Trends in Compliance Activities Through Fiscal Year 2017

September 13, 2018

Reference Number: 2018-30-069

Phone Number / 202-622-6500
E-mail Address / TIGTACommunications@tigta.treas.gov
Website / http://www.treasury.gov/tigta

To report fraud, waste, or abuse, call our toll-free hotline at:

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Treasury Inspector General for Tax Administration
P.O. Box 589
Ben Franklin Station
Washington, D.C. 20044-0589

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TRENDS IN COMPLIANCE ACTIVITIES THROUGH FISCAL YEAR 2017

Highlights

Final Report issued on September 13, 2018

Highlights of Reference Number: 2018-30-069 to the Commissioner of Internal Revenue.

IMPACT ON TAXPAYERS

This report is a compilation of statistical information reported by the IRS. The data presented in this report provide taxpayers and stakeholders with information about how the IRS focuses its compliance resources and the impact of those resources on revenue and compliance over time.

WHY TIGTA DID THE AUDIT

TIGTA conducts this review annually in response to continuing stakeholder interest in the analysis and trending of Collection and Examination function activities. The overall objective was to provide various statistical information regarding Collection and Examination function activities.

WHAT TIGTA FOUND

Although the IRS's compliance program continues to be affected by reductions in the number of staff assigned to work cases, IRS revenues generated by its enforcement operations have steadily increased. Since Fiscal Year (FY) 2013, revenues generated by IRS enforcement operations have increased $3.6 billion. Most recently, enforcement revenue increased from $54.3 billion in FY 2016 to $56.9 billion in FY 2017. The majority of the increase is attributable to assessments from the IRS Examination functions. Enforcement revenue associated with examination assessments increased more than $2.2 billion from FY 2016 to FY 2017.

U.S. taxpayers filed more than 150 million individual income tax returns and forms during FY 2017, and total tax revenues have increased nearly 17 percent over the past five years, from $2.9 trillion in FY 2013 to $3.4 trillion in FY 2017.

Although the rate of employee reductions has declined in recent years, the number of staff assigned to work collection and examination cases has continued to drop over the years with its highest staff level not being seen since its peak in FY 2010. Specifically, the number of Collection and Examination function staff working cases has decreased almost 23 percent since FY 2013. At the same time, the number of delinquent accounts being assigned to the IRS's collection inventories has reached the highest level in at least the past 15 years. A large portion of delinquent accounts closed from the Collection functions, specifically from the Automated Collection System during FY 2017, was a result of moving these delinquencies to inactive or "shelved" inventory. More specifically, the Automated Collection System shelved nearly 470 percent more TDAs in FY 2017 (1.8 million) compared to FY 2016 (320,000), which is generally attributed to tax modules being moved to this inactive inventory in order to provide private collection agencies with inventory.

According to recent statistics, less than 1 percent of returns were examined during FY 2017. While the number of staff in the Examination function has declined, examination assessments generated 21 percent ($12.1 billion) of total enforcement revenues ($56.9 billion) in FY 2017. The IRS's trends continue to show that reductions in staff affect the number of examinations that the IRS is capable of conducting each year. The number of examinations performed by the Small Business/Self-Employed Division continued to decline for the fifth straight year (38 percent decline since FY 2013), while the number of examinations performed by the Large Business and International Division decreased 8 percent from FY 2016 (34,676) to FY 2017 (31,880) and 41 percent since FY 2013.

WHAT TIGTA RECOMMENDED

TIGTA made no recommendations in this report. IRS officials were provided an opportunity to review the draft report and did not provide a formal response.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 13, 2018

MEMORANDUM FOR COMMISSIONER OF INTERNAL REVENUE

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Trends in Compliance Activities Through Fiscal Year 2017 (Audit # 201830018)

This report presents the results of our review to provide various statistical information regarding Collection and Examination function activities. This audit is included in our Fiscal Year 2018 Annual Audit Plan and addresses the major management challenge of Tax Compliance Initiatives.

Although we made no recommendations in this report, we provided Internal Revenue Service officials an opportunity to review the draft report. Internal Revenue Service management did not provide us with a formal response.

If you have any questions, please contact me or Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations).

