



Treasury Inspector General for Tax Administration Office of Audit

IMPROVEMENTS ARE NEEDED IN RESOURCE ALLOCATION AND MANAGEMENT CONTROLS FOR AUDITS OF HIGH-INCOME TAXPAYERS

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Highlights

Highlights of Report Number: 2015-30-078 to the Internal Revenue Service Commissioners for the Large Business and International and the Small Business/Self-Employed Divisions.

IMPACT ON TAXPAYERS

High-income taxpayers are frequently involved in complex entities and financial arrangements that provide greater opportunities for aggressive tax planning. It is important for the IRS to demonstrate that it enforces tax laws equally by ensuring that its compliance strategies are applied fairly to all segments of the taxpayer population.

WHY TIGTA DID THE AUDIT

High-income taxpayers can present a unique challenge to tax administration due to the complexity of their financial affairs. This audit was initiated to evaluate the IRS's efforts to ensure the tax compliance of high-income taxpayers.

WHAT TIGTA FOUND

The IRS has taken steps to improve its audit coverage of high-income taxpayers. The IRS adopted a High-Income and High-Wealth strategy focused on auditing more tax returns related to high-income individuals. As a result, audit coverage of high-income taxpayers has improved. However, the IRS should reevaluate whether the threshold for its High-Income and High-Wealth strategy, set at \$200,000, results in an efficient allocation of examination resources.

Additionally, as part of this strategy, the Large Business and International (LB&I) Division established the Global High Wealth (GHW) Industry to specifically address tax compliance issues of high-income taxpayers. The GHW Industry takes a comprehensive approach in auditing high-income taxpayers by extending the audits beyond the individual income tax return to include examining the entities that these taxpayers control.

However, LB&I Division management has not yet established the GHW Industry as a standalone industry capable of conducting all of its own examinations.

Currently, management is using resources from three other LB&I Division industries to assist with auditing GHW Industry enterprise cases without having evaluated the impact of that decision on those other industries.

TIGTA also found that the complexity of the financial affairs of many high-income taxpayers and the limitations of the IRS's audit information systems prevent the IRS from systemically quantifying GHW Industry audit performance. Further, the LB&I Division has not taken a number of steps to ensure that the GHW Industry evolves into a mature industry. For example, the GHW Industry has not implemented a quality review process for its audits.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS: 1) reevaluate the income thresholds in its High-Income and High-Wealth strategy; 2) conduct a cost/benefit analysis of the GHW Industry's outsourcing initiative; 3) explore system modifications needed to systemically quantify GHW Industry enterprise case examination results; 4) ensure that its management reports accurately reflect that there currently is no audit quality measure for the GHW Industry; 5) establish a permanent ongoing quality review system; and 6) require quality reviews of closed GHW Industry examination cases.

The IRS agreed with four of the six recommendations. However, the IRS does not agree that its decision to outsource GHW Industry enterprise cases requires a cost/benefit analysis and is not planning to explore system modifications needed to better quantify enterprise case examination results. TIGTA believes that both the cost/benefit analysis and better information on examination results would improve program decisions.

READ THE FULL REPORT

To view the report, including the scope, methodology, and full IRS response, go to:

<http://www.treas.gov/tigta/auditreports/2015reports/201530078fr.pdf>.

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