



*Opportunities Exist to Help Seniors and Many
Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

May 31, 2007

Reference Number: 2007-30-075

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

Redaction Legend:

1 = Tax Return/Return Information

Phone Number | 202-927-7037

Email Address | Bonnie.Heald@tigta.treas.gov

Web Site | <http://www.tigta.gov>



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

May 31, 2007

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

FROM:

Michael R. Phillips

Michael R. Phillips

Deputy Inspector General for Audit

SUBJECT:

Final Audit Report – Opportunities Exist to Help Seniors and Many Other Taxpayers That Repeatedly Make Mistakes on Their Individual Income Tax Returns (Audit # 200630004)

This report presents the results of our review of repetitive math error notices received by taxpayers. The overall objectives of this review were to identify taxpayers that have repeatedly received the same math error notices and to determine whether the Internal Revenue Service (IRS) could better address the issues causing these notices.

Impact on the Taxpayer

Many taxpayers that are age 65 or over (seniors), taxpayers that have claimed the Earned Income Credit (EIC), and taxpayers that have computed self-employment tax have received repetitive math error notices (i.e., the taxpayers had received a notice addressing the same issue in the prior year). This condition may indicate that taxpayers do not understand or are repeatedly overlooking specific instructions provided by the IRS; taxpayers do not understand an area of tax law; or the current filing information available to the taxpayers, including notices, is inadequate. Notices should not only inform taxpayers of their errors but should also educate them on the issues, and be a means to ensure the errors do not occur in the future. Unclear or inadequate tax information and notices create additional burden on taxpayers and often result in additional work and expense for the IRS.



Opportunities Exist to Help Seniors and Many Other Taxpayers That Repeatedly Make Mistakes on Their Individual Income Tax Returns

Synopsis

Annually, the IRS sends over 100 million notices to taxpayers; the IRS estimates this costs more than \$400 million.¹ More than 7 million of these notices are math error notices, which inform taxpayers that changes were made to their tax returns as a result of mathematical or clerical errors. The notices explain the nature of the changes and include account statements showing how the changes affect the returns. Overall, the vast majority of taxpayers receiving these notices do not repeat their errors in subsequent years. Further, very few business taxpayers received repeat math error notices. The notices with a higher repeat rate were those sent to individual taxpayers and were related to just a few areas of tax law. Only 5 notices accounted for 40 percent of all repetitive math error notices issued to individual taxpayers, despite being only 13 percent of the total number issued.

Senior taxpayers repeatedly made two errors when computing their taxes: (1) miscomputing their taxable amounts of social security benefits and (2) claiming an incorrect standard deduction. Random nonstatistical samples of 80 senior taxpayers making 1 of these 2 errors showed that 95 percent had prepared their own returns. The average age of these taxpayers was 72, and 24 percent of them were 80 years of age or older.

Also, taxpayers repeatedly made two errors related to the EIC. Most of these taxpayers made calculation errors, and others inappropriately claimed the EIC after having been prohibited from doing so and not recertifying that they were qualified for the EIC. Taxpayers making the repetitive calculation errors had either (1) used the EIC Tables incorrectly year after year or (2) filed a Profit or Loss From Business (Schedule C) but, for 2 years or 3 years in a row, had failed to deduct one-half of their self-employment tax from the earned income amounts before computing the EIC. The issue regarding recertification for the EIC has been reported in prior Treasury Inspector General for Tax Administration audit reports; therefore, we made no recommendations concerning the issue in this report.

Taxpayers also made repetitive errors when computing or reporting their self-employment tax. Many of the taxpayers in our sample calculated the self-employment tax correctly but repeatedly carried the wrong amounts forward to their U.S. Individual Income Tax Returns (Form 1040). Other taxpayers calculated the self-employment tax incorrectly. A common cause was the taxpayers did not begin the computation by multiplying the self-employment earnings by 92.35 percent, as instructed.

¹ Based on a 2001 IRS estimate.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Recommendations

We recommended the Director, Customer Account Services, Wage and Investment (W&I) Division, modify the math error notices that have been sent repeatedly to taxpayers, to provide a clearer and more informative explanation of the errors taxpayers are making. In addition, the Director, Tax Forms and Publications, W&I Division, should make changes to the forms and instructions associated with the provisions that have resulted in issuance of an inordinate number of repetitive notices, including the addition of CAUTION symbols to mark portions of the tax form instructions that appear to be overlooked or misunderstood. Finally, the Commissioner, W&I Division, should continue to build on the research and analysis already performed to develop the most effective ways to simplify tax preparation for senior taxpayers.

Response

The Commissioner, W&I Division, partially agreed with three of our recommendations and disagreed with four recommendations. The Commissioner, W&I Division, agreed that the math error notice related to the computation of the taxable amount of social security benefit should be modified. The Commissioner, W&I Division, also agreed that research should be performed on the senior taxpayer population to identify ways to simplify tax preparation for seniors and plans to include such research in the Taxpayer Assistance Blueprint Research Plan which is currently under development. To address the EIC issues, the Commissioner agreed to bold the filing status headings at the top of the EIC Tables and will perform additional analysis of errors made computing EIC to determine the causes and implement solutions. However, the Commissioner, W&I Division, believes it is impractical to address in a notice all of the possible reasons taxpayers made the errors in the repetitive notices we identified. The Commissioner, W&I Division, also believes CAUTION symbols should be used judiciously and only for major issues, and also added that the IRS has no data to substantiate whether using such symbols changes taxpayer behavior or reduces these types of errors. The other changes we recommended to improve tax form instructions were also rejected. Management's complete response to the draft report is included as Appendix V.

Office of Audit Comment

We believe the IRS has overlooked opportunities to educate and inform taxpayers, reduce taxpayer burden, and simplify the filing process. This report identifies specific groups of taxpayers, particularly senior taxpayers, making specific errors. Knowing the types of errors taxpayers make on a recurring basis provides the IRS with a prime opportunity to help taxpayers avoid making the same error in the future. We agree that CAUTION symbols should be used judiciously and for major tax issues, but we believe that taxpayers repeatedly making specific errors regarding the taxability of social security income and calculation of EIC or



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

self-employment tax are issues of much greater magnitude than many of those currently receiving CAUTIONs. While there is a sizeable body of outside data available on the use of “warnings,” which indicates that warnings, when used correctly, have a strong role in effecting people’s behavior, we believe that if the IRS has questions regarding the effectiveness of these warnings, it has a responsibility to gather data for itself regarding the effectiveness of CAUTIONs as well as the other changes to notices and instructions discussed in this report.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-5894.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Table of Contents

Background	Page 1
Results of Review	Page 4
Many Senior Taxpayers Repeatedly Made Errors When Computing the Taxable Amount of Social Security Benefits and Determining Their Standard Deduction.....	Page 4
<u>Recommendation 1:</u>	Page 9
<u>Recommendation 2:</u>	Page 10
<u>Recommendation 3:</u>	Page 11
Taxpayers Claiming the Earned Income Credit Repeatedly Made Two Types of Errors	Page 12
<u>Recommendation 4:</u>	Page 16
<u>Recommendation 5:</u>	Page 17
Taxpayers Made Repetitive Errors When Computing and Reporting Their Self-Employment Tax	Page 17
<u>Recommendations 6 and 7:</u>	Page 19
Appendices	
Appendix I – Detailed Objectives, Scope, and Methodology.....	Page 21
Appendix II – Major Contributors to This Report	Page 23
Appendix III – Report Distribution List	Page 24
Appendix IV – Math Error Notices Reviewed	Page 25
Appendix V – Management’s Response to the Draft Report	Page 31



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Abbreviations

EIC	Earned Income Credit
IRS	Internal Revenue Service
ITIN	Individual Taxpayer Identification Number
SSN	Social Security Number
TIGTA	Treasury Inspector General for Tax Administration
W&I	Wage and Investment



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Background

The Internal Revenue Service's (IRS) mission is to provide America's taxpayers with top-quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all. Notices informing taxpayers of errors, tax law, and appropriate methods of filing are essential to achievement of the mission. The IRS has a responsibility to fulfill its mission efficiently and cost effectively. As stated in a 2001 Treasury Inspector General for Tax Administration (TIGTA) report,¹ the IRS estimates its notice operations cost \$472 million annually, with about 60 percent of these costs attributable to the downstream impact of issued notices (i.e., handling subsequent correspondence, telephone calls, and remittances from taxpayers). Annually, the IRS sends more than 100 million notices to taxpayers, including more than 7 million math error notices.

The IRS sends math error notices to taxpayers informing them that changes were made to their tax returns as a result of mathematical or clerical errors made on their returns. These notices explain the nature of the changes and include account statements showing how the changes affect the returns. Math error notices, and the ability to simply correct certain errors made by taxpayers, originated out of the recognition that some errors on tax returns did not justify the expense of an audit. Congress authorized the IRS to correct certain math errors that appeared on the face of a tax return without opening an audit on the taxpayer.

Issuance of repetitive math error notices may be an indicator that taxpayers do not understand or are repeatedly overlooking specific instructions provided by the IRS; taxpayers do not understand an area of tax law; taxpayers require additional education on a particular tax law or filing requirement; or the current filing information available to the taxpayer, including the notices, is inadequate. Notices should not only inform taxpayers of their errors but should educate them on the issues, and be a means to ensure the errors do not occur in the future. Unclear or inadequate tax information and notices create an additional burden on taxpayers and often result in additional work and expense for the IRS.

Notices should not only inform taxpayers of their errors but should educate them on the issues and be a means to ensure the errors do not occur in the future.