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Abbreviations

ACS	Automated Collection System
ASFR	Automated Substitute for Return
CSCO	Compliance Services Collection Operations
EITC	Earned Income Tax Credit
FTE	Full-Time Equivalent
FY	Fiscal Year
IRS	Internal Revenue Service
LB&I	Large Business and International
PCA	Private Collection Agency
SB/SE	Small Business/Self-Employed
TDA	Taxpayer Delinquent Account
TDI	Taxpayer Delinquency Investigation
TIGTA	Treasury Inspector General for Tax Administration
W&I	Wage and Investment

Background

Given the responsibility for administration of the Nation's tax code, the Internal Revenue Service (IRS) must consider its mission in planning and executing various legislative changes as well as in evaluating its performance and the results of its programs. The IRS's mission is to:

> *Provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.*

Each year, the Treasury Inspector General for Tax Administration (TIGTA) conducts this review of nationwide compliance statistics for the IRS's Collection and Examination function activities.[1] Our data analyses were performed in TIGTA's Baltimore, Maryland, office during the period February through June 2018. Nationwide data from IRS management information systems were used during our review. Due to time and resource constraints, we did not audit the IRS systems to validate the accuracy and reliability of that information. We did not assess internal controls because doing so was not applicable within the context of our objective. Our analyses were limited to identifying changes and trends in IRS data.

Detailed information on our objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II. Detailed charts and tables referred to in the body of this report are included in Appendix IV. A glossary of terms is included in Appendix VI.

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

[1] TIGTA did not perform this review in Fiscal Year 2012.

Results of Review

The Majority of Taxpayers Meet Their Tax Obligations, but the Internal Revenue Service Faces Challenges in Enforcing the Tax Law

U.S. taxpayers filed more than 150 million individual income tax returns and forms during Fiscal Year (FY) 2017. Businesses filed nearly 11 million income tax returns and forms. These filings make up approximately two-thirds of the 245 million returns and forms that the IRS received from taxpayers in FY 2017.[2] The IRS also received almost 30 million employment tax returns, more than one million excise tax forms, and approximately 279,000 estate and gift tax forms.[3] These returns and forms supported the more than $3.4 trillion in total revenues the IRS collected for FY 2017.

Total tax revenues have increased nearly 17 percent over the past five years, from $2.9 trillion in FY 2013 to $3.4 trillion in FY 2017. The majority of this growth is from increases in revenues associated with employment taxes, estate and gift taxes, and individual income taxes. Specifically, from FY 2013 to FY 2017, employment tax revenues have increased from $898 billion to $1.1 trillion, estate and gift taxes from $19.8 billion to $23.8 billion, and individual income taxes from $1.5 trillion to $1.8 trillion.[4] In order to help the majority of taxpayers meet their tax obligations timely, 22 percent of the IRS's overall FY 2017 funding is in the taxpayer services appropriation.

Taxpayer services, such as filing and account services, taxpayer assistance, and providing taxpayer advocacy services, are important to ensure that taxpayers receive the help that they need in meeting their tax obligations. The IRS reported a level of service of 79.1 percent on its telephone operations in the 2017 Filing Season. The IRS maintains 363 Taxpayer Assistance Centers, although 24 centers are not open because they are not staffed. Also, four Taxpayer

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[2] IRS reports that the remainder of the 245 million returns and forms includes but is not limited to forms such as Form 1040-ES, *Estimated Tax*; Form 1041, *U.S. Income Tax Return for Estates and Trusts*; Form 941-X, *Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund*; Form 943-X, *Adjusted Employer's Annual Federal Tax Return for Agricultural Employees or Claim for Refund*; Form 944-X, *Adjusted Employer's Annual Federal Tax Return or Claim for Refund*; Form 1040-X, *Amended U.S. Individual Income Tax Return*; Form 1041-A, *U.S. Information Return Trust Accumulation of Charitable Amounts*; Form 1120-X, *Amended U.S. Corporation Income Tax Return*; and Form 4868, *Application for Automatic Extension of Time to File U.S. Individual Income Tax Return*.

[3] IRS, Publication 55B, *Internal Revenue Service Data Book, 2017*, p. 4 (Mar. 2018), available at https://www.irs.gov/statistics/soi-tax-stats-irs-data-book.

[4] IRS, Publication 55B, *Internal Revenue Service Data Book, 2017*, p. 14–15 (Mar. 2018). See Appendix IV, Figure 1.

