

December 2008

# TAX ADMINISTRATION

## IRS's 2008 Filing Season Generally Successful Despite Challenges, although IRS Could Expand Enforcement during Returns Processing



GAO

Accountability \* Integrity \* Reliability



Highlights of [GAO-09-146](#), a report to congressional requesters

## Why GAO Did This Study

The tax filing season is when the Internal Revenue Service (IRS) has most of its contacts with taxpayers, answering questions and processing returns and refunds. The 2008 filing season was particularly challenging due to the unanticipated mandate to make economic stimulus payments. The filing season is also the start of IRS's efforts to ensure the newly filed returns are compliant with the tax laws. GAO was asked to assess IRS's performance, describe the costs and foregone revenue of administering the economic stimulus payments, and identify any opportunities for improving filing season compliance checks. GAO analyzed IRS performance data, reviewed IRS operations, and interviewed IRS officials.

## What GAO Recommends

GAO recommendations include that IRS use its existing legal authority to correct child and dependent care credit claims on returns filed using "Married Filing Separately," and study the effectiveness of combining data on noncustodial parents and other taxpayer characteristics to verify earned income tax credit claims.

In response, the IRS Deputy Commissioner agreed with our recommendations and outlined the actions that IRS would take.

GAO suggests that the Congress provide IRS with legal authority to automatically correct returns for individual retirement account contributions that violate the dollar or age limits. IRS supported our suggestion.

To view the full product, including the scope and methodology, click on [GAO-09-146](#). For more information, contact James White at (202) 512-9110 or [WhiteJ@gao.gov](mailto:WhiteJ@gao.gov).

## TAX ADMINISTRATION

### IRS's 2008 Filing Season Generally Successful Despite Challenges, although IRS Could Expand Enforcement during Returns Processing

#### What GAO Found

IRS successfully processed 150 million returns and issued 105 million refunds for \$246 billion as of September 12, 2008. In addition, IRS issued 116 million stimulus payments totaling \$94 billion. However, taxpayers' access to IRS's telephone assistors was substantially lower than last year because of an unanticipated increase in telephone call volume. Calls to IRS more than doubled to 118 million as many taxpayers had questions about the amount of their stimulus payment or its timing. IRS acted to answer the calls including shifting hundreds of staff from collection cases to telephone assistance. IRS took other actions such as adding features to its Web site that answered stimulus-related questions and likely diverted some calls. Regardless, taxpayers' ability to get through to IRS telephone assistors declined from about 81 percent of waiting callers getting through last year to about 57 percent from January through June 30 of this year.

IRS expects the costs and foregone revenue associated with issuing the economic stimulus package (ESP) payments to reach about \$960 million, of which \$655 million is revenue foregone due to the shift of collections staff to telephone service.

There are two areas where IRS does not use its current legal authority to automatically correct errors when processing tax returns. One involves eligibility for the child and dependent care credit by taxpayers who are "Married Filing Separately." Taxpayers in this filing status are not eligible for the credit, but IRS allows the credit to be claimed, issues refunds, and then audits taxpayers to try to recover the money. The second is that IRS does not use its existing legislative authority to verify earned income tax credit claims by noncustodial parents—in 2006, \$91 million of claims were unverified. IRS has plans to study one option for verifying these claims, but is not planning to study another option, combining federal data on noncustodial parents and other taxpayer characteristics to automatically determine eligibility. Finally, there are two areas where IRS lacks legal authority, but has the technical ability to use automated error checks. IRS could prevent (1) individuals from deducting contributions to individual retirement accounts above the allowable limit and (2) individuals from violating the age requirements for such contributions.

Individual Income Tax Returns Processed, 2006–2008 Filing Seasons

	Electronic returns		Total returns in millions
	Number in millions	Percentage of total returns	
Jan. 1--Sept. 12, 2008	88	59	150
Jan. 1--Sept. 11, 2007	79	59	135
Jan. 1--Sept. 10, 2006	72	55	131

Source: GAO analysis of IRS data.

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United States Government Accountability Office  
Washington, DC 20548

December 12, 2008

The Honorable Max Baucus  
Chairman  
The Honorable Charles E. Grassley  
Ranking Member  
Committee on Finance  
United States Senate

The Honorable John Lewis  
Chairman  
The Honorable Jim Ramstad  
Ranking Member  
Subcommittee on Oversight  
Committee on Ways and Means  
House of Representatives

Effective and timely taxpayer service and enforcement programs, working together, can provide faster refunds, reduce the burden on taxpayers of complying with tax laws, help identify and correct errors before interest is owed by the taxpayer, and help to ensure that taxpayers receive tax benefits for which they are eligible. The filing season is when most taxpayers interact with the agency and perhaps is the Internal Revenue Service's (IRS) best opportunity to combine service and enforcement.<sup>1</sup>

Filing season services include processing individual income tax returns and refunds and providing taxpayer services through telephone, Web site, and face-to-face assistance. In previous reports and testimonies, we said that IRS has made significant progress improving taxpayer service since the passage of the IRS Restructuring and Reform Act of 1998.<sup>2</sup> A significant challenge for IRS during the 2008 filing season was the passage of the

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<sup>1</sup> Most taxpayers file their tax returns between January 1 and April 15, which is the deadline for filing individual income tax returns. However, millions of taxpayers receive extensions from IRS, which allows them to delay filing until as late as October 15.

<sup>2</sup> Pub. L. No. 105-206 (1998). See, for example, GAO, *Tax Administration: Most Filing Season Services Continue to Improve, but Opportunities Exist for Additional Savings*, [GAO-07-27](#) (Washington, D.C.: Nov. 15, 2006).

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Economic Stimulus Act of 2008, which mandated that IRS send stimulus payments to over 100 million households.<sup>3</sup>

During the filing season, enforcement begins with IRS's math error program, where IRS uses its computers to identify errors such as calculation mistakes or omitted or inconsistent entries. Where possible, IRS uses its math error authority (MEA) to correct certain errors before interest is owed by the taxpayer, to provide faster refunds and to help ensure that taxpayers receive tax credits for which they are eligible.<sup>4</sup>

In light of the importance of IRS's performance during the tax filing season, you asked us to (1) assess IRS's performance relative to goals and prior years' performance, including identifying factors that affect performance such as the economic stimulus package (ESP); (2) describe IRS's time frames and planned versus actual costs, including foregone revenue, associated with the passage and implementation of ESP legislation; and (3) identify opportunities, if any, for improving compliance by expanding MEA. We provided testimony on IRS's 2008 interim performance before the Subcommittee on Financial Services and General Government, Committee on Appropriations, U.S. Senate, on April 16, 2008, and the Subcommittee on Oversight, Committee on Ways and Means, House of Representatives, on June 19, 2008; we also issued a report to the Subcommittee on Oversight, Committee on Ways and Means, House of Representatives, on March 13, 2008.<sup>5</sup>

We based our assessment on the results and analyses of IRS data and reports, workload and performance information, observations of IRS's operations, interviews with IRS officials, information from representatives of some of the larger tax preparation companies and professional associations that represent preparers providing tax assistance, and reports

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<sup>3</sup> Pub. L. No. 110-185 (2008). GAO, *Internal Revenue Service: Fiscal Year 2009 Budget Request and Interim Performance Results of IRS's 2008 Tax Filing Season*, [GAO-08-567](#) (Washington, D.C.: Mar. 13, 2008).

<sup>4</sup> IRS is granted MEA in 26 U.S.C. § 6213(b). It can only be used for certain purposes specified by the Congress in 26 U.S.C. § 6213(g)(2). If it is not specified in the statute, IRS cannot pursue assessment and collection activities without issuing a statutory notice of deficiency.

<sup>5</sup> GAO, *Internal Revenue Service: Assessment of the Fiscal Year 2009 Budget Request*, [GAO-08-620T](#) (Washington, D.C.: Apr. 16, 2008), and *Tax Administration: Data on the Effects of the Economic Stimulus Program on the Internal Revenue Service's Telephone Service and Costs*, [GAO-08-916T](#) (Washington, D.C.: June 19, 2008); and [GAO-08-567](#).

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by the Treasury Inspector General for Tax Administration (TIGTA). We conducted this performance audit from January through October 2008, 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 assessed the reliability of data used in this report by (1) performing electronic testing of required data elements, (2) reviewing existing information about the data and the system that produced them, and (3) interviewing agency officials knowledgeable about the data. We determined that the data were sufficiently reliable for the purpose of this report. More detail on our scope and methodology can be found in the scope and methodology section.

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## Results in Brief

Even with the significant new workload associated with ESP, IRS delivered a generally successful filing season—with one key exception—access to telephone assistors. As of September 12, 2008, IRS had processed 150 million individual income tax returns, including almost 9 million ESP-only tax returns from people who would not otherwise have to file a return. In addition, IRS processed 105 million tax refunds totaling \$246 billion, plus 116 million stimulus payments totaling \$94 billion. However, taxpayers' access to IRS's telephone assistors was substantially lower than last year. As of June 30, 2008, call volume more than doubled to over 118 million calls largely due to taxpayers with ESP-related questions. According to IRS officials, the call volume strained telephone resources and contributed to a significant decline in access to live telephone assistance, especially beginning in early May. As a result, many people waited longer, were disconnected, or abandoned their calls before reaching an IRS assistor. On a positive note, the accuracy of the telephone assistors' responses to tax law and account questions continued to be above 90 percent. Further, IRS provided ESP information and tools on its Web site that significantly increased its use and likely diverted some taxpayer questions from the telephones to the Web site.

