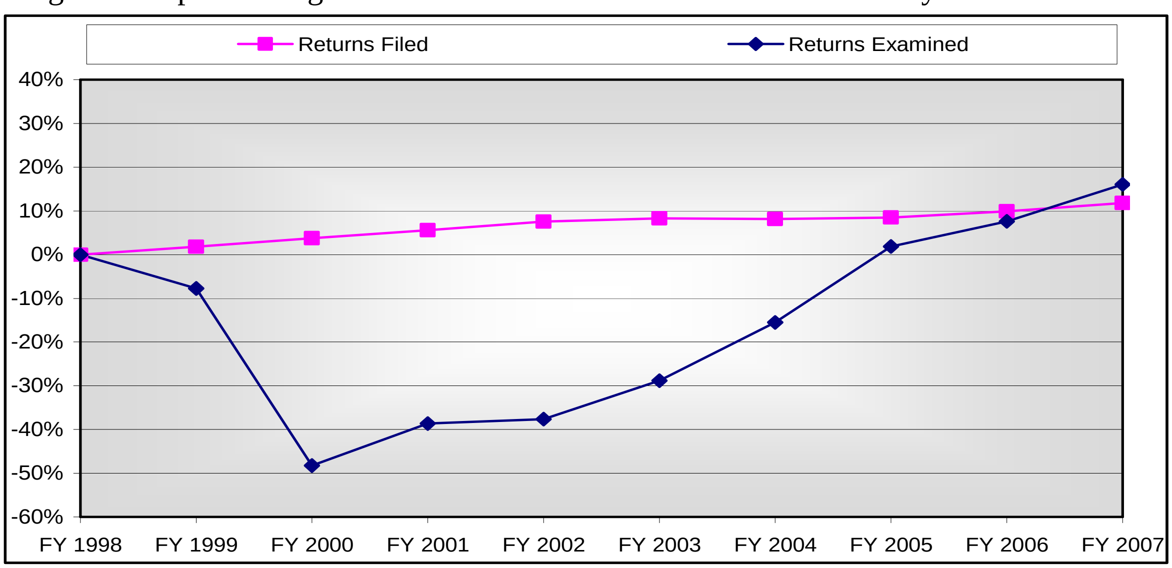
Source: Analysis of Examination Closed Case Database and IRS Data Book.

Figure 29. Examination Coverage of Forms 1040. After remaining relatively unchanged for 3 years, the number of Forms 1040 filed increased slightly in each of the last 3 fiscal years. The growth in the number of Forms 1040 examined has slowed since FY 2005.



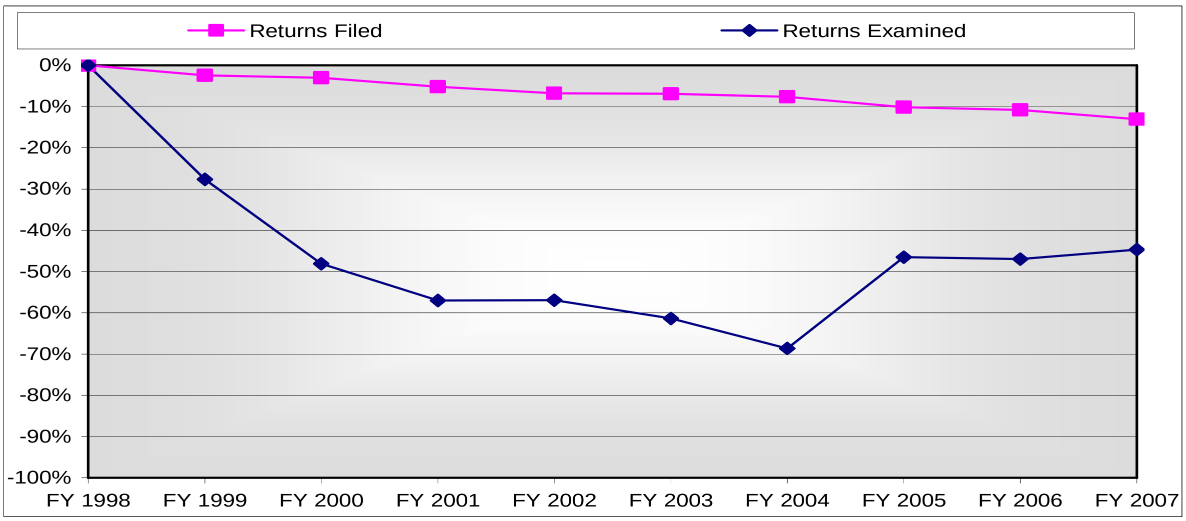
Source: TIGTA analysis of IRS Data Book.

Figure 30. Examination Coverage of Forms 1040 – Percentage Change From FY 1998. Examination coverage of Forms 1040 reached a 10-year low in FY 2000, but the growth in coverage has outpaced the growth in the number of Forms 1040 filed each year since FY 2002.