Assistance Centers closed due to lack of staff during FY 2017. However, the IRS expects to continue providing face-to-face service through virtual service delivery at partner locations.[5] Maintaining sufficient personnel to support the various aspects of administering the Nation's tax laws is a challenge that the IRS has been working through for several years.

In FY 2017, the number of IRS employees continued recent declines. Since FY 2010, when the IRS had more than 107,000 employees on hand, its workforce has been reduced by nearly 25 percent. In total, the IRS ended FY 2017 with approximately 81,000 employees, a 2 percent decline from its approximately 83,000 employees in FY 2016. Based on trends in funding and salary costs, the attrition of IRS human resources will likely continue. Furthermore, there will likely be a significant reduction in experience levels given that the IRS has reported that more than 33 percent, or 27,000, of its employees are age 56 or older and many are or will become eligible to retire in the near future.

Enforcing the tax laws

The challenges of enforcing the tax laws are evident in the IRS's Tax Gap analysis. The gross Tax Gap is the amount of true tax liability that is not paid voluntarily and timely. The IRS updated its estimate of the gross Tax Gap to be $458 billion for Tax Years 2008 through 2010.[6] The IRS breaks the gross Tax Gap into three components, nonfiling, underreporting, and underpayment. It is estimated that these components contribute $32 billion, $387 billion, and $39 billion, respectively, to the gross Tax Gap. For taxpayers not subject to withholding but who are subject to substantial information reporting to the IRS, *e.g.*, Form W-2, *Wage and Tax Statement*, and the Form 1099 series of miscellaneous income forms, income reporting compliance is estimated to be 93 percent. Individual income reporting compliance is estimated to be even higher (99 percent) when subject to both withholding and information reporting.

While the gross Tax Gap reflects tax liabilities not paid voluntarily or timely, the IRS's enforcement efforts collected approximately 12 percent of the gross Tax Gap each year since FY 2013.[7] While this may happen in a number of ways, through taxpayers preemptively filing returns or paying tax obligations that may be late, the IRS's enforcement operations are

[5] Virtual Service Delivery allows taxpayers to remotely interact with an IRS employee through both video and audio. For example, a taxpayer can access an IRS virtual service workstation at a public library or nonprofit and interact with an IRS employee located at a Taxpayer Assistance Center.

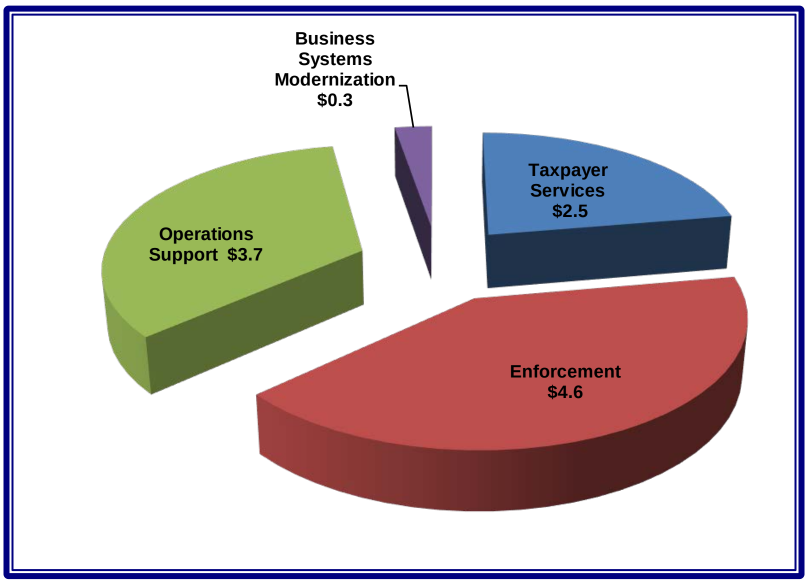
[6] IRS, Publication 1415, *Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2008–2010* (May 2016), available at http://www.irs.gov/uac/IRS-The-Tax-Gap. Unlike prior Tax Gap estimates that pertain to a single tax year, these estimates reflect an estimated average compliance rate and associated average annual Tax Gap for Tax Years 2008 through 2010. The annual gross Tax Gap was estimated to be $345 billion in 2001, $450 billion in 2006, and $458 billion in Tax Years 2008 through 2010. The IRS noted that the December 2007 through June 2009 recession and the weak recovery that followed contributed to the gross Tax Gap remaining substantially unchanged from the previous Tax Year 2006 estimate.