IRS expects the costs and foregone revenue associated with implementation of ESP to reach up to \$960 million—\$305 million in costs plus \$655 million in foregone revenue. Foregone revenue results from IRS's decision to shift hundreds of staff from collection cases to telephone assistance. Because of the timing of ESP, IRS did not have time to hire, conduct background checks, and train additional staff to handle the increased telephone volume. According to officials, IRS mitigated the cost of implementing ESP by working with national organizations such as

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AARP to help with the outreach to the population of retirees, disabled veterans, and low-wage workers who usually are exempt from filing a tax return, but were eligible for stimulus payments. IRS estimates that 82 percent of this population participated in ESP, which is better than participation rates for some other benefit programs, such as the Earned Income Tax Credit (EITC). IRS plans to issue a report on ESP to document lessons learned in December, 2008.

We identified two areas where IRS could expand the use of its existing MEA and two other areas where authority would be useful if granted. In one area, by not using its existing MEA to verify a taxpayer's "Married Filing Separately" filing status for eligibility for the child and dependent care credit, IRS may create financial difficulties for up to several thousand taxpayers who, as a result of an audit, may find that they have to repay the credit, plus penalties and interest. Although taxpayers in this filing status are not eligible for the credit, IRS allows the credit to be claimed, issues refunds, and then audits taxpayers to try to recover the money. Further, IRS could use its authority to notify taxpayers of a possible change in their filing status that would make them eligible for the credit. The second area that IRS does not use its existing MEA is to verify EITC claims by noncustodial parents—in 2006, \$91 million of such claims were unverified. IRS has plans to study one option for verifying these claims, but is not planning to study another option, combining data from the Federal Registry of Child Support Orders (FCR) database on non-custodial parents and other taxpayer characteristics to automatically determine eligibility. In addition, there are two areas where IRS lacks legal authority, but has the technical ability to use automated error checks during returns processing. The first would be to prevent individuals from deducting contributions to individual retirement accounts above the allowable limit. These taxpayers incorrectly claim the amount intended for people over 50 making IRA "catch-up" contributions.<sup>6</sup> The second would prevent individuals from violating the 70 ½ age limitation for making these contributions.

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<sup>6</sup> A "catch up" contribution allows taxpayers who will be at least 50 by the end of the tax year to contribute an additional amount to a traditional or Roth IRA. In 2008, taxpayers under age 50 could contribute \$5,000 to a traditional IRA, while those over age 50 could contribute \$6,000.



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We are making recommendations that the Commissioner of Internal Revenue to direct the appropriate officials to

1. use IRS's existing MEA to identify and correct child and dependent care credit claims on "Married Filing Separately" returns;
2. include information on math error notices to inform taxpayers that they may be eligible for the child and dependent care credit if they file under a different status, such as "Single," "Married Filing Jointly," "Head of Household," or "Qualifying Widow(er) with a dependent child;" and
3. assess the effectiveness of combining FCR and other data on taxpayer characteristics to verify the eligibility of EITC claims from noncustodial parents.

This report includes two matters for congressional consideration—to provide IRS with the authority to use math error checks to identify and correct ineligible (1) individual retirement account (IRA) "catch-up" contributions, and (2) contributions to IRAs from taxpayers over age 70-½.

In commenting on a draft of this report, the IRS Deputy Commissioner agreed with our recommendations and outlined IRS's actions to address those recommendations (see app. I). With respect to the matters for congressional consideration, she supported both suggestions and stated that they could further increase compliance and improve taxpayer service.

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## Scope and Methodology

To assess IRS's 2008 filing season performance in the key filing season activities compared to goals and past performance, report on the effect of ESP, and highlight areas where IRS could expand use of MEA, we

- reviewed and analyzed IRS reports, testimonies, budget submissions, and other documents and data, including workload data, data related to IRS's performance measures and goals, and data on taxpayer usage of services and other statistics such as the number of paid preparers;
- observed operations at IRS's Atlanta, Georgia, paper submission processing center, the Atlanta call site, the Joint Operations Center (which manages IRS's telephone services) in Atlanta, and IRS's walk-in locations in Atlanta and Baltimore, Maryland, and selected these offices for a variety of reasons, including the location of key IRS managers, such as those responsible for telephone and walk-in site services;
- tested for statistically significant differences between annual performance measures based on IRS sample data;

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- analyzed staffing data for paper and electronic filing, and telephone assistance;
  - reviewed information from organizations, such as Keynote Systems, which evaluate Internet performance;
  - interviewed representatives of some of the larger private and nonprofit organizations that prepare tax returns, such as H&R Block, and trade organizations that represent both individual paid preparers, tax preparation companies, and professional associations, including the American Institute of Certified Public Accountants;
  - reviewed TIGTA reports and interviewed TIGTA officials about IRS's performance and initiatives;
  - interviewed IRS officials about current operations, performance relative to 2008 performance goals and prior filing season performance, trends, significant factors, and initiatives that affected or were intended to improve performance, monitoring, and oversight of paid tax preparers;
  - reviewed IRS data on math errors, information on IRS's process for identifying and correcting math errors, legislation providing IRS with math error authority;
  - interviewed IRS officials, including those from the EITC office, about MEA;
  - reviewed reports on MEA from the National Taxpayer Advocate (NTA) and TIGTA; and
  - reviewed our prior reports and followed up on our recommendations made in those reports.

This report discusses numerous filing season performance measures and data that cover the quality, accessibility, and timeliness of IRS's services. We assessed the reliability of data used in this report by (1) performing electronic testing of required data elements, (2) reviewing existing information about the data and the system that produced them, and (3) interviewing agency officials knowledgeable about the data. We determined that the data were sufficiently reliable for the purpose of this report. To the extent possible, we corroborated information from interviews with documentation and data and where not possible, we attribute the information to IRS officials. We reviewed IRS documentation, interviewed IRS officials about computer systems and data limitations, and compared those results to our standards of data reliability.<sup>7</sup> Data limitations are discussed where appropriate. We conducted our work primarily at IRS headquarters in Washington, D.C., walk-in sites offices at

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<sup>7</sup> GAO, *Assessing the Reliability of Computer-Processed Data*, GAO-02-15G (Washington, D.C.: Sept.1, 2002).

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Baltimore, Maryland, the Wage and Investment Division headquarters and walk-in sites in Atlanta, Georgia.

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## Background

IRS's filing season is an enormous and critical undertaking and consists of two primary activities, processing well over 100 million individual income tax returns and refunds and providing millions of taxpayers with telephone, Web site, and face-to-face assistance. The following describes the processing of tax returns.

- Most taxpayers file their individual income tax returns electronically, although millions still mail paper returns. Electronic filing is faster, which allows taxpayers to receive refunds faster, and is less prone to transcription and other errors, and provides IRS with significant cost savings.
- Taxpayers below an income ceiling can access the Free File program offered through IRS's Web site by a consortium of 19 tax preparation companies that offer free on-line tax preparation and filing services for qualifying taxpayers.
- IRS continues to develop and deliver a number of Business Systems Modernization programs, including releases of the Customer Account Data Engine (CADE). CADE is intended to eventually replace IRS's antiquated Master File legacy processing system and facilitates faster refund processing and provides IRS with more up-to-date account information.

IRS provides a variety of taxpayer services, including the following.

- IRS has toll-free assistance telephone lines which taxpayers can call with questions about tax law or their refunds. Depending on how taxpayers respond to menu choices, questions are answered by automated messages or calls are routed to telephone assistors located at 24 call sites around the country.
- IRS offers assistance through its Web site, including "Where's My Refund?", which enables taxpayers to use the Web site to determine whether the agency received their tax returns and processed their refunds. Taxpayers can also download forms, instructions, and publications, research their own tax law issues through Frequently Asked Questions or Tax Topics, and receive help with specific tax law questions and procedural questions via e-mail.
- IRS offers assistance at nearly 12,000 volunteer sites, which helps IRS serve traditionally underserved taxpayer segments, including elderly, low-income, and disabled taxpayers, and taxpayers with limited-English proficiency. Additionally, IRS has 401 walk-in sites where

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taxpayers can receive basic tax law and account assistance from IRS staff and have returns prepared if their annual income is \$40,000 or less.<sup>8</sup>

In addition to depending on IRS, taxpayers depend heavily on paid tax return preparers or commercial tax preparation software during the filing season. Paid preparers are a critical part of the nation's tax administration system because of the wide variety of assistance they offer taxpayers, including help understanding tax obligations, return preparation and electronic filing, and providing forms and publications. In 2007, 59 percent of individual taxpayers had their return prepared and filed by paid preparers and about 16 percent prepared their return using commercial tax preparation software.

Late tax law changes create filing season challenges for IRS. This can be particularly true if, like ESP, the changes are complex and significantly increase filing season workload (for a detailed description of IRS's implementation of ESP, see app. II). ESP contained complex rules about eligibility, amount of the rebate, and filing requirements.

Over the years, the Congress granted IRS legal authority to cover 11 areas so that the agency could correct return errors during processing, including calculation errors and entries that are inconsistent or exceed statutory limits, without having to issue the taxpayer a statutory notice of deficiency (see app. III for further details on the MEA process and authorities). We have reported that prompt compliance checks such as these are important because as unpaid taxes age, the likelihood of collecting all or part of the amount owed decreases, due in part to continued accrual of interest and penalties on the outstanding federal taxes.<sup>9</sup> MEA also provides a taxpayer service as it allows taxpayers to receive their refunds faster, corrects return errors before interest is accrued, and can avoid time consuming interaction with IRS while the error is being resolved.