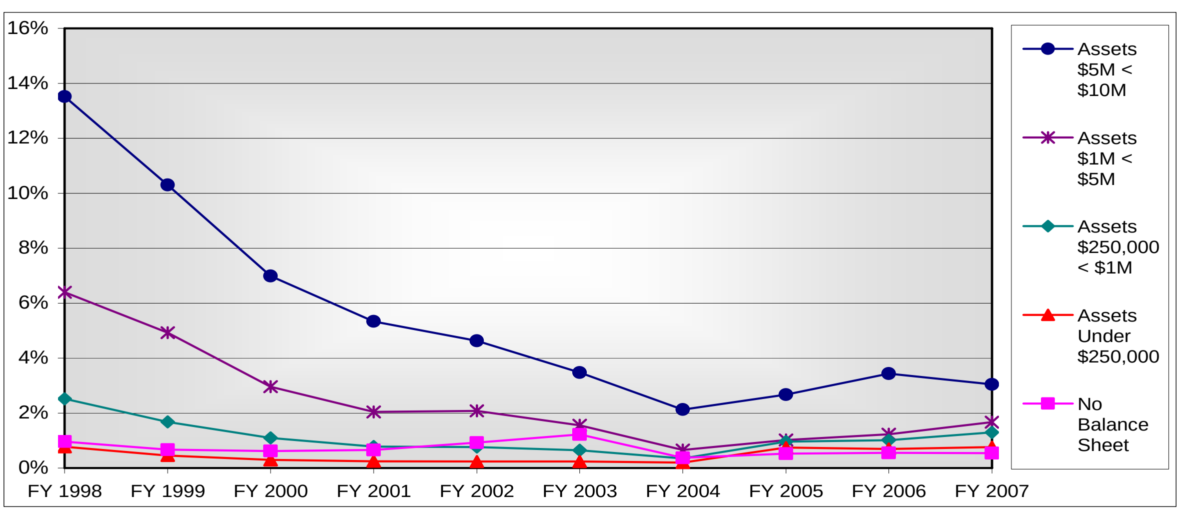
Source: TIGTA analysis of IRS Data Book.

Figure 31. Examination Coverage of Corporate Income Tax Returns – Percentage Change From FY 1998. Overall, the number of corporate tax returns filed (excluding U.S. Income Tax Return for an S Corporation (Form 1120S) and U.S. Income Tax Return for a Foreign Corporation (Form 1120-F)) continued to decrease during FY 2007, while the percentage of those tax returns examined increased. Overall, 1 of every 75 corporate tax returns was examined.



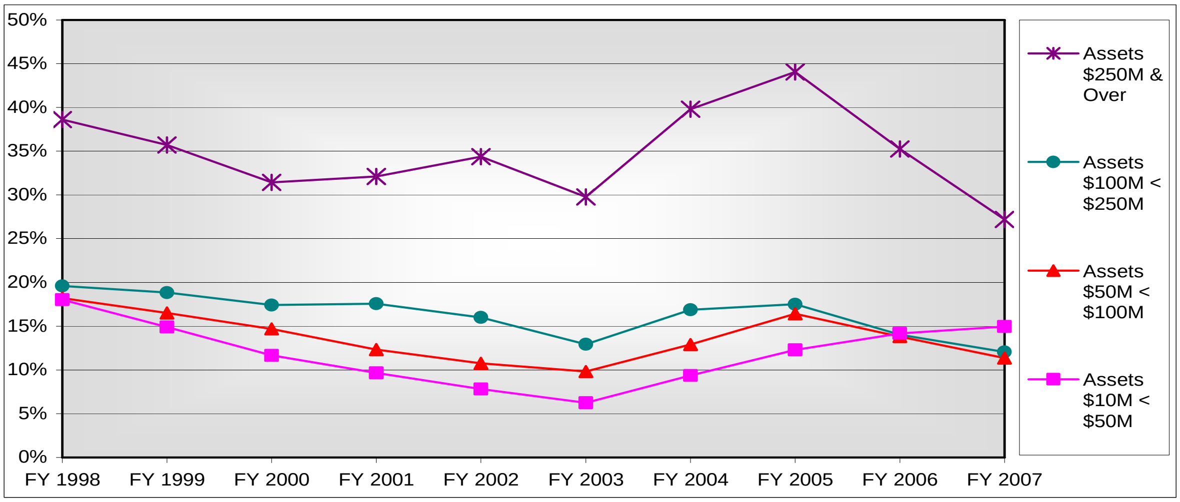
Source: TIGTA analysis of IRS Data Book.

Figure 32. Percentage of Corporate Income Tax Returns Examined – Corporations With Assets of Less Than $10 Million. During FY 2007, the overall examination coverage rate for corporate tax returns with no balance sheet or with assets of less than $10 million increased for all categories, except the categories of "no balance sheet" and "assets of from $5 million to $10 million."