During this audit, we computer identified taxpayers filing Employer's Quarterly Federal Tax Returns (Form 941), U.S. Corporation Income Tax Returns (Form 1120), and U.S. Individual Income Tax Returns (Form 1040 series) that had repeatedly received the same math error notices for Tax Years 2002 - 2004 returns.

¹ *Increased Management Attention Is Needed to Ensure the Success of Future Notice Redesign Efforts* (Reference Number 2002-30-040, dated December 2001).



Opportunities Exist to Help Seniors and Many Other Taxpayers That Repeatedly Make Mistakes on Their Individual Income Tax Returns

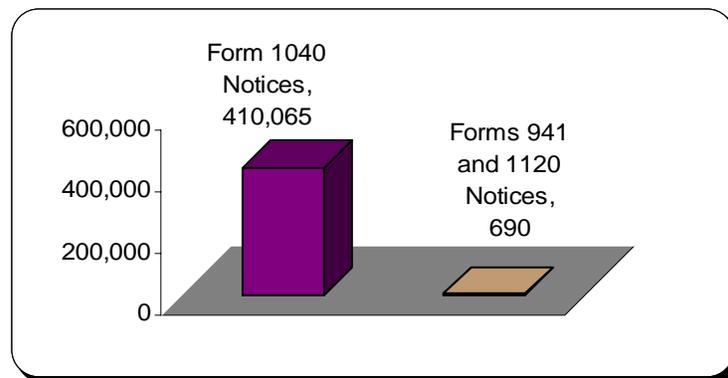
Overall, the vast majority of taxpayers receiving these notices do not repeat their errors in subsequent years. Further, very few business taxpayers received repeat math error notices. The notices with a higher repeat rate were those sent to individual taxpayers and were related to just a few areas of tax law.

Our review of all math error notices issued to Forms 941 and 1120 filers showed the IRS had sent 155,644 notices for Tax Years 2002 - 2004. We estimate only 690 notices (.44 percent) were repetitive. Due to the minimal number of taxpayers affected and the low percentage of notices sent to taxpayers on a repeated basis, we did not perform any additional analysis on the math error notices associated with Forms 941 or 1120.

We found that significantly more taxpayers filing a Form 1040 series return had received repeat notices. Because of the higher numbers, we focused on 35 math error notices that either had high volumes or addressed errors we considered to be significant to taxpayers. See Appendix IV for a list of the math error notices included in our review.

The IRS sent more than 12.5 million math error notices to individual taxpayers for Tax Years 2002 - 2004. Of those, an estimated 410,065 notices (3.2 percent), affecting 327,044 taxpayers, were repetitive notices (i.e., the taxpayers had received a notice addressing the same issue in the prior year). Further review of these notices indicated that only 5 notices accounted for 40 percent of all repetitive math error notices issued, despite being only 13 percent of the total number issued.

Figure 1: Repetitive Notice Volumes (Tax Years 2002 - 2004)



Source: TIGTA computer extracts.

This audit was performed at the IRS Campus² in Ogden, Utah, and included reviews of tax returns filed nationwide. It also included discussions with employees from the Tax Forms and Publications, Submission Processing, Strategy and Finance, Earned Income Tax Credit Strategic

² Campuses are 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.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Operations, and Notice Gatekeeper functions in the IRS Wage and Investment (W&I) Division. The audit was performed during the period October 2005 through November 2006 in accordance with *Government Auditing Standards*. Detailed information on our audit objectives, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Results of Review

Many Senior Taxpayers Repeatedly Made Errors When Computing the Taxable Amount of Social Security Benefits and Determining Their Standard Deduction

Some Federal tax law provisions have been passed specifically to benefit senior taxpayers. They include an increased standard deduction, credits for the elderly, and a higher gross income threshold for filing. Other tax provisions become applicable as taxpayers grow older and affect their social security benefits, retirement plan distributions, pensions and annuities, and medical expenses. The IRS must ensure these taxpayers fully understand the tax provisions that affect them and how to report and comply with these provisions.

Two tax provisions affecting senior taxpayers had been inappropriately applied by a large number of taxpayers on a repeated basis. They include computation of the taxable amount of social security benefits and the determination of the appropriate standard deduction.

Taxpayers made errors in calculating the taxable amount of Social Security benefits

When a taxpayer makes an error computing his or her taxable amount of social security benefits, the IRS corrects the mistake and sends the taxpayer a math error notice that reads:

“We changed the amount of social security benefits on page 1 of your tax return because there was an error in the computation of the taxable amount.”

For Tax Year 2004, the IRS sent 196,709 notices to senior taxpayers explaining that they had miscomputed their taxable amounts of social security benefits. More than 34,000 (17 percent) of these taxpayers were receiving this notice for the second time; we estimate more than 10,000 taxpayers were receiving it for a third time.³

Our review of a sample of 40 taxpayers that had received the notice in multiple years revealed the following:

- The average age of these taxpayers in 2003 was 71 (25 percent of the taxpayers were 80 years of age or older).

³ We had to estimate the number of taxpayers receiving some of the notices for the third year, based on random nonstatistical samples because different numbers were assigned to the notices used to address the errors; therefore, our computer programs did not identify the notice as a repeat notice in the third year.



***Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns***

- Ninety percent (36 of 40) had prepared their own tax returns.
- Fifty-three percent (21 of 40) had reported their social security benefits as partially taxable but had calculated the taxable amount incorrectly 2 years or 3 years in a row [REDACTED]
- Thirty percent (12 of 40) had incorrectly claimed all or none of their social security benefits as taxable for 2 years or 3 years in a row [REDACTED]
- The remaining 7 taxpayers [REDACTED] had made a combination of the errors listed above.

Taxpayers made errors in calculating the allowable standard deduction

Taxpayers who are age 65 or older and/or are blind qualify for a higher standard deduction. When taxpayers qualify for but do not claim the higher amount, the IRS automatically corrects their returns and issues them a notice stating:

“We changed the amount claimed as standard deduction on page 2 of your tax return. You are entitled to a higher standard deduction if you and/or your spouse are age 65 or older and/or blind.”

The number of senior taxpayers that claimed the incorrect amount of standard deduction during Tax Year 2004 totaled 101,579. More than 16,000 of these taxpayers (16 percent) were receiving this notice for the second time; we estimate more than 4,400 were receiving it for a third time.

Our review of a sample of 40 taxpayers that had received the notice in multiple years revealed the following:

- The average age of these taxpayers in 2003 was 74 (23 percent of the taxpayers were 80 years of age or older).
- All (40 of 40) had prepared their own tax returns.
- Eighty-five percent (34 of 40) had claimed the ordinary amount of standard deduction for their particular filing status (Single or Married Filing Jointly) 2 years or 3 years in a row.

- [REDACTED]

Complexity of the tax law associated with computing the taxable amount of social security benefits and calculating the correct standard deduction appears to be the cause of many errors,



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

particularly when taxpayers prepare their own returns. In discussions with IRS employees, they stated that they have made attempts to simplify the worksheet used to compute the taxable portion of social security benefits. However, the computation remains complex and the repetitive errors by taxpayers indicate these areas may need additional attention by the IRS.

To assess the potential causes for these repetitive errors and to determine if the IRS could realistically do more to reduce these repetitive errors, we reviewed the forms, instructions, and notices associated with the provisions and found that improvements could be made. We also found that extensive consideration has been given to simplifying tax preparation for senior taxpayers, but more action needs to be taken.

Improvements to math error notices can be made

The math error notice sent to taxpayers explaining that an error was made on their taxable amount of social security does not correctly explain the action taken by the IRS and could cause some confusion. It reads,

“We changed the amount of social security benefits on page 1 of your tax return because there was an error in the computation of the taxable amount.”

Actually, the error that occurred in the computation will have no bearing on the taxpayer’s social security benefits, as stated in the notice. Only the amount computed as taxable social security benefits will be changed. We recognize that the wording of this notice may not be the cause of repetitive errors made by taxpayers, but it should be changed nonetheless.

The math error notice sent to senior taxpayers qualifying for a larger standard deduction is brief and clearly explains what the error was. It reads,

“We changed the amount claimed as standard deduction on page 2 of your tax return. You are entitled to a higher standard deduction if you and/or your spouse are age 65 or older and/or blind.”

However, additional wording could be used to better inform and educate taxpayers, to help them avoid the error in the future. For example, including a comparison of the standard deduction available to senior taxpayers with the common standard deduction may help senior taxpayers more clearly understand and remember that a higher standard deduction is available.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Improvements to forms and instructions can be made

The computation to determine the tax on social security benefits is fairly complicated, especially for taxpayers that are not well versed in tax law. Senior taxpayers that prepare their own returns each year need to be clearly informed of the IRS programs and customer assistance that is available to them beyond written publications, such as toll-free telephone assistance and Tax Counseling for the Elderly. This should help reduce the errors made by senior taxpayers and reduce the burden on them.

In addition, the forms and instructions designed to ensure senior taxpayers receive the proper amount of standard deduction could be improved. From the returns in our samples, it was clear that some taxpayers were not following the instructions and may not have been sure they were entitled to a higher standard deduction. Neither the Form 1040 nor the Form 1040 Instructions specifically explains that, if a taxpayer or his or her spouse is age 65 or older (or born before a specific year), he or she is entitled to a higher standard deduction. The wording used on the Form 1040 explains that calculation of the standard deduction is based on the box(es) checked on certain lines.