MEA can also help ensure taxpayers receive the tax benefits for which they are eligible. For example, between tax years 2003 and 2006, using its MEA, IRS identified over 500,000 occurrences of taxpayers under-claiming the EITC with the result that an additional \$130 million was provided to

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<sup>8</sup> This limitation approximates the amount set in the Internal Revenue Code for claiming the EITC. IRS has required appointments for taxpayers seeking this assistance since 2003.

<sup>9</sup> See, for example, GAO, *Tax Compliance: Businesses Owe Billions in Federal Payroll Taxes*, [GAO-08-617](#) (Washington, D.C.: July 25, 2008).

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those claimants. Without MEA, most of these errors would not likely have been identified and thousands of low income taxpayers would likely have received less than they were entitled.

Because math error checks are automated and require little contact with taxpayers, they provide IRS with an enforcement tool that is low cost and less intrusive and burdensome to taxpayers than audits. By using its MEA, IRS reported preventing \$460 million from reaching ineligible taxpayers in fiscal year 2006.

The NTA—who heads the program that helps resolve taxpayers' tax problems with IRS and recommends changes to mitigate taxpayer problems—noted some concerns about IRS's use of MEA in its 2006 report to Congress.<sup>10</sup> NTA reported that, because MEA allows IRS to summarily assess the tax before a taxpayer has the opportunity to challenge the assessment, it should be used in specific and narrow circumstances. Because taxpayer rights are different under MEA, NTA expressed concern that math error notices did not provide enough detail for the recipient to understand what had occurred, their rights, and how they could request abatement. NTA also reported that IRS was using math error checks in some limited areas where it was not clear that IRS had the authority. In its response to the NTA's 2006 report, IRS reported that it resolved the issues raised by NTA. While the NTA acknowledges that the IRS has made significant improvements to the math error notice process, it still notes that IRS could improve how it is administering MEA.

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<sup>10</sup> The National Taxpayer Advocate, *National Taxpayer Advocate—2006 Annual Report to Congress* (Washington, D.C.: Dec. 31, 2006).

## Despite the Increased Volume of Tax Returns Due to the Economic Stimulus, IRS's Filing Season was Successful Compared to Previous Years' with the Exception of Access to Telephone Assistance

As of September 12, 2008, IRS processed 150 million individual income tax returns, including almost 9 million ESP-only returns, and processed 105 million tax refunds totaling \$246 billion. IRS processed 16 million Form 1040As on paper, a 92 percent increase from last filing season, largely due to ESP. According to IRS officials, this increase was especially burdensome not only because paper processing is more labor-intensive and expensive than electronic processing, but also because claimants made many errors on ESP-only returns, which IRS had to manually correct. As of September 12, IRS had processed 116 million stimulus payments totaling almost \$94 billion.

As shown in table 1, the percentage of electronically filed returns is similar to last year's when ESP-only returns are included. Excluding the almost 9 million ESP-only returns, most of which were filed on paper, the number of taxpayers who filed electronically increased from 59 percent to 62 percent of total returns.

**Table 1: Individual Income Tax Returns Processed, 2006-2008 Filing Seasons**

		Electronic returns		Total returns in millions
		Number in millions	Percentage of total returns	
2008 (Jan. 1—Sept. 12, 2008)	Total returns (ESP returns included)	88	59	<b>150</b>
	ESP returns excluded	87	62	<b>141</b>
2007 (Jan. 1—Sept. 11, 2007)		79	59	<b>135</b>
2006 (Jan. 1—Sept. 10, 2006)		72	55	<b>131</b>

Source: GAO analysis of IRS data.

The increase in electronic filing is due, in part, to the Free File program. The number of taxpayers who filed electronically through Free File increased 24 percent, after a 2 percent decline in participation last year, to 3.8 million. According to IRS officials, this increase is due to greater taxpayer awareness and enhanced marketing.

As of August 8, CADE posted 30.5 million returns, slightly exceeding IRS's goal of 30 million and significantly up from the 11 million returns CADE posted as of last year. As we have previously reported, a major benefit of CADE is that direct deposit refunds are issued by CADE 1 to 5 business days faster than the current legacy system, and paper check refunds are

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issued 4 to 8 business days faster because CADE posts information daily.<sup>11</sup> CADE also was successful in processing 24 million stimulus payments and contributed to IRS's early distribution of some stimulus payments. ESP-only payments processed through CADE, rather than the legacy Master file, were issued up to 4 days earlier than the first scheduled disbursement date.

Despite the additional volume, IRS met or exceeded goals for seven out of eight of the processing measures (see app. IV for details). The one measure where performance was significantly below IRS's goal and last year's level was the refund error rate, i.e., the percentage of refunds with IRS-cause errors issued to taxpayers by IRS. According to IRS officials, this performance was due to a programming change and did not delay the processing of returns or refunds.

We have previously reported that IRS's ability to maintain or improve taxpayer service will likely depend on its continued ability to find efficiencies, particularly through increased electronic filing.<sup>12</sup> Consistent with this approach, IRS released the "Advancing E-File Study" in November 2008, which is the foundation for the agency's strategy and planned actions to reach the congressionally-set goal of 80 percent of individual returns filed electronically.<sup>13</sup>

In recent reports, we suggested two options for increasing electronic filing or reducing paper processing. One would be for Congress to mandate electronic filing by large paid tax return preparers.<sup>14</sup> Currently, many returns prepared by preparers on computers are printed and mailed to IRS, which then have to be transcribed. Our other option is to require bar coding on paper returns that were prepared by taxpayers using

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<sup>11</sup> [GAO-08-38](#).

<sup>12</sup> [GAO-07-27](#).

<sup>13</sup> The Congress set this long-term electronic filing goal in the IRS Restructuring and Reform Act of 1998, which was to have 80 percent of all individual income tax returns filed electronically by 2007. While we previously reported that IRS was not on track to achieve this goal (see GAO, *Tax Administration: IRS Improved Some Filing Season Services, but Long-term Goals Would Help Manage Strategic Trade-offs*, [GAO-06-51](#) [Washington, D.C.: Nov. 14, 2005]), the IRS Oversight Board recommended extending the goal to 2012 (see IRS Oversight Board [2008] *Electronic Filing 2007: Annual Report to Congress*, (Washington, D.C., 2007).

<sup>14</sup> [GAO-07-27](#).

commercial tax preparation software. Bar coding would eliminate IRS's transcription costs and errors.<sup>15</sup> IRS agreed to study this recommendation.

Paid preparers prepared over 81 million returns, which was 59 percent of all individual tax returns in the 2007 filing season. Because IRS has limited ability to identify paid preparers and match them with the returns they prepared, we recently reported that IRS has limited information about the accuracy of these returns and recommended that IRS develop a plan to require a single identification number for paid preparers, which could facilitate research on paid preparers' influence on taxpayer compliance.<sup>16</sup> IRS agreed to explore the use of a single identification number to enhance IRS's ability to identify paid preparers.

### Telephone Performance Was Substantially Lower Compared to Last Year's Due to the High Volume of Stimulus-Related Calls, with the Greatest Downturn Beginning in Early May

Taxpayers' access to IRS's telephone assistors was substantially lower than last year's because, according to IRS, it received an unprecedented number of calls primarily due to ESP-related questions. As table 2 shows, through June 30 of this year, IRS received over 118 million calls, more than double the total number of calls from last year. However, compared to last year, more than twice as many callers abandoned their calls and nearly 10 times as many were disconnected by IRS.

**Table 2: Call Volume by Call Type (in millions)**

	2007	2008	Percentage Change
Assistor calls answered <sup>a</sup>	21.5	27.0	26
Automated calls completed	20.8	43.0	107
Calls abandoned by caller	13.3	34.4	159
IRS courtesy disconnects and busy signals	1.3	13.6	946
<b>Total</b>	<b>56.9</b>	<b>118.0</b>	<b>107</b>

Source: GAO analysis of IRS data.

<sup>a</sup>Telephone data cover the date range of January 1 through June 30.

<sup>15</sup> [GAO-08-38](#). Additionally, IRS is considering a major modernization program that would include replacing the two legacy systems with contracts expiring in 2012. According to IRS officials, IRS's proposed modernization program would need to receive funding in the fiscal year 2010 budget in order to allow 2 years between the launch and testing of the new system and the retirement of the existing ones. However, IRS officials reported developing options in case they did not receive funding in fiscal year 2010.