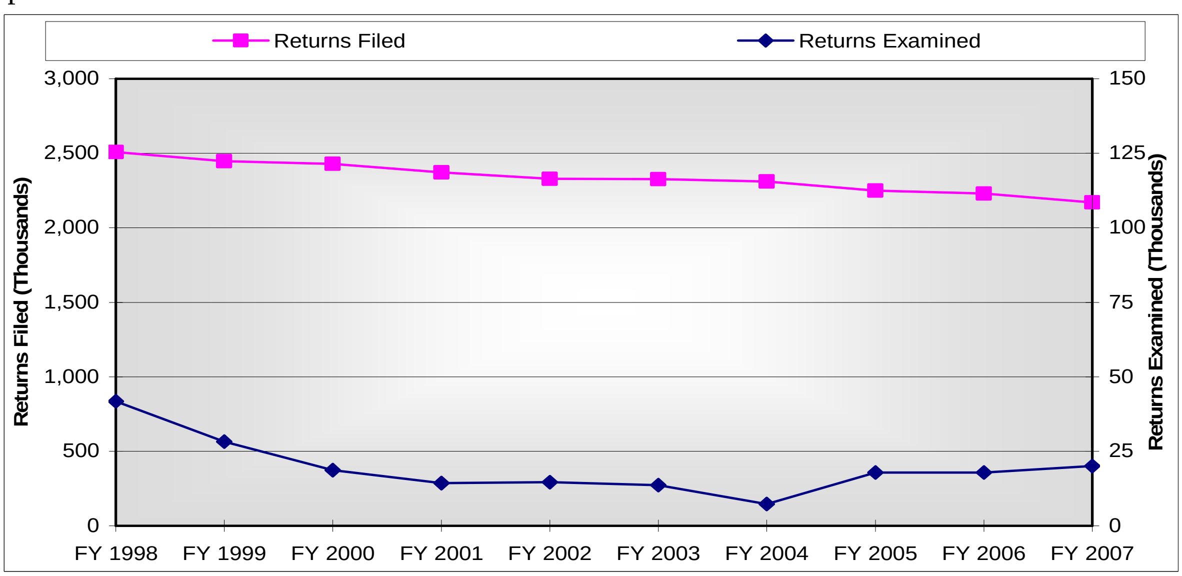
Source: TIGTA analysis of IRS Data Book.

Figure 33. Percentage of Corporate Income Tax Returns Examined – Corporations With Assets of $10 Million and Greater. During FY 2007, the overall examination coverage rate for corporate tax returns with assets of $10 million and greater decreased by almost 10 percent. However, the rate for those returns with assets of $250 million and greater decreased by almost 23 percent.



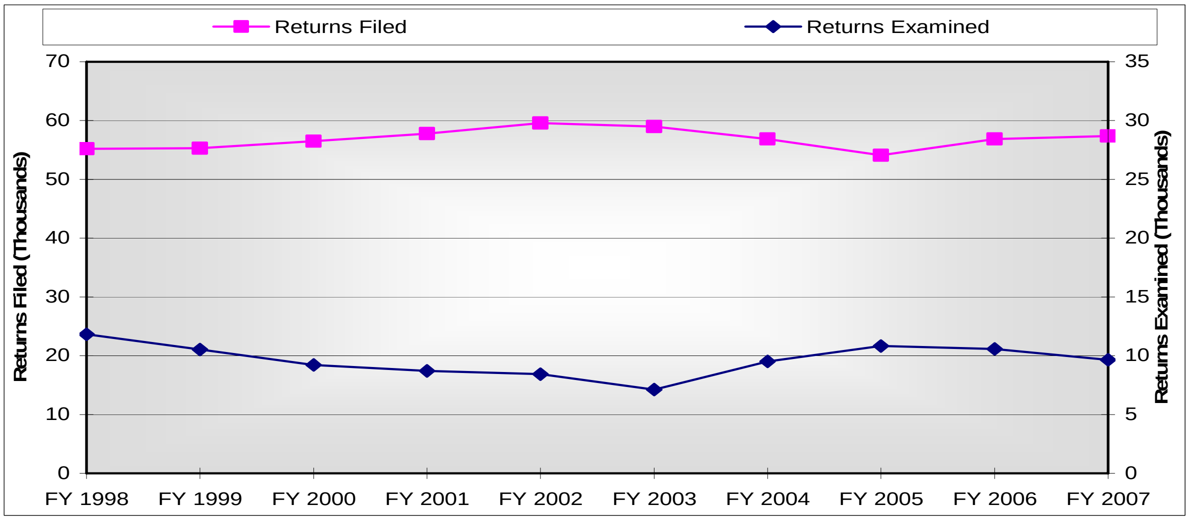
Source: TIGTA analysis of IRS Data Book.

Figure 34. Examination Coverage of Corporations With Assets of Less Than $10 Million. The number of corporate tax returns filed with assets of less than $10 million dropped by almost 3 percent during the year, while the number of tax returns examined increased by just over 12 percent.



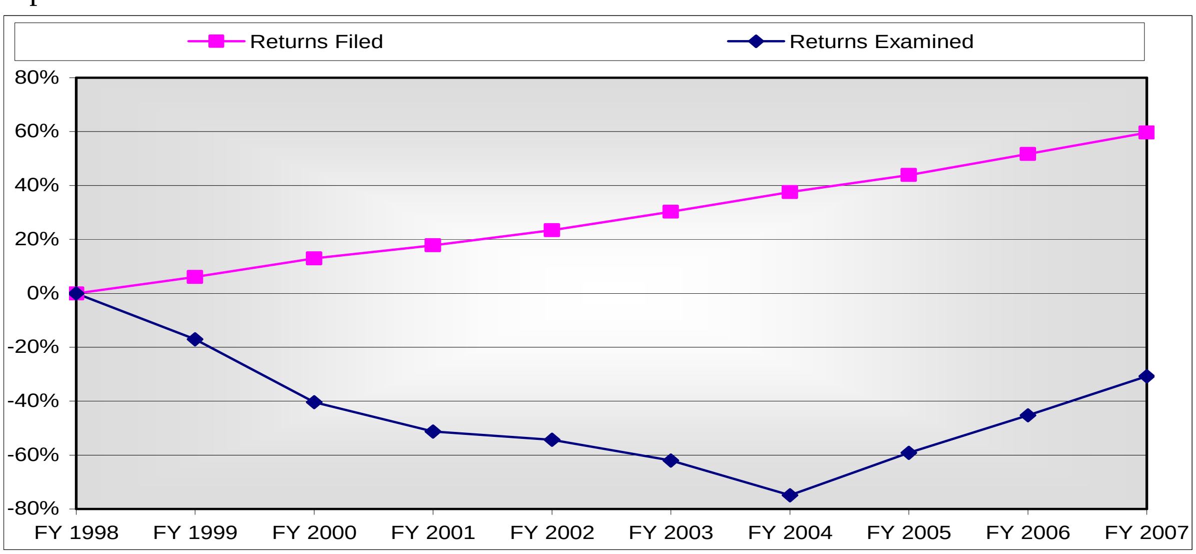
Source: TIGTA analysis of IRS Data Book.