On Form 1040, taxpayers are instructed to check boxes if they (spouse included) are blind and/or were born before a specific date. Then they are instructed to “see left margin” of the Form 1040, where there is a box containing guidance for the standard deduction. That guidance directs taxpayers who checked boxes to turn to a page in the Form 1040 Instructions; however, the guidance in the left margin of Form 1040 also lists the standard deduction amounts for all other taxpayers. It is these amounts that the senior taxpayers in our samples almost always used as their standard deduction amounts.

The multi-action method that must be used by seniors to determine their allowable standard deduction (in which senior taxpayers check boxes then go to additional instructions) is confusing because some taxpayers do not realize they are entitled to a higher standard deduction due to their age.

Efforts to simplify tax return preparation have been considered

The IRS has recently considered actions to address the additional tax complexities faced by senior taxpayers. However, the actions considered were not implemented. In January 2004, the IRS Commissioner and a former Deputy Commissioner requested that the IRS consider and research methods of simplifying the tax-preparation process for senior taxpayers. This included considering the development of a new tax form.

Later that year, the House of Representatives introduced H.R. 4109, the Simple Tax for Seniors Act. The bill would have required the IRS to offer a simplified tax form for individuals age 65 and older. The form would have been designated Form 1040S and would have been similar to the Income Tax Return for Single and Joint Filers With No Dependents (Form 1040EZ). The form was intended to be available for senior taxpayers regardless of their receipt of social



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

security benefits or any distributions from retirement plans, their receipt of interest and dividends, the amount of their capital gains and losses, and their taxable income. The bill passed the House of Representatives under suspension of the rules by a vote of 418-0 on June 2, 2004. The Senate, however, did not act on the bill.

The IRS conducted research to determine the viability of the Form 1040S and ultimately concluded the potential number of seniors (estimated by the IRS to be 10.8 million) who would benefit from a separate tax form would not justify the complexity and costs associated with the introduction of a fourth Form 1040 series tax form. The IRS estimated only 2.9 million of the 10.8 million seniors would prepare their own returns without the use of software.

While analyzing the feasibility of creating a new form, the IRS considered creating an additional schedule (Schedule O) that could be used to simplify tax provisions facing senior taxpayers. As this schedule was developed, however, its initial purpose (helping senior taxpayers) diminished, and development of a schedule that could reduce the overall complexity of Form 1040 became the focus. Development of Schedule O is currently an ongoing project, and its feasibility is still being determined. Benefiting senior taxpayers, however, is no longer its purpose.

To identify other areas where tax complexities could be reduced, Congress required the IRS Commissioner, in Section 4022 of the IRS Restructuring and Reform Act of 1998,⁴ to submit each year to both the House Ways and Means Committee and Senate Finance Committee a report with recommendations for reducing tax complexities by, among other things, considering common errors made by taxpayers in filling out their returns.

The two issues affecting senior taxpayers discussed above appear to qualify for this report. For example, the complexity of computing the taxable amount of social security benefits is causing a high rate of errors among senior taxpayers. As mentioned previously, 53 percent (21 of 40) had miscalculated the taxable amounts for 2 years or 3 years in row. A more simplified method to determine the taxable amount would decrease the burden on taxpayers and enable the IRS to save resources.

Also, determining the standard deduction for senior taxpayers is complex and is causing a high rate of errors. The Tax Year 2006 Standard Deduction Chart for People Who Were Born Before January 2, 1942, or Were Blind includes 12 possible choices based on the number of boxes checked and filing status. Due to the Chart's complexity, the IRS is unable to include the amount of standard deduction the senior taxpayer qualifies for on the Form 1040 itself and must require the taxpayer to obtain the amount from a chart in the Form 1040 Instructions.

IRS emphasis on simplifying tax issues affecting older taxpayers should remain important because a large portion of the taxpaying public is shifting into the senior taxpayer bracket. According to the U.S. Census Bureau, the number of persons age 65 and older is expected to

⁴ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

increase from approximately 35 million in 2000 to an estimated 71 million in 2030, and the number of persons age 80 and over is expected to increase from 9.3 million in 2000 to 19.5 million in 2030.

Recommendations

Recommendation 1: The Director, Customer Account Services, W&I Division, should:

- Correct the math error notice sent to taxpayers notifying them of an error made computing their taxable amount of social security benefit to explain the action actually taken by the IRS. Currently, the notice erroneously indicates the IRS changed the amount of social security benefits, rather than correctly explaining that it changed the taxable amount of social security benefits.
- Add information in both the repetitive notices affecting senior taxpayers that would better educate and inform senior taxpayers about the errors made. This could include the customer service assistance available to help them (e.g., toll-free telephone numbers, the Volunteer Income Tax Assistance Program, web sites, publications) and examples, such as a comparison of the standard deduction available to senior taxpayers with the common standard deduction, to help these taxpayers more clearly understand and remember that a higher standard deduction is available to them.

Management's Response: IRS management partially agreed with this recommendation. The Commissioner, W&I Division, agreed to correct the math error notice sent to taxpayers notifying them of an error made computing their taxable amount of social security benefit. The IRS plans to rewrite the notice to correctly state that the taxpayer made an error computing the “taxable amount of their social security benefit.”

The Commissioner, W&I Division, disagreed with the second portion of our recommendation, stating the IRS issues notices on a case-by-case basis rather than to particular groups of taxpayers such as seniors. However, to address this issue, Submission Processing will coordinate with the W&I Division Stakeholder Partnerships, Education, and Communication organization to develop and distribute a fact sheet of common errors made by seniors that can be disseminated to a variety of media sources.

Office of Audit Comment: We agree that distributing additional information for seniors through the media could be beneficial. However, providing senior taxpayers who are making specific errors with information that specifically addresses those errors would be the most effective. Knowing the types of taxpayers and the types of errors they are making provides the IRS with a direct and a prime opportunity to educate and inform them.

We recognize that the “IRS issues notices on a case-by-case basis rather than to particular groups of taxpayers such as seniors.” However, the vast majority of taxpayers that



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

receive the two notices addressed in our recommendation are sent to senior taxpayers. Seventy-five percent of our sample of taxpayers receiving repeat notices because their social security tax computation was incorrect were 65 years of age or older. Ninety-five percent of the taxpayers were over the age of 55. Also, the Social Security Administration, Office of the Actuary, indicated that as of the end of 2003, 71 percent of taxpayers receiving social security were age 65 or older. The notice sent to taxpayers informing them that an error was made would provide the IRS with a key opportunity to warn them of common errors made. For instance, a paragraph could be included in the notice stating, "If you are receiving this notice and are aged 65 or older, please be advised of the following common errors to avoid in the future." Then, simply state the common errors and provide them with the IRS help that is available.

In addition, due to the nature of the tax provision itself, almost all taxpayers receiving a notice informing them that they are entitled to a higher standard deduction will be aged 65 and older, providing the IRS with another prime opportunity to warn senior taxpayers of common errors. We recognize that some of these notices will be sent to blind taxpayers (many of which will be older than 65); however, the vast majority, and in the case of our audit sample, 100 percent, will be sent to taxpayers that are 65 or older.

Finally, based on our audit sample, the notices sent appear to adequately address the errors caused by taxpayers; however, they do nothing to explain why the error was made or what the taxpayers could do in the future to avoid making it again. Providing additional direction to the taxpayers to help them avoid the mistake in the future by stating that their standard deduction amount cannot be obtained from off the front of the Form 1040 and must be obtained within the instructions themselves, may not only help them avoid the mistake in the future but is fundamental to taxpayer education.

Recommendation 2: The Director, Tax Forms and Publications, W&I Division, should identify complicated tax law provisions affecting senior taxpayers and include specific references to the services that are available to them within those provisions' instructions and, where possible, on the tax form(s).

Management's Response: IRS management disagreed with this recommendation. The Commissioner, W&I Division, believes other outreach and communication channels focused on seniors would be more effective than placing specific references to services available to seniors throughout form instructions or on the forms themselves. The Commissioner, W&I Division, stated each page of the instructions for Form 1040 already includes a footnote that refers taxpayers that need more information or forms to a page in the instructions entitled "Quick and Easy Access to Tax Help and Forms." Also, *Older Americans' Tax Guide* (Publication 554) includes a section entitled, "How to Get Tax Help." Finally, additional information in the Form 1040 Instructions advises taxpayers of the services available to seniors through the Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Office of Audit Comment: We believe that a combination of efforts would best achieve the objective. Focusing on all seniors would be beneficial when specific problems cannot be identified. However, when specific problems can be pinpointed, those issues should be specifically addressed (i.e., senior taxpayers that commonly claim an incorrect amount of standard deduction as noted in our report).

Many of the examples cited in management's response are generic and apply to all taxpayers. Those that apply to seniors are either not noted in the Form 1040 Instructions or are very difficult to find. Publication 554 is never mentioned in the Form 1040 General Instructions and the section in the Form 1040 Instructions that advises seniors of the services available to them is difficult to identify in the 80-plus page document; it is listed on page 65 under the heading "General Information." Furthermore, reference to these instructions in the Index to Instruction is only found under the heading of "Free tax help" despite a heading in the Index entitled "Elderly persons."

We do not believe requiring seniors to order a technical publication or having an obscure paragraph that explains where seniors can go to obtain additional help is commensurate with a request made in 2004 by the IRS Commissioner and a former Deputy Commissioner that the IRS consider and research methods of simplifying the tax-preparation process for senior taxpayers. Nor do we believe the examples mentioned in the IRS' response that focus on seniors meets the spirit of the legislation passed by the House of Representatives that would have required the IRS to offer a simplified tax form for individuals age 65 and older.