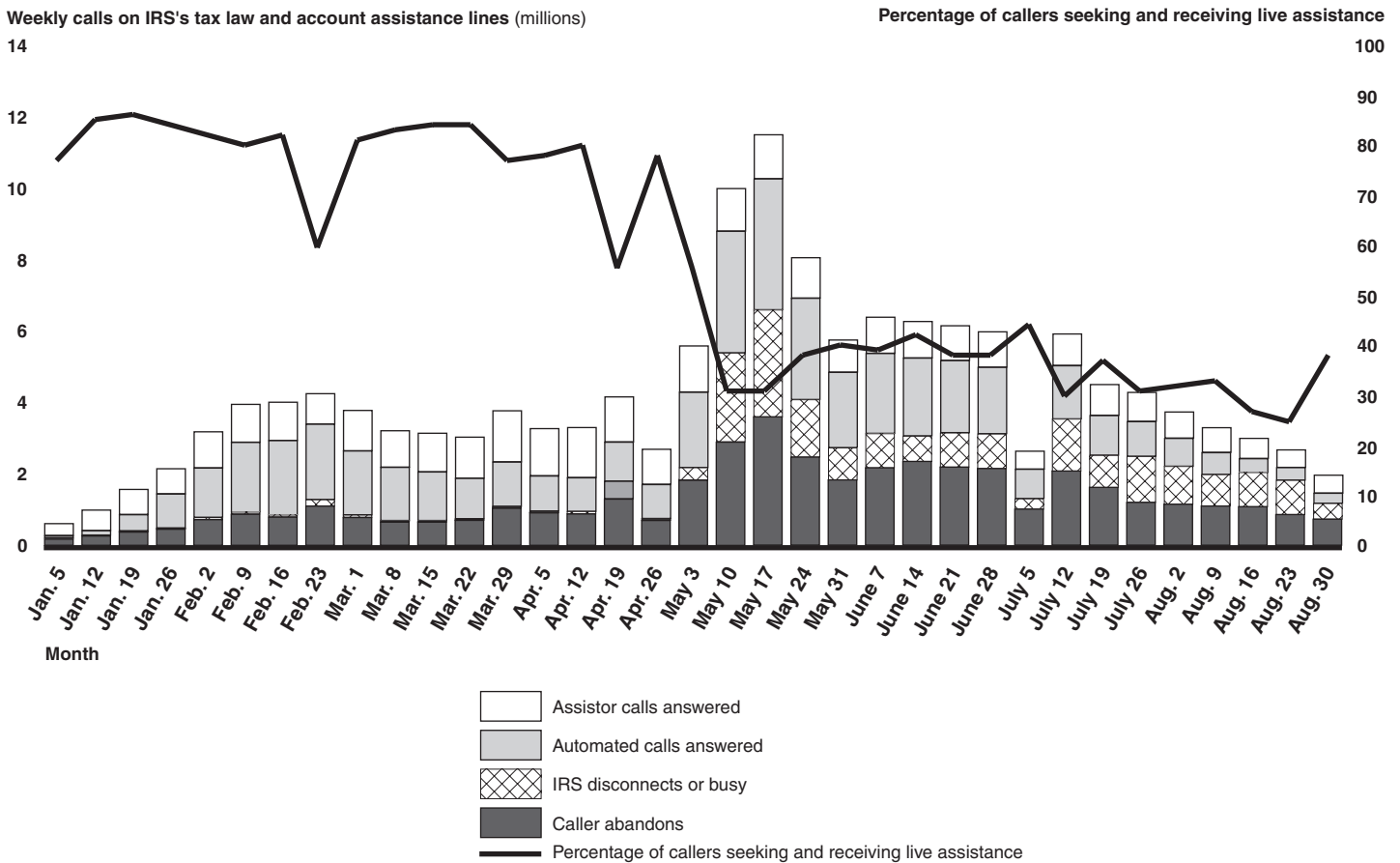
<sup>16</sup> [GAO-08-567](#).



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On the basis of its experience with the stimulus rebates in 2001 and 2003, IRS took steps to facilitate telephone service, including establishing a dedicated toll-free Rebate Hotline for callers with ESP-related questions in February. As of June 30, IRS answered 37 million calls made to its Rebate Hotline. However, the unprecedented call volume strained IRS telephone resources and contributed to a significant decline in the telephone level of service. Calls to IRS spiked in the first three weeks of May around the same time that the first rounds of stimulus checks were issued (see fig. 1). According to IRS officials, taxpayers' confusion over when they would receive their payment, or how much they received contributed to the high call volume. During these weeks, the percentage of callers waiting for an assistor and getting through fell below 50 percent and subsequently did not surpass that mark.

**Figure 1: IRS Toll-free Calls and Percentage of Callers Seeking and Receiving Live Assistance (January 1, 2008–August 30, 2008)**



Source: GAO analysis of IRS data.

Note: Weekly calls are those seeking tax law and account information assistance and do not include calls to IRS's compliance division.

The increased call volume also contributed to a decline in related performance indicators and measures. As previously noted, the number of callers who received busy signals or were disconnected from IRS increased as did the caller abandon rate. Further, as shown in table 3, the average speed of answer—the length of time taxpayers wait to get their calls answered—nearly doubled from last year.

**Table 3: IRS Telephone Performance, 2005-2008 Filing Seasons**

	2005	2006	2007	2008
Percentage of callers seeking and receiving live assistance	82.2	81.0	80.9	56.7
Average speed of answer (minutes)	4.3	3.9	4.6	8.6

Source: GAO analysis of IRS data.

Note: Telephone performance data are based on the date range of January 1 through June 30.

In addition to the Rebate Hotline, service on other toll-free lines, such as tax law and account assistance, was affected as well. For example, IRS estimated that from early May, when IRS began issuing ESP payments, through the end of June about 30 percent of callers to other toll-free lines asked ESP-related questions in addition to their primary question. When the caller asked an ESP-related question, the assistor was instructed not to transfer the caller to the rebate hotline, but instead to answer the question. As a result, the level of service on some other telephone applications not related to the Rebate Hotline also declined this year, according to IRS officials.

Even with the increased volume of calls, the accuracy of the telephone assistors' responses to tax law and account questions was comparable to the same time period last year and met IRS's goals (see table 4). Since 2005, IRS has maintained a level of accuracy of about 90 percent.

**Table 4: IRS Telephone Assistor Accuracy Performance, 2004-2008 Filing Seasons**

	2005 Actual	2006 Actual	2007 Actual	2008 Actual	Fiscal Year 2008 goals
Accuracy measures <sup>a</sup>					
Tax law accuracy rate (in percentages) <sup>b</sup>	89.5 +/-0.6	90.6 +/-0.6	90.7 +/-0.9	90.3 +/-0.9	91.0
Accounts accuracy rate (in percentages) <sup>b</sup>	91.3 +/-0.4	93.3 +/-0.3	93.2 +/-0.5	93.5 +/-0.4	93.5

Source: GAO analysis of IRS data.

<sup>a</sup>Based on representative samples and from January through June for 2004, 2005, 2006, 2007 and 2008.

<sup>b</sup>The percentage of calls in which telephone assistors provided accurate answers for the call type and took the appropriate action, with a 90 percent confidence interval.

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During the course of our filing season work, we identified some opportunities to reduce ESP-related calls. On May 21, 2008, we sent a letter to the IRS Commissioner that suggested four options for his consideration. IRS implemented three of the four options. IRS re-ordered the Frequently Asked Questions page on IRS's Web site to put the most common questions addressed by assistors first. IRS added text to the payment schedule page on its Web site and a message for telephone assistors that provided more detail as to when various types of taxpayers should expect to receive their refunds. IRS modified the Rebate Hotline script to include an automated "Most Frequently Asked Questions" (FAQs) option by adding the FAQs to the automated messaging in the call waiting queue. The option IRS did not implement was to expand outreach efforts in the press about the timing and calculation of stimulus payments. IRS officials concluded that this information might unintentionally create more calls. Although we believe that additional and more accurate outreach would have been useful for reducing public confusion, we acknowledge IRS's position that many of the calls have required specific explanations that could not have been handled in mass public outreach.

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### IRS Provided Tools through its Web Site That Significantly Increased Use and Potentially Diverted Calls

IRS provided tools and information through its Web site on ESP and adjusted the information quickly. For example, on the day the legislation was passed, IRS posted information on IRS.gov with details about ESP. Within a month, IRS launched the Stimulus Payment Calculator. IRS also provided a "Where's My Stimulus Payment?" feature, launched May 1, 2008 (see app. II for more details on ESP timeline).

These ESP-related features resulted in a dramatic increase in the volume of taxpayer visits, as shown in table 5; visits to IRS's Web site increased 74 percent; however, if taxpayer visits to ESP-related features were excluded, visits were slightly down from last year.

**Table 5: IRS Web Site Use, 2006-2008 through July (in thousands)**

<b>Uses</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>Percentage change— 2007 to 2008</b>
Total visits	152,345	168,332	292,331	74
Where's My Refund?	30,663	30,746	37,871	23
Economic Stimulus—related visits	n/a	n/a	65,982	n/a
Where's My Economic Stimulus Payment?	n/a	n/a	36,994	n/a
Economic Stimulus Calculator	n/a	n/a	27,062	n/a
Other visits (including ESP features)	121,681	137,586	124,422	-10
Downloads	160,477	120,596	126,945	5
Searches	88,250	101,072	120,263	19

Source: GAO analysis of IRS data.

Although difficult to quantify, considering the large number of visits to ESP-related features on IRS's Web site, it is likely that ESP information and features on IRS.gov provided sufficient information to divert taxpayers' questions from IRS's Rebate Hotline.

One measure of the quality of IRS's Web site is its ranking in the Keynote Systems top 40 government Web sites. During the 2008 filing season, IRS.gov ranked first or second in response time out of the top 40 government Web sites in the Keynote Government Index weekly ratings, compared to ranging between third and sixth place last filing season.<sup>17</sup>

<sup>17</sup> The Keynote Government Index measures and benchmarks the performance of the home pages of 40 major U.S. federal government Web sites from the 10 largest U.S. metropolitan areas.