Figure 35. Examination Coverage of Corporations With Assets of $10 Million and Greater. During FY 2007, the number of corporate tax returns filed with assets of $10 million and greater increased by almost 1 percent, while the number of returns examined decreased by almost 9 percent.



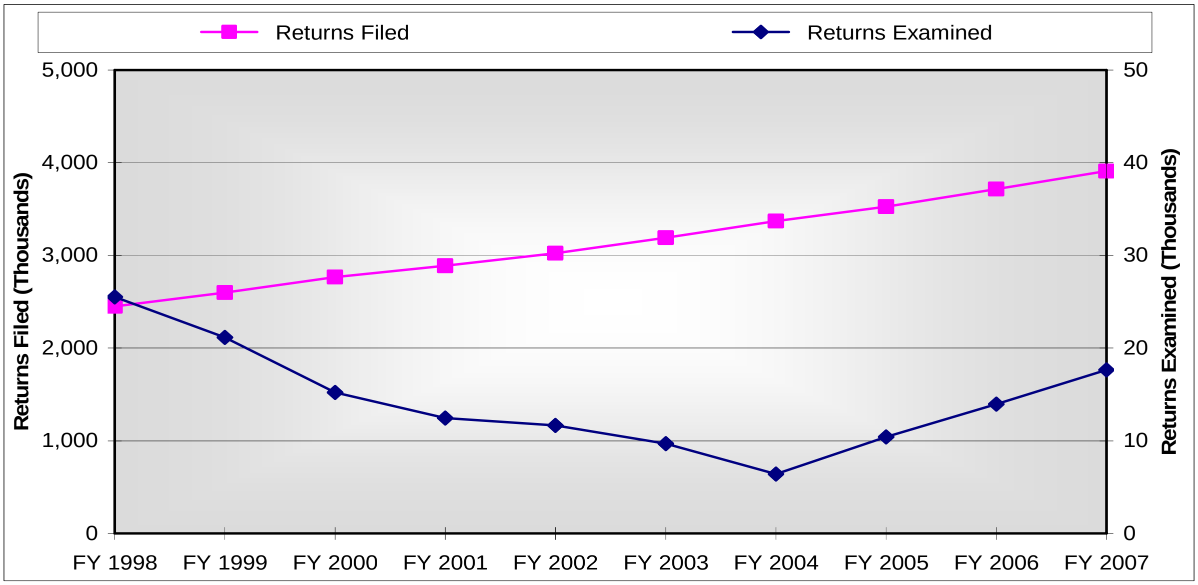
Source: TIGTA analysis of IRS Data Book.

Figure 36. Examination Coverage of Forms 1120S – Percentage Change From FY 1998. After decreasing each year since FY 1998, the percentage of Forms 1120S examined has increased significantly since FY 2004. The increase can be partly attributed to examinations of Forms 1120S as part of a National Research Project. Most of those examinations have been completed.



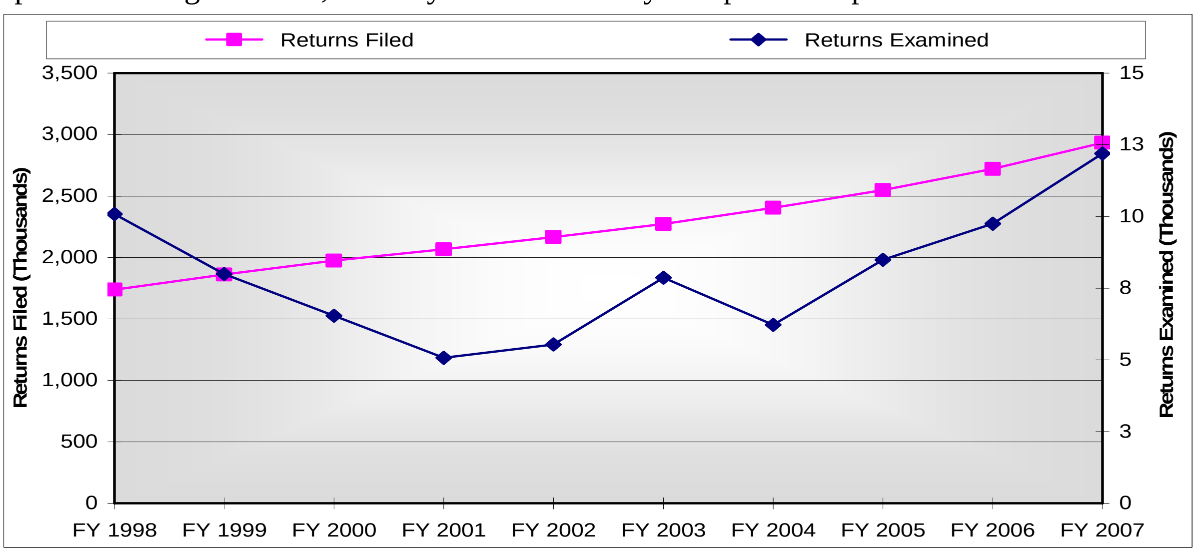
Source: TIGTA analysis of IRS Data Book.