Recommendation 3: The Commissioner, W&I Division, should work with the Tax Forms and Publications function and other pertinent functions to build on research and analysis already performed in determining the most effective ways to simplify tax preparation for senior taxpayers. In addition, tax complexities identified in this audit report should be elevated for inclusion in the IRS Commissioner's annual report on tax complexities to the House Ways and Means Committee and Senate Finance Committee.

Management's Response: IRS management partially agreed with this recommendation. The Commissioner, W&I Division, stated that the Taxpayer Assistance Blueprint Research Plan, which is currently under development, will include research on the senior population that will provide information to help identify the most effective ways to simplify tax preparation for seniors. However, the Commissioner, W&I Division, did not agree to elevate the tax complexities identified in this audit report to the annual report on tax complexities to the House Ways and Means Committee and Senate Finance Committee because he believes there are more effective ways of elevating the issues to Congress.

Office of Audit Comment: Despite the specific call for such a report in the IRS Restructuring and Reform Act of 1998, we are less concerned about the vehicle used to



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

elevate these complexity issues to Congress than we are with the fact that they should be raised. However, the IRS should identify a responsible official and determine a reasonable date by which these specific complexity issues will be raised.

Taxpayers Claiming the Earned Income Credit Repeatedly Made Two Types of Errors

Taxpayers claiming the Earned Income Credit (EIC) have repeatedly made errors in two areas: (1) computation of the EIC amount and (2) completion of the recertification process required for taxpayers who were prohibited from claiming the EIC after an IRS examination of their tax returns.

Taxpayers made errors in computing the EIC

The notice sent to taxpayers to inform them that they made an error when computing the EIC reads,

“We changed the amount claimed as Earned Income Credit (EIC) on your tax return. The amount claimed as EIC was figured or entered incorrectly on your tax return.”

For Tax Year 2004, the IRS sent 269,011 math error notices to taxpayers notifying them of a miscalculation of their EIC amounts. More than 44,000 taxpayers (16 percent) were receiving this notice for a second time; we estimate at least 18,797 were receiving it for a third time.

Our review of a sample of 40 taxpayers receiving this same error notice in multiple years revealed the following:

- Seventy percent (28 of 40) had prepared their own tax returns.
- Sixty-eight percent (27 of 40) had used the EIC Tables incorrectly to determine the amount of EIC for 2 years or 3 years in a row. Of these 27 taxpayers, 16 had used an incorrect filing status (6 of the 16 taxpayers had used paid preparers) on every return.
- Eighteen percent (7⁵ of 40) filed a Profit or Loss From Business (Schedule C) but had failed to deduct one-half of their self-employment tax from the earned income amounts before computing the EIC for 2 years or 3 years in a row.

We also reviewed the forms and instructions associated with the EIC tax law provision, to identify any potential causes for these repetitive taxpayer errors and to determine if changes could be made by the IRS.

⁵ These 7 taxpayers accounted for 35 percent of those in our sample that had filed a Schedule C.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Improvements to math error notices can be made

The wording of the notice that informs taxpayers that an error was made in the amount of EIC claimed is intentionally generic because, according to IRS instructions, it is to be used “when the taxpayer made a mistake computing the EIC amount and no other EIC notice applies.”

However, revising the notice to include information that warns taxpayers of common errors made may help them avoid the same mistakes in the future. Our review clearly showed that taxpayers commonly misread the EIC Table and Schedule C filers often forgot to deduct one-half of their self-employment tax from the earned income amount before computing the EIC.

Improvements to the EIC instructions and Table can be made

In the EIC Table, a high number of taxpayers have repeatedly had trouble differentiating between the column used by those with a Single, Head of Household, or Qualifying Widow(er) filing status and the column used by those with a Married Filing Jointly filing status. Therefore, we believe the format of the columns in the EIC Table should be revised. Currently, the columns are side by side with minimal separation (thin line) and are labeled with small print. Horizontal shading is used to separate the rows listing the dollar amounts.

The filing status columns could be better distinguished and emphasized by using shading to differentiate the columns rather than the dollar amounts. This would be consistent with the Tax Table in the Form 1040 Instructions and appears to be a better use of shading. In addition, large, bold fonts could be used to better identify the columns. If the IRS has concerns that the EIC Table and the Tax Table would look too similar, a different color of shading could be used for the EIC Table. A comparison of the IRS EIC Table (Tax Year 2006 Draft) and possible modifications (TIGTA revision) are shown in Figure 2.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

**Figure 2: IRS 2006 EIC Table
(DRAFT 2006 Form 1040 Instructions,
pg. 56)**

**Figure 2: TIGTA Revision of the
2006 EIC Table**

2006 Earned Income Credit (EIC) Table- Continued

If the amount you are looking up from the worksheet is--		And your filing status is --					
		Single, head of household, or qualifying widow(er) and you have --			Married filing jointly and you have --		
		No children	One child	Two children	No children	One child	Two children
At least	But less than	Your credit is --			Your credit is --		
16,000	16,050	0	2,553	4,280	0	2,747	4,536
16,050	16,100	0	2,545	4,270	0	2,747	4,536
16,100	16,150	0	2,537	4,259	0	2,747	4,536
16,150	16,200	0	2,529	4,249	0	2,747	4,536
16,200	16,250	0	2,521	4,238	0	2,747	4,536
16,250	16,300	0	2,513	4,227	0	2,747	4,536
16,300	16,350	0	2,505	4,217	0	2,747	4,536
16,350	16,400	0	2,497	4,206	0	2,747	4,536
16,400	16,450	0	2,489	4,196	0	2,747	4,536
16,450	16,500	0	2,481	4,185	0	2,747	4,536
16,500	16,550	0	2,473	4,175	0	2,747	4,536
16,550	16,600	0	2,465	4,164	0	2,747	4,536
16,600	16,650	0	2,457	4,154	0	2,747	4,536
16,650	16,700	0	2,449	4,143	0	2,747	4,536
16,700	16,750	0	2,441	4,133	0	2,747	4,536
16,750	16,800	0	2,443	4,122	0	2,747	4,536
16,800	16,850	0	2,425	4,112	0	2,747	4,536
16,850	16,900	0	2,417	4,101	0	2,737	4,522
16,900	16,950	0	2,409	4,091	0	2,729	4,512
16,950	17,000	0	2,401	4,080	0	2,721	4,501
17,000	17,050	0	2,393	4,070	0	2,713	4,491
17,050	17,100	0	2,385	4,059	0	2,705	4,480
17,100	17,150	0	2,377	4,048	0	2,697	4,470
17,150	17,200	0	2,369	4,038	0	2,689	4,459
17,200	17,250	0	2,361	4,027	0	2,681	4,449

2006 Earned Income Credit (EIC) Table- Continued

If the amount you are looking up from the worksheet is--		And your filing status is --					
		Single, head of household, or qualifying widow(er) and you have --			Married filing jointly and you have --		
		No children	One child	Two children	No children	One child	Two children
At least	But less than	Your credit is --			Your credit is --		
16,000	16,050	0	2,553	4,280	0	2,747	4,536
16,050	16,100	0	2,545	4,270	0	2,747	4,536
16,100	16,150	0	2,537	4,259	0	2,747	4,536
16,150	16,200	0	2,529	4,249	0	2,747	4,536
16,200	16,250	0	2,521	4,238	0	2,747	4,536
16,250	16,300	0	2,513	4,227	0	2,747	4,536
16,300	16,350	0	2,505	4,217	0	2,747	4,536
16,350	16,400	0	2,497	4,206	0	2,747	4,536
16,400	16,450	0	2,489	4,196	0	2,747	4,536
16,450	16,500	0	2,481	4,185	0	2,747	4,536
16,500	16,550	0	2,473	4,175	0	2,747	4,536
16,550	16,600	0	2,465	4,164	0	2,747	4,536
16,600	16,650	0	2,457	4,154	0	2,747	4,536
16,650	16,700	0	2,449	4,143	0	2,747	4,536
16,700	16,750	0	2,441	4,133	0	2,747	4,536
16,750	16,800	0	2,443	4,122	0	2,747	4,536
16,800	16,850	0	2,425	4,112	0	2,747	4,536
16,850	16,900	0	2,417	4,101	0	2,737	4,522
16,900	16,950	0	2,409	4,091	0	2,729	4,512
16,950	17,000	0	2,401	4,080	0	2,721	4,501
17,000	17,050	0	2,393	4,070	0	2,713	4,491
17,050	17,100	0	2,385	4,059	0	2,705	4,480
17,100	17,150	0	2,377	4,048	0	2,697	4,470
17,150	17,200	0	2,369	4,038	0	2,689	4,459
17,200	17,250	0	2,361	4,027	0	2,681	4,449

Source: Draft 2006 Form 1040 Instructions and TIGTA revision.