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**Taxpayer Usage Increased at Volunteer Sites, and although IRS is Making Limited Progress Assessing Quality, Tax Law Quality Declined at Walk-in Sites**

Volunteer partners prepared 3.2 million returns, which is a 31 percent increase compared to last year, with virtually the same number of sites. IRS officials attribute this growth mainly to increased word-of-mouth promotion of sites and ESP outreach efforts of volunteer partners. In contrast, the total number of taxpayer contacts at IRS's 401 walk-in sites declined slightly in the 2008 filing season compared to previous years.

In order to assess the quality of the assistance at volunteer sites, IRS conducts mystery shopping, site, and tax return reviews.<sup>18</sup> This filing season, IRS officials conducted 85 mystery shopping reviews for which the accuracy rate for return preparation averaged 75 percent at volunteer sites. While this is an improvement from last year, we are still concerned that, because of the low number of mystery shopping reviews conducted, the quality of volunteer-prepared returns remains largely unknown and information as a whole is unavailable.

IRS is in the process of improving how it measures the efficacy of its outreach efforts. In response to our recommendation, IRS has hired a contractor to conduct surveys and focus groups to assess the IRS partners', such as the AARP, ability to reach their target populations, e.g., the elderly and limited English proficiency and rural populations, and measure the effectiveness and quality of that outreach.<sup>19</sup>

In response to another one of our recommendations, to further improve its quality assessment at walk-in sites, IRS has expanded contact recording—a system IRS uses to record and assess the quality of other interactions between its employees and taxpayers—at walk-in sessions to include return preparation.<sup>20</sup> According to IRS officials, the agency hired adequate staff to review the recorded sessions, which are considerably longer for return preparation assistance than for tax law or account assistance. Further, IRS officials report that by the start of the 2009 filing season, contact recording of return preparation will be operational at 306 sites.

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<sup>18</sup> Mystery shopping involves IRS officials visiting volunteer sites posing as taxpayers to assess the experience of the taxpayers. Site reviews assess whether volunteer preparers were adhering to minimum quality standards required by all sites. Return reviews determine whether the tax law was applied properly for critical items and resulted in an accurate return based on the taxpayer interview and supporting documentation.

<sup>19</sup> GAO-08-38.

<sup>20</sup> GAO-08-38.

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The accuracy of account assistance at IRS walk-in sites was 85 percent, similar to last year. However, the accuracy of tax law assistance declined significantly to 68 percent, down from 80 percent last year. According to IRS officials, this decline was, in part, due to the timing for hiring and training hundreds of new staff, which was dependent on when IRS received funding. Further, those staff had to be trained on a new IRS's interactive tax law assistance guide at the beginning of the filing season. IRS officials expect tax law accuracy to improve for the 2009 filing season as walk-in site staff gain experience with the new guide.

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## The Costs and Foregone Revenue Associated with Implementing ESP Are Expected to Reach over \$900 Million and IRS Plans to Document Lessons Learned

Based on IRS data, the estimated costs and foregone revenue of implementing ESP will reach up to \$960 million. This includes \$202 million IRS received in a supplemental appropriation in fiscal year 2008, plus funding transferred from the Financial Management Service and IRS's user fee accounts (see table 6).<sup>21</sup> Because IRS anticipates the need for continued funding associated with the implementation of ESP, it requested an amendment to its fiscal year 2009 budget to receive an additional \$68 million, \$29 million of which it has already received under a continuing resolution. This funding would be used, in part, to cover telephone demand, which IRS expects to remain well above normal in 2009 due in part to ESP.

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<sup>21</sup> The Social Security Administration and Financial Management Service also received \$31 million and \$64 million respectively to administer ESP.

**Table 6: IRS Estimated Costs and Foregone Revenue Associated with Implementing ESP (dollars in millions)**

<b>Source of funding</b>	
Supplemental appropriations: operations support (e.g., postage, IT support, printing)	\$202
Additional requested funding in fiscal year 2009	\$39
Funding received under fiscal year 2009 continuing resolution	\$29
Funding transferred from the Financial Management Service	\$23
IRS user fees transferred	\$12
<b>Total funding</b>	<b>\$305</b>
<b>IRS estimates of foregone revenue from shifting Automated Collection System staff to answer ESP-related calls</b>	<b>\$655</b> <b>(As of August 9, 2008)</b>
<b>Taxpayers' costs</b>	<b>Reduced access to IRS's telephone assistants</b>

Source: GAO analysis of IRS data.

Because of the timing of ESP, IRS officials said that they did not have time to hire, conduct background checks on, and train additional staff to handle the increased telephone volume. Instead, IRS shifted hundreds of Automated Collection System (ACS) staff to answer calls to the Rebate Hotline from March through August 2008.

As of August, IRS reported \$655 million in foregone revenue because of ACS staff being taken off their collections work to answer the unprecedented volume of calls related to ESP. As we previously reported, IRS considered alternatives to shifting ACS staff, including contracting out, using other staff, or using Social Security Administration (SSA) staff, but decided the alternatives were not feasible.<sup>22</sup> According to IRS officials, while IRS expected some foregone revenue and paper backlog associated with the use of collections and other staff, it determined that delivering and supporting ESP was its highest priority, after the filing season.

<sup>22</sup> GAO, *Internal Revenue Service: Assessment of the Fiscal Year 2009 Budget Request*, [GAO-08-620T](#) (Washington, D.C.: Apr. 16, 2008).



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According to IRS officials, volunteer partners helped IRS mitigate the costs of delivering ESP to the targeted population of benefits recipients. These partners played a key role in funding and carrying out outreach to inform targeted groups, e.g., elderly, limited English proficiency, disabled, about their eligibility for the economic stimulus. For example, AARP supplied economic stimulus information on its Web site and in its monthly bulletin, and IRS officials reported that AARP paid for one of the mailings to people over 65 who may have been eligible for a stimulus payment, but had not yet filed a tax return. According to IRS officials, partly because of the efforts of the volunteer partners, 82 percent of the targeted individuals eligible for the economic stimulus participated in the program. This level of participation is relatively high compared to some other programs. For example, we have previously reported that participation rates in entitlement programs generally range from about 47 percent for the Food Stamp Program, to 75 percent for the EITC program.<sup>23</sup>

Consistent with best practices for government organizations, IRS is compiling a report on ESP that will summarize the costs to implement ESP and the effects on filing season operations. IRS is working to verify the cost information associated with ESP. As part of its report, IRS hired a contractor to conduct a lessons-learned study, which is due to be issued in December 2008.

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## IRS Does Not Fully Use Its Existing MEA and Congressional Expansion of MEA in Two New Areas Could Enhance Enforcement at Low Cost

IRS has authority to disallow child and dependent credit claims on returns with the filing status of “Married Filing Separately;” however, if taxpayers use this filing status, they would not be eligible for the credit. Under IRS’s procedures, it processes all returns with child and dependent care claims and issues refunds as appropriate. IRS then audits the taxpayer who made the claims using “Married Filing Separately” as appropriate. IRS audited about 6,000 of these cases in 2005. After verifying the claim is ineligible, IRS would be left trying to collect the money from taxpayers, who may have spent the money and now owe back taxes, plus penalties and interest. For lower-income taxpayers, this may represent a substantial financial burden.

Some taxpayers claiming child and dependent care credits may file as “Married Filing Separately” by mistake. They could be eligible for the credit if they file using a different status, such as “Single,” “Married Filing

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<sup>23</sup> GAO-05-221.

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Jointly,” “Head of Household,” or “Qualifying Widow(er) with a Dependent Child. Using audits to correct such mistakes is labor intensive for IRS. IRS officials confirmed that, if IRS used its MEA in these cases, then it could inform the taxpayer of their potential eligibility in the associated math error notices.

A second area where IRS has MEA but does not use it is to disallow EITC claims is when taxpayers are listed as the noncustodial parent in the FCR. Noncustodial parents are generally ineligible for EITC, because in most but not all cases, the child[ren] have not lived with the noncustodial parent for more than the required 6 months of the tax year to meet EITC eligibility.<sup>24</sup> According to EITC officials, IRS does not use its MEA in these cases because the child may have lived with the non-custodial parent for more than 6 months, meeting the residency requirements for eligibility; however, the FCR may not reflect this living arrangement. Instead of using its MEA, IRS audits less than 2 percent of these cases; however, it does not audit more cases because audits are labor intensive. As a consequence, most of the more than 41,000 claims for \$91 million in 2006 by noncustodial parents were allowed without verification. IRS does not know how many of these claims were incorrect, but for the claims it audited, the error rate was about 91 percent of claims for 2006.<sup>25</sup>

IRS officials reported that, as part of their 2009 EITC Research Plan, they plan to review the reliability and applicability of linking the custodial information in the FCR to EITC eligibility. They stated that if the FCR is found to be sufficiently reliable, IRS could use its MEA to automatically identify and correct ineligible EITC claims.

By focusing on FCR data alone, IRS’s review may be missing another way to use MEA to verify EITC claims by noncustodial parents and minimize the chance of disallowing eligible claims. IRS could combine FCR data with factors it currently uses to select returns for audits, factors such as taxpayer characteristics like filing status. In a limited sample of returns

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<sup>24</sup> Some taxpayers may be eligible for a lower EITC credit amount even if they do not have children.