Figure 37. Examination Coverage of Forms 1120S. The number of Forms 1120S filed has increased at an average rate of 162,000 per year since FY 1998, to just over 3.9 million in FY 2007. While the number of examinations increased during the last 3 years, only about 1 of every 221 Forms 1120S was examined during FY 2007.



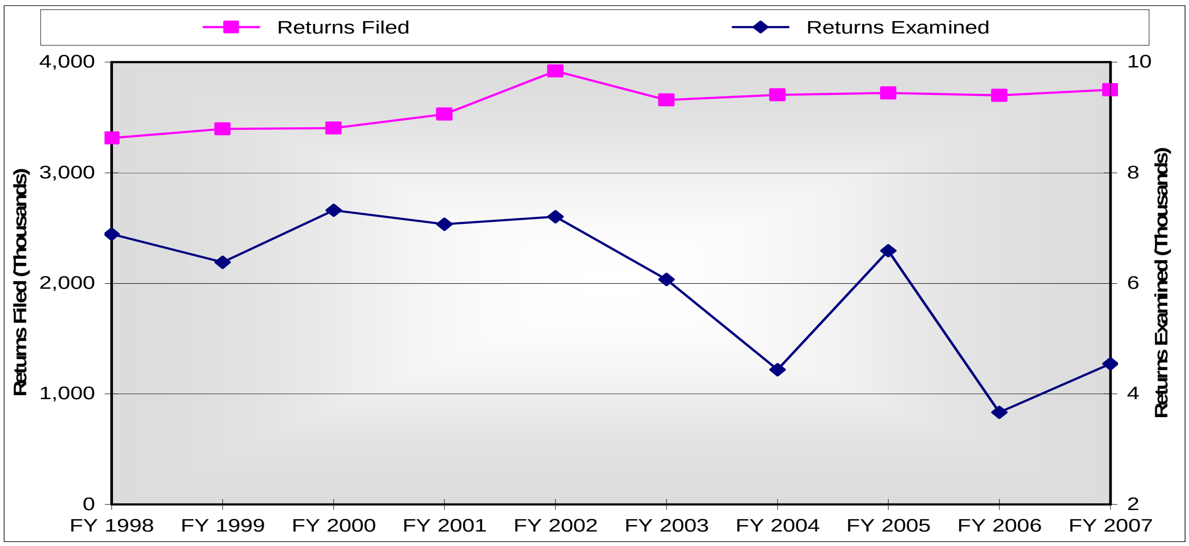
Source: IRS Data Book.

Figure 38. Examination Coverage of Partnership Income Tax Returns. The number of partnership tax returns filed has increased at an average rate of nearly 133,000 per year since FY 1998, to just over 2.9 million in FY 2007. The number of returns examined increased by 25 percent during FY 2007, but only about 1 of every 241 partnership returns was examined.



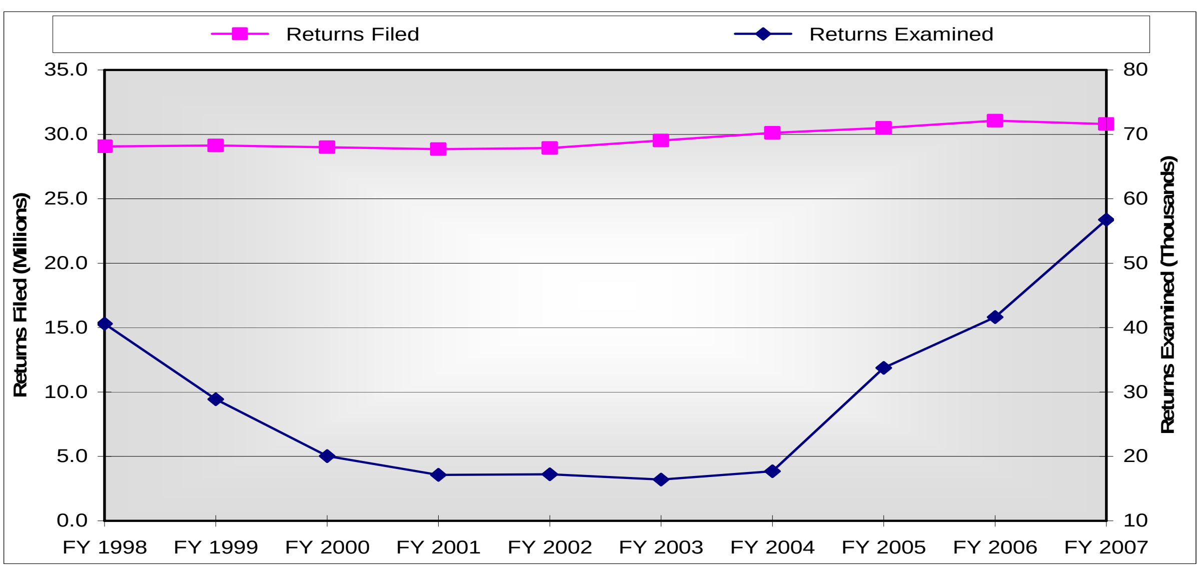
Source: IRS Data Book.