[7] In FY 2017, the IRS collected $56.9 billion through enforcement actions.

responsible for ensuring the filing and payment compliance of taxpayers who may otherwise not meet their tax obligations.

Making up a significant part of the IRS's expenditures and budget allocations, enforcement activities such as collecting delinquent taxes and examining tax returns play a vital role in the IRS's efforts to promote compliance across the broad spectrum of taxpayers. Appropriations supporting these efforts were little changed for the IRS in FY 2017, with $11.2 billion (approximately the same amount as appropriated in FY 2016) provided to the IRS to help taxpayers understand and meet their tax responsibilities and enforce the law with integrity and fairness. In FY 2017, funding for the enforcement of tax laws and Operations Support decreased by a total of $122 million, while the funding for Taxpayer Services increased by the same amount. Figure 1 shows the amount of appropriation by core area for FY 2017.

Figure 1: FY 2017 Funding by Core Appropriation (in Billions)



Source: TIGTA analysis of IRS budget appropriations.

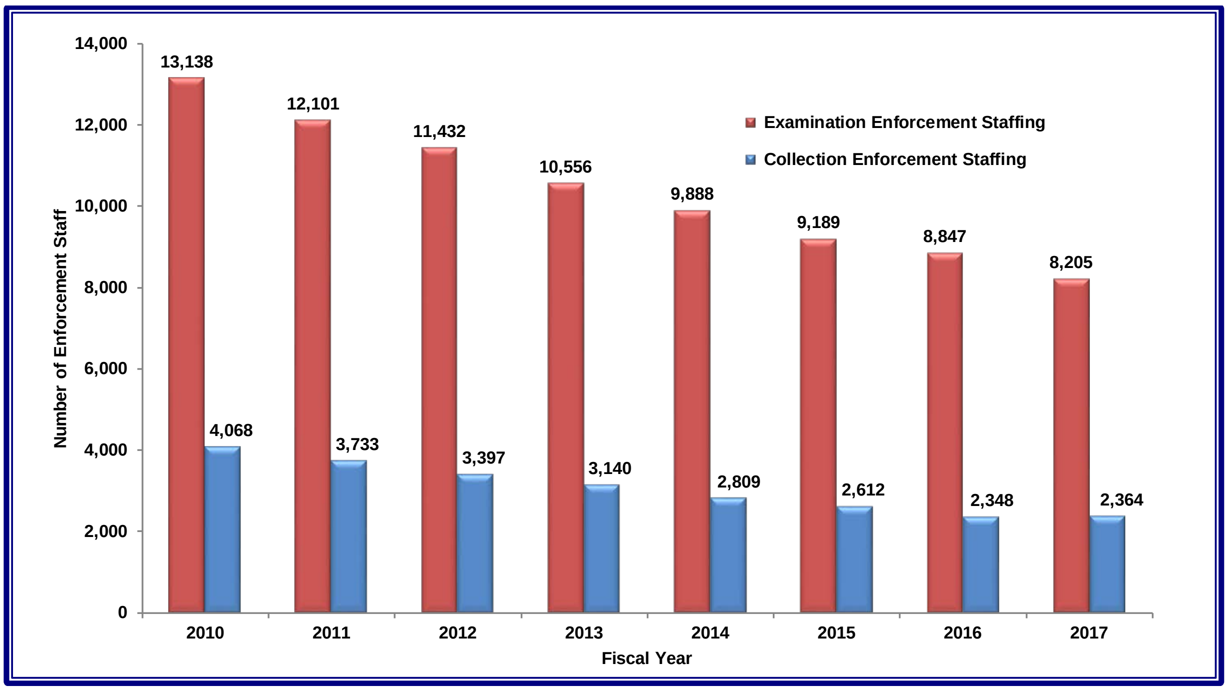
Over the past several years, the IRS's budget has increased more than 2.5 percent from the $10.9 billion in appropriations it received in FY 2015, but the budget remains 7.5 percent less than the amount provided in FY 2010. It is incumbent on the IRS to ensure that monetary resources are used in an increasingly efficient manner. As part of its FY 2017 Management Discussion and Analysis, the IRS notes several key challenges that are a priority, including identity theft, cybersecurity, and taxpayers' increasing demand for online services.[8] Such priorities are balanced with the IRS's key responsibilities of providing efficient and effective

[8] IRS, *Management's Discussion & Analysis, Fiscal Year 2017*.

taxpayer services and enforcing the tax laws. Such a balance is not possible without a workforce that supports the programs that ensure an effective tax administration system.