<sup>25</sup> As in all cases, a taxpayer receiving a math error notice has 60 days from the date of the notice to request that IRS abate the tax. If the taxpayer requests that the tax be abated, IRS must then use the general deficiency procedures under 26 U.S.C. § 6212 if it believes that the additional tax is in fact due. Unless a taxpayer requests abatement of a math error assessment, however, he or she cannot challenge the assessment through IRS deficiency procedures or petition the Tax Court.

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from tax year 2006, audit data show that the FCR combined with audit selection factors such as filing status allowed IRS to accurately identify ineligible EITC claims by noncustodial parents in 98 percent of cases. Without including a more thorough assessment of this approach in its FCR review, IRS will not know the extent to which more accurate eligibility decisions could be made. Because the agency has MEA to use the FCR, the agency does not need additional authority to use FCR together with the audit selection factors.

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## Two Areas Where IRS Could Use Math Error Checks, but Would Need Legislative Authority

We identified two areas related to IRA contributions where IRS officials reported that they have the technical ability to accurately identify and correct math errors and did so as recently as 2006. However, at that time, IRS Chief Counsel determined that the Congress would need to grant IRS additional MEA to use age-based information to automatically disallow certain ineligible IRA contributions and thus IRS discontinued the use of math error checks in these areas.

First, some taxpayers under the age of 50 claim IRA contribution amounts that are more than allowed. These taxpayers incorrectly claim the amount intended for people over 50 making IRA “catch-up” contributions. In 2004, IRS identified 24,000 incidences of these IRA contribution overclaims resulting in \$23.2 million in underreported taxes. IRS used age data from the SSA database to check for age eligibility of these contributions. IRS counsel determined that the agency does not have MEA to use age-based data in this manner, although IRS has and does use age data from the SSA database for other math error types, such as EITC eligibility.

Second, some taxpayers over the age of 70-½ claim contributions to a traditional IRA, which they are not entitled to make. By law, taxpayers over the age of 70-½ cannot make contributions to traditional IRAs. TIGTA found that in 2006, 1,826 taxpayers over the age of 70-½ improperly claimed \$4 million in IRA deductions for an estimated loss of revenue of \$601,000. IRS used age data from the SSA database to check for age eligibility of these contributions. IRS officials believe that this problem is likely to become significantly larger as the population ages. However, IRS currently lacks MEA to identify and correct ineligible claims.

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## Conclusion

Despite the challenges of the economic stimulus program, IRS was generally successful providing service to taxpayers during the 2008 filing season. The major exception was telephone service, where the large, unanticipated increase in call volume caused by ESP significantly affected performance.

Although IRS focuses on taxpayer service during the filing season, it also uses MEA to conduct important compliance checks while processing tax returns. There are two areas where IRS could use its existing authority more fully and where the agency could improve service through notices informing taxpayers of potential eligibility for child and dependent care credits. With additional MEA, IRS could further increase compliance, improve taxpayer service, and gain additional efficiencies.

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## Recommendations for Executive Action

We recommend that the Commissioner of Internal Revenue direct the appropriate officials to

- (1) use IRS's existing MEA to identify and correct child and dependent care credit claims on "Married Filing Separately" returns;
- (2) include information on math error notices to inform taxpayers that they may be eligible for the child and dependent care credit if they file under a different status, such as "Single," "Married Filing Jointly," "Head of Household," or "Qualifying Widow(er) with a dependent child"; and
- (3) assess the effectiveness of combining FCR and other data on taxpayer characteristics to verify the eligibility of EITC claims from noncustodial parents.

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## Matters for Congressional Consideration

Given the potential for improving compliance now and in the future, the Congress should provide IRS with the authority to use math error checks to identify and correct returns with ineligible (1) IRA "catch-up" contributions, and (2) contributions to traditional IRAs from taxpayers over age 70-½.

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## Agency Comments and Our Evaluation

The Deputy Commissioner of Internal Revenue provided written comments in a December 4, 2008 letter in which she agreed with all our recommendations and outlined IRS's actions to address those recommendations. With respect to child and dependent care credit claims on "Married Filing Separately" returns, IRS plans to make programming changes that will allow the agency to use math error checks to identify and

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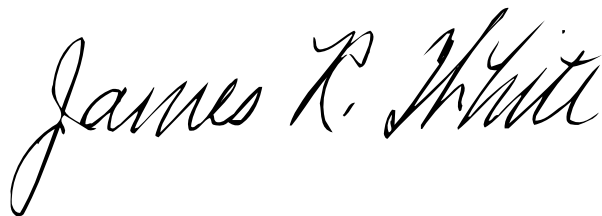
correct claims, and create notices to inform taxpayers of their possible eligibility for the child and dependent care credit if they file under a different status. For the recommendation to assess the effectiveness of combining FCR with other data on taxpayer characteristics, IRS plans to do so as part of its study on the reliability and applicability of non-custodial information in the FCR.

The Deputy Commissioner also supported our suggestions for congressional consideration to provide IRS with legal authority to automatically correct returns for individual retirement account contributions that violate the dollar or age limits. She further stated that they could increase compliance and improve taxpayer service.

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As agreed with your offices, unless you publicly announce its contents earlier, we plan no further distribution of the report until 30 days after its date. At that time, we will send copies of this report to the Secretary of the Treasury, the Commissioner of Internal Revenue; the Director, Office of Management and Budget; relevant congressional committees; and other interested parties. This report is available at no charge on GAO's web site at <http://www.gao.gov>.

For further information regarding this report, please contact James R. White, Director, Strategic Issues, on 202-512-9110 or [whitej@gao.gov](mailto:whitej@gao.gov). Contacts for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Individuals making key contributions to this report include Joanna Stamatiades, Assistant Director; Shea Bader; Julia Jebo; Karen O'Connor; Cheryl Peterson; and Neil Pinney.



James R. White  
Director, Tax Issues  
Strategic Issues Team

# Appendix I: Comments from the Internal Revenue Service



DEPUTY COMMISSIONER

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

December 4, 2008

Mr. James R. White  
Director, Tax Issues  
U.S. Government Accountability Office  
441 G Street, N.W.  
Washington, DC 20548

Dear Mr. White:

I have reviewed your draft report entitled *TAX ADMINISTRATION: IRS's 2008 Filing Season Generally Successful Despite Challenges, Although IRS Could Expand Enforcement During Returns Processing*. I appreciate your recognition of our significant achievements in successfully delivering the 2008 filing season which you note was particularly challenging due to the impact of the Economic Stimulus Payment (ESP) legislation.

Processing – We again had an outstanding filing season, successfully implementing significant and sometimes extremely late tax law changes. These included the ESP legislation, Mortgage Forgiveness Debt Relief Act, and extension of several expiring provisions, such as the Alternative Minimum Tax (AMT) patch, deduction for state and local sales taxes, educator expense deduction, and the tuition and fees deduction. Through November 7, 2008, we processed over 155 million individual income tax returns and issued over 107 million refunds, totaling nearly \$259 billion, which includes 8.5 million returns filed solely for purposes of claiming an Economic Stimulus Payment.

Electronic filing grew again this year with 89.9 million, or 58 percent, of individual taxpayers filing electronically. The remaining 65.1 million were filed on paper. The number of returns filed electronically increased 12.4 percent over last year, which exceeds the 9.2 percent increase we achieved in the prior year. This 12.4 percent increase is markedly higher than the 7.3 percent increase for 2008 projected in the fall of 2007.

The most significant increase in e-file occurred in the number of taxpayers who filed from their home computer. Over 26.9 million returns were filed from home computers, nearly a 19.4 percent increase from the prior year. Over 4.7 million taxpayers took advantage of the free online filing services offered by the Free File Alliance. Also notable is the fact that over 82.5 million taxpayers electronically signed their electronic returns, further increasing the efficiency of e-file.

Successful implementation of the Customer Account Data Engine (CADE) continued during 2008 with several releases successfully deployed during 2008. In addition to the main functionality, CADE handled economic stimulus payments for CADE taxpayers. The CADE Release 4.1 was deployed in July 2008, and introduced new functionality, including the ability to verify last marital status, and to process Surviving Spouse, Deceased, and Prior Year returns. This release also accepted Treasury overpayment offsets and issued Computer Paragraphs 08, to inform the taxpayer they may qualify for a refund from the Additional Child Tax Credit and Computer Paragraph 53, explaining that the refund will be issued as a paper check. This has resulted in the ability to maintain accounts within CADE that otherwise would have returned to the Individual Master File, thereby retaining for these taxpayers CADE's benefits of faster refunds and much more up-to-date account information. As of November 14, 2008, CADE posted over 30.5 million returns and disbursed over 29 million refunds for more than \$44.1 billion. In addition, CADE processed 23.7 million stimulus payments totalling \$18.2 billion.

Telephone Performance - We appreciate your recognition that the unprecedented increase in taxpayer demand generated by the ESP legislation had a significant impact on telephone access. The Stimulus legislation surfaced in the media in January and was passed in February, 2008. We reacted quickly by adopting a multi-phase approach to provide timely and meaningful information to ESP customers as the details of these payments unfolded. We did this while at the same time ensuring that our traditional filing season customers had access to timely tax information, which is critical in promoting voluntary tax compliance.

The ESP legislation had a dramatic impact on our telephone program, resulting in more than twice the number of toll-free calls in the January - June period of 2008 than in 2007 (118 million versus 57 million). Automated Calls and Web Services more than doubled from last year's volumes while Assistor Calls Answered increased by 26 percent. The IRS.gov website proved to be a valuable resource to taxpayers, reflecting a 24 percent increase in "Where's my Refund" inquiries, while our new "Where's my Rebate" tool experienced 37 million completed inquiries.