Figure 39. Examination Coverage of Fiduciary Income Tax Returns. During FY 2007, the number of income tax returns filed by estates and trusts increased slightly, and the number of tax returns examined increased by almost 24 percent. Only about 1 of every 826 fiduciary income tax returns was examined.



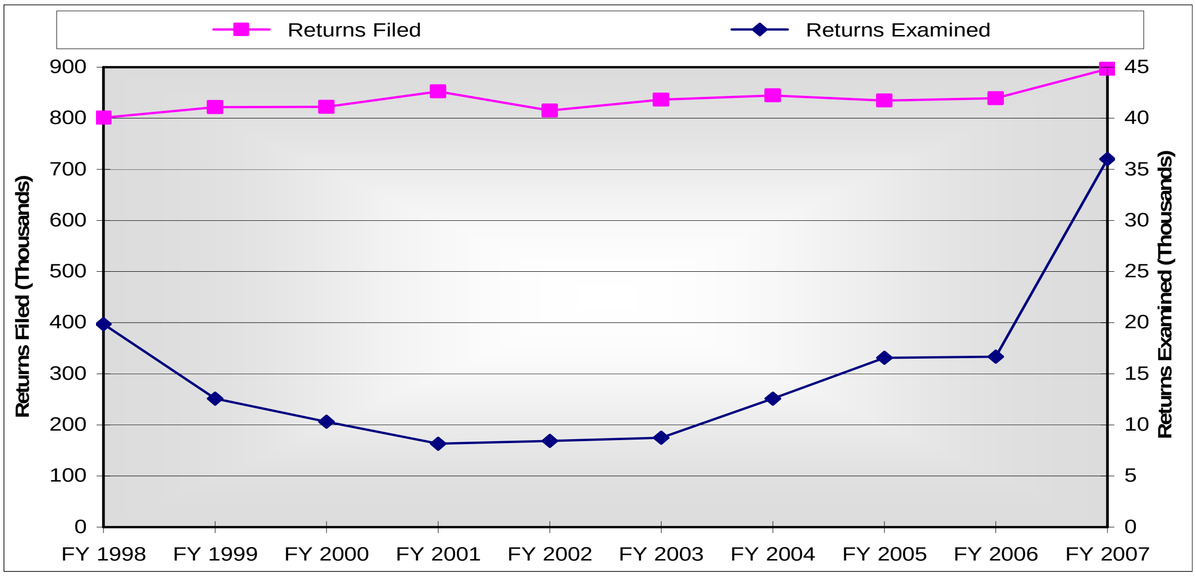
Source: IRS Data Book.

Figure 40. Examination Coverage of Employment Tax Returns. The number of employment tax returns filed decreased by almost 1 percent this year, but the number of tax returns examined increased by just over 36 percent. About 1 of every 543 employment tax returns was examined.



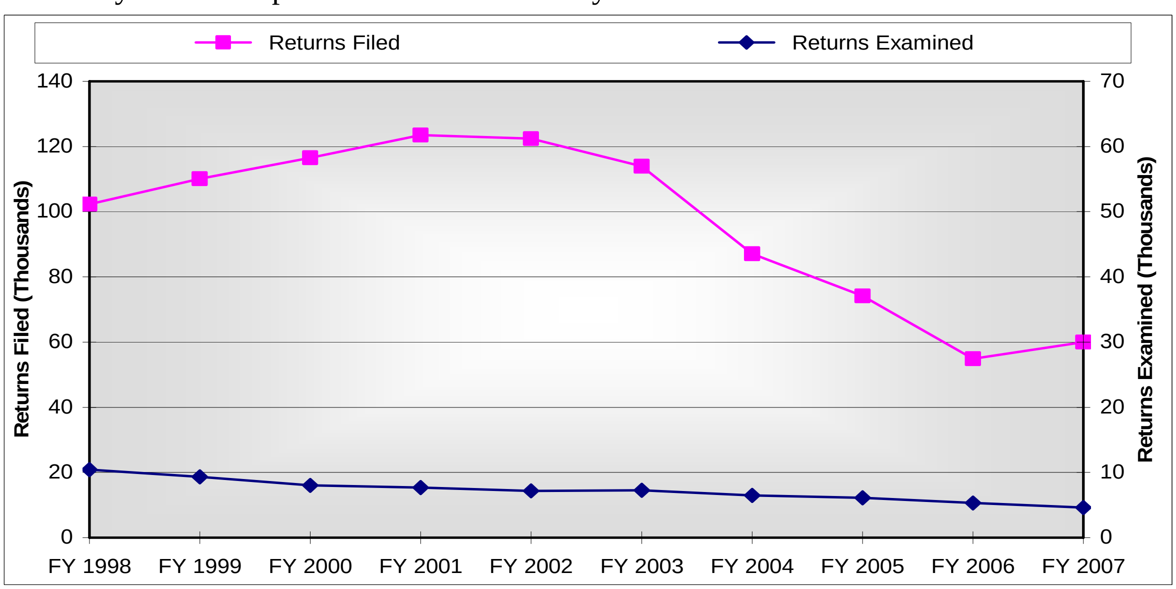
Source: IRS Data Book.