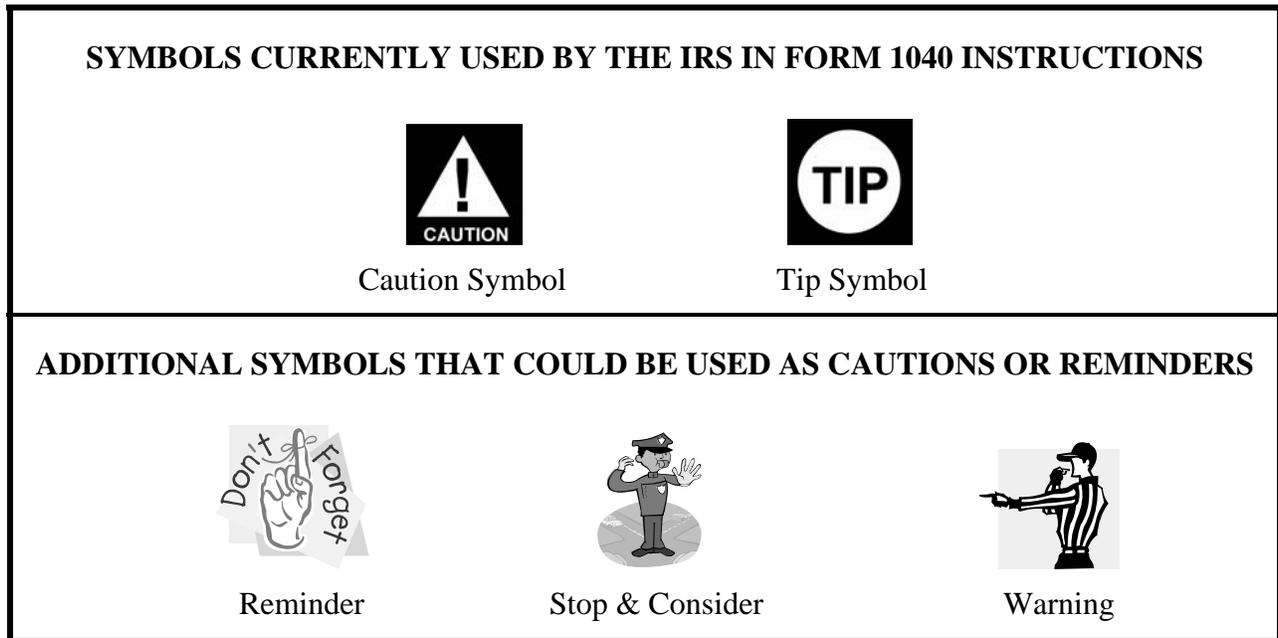
In some instances, the IRS uses symbols to provide helpful information to taxpayers in the form of “TIP” and “CAUTION” symbols. A CAUTION symbol added to the portion of the instructions that alerts a taxpayer filing with a Schedule C to reduce earned income by one-half of his or her self-employment tax before computing the EIC (Worksheet B – Earned Income Credit – Lines 66a and 66b) may help the taxpayer avoid making that error year after year. In discussions with us, the IRS expressed some hesitancy to add more CAUTIONS to instructions, for fear that overuse may reduce their effectiveness. However, we found Worksheet B currently contained only one CAUTION, whereas instructions for Form 1040 Line 21 (Other Income) contain three CAUTIONS and two TIPS.

In addition to “TIP” and “CAUTION” symbols, the IRS could adopt additional symbols to serve as warnings or reminders (see Figure 3). This would help maintain the effectiveness of the current symbols by avoiding overuse.



Opportunities Exist to Help Seniors and Many Other Taxpayers That Repeatedly Make Mistakes on Their Individual Income Tax Returns

Figure 3: Instructional Symbols



Source: Form 1040 Instructions and TIGTA suggestions.

Taxpayers made errors in the EIC recertification process

The math error notice that is sent to taxpayers repeatedly regarding the IRS' EIC Recertification Program reads,

“We can’t allow the amount claimed as Earned Income Credit on page 2 of your tax return. We have no record of receiving Form 8862, Information to Claim Earned Income Credit After Disallowance, recertifying that you are eligible for the credit. You need to file Form 8862, which we have included with this notice for your convenience.”

It is generated when taxpayers claim the EIC after having been prohibited from doing so due to an IRS examination. A recertification indicator is placed on the taxpayer’s account, and he or she is unable to claim the credit until he or she proves eligibility (i.e., recertifies). An Information to Claim Earned Income Credit After Disallowance (Form 8862) is used to do this.

We determined issuance of many of these repetitive recertification notices could be attributed to problems with the IRS’ administration of the EIC Recertification Program. Prior TIGTA audit



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

reports⁶ described a number of inaccuracies and inconsistencies with the Program, including the IRS' (1) failure to timely remove the recertification indicators from some taxpayer accounts and (2) improper removal of the indicator from other accounts, which then allowed taxpayers to receive the EIC without recertifying for it.

Almost 70,000 of these notices were sent to taxpayers who had filed individual income tax returns for Tax Year 2004; 30 percent were repetitive notices affecting 20,536 taxpayers. We estimated 4,261 taxpayers received the notice for at least a third year. We reviewed these returns and found issuance of the math error notices could generally be attributed to problems with the EIC Recertification Program we had previously identified. Many of the issues raised in the prior TIGTA reports have been addressed or are being addressed, and corrective actions should reduce the number of these repetitive notices being issued. Therefore, we are making no recommendations to address the EIC Recertification Program in this report.

Recommendations

Recommendation 4: The Director, Customer Account Services, W&I Division, should include additional information in the notice to alert taxpayers to common EIC computational errors.

Management's Response: IRS management disagreed with this recommendation. The Commissioner, W&I Division, stated there is no data to substantiate the assertion that including additional information in the notice would improve accuracy. To the contrary, the IRS believes that including additional information would likely make the notice more confusing to taxpayers.

Office of Audit Comment: Based on our review, we found taxpayers were significantly more likely to receive this notice multiple times than most other notices. This is certainly data enough to substantiate that some action is warranted by the IRS to improve the notice, whether that would be providing more information regarding common errors or implementing another method of improvement. Interestingly, the IRS offers no data to support that the additional information recommended by the TIGTA would confuse taxpayers. We believe, at a minimum, the IRS should test changes to the notice and gather data to determine if taxpayers with more information were confused or were able to avoid repeating their errors.

⁶ *Improvements Are Needed in the Earned Income Credit Recertification Program* (Reference Number 2001-40-030, dated December 2000) and *The Earned Income Recertification Program Continues to Experience Problems* (Reference Number 2005-40-039, March 2005).



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Recommendation 5: The Director, Tax Forms and Publications, W&I Division, should:

- Enhance the instructions for computing the EIC by making improvements to the EIC Table. A more effective use of shading and a more judicious use of bolding and font size may reduce the number of repetitive errors made by taxpayers when determining how much EIC they can claim.
- Use CAUTION symbols to mark portions of tax form instructions that appear to be overlooked or misunderstood. This may benefit taxpayers by helping them avoid common repetitive mistakes. As noted in this report, a CAUTION symbol could be helpful in the instructions for taxpayers that file a Schedule C and claim the EIC.

Management's Response: IRS management partially agreed with this recommendation. The Commissioner, W&I Division, agreed to differentiate the filing status columns on the EIC Table by using bolding to help taxpayers select the correct column for their EIC amount. The IRS did not agree to use CAUTION symbols to mark portions of tax form instructions that appear to be overlooked or misunderstood based on the number of repeat notices our audit identified. However, the IRS agreed to revise the instructions for line 31 of Schedule C to remind taxpayers to deduct one-half of the self-employment tax amounts from earned income to compute the EIC. In addition, the Director, Earned Income and Health Coverage Tax Credits, plans to conduct an analysis of the EIC computation math error to determine reasons for its occurrence, identify and test potential solutions, and implement successful solutions.

Office of Audit Comment: While we believe the corrective actions agreed to by the IRS may help to reduce the number of repetitive math errors related to the EIC, we believe that better use of shading on the EIC Table (particularly using color) and the use of CAUTION symbols would have a greater effect.

Taxpayers Made Repetitive Errors When Computing and Reporting Their Self-Employment Tax

Self-Employment Tax (Schedule SE, Form 1040) is used by taxpayers to calculate the tax due on net earnings from self-employment. For certain errors, the IRS sends a notice to taxpayers that reads,

“We changed the amount of self-employment tax on page 2 of your tax return because there was an error on Schedule SE, Self-Employment Tax. The error was in the:

- *computation of the self-employment tax on Schedule SE and/or*
- *transfer of that amount to page 2 of your tax return.”*



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

For Tax Year 2004, the IRS sent 81,839 of these notices to taxpayers informing them of a miscalculation made in their self-employment tax. More than 9,500 (12 percent) of these taxpayers were receiving this same notice for the second time; we estimate at least 3,351 taxpayers were receiving it for a third time.

Our review of a sample of 40 taxpayers that had received this same error notice for at least 2 years revealed the following:

- Fifty-five percent (22 of 40) had not correctly transferred the amount of self-employment tax they had computed to the Forms 1040 for 2 years or 3 years in a row. Eighteen of the 22 taxpayers had erroneously transferred exactly 50 percent of their self-employment tax (the same amount as that used as an adjustment to gross income) to Form 1040, while 4 had not transferred any amount. Notably, of the 22 taxpayers that had made transfer errors, 17 had accurately computed the self-employment tax on all of their returns. This is an indicator that these taxpayers have the ability to complete this portion of their individual returns but either lack the understanding or are overlooking instructions necessary to transfer the correct amounts.
- Thirty-eight percent (15 of 40) had computed self-employment tax incorrectly for 2 years or 3 years in a row. A common problem for 7 of the 15 taxpayers was that they had not begun the computation by multiplying the self-employment earnings by 92.35 percent on all of their returns.
- Ninety percent of the taxpayers had prepared their own returns.

To determine whether the IRS could reduce the number of notices sent multiple times to the same taxpayers, we evaluated the math error notice and the IRS forms and instructions that pertain to the self-employment tax computation.

Improvements to the math error notice can be made

The math error notice sent to taxpayers is very generic and simply tells the taxpayer that the error was in either the computation of the tax or the transfer of the tax amount from the Schedule SE to the appropriate line on Form 1040. Additional information could be added to the notice explaining common errors to avoid. Because 63 percent of the taxpayers included in our review made 2 very specific errors repeatedly,⁷ taxpayers may benefit from a warning concerning these errors.