Prior to the passage of the ESP, Accounts Management was on target to meet or exceed all toll-free performance goals. Despite careful planning and aggressive mitigation strategies, the extraordinarily high call demand experienced did have an impact on our ability to deliver volume driven measures such as Customer Service Representative Level of Service (CSR LOS) and Average Speed of Answer (ASA). The CSR LOS achieved through the April 15 filing deadline was 77 percent but began to decline to a January - June cumulative rate of 57 percent as taxpayers called in historically high numbers (12M calls in one week). The majority of whom wanted to know when they would receive their rebate. We did, however, exceed our goals in our other strategic performance measures including Calls Answered, Services Provided, Automated Services Provided, Customer Contacts Resolved and Self Assistance



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Participation Rate. Also noteworthy is that despite the challenges we faced this year, we have continued our high performance in the accuracy of our responses to our toll-free customers. We exceeded our goals and achieved tax law and account call accuracy rates of 90.3 percent and 93.5 percent, respectively.

Walk-In Assistance - During the Fiscal Year (FY) 2008 filing season, the IRS continued to provide services at all 401 Taxpayer Assistance Centers (TACs). We continued to implement Contact Recording at 188 of the 401 TACs to better measure the accuracy of tax law and account assistance. Contact Recording is targeted to be operational at 306 sites by the end of FY 2009. For the FY 2008 filing season, IRS implemented a new tax law decision support tool called the Interactive Tax Law Assistant (ITLA). This new tool builds the probes and responses in a logical fashion so that the same tax law information would be provided to taxpayers regardless of delivery method and thus enhances the accuracy of the answers. This year, TACs achieved an 85 percent tax law accuracy rate. We expect tax law accuracy to improve for the FY 2009 filing season as walk-in staff gain experience with using ITLA. In addition, the TACs' provided assistance with ESP, which contributed to an increase in the volume of contacts at the TACs from February 15, 2008, through May 31, 2008 compared to the same period in 2007. The Stimulus contacts through May 31, 2008 totaled 289,000.

Volunteer Assistance - During the FY 2008 filing season, approximately 78,843 IRS-supported volunteers in 11,840 locations provided assistance to traditionally underserved populations. These include individuals with low income, the elderly, the disabled, and those with limited-English proficiency. The Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) volunteers prepared over 3.5 million returns, an increase of 33.2 percent over the prior year. We equate this large increase to the ESP legislation, as many taxpayers who normally did not have a filing requirement filed returns to receive their payment. Excluding ESP returns, we estimate the increase to be 14.2 percent.

We continue to see steady improvement in the accuracy of returns prepared by our volunteers. While results obtained from specialized IRS and Treasury Inspector General for Tax Administration (TIGTA) reviews provided an indication of the IRS volunteer sites' performance, the IRS also conducted approximately 963 return reviews at 337 volunteer sites nationwide. The results of these reviews provide key information to base-line improvement goals and strategies for the filing season ahead. In order to assist with the determination of volunteer accuracy, Stakeholder Partnerships, Education and Communication (SPEC) has established an FY 2009 Centralized Volunteer Return Reviewer Cadre. Centralized management of a dedicated group of reviewers will provide SPEC with consistent, reliable measures of accuracy. This information will be analyzed by way of quality improvement principles. It will be used to formulate improvement opportunities during FY 2010.



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**Appendix I: Comments from the Internal Revenue Service**

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In addition to return preparation, IRS volunteer partners provided a significant service in educating taxpayers of their tax obligations and available benefits, such as the Earned Income Tax Credit (EITC) and ESP. More than 650 million outreach contacts were made during 2008. These contacts included 219 million messages about the ESP through both media and non-media channels. These strategic partnerships with volunteer organizations leverage IRS resources and allow the IRS to reach far more taxpayers through trusted local community sources.

Website - The IRS website, IRS.gov, is consistently one of the most heavily used government web sites. As of November 8, 2008, the website has been visited more than 332 million times, a 65.9 percent increase over 2007. These visits resulted in more than 2 billion page views, an almost 67.3 percent increase over 2007. Visits are the measurement of actions beginning when a visitor views their first web page on IRS.gov and ends when the visitor leaves the website. Taxpayers and practitioners also downloaded more than 154 million forms, publications, instructions, and other documents.

We agree the two Matters for Congressional Consideration noted in your report have merit and could further increase compliance and improve taxpayer service.

Responses to your specific recommendations are enclosed. I appreciate your observations on the successful filing season for 2008, and if you have any questions, please contact Floyd Williams, Director, Legislative Affairs, at (202) 622-3720.

Sincerely,



Linda E. Stiff

Enclosure

Enclosure

Recommendation

Use IRS's existing MEA to identify and correct child and dependent care credit claims on "Married Filing Separately" returns.

Comment

We agree with this recommendation and will submit a Universal Work Request (UWR) by December 31, 2008, to implement programming by January 2010; however, implementation of the programming is contingent on Modernization & Information Technology Services (MITS) UWR priorities and funding.

Recommendation

Include information on math error notices to inform taxpayers that they may be eligible for the child and dependent care credit if they file under a different status, such as "Single", "Married Filing Jointly", "Head of Household", or "Qualifying Widow(er) with a dependent child".

Comment

We agree with this recommendation and will submit a UWR by December 31, 2008, to implement programming by January 2010; however, implementation of the programming is contingent on MITS UWR priorities and funding.

Recommendation

Assess the effectiveness of combining FCR and other data on taxpayer characteristics to verify the eligibility of EITC claims from non-custodial parents.

Comment

We agree with this recommendation. The IRS already plans to study the reliability of non-custodial information in the Federal Case Registry (FCR). We will add a review of the possibility of developing methods to further refine the selection process before applying math error authority based on the FCR. Our goal will be to ensure that, if the IRS implements this Math Error Authority (MEA), it will apply only to those taxpayers who are not eligible for the Earned Income Tax Credit.

# Appendix II: Key Dates and Activities of the 2008 Filing Season

**Figure 2: Timeline for the 2008 Filing Season**

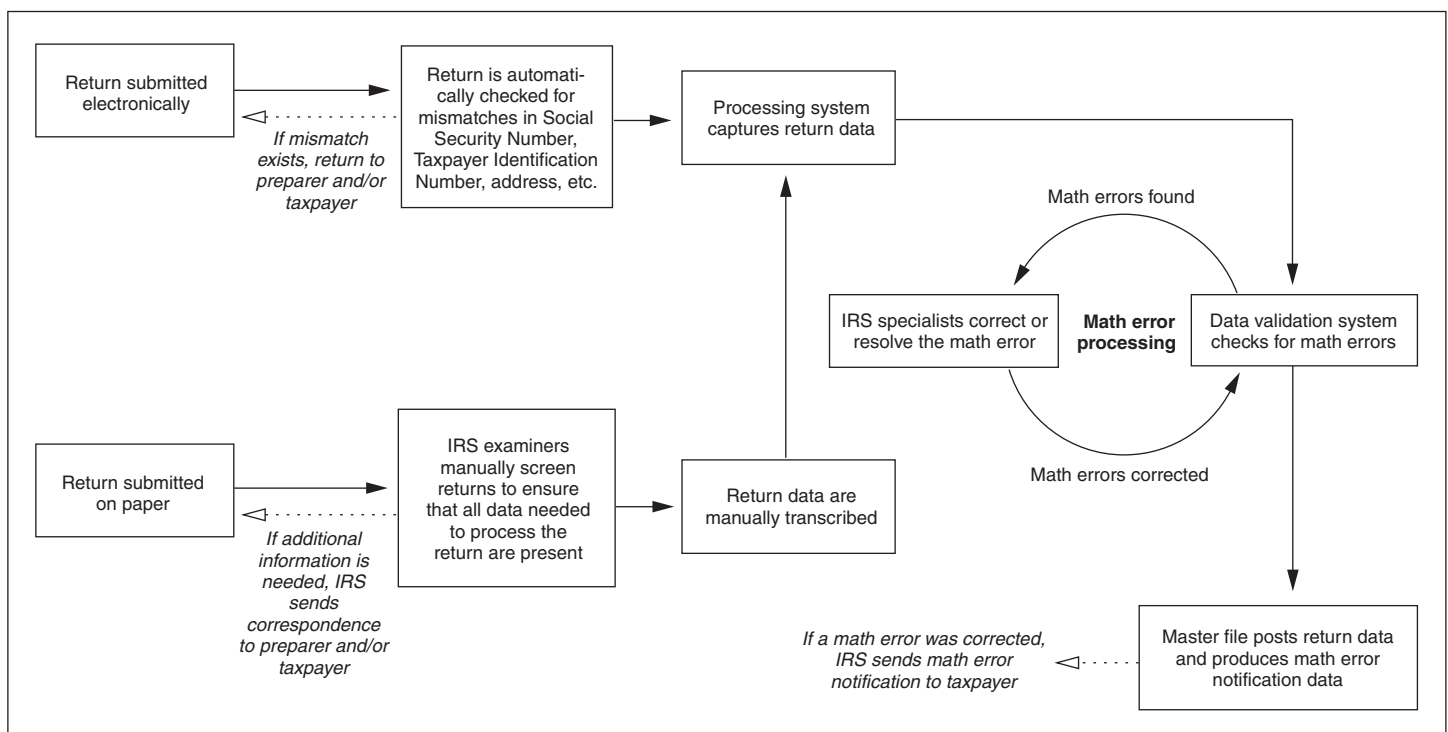
<b>2007 Dec.</b>	12/20: The Congress passes Alternative Minimum Tax (AMT) patch.
<b>2008 Jan.</b>	1/1: Filing season begins for most individual filers.
<b>2008 Feb.</b>	2/11: IRS begins accepting returns affected by the AMT patch on schedule. 2/13: The President signs the Economic Stimulus Act of 2008, which authorizes \$202 million in supplemental appropriations for Internal Revenue Service (IRS). IRS expands content on its Web site to include stimulus features and information. 2/18: IRS changes the recorded message on the toll-free phone line to include economic stimulus information.
<b>2008 March</b>	3/1: Automated Collection System (ACS) employees are trained to answer stimulus calls. 3/3: ACS staff starts answering Economic Stimulus Package (ESP) related calls. 3/4: IRS sends the first ESP notice to the 132.9 million taxpayers who filed a tax return in 2006 at a cost of an estimated \$45 million. 3/14: IRS activates the Rebate Hotline, opens electronic-file and Free-file for stimulus returns, and adds an economic stimulus calculator to the Web site. IRS does a second mailing to the 20 million recipients of social security and veterans benefits not required to file a 2007 tax return. 3/29: IRS hosts partner-assisted Super Saturday activities to inform eligible taxpayers about the stimulus at nearly 700 sites in all 50 states and the District of Columbia.
<b>2008 April</b>	4/15: Filing deadline for individual returns. 4/26: The level of service on IRS's toll-free calls starts to decline, bottoming at 31 percent of callers actually reaching an assistor. 4/28: IRS begins transmitting direct deposit economic stimulus payments a week ahead of the posted schedule. 4/28 - 7/11: IRS mails a notice in conjunction with the payments to all confirmed recipients of the stimulus explaining the calculation, amount, and delivery date of their payment.
<b>2008 May</b>	5/9: IRS receives 1.69 million calls to the Rebate Hotline, the highest call volume for a single day. 5/17: IRS receives 12 million calls to its telephone lines. This is the highest weekly volume IRS has ever experienced.
<b>2008 July</b>	7/11: Last batch of ESP paper checks sent out to those who filed by April 15. 7/14: IRS awards contract to conduct a lessons learned study. 7/18-31: IRS sends a third notice—at a cost of around \$2 million—to target the estimated 5 million Social Security Administration and Veterans' Administration recipients who have yet to file for their stimulus payment.