Figure 41. Examination Coverage of Excise Tax Returns. The number of excise tax returns filed increased by almost 7 percent, while the number examined increased by almost 116 percent during FY 2007.



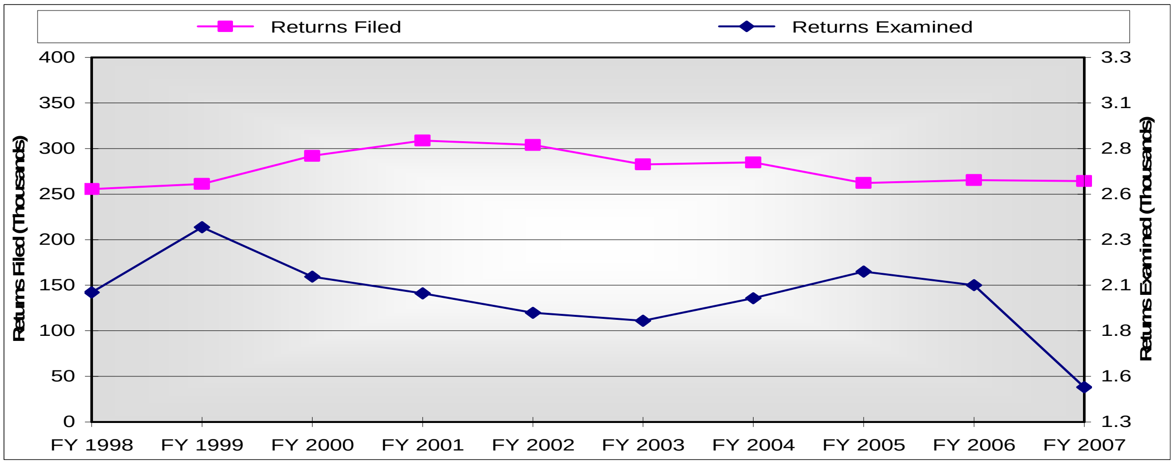
Source: IRS Data Book.

Figure 42. Examination Coverage of Estate Tax Returns. During FY 2007, the number of estate tax returns filed increased by just over 9 percent, and the number of returns examined decreased by almost 13 percent. About 1 of every 13 estate tax returns was examined.



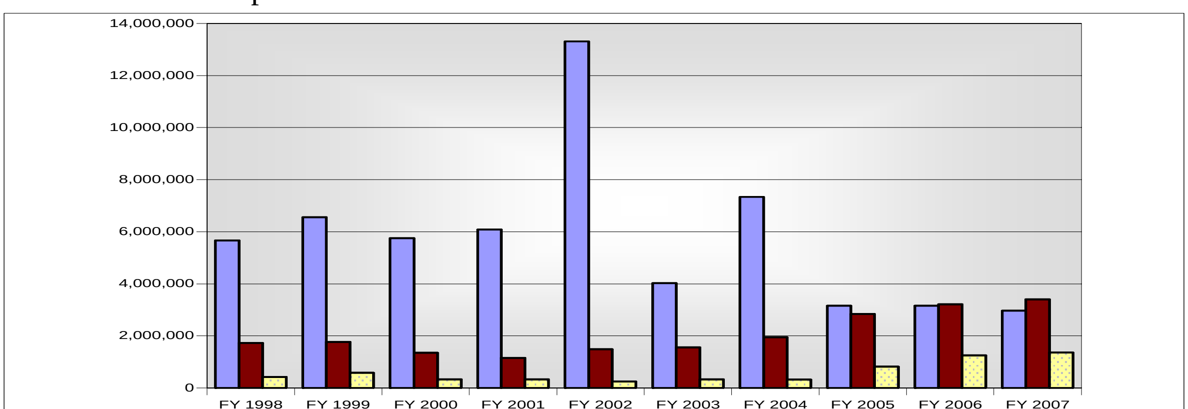
Source: IRS Data Book.

Figure 43. Examination Coverage of Gift Tax Returns. The number of gift tax returns filed decreased by less than 1 percent during FY 2007. However, the number of returns examined decreased by more than 27 percent.



Source: IRS Data Book.

Figure 44. Other Compliance Contacts on Forms 1040. The number of contacts for Math Error Program cases decreased slightly during FY 2007 after remaining virtually unchanged during the 2 prior years. The numbers of contacts for Underreporter Program and Automated Substitute for Return system[1] cases increased. The spike in the number of contacts for Math Error Program cases in FY 2002 was the result of taxpayer confusion over the Rate Reduction Credit. Much of the spike in FY 2004 was due to Child Tax Credit issues.



	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
Math Error	5,668,906	6,552,290	5,751,462	6,082,967	13,315,765	4,024,981	7,342,484	3,163,794	3,159,077	2,965,745
Underreporter	1,726,098	1,770,695	1,353,545	1,161,901	1,491,139	1,561,068	1,948,363	2,837,149	3,209,000	3,403,000
ASFR	426,495	584,142	332,427	333,770	242,637	335,032	326,407	820,845	1,253,000	1,356,000

Source: IRS Data Book. ASFR = Automated Substitute for Return system.

[1] The IRS adjusted how these cases are captured. We used revised numbers for FYs 2003 through 2005 to be consistent with the other fiscal years.