The available enforcement personnel (revenue officers, revenue agents, and tax compliance officers) within the IRS have declined in a manner consistent with the IRS's overall loss of employees. Although the rate of these losses has declined in recent years, the number of staff assigned to work collection and examination cases has decreased year after year since peaking in FY 2010. More specifically, the collection and examination staff working cases has decreased almost 39 percent since FY 2010. However, the rate of staffing declines has begun to level out, with the declines during FY 2016 and FY 2017 (606 and 626, respectively) being less than half of the staff that was lost from FY 2010 to FY 2011 (1,372). Figure 2 shows the decline in enforcement staff working cases within the IRS's Collection and Examination functions.[9]

Figure 2: Enforcement Personnel by Fiscal Year[10]



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

Declines in enforcement staff contrast with the enforcement revenue generated by the IRS's operations. Enforcement revenue collections increased $2.6 billion, from $54.3 billion in FY 2016 to $56.9 billion in FY 2017, and rose $3.6 billion from FY 2013, when it generated

[9] Collection and Examination functions staff located in field offices, excluding management and overhead staff.
[10] Collection personnel presented includes bag-carrying revenue officers (a bag-carrying revenue officer is one who has five or more assigned cases on ICS) but excludes ACS personnel.

$53.3 billion.[11] The bulk of the increase is attributed to assessments from the IRS Examination functions that occurred from FY 2016 to FY 2017. Enforcement revenue associated with examination assessments increased more than $2.2 billion from FY 2016 to FY 2017. The IRS attributes the increase to a small number of large corporate cases that accounted for more than $2 billion dollars.

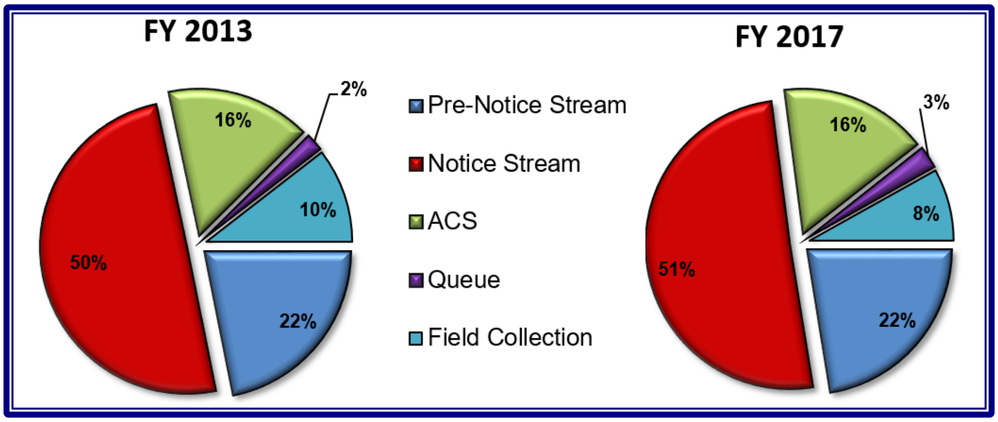
The importance of collecting examination assessments was stressed in the FY 2016 TIGTA report which noted that an average of 9 percent of all Taxpayer Delinquent Account (TDA) modules established during the time period from FYs 2011 through 2015 were the result of an examination assessment.[12] For the same period, the dollar value of delinquent accounts resulting from examination assessments involved an average of approximately $21.7 billion each year. TIGTA noted that collectability procedures were not always followed and that examiners did not always coordinate with the Collection function. The FY 2017 increase in enforcement revenue associated with examination assessments further highlights the importance of coordination and collaboration between the IRS's enforcement functions.

Collection Function Compliance Activities

The mission of IRS's Collection function is to collect delinquent taxes and secure delinquent tax returns through the fair and equitable application of the tax laws, including the use of enforcement tools when appropriate, and to educate taxpayers to facilitate future compliance. From FY 2013 to FY 2017, the number of full-time equivalents (FTE) assigned to the Collection function have declined by 24 percent at campus locations and by 42 percent within the field. At the same time, approximately 51 percent of the total enforcement revenue collected in FY 2017 ($56.9 billion) was collected within the collection notice stream ($28.7 billion), with the remainder collected prior to the notice stream ($12.8 billion) (*e.g.*, Examination, Office of Appeals), by the Automated Collection System (ACS) ($9.4 billion), by Field Collection ($4.6 billion), or when assigned to the queue ($1.4 billion).[13] Figure 3 shows a comparison of enforcement revenue collected during FY 2013 and FY 2017.