⁷ Eighteen (45 percent) of 40 taxpayers had erroneously transferred exactly 50 percent of their self-employment tax to the Form 1040, and 7 (18 percent) of the 40 had failed to multiply their self-employment earnings by 92.35 percent at the beginning of the tax computation.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Improvements to forms and instructions can be made

The IRS forms and instructions relating to the computation of the self-employment tax appear to be clearly written. However, due to commonality among the errors made, additional warnings or cautions should be used to help taxpayers avoid repeating those particular errors each year.

Forty-five percent of the taxpayers reviewed had incorrectly transferred to their Forms 1040, for multiple years, exactly 50 percent (rather than 100 percent as required) of the correct amount of self-employment tax computed. This indicates that, even though instructions appear clear, taxpayers are confused regarding the amount of tax that should be transferred to the Form 1040.

In addition, 7 of the 15 taxpayers that had repeatedly made computational errors had failed to multiply self-employment income by 92.35 percent to arrive at "net earnings from self-employment" prior to multiplying the amount by the actual tax rate. Again, a simple warning may help taxpayers avoid repeating this error.

Recommendations

Recommendation 6: The Director, Customer Account Services, W&I Division, should include additional information in the notice to alert taxpayers of common mistakes made when computing self-employment tax.

Management's Response: IRS management disagreed with this recommendation. The Commissioner, W&I Division, believes adding information in the notice to alert taxpayers of common errors will confuse taxpayers' understanding of the intent of the notice and because there are a relatively small number of taxpayers to whom notices are issued for such errors. The IRS cited the small percentage of taxpayers that make self-employment computation errors in comparison to the total that file.

Office of Audit Comment: In our opinion, the purpose of a notice is not just to inform taxpayers of their errors, but to educate them on the issues to ensure the errors do not occur in the future. We believe a notice could be crafted that would not only explain the taxpayers' error but could also better inform the taxpayers. Our recommendation would help the 80,000 plus taxpayers (81,839 during tax year 2004) that receive such a notice each year. We believe this number is significant enough to warrant action by the IRS.

Recommendation 7: The Director, Tax Forms and Publications, W&I Division, should use CAUTION symbols to identify the two areas in the instructions for computing self-employment tax where mistakes are common.

Management's Response: IRS management disagreed with this recommendation. The Commissioner, W&I Division, stated there is no data to substantiate the value of using CAUTION symbols relating to the self-employment tax computations and believes



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

these symbols will not change taxpayer behavior. The IRS is judicious in using CAUTION symbols in instructions so that only major issues are emphasized. The IRS believes other communication channels would be more effective.

Office of Audit Comment: The IRS' response that it will not add CAUTION symbols because there is no data to substantiate the value of using these symbols relating to self-employment tax computations seems to be inconsistent with both its mission (to help taxpayers understand and meet their tax responsibilities) and its actions (the IRS already uses CAUTION symbols throughout the Form 1040 Instructions). To cite a lack of data for not using these symbols here does not make sense, unless the IRS believes self-employed taxpayers would react differently to CAUTION symbols than other taxpayers. Certainly if there is a chance that making a simple change to forms and instructions might prove helpful to taxpayers, the IRS has an obligation to test the change and gather the data. There is a sizeable body of outside data available on the use of "warnings" and they indicate that warnings, used correctly, have a strong role in affecting people's behavior.

We agree with the IRS that CAUTION symbols should be used judiciously and for major tax issues. However, in our opinion, the use of these symbols to address the frequently made errors identified in this report meets the criteria better than some of the uses currently employed by the IRS. For example, the following CAUTIONS are included in the Form 1040 Instructions:

"Private delivery services cannot deliver items to P.O. boxes. You must use the U.S. Postal Service" and

"You may have to pay an additional tax if you received a taxable distribution from a Coverdell ESA (education savings account) or a QTP (Qualified Tuition Program)."

While both of these statements contain good information, it is certainly questionable whether they qualify as "major issues." We believe CAUTION symbols would be better used for errors often encountered by taxpayers completing their taxes, such as the ones identified throughout this report.

The CAUTION symbol is already used approximately 35 times in the 87 pages of General Instruction. Furthermore, the TIP symbol, which is similar to the CAUTION symbol in size, shape, and color, is used more than 35 times. The constant use of these similar symbols can diminish their effectiveness. This is, in part, why we suggested the use of additional symbols as noted on page 14 of this report. Symbols that more closely represent their intended message are considered more effective.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Appendix I

Detailed Objectives, Scope, and Methodology

The overall objectives of this review were to identify taxpayers that have repeatedly received the same math error notices and to determine whether the IRS could better address the issues causing these notices. To accomplish the objectives, we:

- I. Identified taxpayers that had received the same math error notices repeatedly.
 - A. Obtained computer extracts from the IRS Return Transaction File¹ that identified taxpayers that had filed Employer's QUARTERLY Federal Tax Returns (Form 941), U.S. Corporation Income Tax Returns (Form 1120), and U.S. Individual Income Tax Returns (Form 1040) and had repeatedly received the same taxpayer notices (based on notice numbers). For each year reviewed, the Return Transaction File contained more than 24 million Forms 941, more than 2.2 million Forms 1120, and more than 126 million Forms 1040 (Tax Years 2002 – 2004).
 1. Identified Form 941 filers that had received the same notice in at least 6 of the 12 quarters for which they filed Forms 941 (Tax Years 2002 - 2004).
 2. Identified Form 1120 and Form 1040 filers that had received the same notice annually over both a 2-year period (Tax Years 2003 and 2004) and a 3-year period (Tax Years 2002 - 2004).
 - B. Randomly sampled (nonstatistical) and reviewed 48 specific returns identified in the computer extract, and scanned many more returns to assess the accuracy of the data, and determined the data to be reliable. Tests conducted to assess the data's reliability included matching extracted data to original IRS databases and also verifying that the returns extracted met required criteria.
 - C. Identified those taxpayers that had repeatedly received the same notice and determined the most frequently repeated taxpayer notices (by notice number) sent to taxpayers for each type of return (Forms 941, 1120, and 1040).
- II. Evaluated the notices that are frequently sent to taxpayers and determined whether the IRS could better address the problems (i.e., reduce the volumes of notices that have to be issued).
 - A. Identified the volume of each notice that was issued for multiple years.

¹An IRS database containing the line items transcribed during return processing and includes other fields such as math calculations.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

- B. For each particular notice, selected a random nonstatistical sample of 40 taxpayers that had repetitively received the notice, ordered the returns that had prompted issuance of the notice, and determined the reason(s) for issuance of the notice. We selected our random nonstatistical samples by using a random number generator to identify 40 cases from the population of taxpayers receiving each repetitive math error notice. We used random nonstatistical samples because we were not projecting outcomes from our samples. The math error notices sampled included Math Error Notice 131 (population 34,101), Notice 192 (population 16,318), Notice 285 (population 44,229), Notice 268 (population 9,574), and Notice 653 (population 20,536). Please see Appendix IV for notice explanations.
- C. Determined what efforts (e.g., education, notice clarity), if any, the IRS could take to reduce the number of notices it has to issue.
- D. We performed a risk assessment to identify any internal control weaknesses that needed to be included in our audit tests. We determined the IRS did not have controls to identify repetitive notices and, accordingly, we identified recommendations in our report to address the control deficiencies.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Appendix II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs)
Kyle R. Andersen, Director
Larry Madsen, Audit Manager
L. Jeff Anderson, Senior Auditor
Kyle Bambrough, Senior Auditor
Annette Bates, Senior Auditor
Bill Russell, Senior Auditor
Layne Powell, Information Technology Specialist



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner, Wage and Investment Division SE:W
Director, Customer Account Services, Wage and Investment Division SE:W:CAS
Director, Customer Assistance, Relationships and Education SE:W:CAR
Director, Media and Publications SE:W:CAR:MP
Director, Submission Processing, Wage and Investment Division, SE:W:CAS:SP
Director, Tax Forms and Publications, Wage and Investment Division SE:W:CAR:MP:T
Field Director, Submission Processing (Cincinnati) SE:W:CAS:SP:C
Field Director, Submission Processing (Fresno) SE:W:CAS:SP:F
Field Director, Submission Processing (Kansas City) SE:W:CAS:SP:KC
Field Director, Submission Processing (Ogden) SE:W:CAS:SP:O
Director, Office of Legislative Affairs CL:LA
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaisons:
 Commissioner, Small Business/Self Employed Division SE:S:COM
 Commissioner, Wage and Investment Division SE:W:S



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Appendix IV

Math Error Notices Reviewed

This is a list of the math error notices we reviewed during the audit. We have presented the narrative information for each type of notice as it is shown in *IRS Processing Codes and Information* (Document 6209, Rev. 1-2006).

101 We changed your filing status. We refigured your tax using the Single filing status based on the information on your tax return.

108 We changed your filing status. We refigured your tax using the Single filing status. Your return was filed using the Head of Household filing status. The name of the dependent that qualifies you for the Head of Household filing status was not present on your tax return.

121 We changed the amount of business income or loss on page 1of[sic] your tax return because there was an error on Schedule C/C-EZ, Profit or Loss From Business. The error was in the:

- computation of the net profit or loss on Schedule C/C-EZ and/or
- transfer of that amount to page 1 of your tax return.

122 We changed the amount of capital gain or loss on page 1 of your tax return because there was an error on Schedule D, Capital Gains and Losses. The error was in the:

- computation of the capital gain or loss and/or
- transfer of that amount to page 1 of your tax return.