Figure 45. Other Compliance Contacts – Percentage of Form 1040 Coverage. The level of coverage for Math Error Program cases has remained relatively unchanged since FY 2005, while it has been increasing for Underreporter Program and Automated Substitute for Return system cases. The Math Error Program aberrations in FYs 2002 and 2004 are explained in Figure 44.

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY2003	FY 2004	FY 2005	FY 2006	FY 2007
Math Error	5,668,906	6,552,290	5,751,462	6,082,967	13,315,765	4,024,981	7,342,484	3,163,794	3,159,077	2,965,745
Coverage Rate	4.63%	5.25%	4.53%	4.70%	10.22%	3.08%	5.59%	2.38%	2.36%	2.21%
Underreporter	1,726,098	1,770,695	1,353,545	1,161,901	1,491,139	1,561,068	1,948,363	2,837,149	3,209,000	3,403,000
Coverage Rate	1.43%	1.44%	1.08%	0.91%	1.15%	1.20%	1.49%	2.16%	2.42%	2.54%
ASFR	426,495	584,142	332,427	333,770	242,637	335,032	326,407	820,845	1,253,000	1,356,000
Coverage Rate	0.35%	0.48%	0.27%	0.26%	0.19%	0.26%	0.25%	0.63%	0.94%	1.01%

Source: TIGTA analysis of IRS Data Book. ASFR = Automated Substitute for Return system.

Figure 46. Numbers and Percentages of Individual and Business Tax Returns Examined. Figure 46 shows the numbers and percentages of examination coverage.

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
Individual Returns										
Individuals (Forms 1040)	1,192,780	1,100,273	617,765	731,756	743,881	849,296	1,007,874	1,215,308	1,283,950	1,384,563
Coverage Rate	0.99%	0.90%	0.49%	0.58%	0.57%	0.65%	0.77%	0.93%	0.97%	1.03%
Business Returns										
Corporations Less Than $10 Million	41,818	28,268	18,623	14,332	14,655	13,608	7,294	17,858	17,849	20,020
Coverage Rate	1.67%	1.16%	0.77%	0.60%	0.63%	0.58%	0.32%	0.79%	0.80%	0.92%
Corporations $10 Million and Greater	11,830	10,537	9,212	8,718	8,443	7,125	9,523	10,829	10,578	9,644
Coverage Rate	21.43%	19.05%	16.30%	15.08%	14.17%	12.08%	16.74%	20.02%	18.60%	16.81%
S Corporations (Forms 1120S)	25,522	21,169	15,200	12,437	11,646	9,695	6,402	10,417	13,970	17,657
Coverage Rate	1.04%	0.81%	0.55%	0.43%	0.39%	0.30%	0.19%	0.30%	0.38%	0.45%
Partnerships	10,082	7,991	6,539	5,070	5,543	7,871	6,226	8,489	9,752	12,195
Coverage Rate	0.58%	0.43%	0.33%	0.25%	0.26%	0.35%	0.26%	0.33%	0.36%	0.42%
Fiduciaries	6,890	6,382	7,318	7,070	7,206	6,068	4,438	6,591	3,669	4,544
Coverage Rate	0.21%	0.19%	0.22%	0.20%	0.18%	0.17%	0.12%	0.18%	0.10%	0.12%
Employment	40,595	28,898	20,074	17,163	17,252	16,408	17,698	33,748	41,646	56,738
Coverage Rate	0.14%	0.10%	0.07%	0.06%	0.06%	0.06%	0.06%	0.11%	0.13%	0.18%
Excise	19,858	12,562	10,294	8,169	8,426	8,756	12,560	16,563	16,678	36,018
Coverage Rate	2.48%	1.53%	1.25%	0.96%	1.03%	1.05%	1.49%	1.98%	1.99%	4.02%
Estates	10,451	9,319	8,024	7,707	7,151	7,265	6,455	6,081	5,299	4,616
Coverage Rate	10.22%	8.46%	6.89%	6.24%	5.84%	6.38%	7.41%	8.20%	9.66%	7.70%
Gift	2,010	2,369	2,097	2,005	1,899	1,855	1,979	2,125	2,051	1,490
Coverage Rate	0.79%	0.91%	0.72%	0.65%	0.63%	0.66%	0.69%	0.81%	0.77%	0.56%

Source: TIGTA analysis of IRS Data Book

Appendix VI

Prior Treasury Inspector General for Tax Administration Compliance Trends Reports

Management Advisory Report: Evaluation of Reduction in the Internal Revenue Service's Compliance Activities (Reference Number 2000-30-075, dated May 2000).

Management Advisory Report: Tax Return Filing and Examination Statistics (Reference Number 2001-30-175, dated September 2001).

Management Advisory Report: Analysis of Trends in Compliance Activities Through Fiscal Year 2001 (Reference Number 2002-30-184, dated September 2002).

Trends in Compliance Activities Through Fiscal Year 2002 (Reference Number 2003-30-078, dated March 2003).

Trends in Compliance Activities Through Fiscal Year 2003 (Reference Number 2004-30-083, dated April 2004).

Trends in Compliance Activities Through Fiscal Year 2004 (Reference Number 2005-30-055, dated March 2005).

Trends in Compliance Activities Through Fiscal Year 2005 (Reference Number 2006-30-055, dated March 2006).

Trends in Compliance Activities Through Fiscal Year 2006 (Reference Number 2007-30-056, dated March 27, 2007).