[11] See Appendix IV, Figure 2.
[12] TIGTA, Ref. No. 2016-30-070, *Examination Collectibility Procedures Need to Be Clarified and Applied Consistently* p. 2 (Sept. 2016).
[13] Enforcement revenue details are based on our analysis of details from the Enforcement Revenue Information System, which is a compilation of cross-functional IRS databases that track direct hours spent on cases; the life span of enforcement cases, assessments, recommendations, and collections; and the timing of revenue collected from all IRS enforcement actions.

Figure 3: Enforcement Revenue Collected During FY 2013 and FY 2017[14]



Source: TIGTA analysis of Enforcement Revenue Information System data.

The notice stream is a systemic process that occurs when the IRS sends a series of balance due notices to the taxpayer to prompt a reply or payment by the taxpayer. The IRS uses an "assembly line" approach for its collection cases, starting with a preset number of automatically generated balance due notices (notice stream), followed by assignment to the ACS, which is followed by placement in the queue for assignment to revenue officers.[15]

The total number of tax modules for which balance due notices were issued has increased over the past five years, from 31.8 million individuals and businesses issued notices in FY 2013 to 33.9 million issued notices in FY 2017. From FY 2013 to FY 2017, the total amount collected from balance due notices on delinquent accounts increased by 24 percent, from $10.3 billion in FY 2013 to $12.7 billion in FY 2017. The trends for individual and business taxpayers have varied. For example, the total amount collected from balance due notices issued to individual taxpayers increased 46 percent, from $6.1 billion in FY 2013 to $9.0 billion in FY 2017. Whereas the amount collected from notices issued to business taxpayers decreased 9 percent, from $4.1 billion in FY 2013 to $3.8 billion in FY 2017.[16]

Employees play a critical role in ensuring that noncompliant taxpayers pay the appropriate amount of tax. These employees work collection cases within the ACS, the queue, and Field

[14] Pre-notice stream enforcement revenue reflects the collection of revenue before tax delinquencies are treated by the collection notice stream or included as collection inventory within the ACS, the queue, or Field Collection. The collection queue is an inventory of unassigned delinquent cases. However, revenue collections may continue to post to delinquent cases while awaiting assignment.

[15] The notice stream begins with the issuance of the statutory notice, which is generated by the Master File, followed by reminder notices, which are generated by the Integrated Data Retrieval System. During the notice stream for individual taxpayers, the IRS's general practice is to send up to four notices at five-week intervals to collect the balances due.

[16] See Appendix IV, Figures 3.

Collection. Overall, the number of employees working collection cases has declined in three of the past five years. Collection employees conduct their work in different locations, including headquarters, in the field, and at various IRS campuses.

While the combined number of collection FTEs has declined 14 percent, from 11,503 in FY 2013 to 9,856 in FY 2017, the fluctuation in resources working in different functions varied greatly. More specifically, the number of FTEs assigned as Collection headquarters personnel increased more than 200 percent from 187 FTEs in FY 2013 to 572 FTEs in FY 2017. IRS management informed us that the increase in headquarters personnel was due to the Collection realignment in FY 2015. Prior to the realignment, Collection Policy, Collection Inventory Delivery and Selection, and Collection Quality and Technical Support functions were not organized within the headquarters function as they are today. In contrast, Collection function resources at campus locations have decreased 24 percent, from 5,768 to 4,371 FTEs in FYs 2013 and 2017, respectively. A similar trend has occurred in the field, in which resources declined 42 percent, from 5,549 FTEs to 3,192 FTEs during the same period.

IRS management indicated that the IRS has several initiatives underway to mitigate the effect of declining resources. For example, the IRS's Online Payment Application allows taxpayers to set up payment agreements without IRS employee interaction. In addition, the ACS is working to redevelop several collection notices to make them more efficient with fewer pages and to guide taxpayers away from calling the ACS by providing them with other options for resolving their issue.