Source: GAO analysis of IRS data.

# Appendix III: Using IRS's Math Error Authority to Process and Correct Returns with Math Errors

In the math error program, IRS uses computer programmed comparisons and calculations to systemically identify math errors during tax return processing (see fig. 3) for correction. These corrections involve mathematical calculation errors, incorrect taxpayer identification numbers, filing status and dependents, and missing schedules or forms. Once the computer programming detects an error, it forwards the tax return account to the Error Resolution System, where an IRS employee takes the appropriate action to resolve the error condition and provide the information needed to generate a notice to the taxpayer.

**Figure 3: Processing and Correcting Returns with Math Errors**



Source: GAO analysis of IRS information.

As early as the first codification of the Internal Revenue law in 1926, the Congress granted IRS math error authority (MEA) so that IRS does not have to provide the taxpayer with a statutory notice of deficiency for math errors. In general, these are errors that must be corrected in order for IRS to process the tax return. A 1976 statutory revision defined the authority to include not only mathematical errors, but other obvious errors such as omissions of data needed to substantiate an item on a return, and provided

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**Appendix III: Using IRS's Math Error  
Authority to Process and Correct Returns  
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a statutory right to file a request for abatement of the assessment within 60 days after the notice is sent. In the 1990s, the Congress extended the authority five times to help determine eligibility for certain tax exemptions and credits. Table 7 summarizes the legislative authority on math error provisions for individual tax returns.

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**Table 7: Math Error Provisions**

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(1)	An error in addition, subtraction, multiplication, or division shown on any return
(2)	An incorrect use of any table provided by IRS with respect to any return if other information in the return makes the incorrect use apparent
(3)	An entry on a return of an item that is inconsistent with another entry of the same or different item on that return
(4)	An omission of information that is required to be supplied on the return to substantiate an entry on that return
(5)	An entry on a return of a deduction or credit in an amount that exceeds the statutory limit for that deduction or credit, if that limit is expressed as a specific monetary amount or as a percentage, ratio, or fraction, and if the component items of that limit appear on the return.
(6)	A correct Taxpayer Identification Number (TIN) not provided on the return as required for the <ul style="list-style-type: none"><li>• Earned Income Tax Credit (EITC),</li><li>• child and dependent care credit,</li><li>• personal or dependent exemption,</li><li>• child tax credit, or</li><li>• Hope and Lifetime Learning credits.</li></ul>
(7)	A return claiming an EITC for net earnings from self-employment, where the self employment tax imposed by IRC § 1401 on those net earnings has not been paid.
(8)	An omission of information required for recertification of eligibility for the EITC.
(9)	An entry on the return of a TIN required for the EITC, the child credit, and the child and dependent care credit, when information associated with that TIN indicates the child does not meet the age eligibility requirements for those credits.
(10)	An entry on the return of a claim for the EITC where the Federal Case Registry of Child Support Orders indicates that the taxpayer is the noncustodial parent of that child.
(11)	A failure to reduce ESP credit on a return related to the Economic Stimulus Act of 2008 by amounts previously advanced.

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Source: GAO analysis.

# Appendix IV: IRS's Processing Performance Relative to 2004-2008 Performance and 2008 Goals

Despite the added individual return volume due to the Economic Stimulus legislation, as of June 30, 2008, IRS met or exceeded seven out of the eight processing performance goals. As shown in table 8, IRS met or exceeded its goals for the percentage of errors included in deposits and correspondence (which was separated into letter and notice errors in previous years); deposit and refund timeliness (i.e., interest foregone by untimely deposits); and productivity and Individual Master File efficiency.

The one measure where performance was below IRS's goal and last year's level was the refund error rate, i.e., the percentage of refunds with IRS-cause errors issued to taxpayers by IRS. According to IRS officials, the increase in the refund error rate is attributed to a programming change that resulted in IRS catching, for example, changes of address or name changes, as it began transcribing data from paper returns. According to IRS officials, because the changes did not result in significant additional transcription, the increased error rate did not result in a delay of refunds or a delay in processing of returns.

**Table 8: IRS Processing Performance, Fiscal Years 2004-2008**

Measure name	Definition	Fiscal year 2004 actual	Fiscal year 2005 actual	Fiscal year 2006 actual	Fiscal year 2007 actual	Fiscal year 2008 actual (through June)	Fiscal year 2008 goal
Deposit error rate	Percentage of payments applied in error by, for example, reimbursing a taxpayer who overpaid when the taxpayer wanted the overpayment credited to next year's tax bill.	3.5% (+/- .31%)	2.2% (+/- .26%)	1.6% (+/- .24%)	1.3% (+/- .22%)	1.1% (+/- .27%)	1.3%
Deposit timeliness— paper- Individual Masterfile	Interest foregone by not depositing monies the business day after receipt, per \$1 million in deposits. Measure assumes an 8 percent interest rate	\$407	\$390	\$354	\$331	\$306	\$320
Correspondence error rate <sup>a</sup> (includes systemic errors) <sup>b</sup>	The percentage of incorrect processing Masterfile notices and letters issued to taxpayers by the processing SP sites.	n/a	n/a	n/a	4.3	3.9% (+/- .36%)	4.3%

**Appendix IV: IRS's Processing Performance  
Relative to 2004-2008 Performance and 2008  
Goals**

Measure name	Definition	Fiscal year 2004 actual	Fiscal year 2005 actual	Fiscal year 2006 actual	Fiscal year 2007 actual	Fiscal year 2008 actual (through June)	Fiscal year 2008 goal
Refund error rate— individual (paper) (includes systemic errors)	Percentage of refunds with IRS-caused errors in the entity information (e.g., incorrect name, Social Security number, or refund amount); includes systemic errors	4.9% (+/- .44%)	5.0% (+/- .48%)	4.5% (+/- .46%)	2.8% (+/- .36%)	3.6% (+/- .52%)	2.7%
Refund interest paid	Amount of refund interest IRS paid per \$1 million of refunds issued.	\$20.55	\$29.21	\$30.12	\$39.60	\$27.29	\$38.00
Refund timeliness— individual (paper)	Percentage of refunds issued within 40 days or less.	98.3% (+/- .17%)	99.2% (+/- .18%)	99.3% (+/- .13%)	98.9% (+/- .19%)	99.2% (+/- .19%)	98.4%
Productivity	Weighted volume of documents processed per staff year expended at the processing centers.	30,405	31,444	32,237	34,313	37,764	36,083
Individual Master File efficiency	Measure of Individual Master File returns processed per staff year expended.	n/a	14,965	19,526	22,031	25,327	23,370

Source: GAO analysis of IRS data.

<sup>a</sup>The Correspondence Error Rate is a weighted combination of the results of the previously used Letter and Notice Error Rate Measures. The weights are based on the actual volumes of letters and notices (as reported in Letter and Notice weighted reports).

<sup>b</sup>Systemic errors are computer-generated errors over which a particular processing center would have no control.

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