Capital losses are limited to \$3,000 (\$1,500 for Married Filing Separately).

131 We changed the amount of social security benefits on page 1 of your tax return because there was an error in the computation of the taxable amount.

Note: Publication 915, Social Security and Equivalent Railroad Retirement Benefits, provides additional information related to computing your taxable social security Benefits. You may call 1-800-TAX-FORM (1-800-829-3676) to order Publication 915, or download it from our web site at www.irs.gov .[sic]



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

- 138 1040¹** - We changed the total income on page 1 of your tax return to include the taxable amount of your employer-provided dependent care benefits. Benefits you received that were more than your childcare expenses must be included as wages on your tax return.
- 141** We changed the amount of total income on page 1 of your tax return because there was an error in the computation.
- 158 1040** - We changed the adjusted gross income section on page 1 of your tax return. The entry for one half[sic] of your self-employment tax was missing or incorrect.
- 177** We changed the amount claimed as medical and dental expenses on your Schedule A, Itemized Deductions, because it was figured incorrectly.
- 180** We changed the amount claimed as total gifts to charity on your Schedule A, Itemized Deductions, because it was figured incorrectly or the amount was not limited to one-half of your adjusted gross income.
- 192** We changed the amount claimed as standard deduction on page 2 of your tax return. You are entitled to a higher standard deduction if you and/or your spouse are age 65 or older and/or blind.
- 194** We changed the amount claimed as standard deduction on page 2 of your tax return:
- No amount was entered for standard deduction, **or**
 - The amount entered for standard deduction was incorrect with the filing status claimed on your return.
- 200** We changed your total exemption amount on page 2 of your tax return because there was an error in the:
- number of exemptions provided on Lines 6a - 6d and/or
 - computation of your total exemption amount.
- 208** We changed the amount of taxable income because there was an error in the subtraction of your exemption or combined standard deduction/exemption amount.
- 209** We changed the amount of tax shown on your return. The amount entered was incorrect based on your taxable income and filing status.
- 210** We changed the amount of tax on Line 43 of your Form 1040 because there was an error in the computation of the Schedule D tax worksheet or Qualified Dividends and Capital Gain tax worksheet.

¹ U.S. Individual Income Tax Return (Form 1040).



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

211 We changed the amount of tax on your return. The tax rates on Qualified Dividends and Capital Gains are generally lower than the standard rates. It appears your tax was not computed using one of these rates or was computed incorrectly.

226 We changed the amount of alternative minimum tax on page 2 of your tax return because there was an error on Form 6251, Alternative Minimum Tax-Individuals. The error was in the computation of alternative minimum taxable income.

240 We changed the amount claimed as credit for the elderly or the disabled on page 2 of your tax return because there was an error on Schedule R/Schedule 3, Credit for the Elderly or the Disabled. The error was in the:

- computation of the credit on Schedule R/Schedule 3, and/or
- transfer of that amount to page 2 of your tax return.

251 We didn't allow part or all of your child tax credit and/or additional child tax credit on page 2 of your tax return. One or more of your children exceeds the age limitation.

252 We changed the amount claimed as child tax credit on page 2 of your tax return because no amount was entered or the amount entered was incorrect based on the number of boxes checked on Line 6c and/or your adjusted gross income. If additional child tax credit is claimed on Line 67, it may also be affected.

268 We changed the amount of self-employment tax on page 2 of your tax return because there was an error on Schedule SE, Self-Employment Tax. The error was in the:

- computation of the self-employment tax on Schedule SE and/or
- transfer of that amount to page 2 of your tax return.

269 We changed the amount of self-employment tax on page 2 of your tax return. We refigured your Schedule SE, Self-Employment Tax, to reflect your true net earnings before multiplying the amount by .9235. You can not reduce your net earnings twice. Section 1402(A)(12) applies to Line 4a of Schedule SE and is not an election.

285 We changed the amount claimed as Earned Income Credit (EIC) on your tax return. The amount claimed as EIC was figured or entered incorrectly on your tax return.

293 We didn't allow the amount claimed as Earned Income Credit on your tax return. You or your spouse must be at least 25, but less than 65 years old, on December 31st of the tax year for which the tax return is being filed.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

295 We changed the amount claimed as additional child tax credit on page 2 of your tax return because there was an error on Form 8812, Additional Child Tax Credit. The error was in the:

- computation of the credit and/or
- transfer of that amount to page 2 of your tax return.

299 We changed the refund amount or the amount you owe on your tax return because the amount entered on your tax return was computed incorrectly.

547 We changed the amount claimed as child tax and/or additional child tax credit on page 2 of your 2003 tax return because:

- No amount was entered, and/or
- The amount entered was incorrect based on your adjusted gross income and the number of boxes checked on Line 6c, and/or
- The credit amount was not correctly reduced by an amount received as an advance payment.

Note: The total amount of child tax credit for which you are eligible must be reduced by any amount received as an advanced payment when figuring the amount to be entered on page 2 of your 2003 tax return.

585 We didn't allow the amount claimed as Earned Income Credit on page 2 of your tax return because Schedule EIC, Earned Income Credit, was incomplete or not attached to your tax return.

604 Each dependent listed on your tax return must have a valid social security Number (SSN) or Individual Taxpayer Identification Number (ITIN). For one or more of your dependents the SSN or ITIN was missing.

As a result, we didn't allow one or more of your exemptions. This change may affect your taxable income, tax, or any of the following credits:

- Credit for Child & Dependent Care Expenses
- Education Credits
- Child Tax Credit
- Additional Child Tax Credit.

If you, your spouse, or any of your dependents do not qualify for an SSN, you may obtain an Individual Taxpayer Identification Number (ITIN) issued by the Internal Revenue Service by filing Form W-7, Application for IRS Individual Taxpayer Identification Number. This number will allow you to file your return and to claim an exemption but you will be ineligible to claim



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

the Earned Income Credit. You may call 1-800-829-3676 to get Form W-7 or download it from our website at www.irs.gov.

605 Each dependent listed on your tax return must have a valid social security Number (SSN) or Individual Taxpayer Identification Number (ITIN). For one or more of your dependents the last name doesn't match our records or the records provided by the Social Security Administration.

As a result, we disallowed one or more of your exemptions. This change may affect your taxable income, tax, or any of the following credits:

- Credit for Child & Dependent Care Expenses
- Education Credits
- Child Tax Credit
- Additional Child Tax Credit

If you, your spouse, or any of your dependents do not qualify for an SSN, you may obtain an Individual Taxpayer Identification Number (ITIN) issued by the Internal Revenue Service by filing Form W-7, Application for IRS Individual Taxpayer Identification Number. This number will allow you to file your return and to claim an exemption but you will be ineligible to claim the Earned Income Credit. You may call 1-800-829-3676 to get Form W-7 or download it from our website at www.irs.gov.

653 We can't allow the amount claimed as Earned Income Credit on page 2 of your tax return. We have no record of receiving Form 8862, Information to Claim Earned Income Credit After Disallowance, recertifying that you are eligible for the credit. You need to file a Form 8862, which we have included with this notice for your convenience.

Note: The IRS may request additional verification in addition to the completed Form 8862.

702 We didn't allow the amount claimed as Earned Income Credit (EIC) on your tax return. The individual taxpayer identification number you gave us for yourself and/or spouse was issued by the Internal Revenue Service and does not qualify you for the credit.

Note: To be eligible for EIC, you, your spouse, and qualifying child or children must use a correct name and SSN issued by the Social Security Administration.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

743 We didn't allow part or all of the amount claimed as earned income credit (EIC) on page 2 of your tax return. For one or more of the children listed on your Schedule EIC, Earned Income Credit:

- The social security Number is missing or
- The last name doesn't match our records or the records of the Social Security Administration.

If you, your spouse, or any of your dependents do not qualify for an SSN, you may obtain an Individual Taxpayer Identification Number (ITIN) issued by the Internal Revenue Service by filing Form W-7, Application for IRS Individual Taxpayer Identification Number. This number will allow you to file your return and to claim an exemption but you will be ineligible to claim the Earned Income Credit. You may call 1-800-829-3676 to get Form W-7 or download it from our website at www.irs.gov .[sic]

748 We didn't allow your personal exemption on Line 6A and Earned Income Credit (EIC) on your tax return. Your social security Number (SSN) or last name doesn't match our records or the records provided by the Social Security Administration.

Note: To be eligible for EIC, you, your spouse and qualifying child or children must use a correct name and SSN issued by the Social Security Administration.

If you, your spouse, or any of your dependents do not qualify for an SSN, you may obtain an Individual Taxpayer Identification Number (ITIN) issued by the Internal Revenue Service by filing Form W-7, Application for IRS Individual Taxpayer Identification Number. This number will allow you to file your return and to claim an exemption but you will be ineligible to claim the Earned Income Credit. You may call 1-800-829-3676 to get Form W-7 or download it from our website at www.irs.gov .[sic]



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Appendix V

Management's Response to the Draft Report



COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

April 13, 2007

RECEIVED
APR 16 2007

MEMORANDUM FOR MICHAEL R. PHILLIPS
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Richard J. Morgante *Richard J. Morgante*
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make Mistakes on Their
Individual Income Tax Returns (Audit # 200630004)

I reviewed your report and I appreciate your recognition that the vast majority of individual taxpayers that receive math error notices do not repeat their errors in subsequent years, and that only a very small number of business taxpayers receive repeat math error notices. We attribute this to our substantial progress in improving the accuracy and clarity of our notices. As you note, the repetitive notices mentioned in your report were linked to just a few areas of tax law:

- Calculating the taxability of Social Security Benefits
- Calculating the allowable standard deduction for taxpayers age 65 and older
- Claiming the Earned Income Credit (EIC)
- Reporting and computing Self-Employment tax

Communicating complex tax law and tax calculation errors to a diverse population of taxpayers will always present challenges as well as opportunities for improvement. We agree there are opportunities for further notice improvement, and as you recommend in the report, we will change the notice regarding Social Security Benefits to clarify that we made a change to "taxable" benefits. However, it is not practical to address in a notice all of the possible reasons taxpayers made the errors that resulted in repetitive notices.

Likewise, we do not agree with your recommendation to use CAUTION symbols to mark portions of tax form instructions that, based upon the number of repeat notices issued, appear to be overlooked or misunderstood. We try to use CAUTION symbols judiciously in instructions so that only major issues are emphasized, and we have no data to substantiate that using CAUTION symbols changes taxpayer behavior or reduces these types of errors.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

2

The report highlights repetitive math errors taxpayers who claimed the EIC made in the computation of EIC amounts. The majority of the repetitive errors included use of the incorrect filing status column in the EIC table and failure by taxpayers also filing Schedule C to reduce earned income by half of the self-employment tax. We agree that the errors associated with the computation of EIC amounts for the estimated 63,000 or 23 percent of taxpayers who repeated the errors, is a problem. However, the other 77 percent who make a computational error in any given year are also important.

Therefore, in addition to the planned enhancements to the EIC table and Schedule C instructions, we plan to conduct a further study of the EIC computation math error in order to identify other potential solutions which may reduce this math error. Additionally, we will continue to work with several advisory groups, including the IRS Advisory Council and Taxpayer Advocacy Panel, to improve Earned Income Credit communications and we will continue to consider their recommendations for improvement of both notices and forms and instructions.

Our detailed comments to your recommendations are attached.

If you have any questions, please contact me at (404) 338-7060, or members of your staff may contact Betsy Kinter, Director, Customer Account Services, at (404) 338-8910.

Attachment



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

Attachment

RECOMMENDATION 1

The Director, Customer Account Services, W&I Division, should:

1 (a) Correct the math error notice sent to taxpayers notifying them of an error made computing their taxable amount of Social Security benefit to explain the action actually taken by the IRS. Currently, the notice erroneously indicates the IRS changed the amount of Social Security benefits, rather than correctly explaining that it changed the taxable amount of Social Security benefits.

1 (b) Add information in both of the repetitive notices affecting senior taxpayers that would better educate and inform senior taxpayers about the errors made. This could include the customer service assistance available to help them (e.g., toll-free telephone numbers, the Volunteer Income Tax Assistance Program, web sites, publications) and examples, such as a comparison of the standard deduction available to senior taxpayers with the common standard deduction, to help these taxpayers more clearly understand and remember that a higher standard deduction is available to them.

CORRECTIVE ACTION

1 (a) We agree with this recommendation. The notice will be rewritten to correctly state that the taxpayer made an error computing the "taxable amount of their Social Security Benefit."

1 (b) We disagree with this recommendation, since IRS issues notices on a case-by-case basis rather than to particular groups of taxpayers such as seniors. However, Submission Processing will coordinate with the Wage and Investment (W&I) Stakeholder Partnerships, Education and Communication organization to (1) develop, and (2) distribute a fact sheet of common errors made by seniors that can be disseminated to a variety of media sources.

IMPLEMENTATION DATE

1 (a) January 1, 2008

1 (b) (1) Develop fact sheet: October 15, 2007

1 (b) (2) Distribute fact sheet: January 15, 2008

RESPONSIBLE OFFICIAL

1 (a) Director, Submission Processing, W&I Division

1 (b) (1) Director, Submission Processing, W&I Division

1 (b) (2) Director, SPEC, W&I Division



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

2

CORRECTIVE ACTION MONITORING PLAN

IRS will monitor these three corrective actions as part of our internal management control system.

RECOMMENDATION 2

The Director, Tax Forms and Publications, W&I Division, should identify complicated tax law provisions affecting senior taxpayers and including specific references to the services that are available to them within those provisions' instructions and, where possible, on the tax form(s).

CORRECTIVE ACTION

We disagree with this recommendation. We believe other outreach and communication channels focused on seniors would be more effective than placing specific references to services available to seniors throughout form instructions (or on the forms themselves). Each page of the instructions for Form 1040 already includes a footnote that refers taxpayers that need more information or forms to a page in the instructions entitled, *Quick and Easy Access to Tax Help and Forms*, which includes ways to contact the IRS via the Internet, mail, walk-in, and phone. Also, Publication 554, *Older Americans' Tax Guide*, includes a section titled, *How to Get Tax Help*, with information on how to contact the IRS. Finally, additional information in the Form 1040 instructions advises taxpayers of the services available to seniors through the Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 3

The Commissioner, W&I Division, should:

3 (a) Work with the Tax Forms and Publications function and other pertinent functions to build on research and analysis already performed in determining the most effective ways to simplify tax preparation for senior taxpayers.

3 (b) In addition, tax complexities identified in this audit report should be elevated for inclusion in the IRS Commissioner's annual report on tax complexities to the House Ways and Means Committee and Senate Finance Committee.



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

3

CORRECTIVE ACTION

3 (a) We agree with this recommendation. The Taxpayer Assistance Blueprint Research Plan, which is currently under development, will include research on the senior population which will provide information to help us identify the most effective ways to simplify tax preparation for seniors.

3 (b) We do not agree with this recommendation. While we agree that significant tax complexities should be elevated to Congress, we believe that there are more effective methods of doing so, such as elevating them through our taxpayer burden studies or as part of the National Taxpayer Advocate's annual report to Congress.

IMPLEMENTATION DATE

3 (a) October 15, 2007

3 (b) N/A

RESPONSIBLE OFFICIAL

3 (a) Director, Strategy & Finance, W&I

3 (b) N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 4

The Director, Customer Account Services, W&I Division, should include additional information in the notice to alert taxpayers to common EIC computational errors.

CORRECTIVE ACTION

We do not agree with this recommendation. There is no data to substantiate the assertion that including additional information in the notice would improve accuracy. To the contrary, we believe that including additional information would likely make the notice more confusing to taxpayers.

IMPLEMENTATION DATE

NA

RESPONSIBLE OFFICIAL

NA

CORRECTIVE ACTION MONITORING PLAN

NA



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

4

RECOMMENDATION 5

The Director, Tax Forms and Publications, W&I Division, should:

5 (a) Enhance the instructions for computing the EIC by making improvements to the EIC Table. A more effective use of shading and a more judicious use of bolding and font size may reduce the number of repetitive errors made by taxpayers when determining how much EIC they can claim.

5 (b) Use CAUTION symbols to mark portions of tax form instructions that appear to be overlooked or misunderstood. This may benefit taxpayers by helping them avoid common repetitive mistakes. As noted in this report, a CAUTION symbol could be helpful in the instructions for taxpayers that file a Schedule C and claim the EIC.

CORRECTIVE ACTION

We partially agree with this recommendation.

5 (a) We agree with this recommendation and will use bolding for the filing status at the top of the EIC Tables to help taxpayers select the correct column for their EIC amount.

5 (b) We do not agree with this recommendation. However, we will revise the instructions for line 31, Schedule C, Profit or Loss from Business (Sole Proprietorship), to remind taxpayers to deduct one-half of the self-employment tax amount from earned income to compute the EIC.

5 (c) We will also (1) conduct an analysis of the EIC computation math error to determine reasons for its occurrence, (2) identify and test potential solutions, and (3) implement successful solutions.

IMPLEMENTATION DATE

5 (a) November 15, 2007

5 (b) Revise instructions for line 31, Schedule C: November 15, 2007

5 (c) (1) Analyze EIC computation math errors and identify potential solutions:
September 15, 2008

5 (c) (2) Test potential solutions: September 15, 2009

5 (c) (3) Implement solutions: September 15, 2010

RESPONSIBLE OFFICIAL

5 (a and b) Director, Tax Forms and Publications, W&I Division

5 (c) (1, 2 and 3) Director, Earned Income & Health Coverage Tax Credits



*Opportunities Exist to Help Seniors and
Many Other Taxpayers That Repeatedly Make
Mistakes on Their Individual Income Tax Returns*

5

CORRECTIVE ACTION MONITORING PLAN

IRS will monitor these three corrective actions as part of our internal management control system.

RECOMMENDATION 6

The Director, Customer Account Services, W&I Division, should include additional information in the notice to alert taxpayers of common mistakes made when computing self-employment tax.

CORRECTIVE ACTION

We disagree with this recommendation because we believe adding information in the notice to alert taxpayers of common errors will confuse taxpayers' understanding of the intent of the notice, and because of the relatively small number of taxpayers to whom notices are issued for such errors. For example, in 2006 math error notices for self-employment tax computation errors were issued for less than one percent of the nearly 18 million Schedules SE filed that year.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 7

The Director, Tax Forms and Publications, W&I Division, should use CAUTION symbols to identify the two areas in the instructions for computing self-employment tax where mistakes are common.

CORRECTIVE ACTION

We do not agree with this recommendation. Since the instructions are clearly written and there is no data to substantiate the value of using CAUTION symbols relating to self-employment tax computations, we do not believe these symbols will change taxpayer behavior. We are judicious in using CAUTION symbols in instructions so that only major issues are emphasized. We believe other communication channels, such as outreach to small businesses, would be more effective.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A