TDA inventory

From FY 2013 to FY 2017, the number of employees within the Collection function have declined, while the collection inventory for delinquent cases increased from 7.7 million to 8.1 million. Balance due accounts are processed in a variety of ways and have the potential to be worked in the different Collection functions. Delinquent accounts not resolved during the notice stream are routed to one of several inventories or functions within the IRS's Collection program.

The Collection function inventories include:

- ***ACS:*** A collection inventory system in which contact representatives at call sites are responsible for answering incoming taxpayer telephone calls and working an inventory of TDAs and Taxpayer Delinquency Investigations (TDI). The ACS generally works cases requiring telephone contact for resolution and those that may realize a benefit from a variety of systemic actions in an attempt to prompt payment and bring taxpayers into compliance. These include but are not limited to systemic notice issuances and systemic enforcement actions such as levies and Notice of Federal Tax Lien filings.
- ***Field Collection:*** A collection program characterized by TDA and TDI cases in which delinquent taxpayers are contacted by revenue officers who work one-on-one with taxpayers to bring them into compliance by filing delinquent returns, paying past due tax

delinquencies, establishing payment plans, or when necessary, taking enforcement actions such as levies, Notice of Federal Tax Lien filings, or seizures of property. IRS management states that the highest risk and most complex collection cases are assigned to Field Collection because those employees have unique skills that enable them to work such cases. However, because they are labor intensive, the cost associated with working these cases is higher than in other collection operations.

- ***Collection queue:*** An inventory of unassigned TDA and TDI cases. The majority of active inventory assigned within Field Collection are selected from available inventory within the queue. Cases in the queue are systemically reviewed after 52 weeks without being assigned to any Collection function. If changes to the case do not warrant assignment to a different Collection inventory or function, the only action taken is an annual reminder notice sent to the taxpayer. In addition, cases in the queue do not undergo systemic actions, such as cases might within the ACS.

The number of delinquent accounts being assigned to the IRS's collection inventories has reached the highest level in at least the past 15 years. TIGTA recently reported that the IRS's ability to assess risk and prioritize workload is especially important considering the decline in employees and growth in tax delinquency work. The report further stated that the IRS's inventory routing decisions and the selection of the most productive and highest priority cases can help mitigate the risks associated with not working a significant percentage of the inventory.[17] During FY 2017, approximately 81 percent of new modules were routed to the ACS, with the remaining inventory routed to the queue, Field Collection, or the Compliance Services Collection Operations (CSCO). Although the total number of TDAs generated for the Collection functions increased 4 percent from FY 2013 to FY 2017, the number of TDAs issued to Field Collection, the queue, and the CSCO decreased by 30 percent, 12 percent, and 79 percent, respectively. Significant declines in the CSCO TDAs can be attributed to a decreasing number of returns processed under the Automated Substitute for Return (ASFR) or Automated 6020(b) programs, which make assessments based on third-party information for taxpayers who have not filed returns.[18]

The bulk of the IRS's TDA inventory is initially routed to the ACS, and the amount of inventory assigned to the ACS has grown each year since FY 2013. From FY 2013 to FY 2017, the number of taxpayers with delinquencies in the ACS has grown 27 percent (from 4.1 million to 5.2 million), and the amount of delinquencies attributed to these taxpayers increased by 27 percent (from $43.9 billion to $55.8 billion). More recently, the number of taxpayers with

[17] TIGTA, Ref. No. 2017-30-069, *Prioritization of Collection Cases Is Inconsistent and Systemic Enforcement Actions Are Limited for Inactive Cases* p. 6 (Sept. 2017).
[18] See Appendix IV, Figure 5.

delinquencies in the ACS and the dollar amount of these delinquencies increased 4 and 3 percent from FY 2016, from 5 million taxpayers and $54 billion, respectively.[19]

The number of taxpayers with TDAs in the queue decreased 8 percent (to 859,745) from the number of taxpayers in the queue at the end of FY 2016 (937,514).[20] At the same time, the value of the tax delinquencies in the queue decreased by approximately 20 percent, from $55.8 billion in FY 2016 to $44.7 billion in FY 2017. Although many of the cases in the queue may be assigned to be worked, a significant number of taxpayers may be sent only an annual reminder notice in attempt to resolve the delinquency.[21]

Collections on TDAs assigned to the Collection functions increased for all except the CSCO. Most notably, collections on TDAs within the queue increased more than 30 percent from FY 2016 ($1.1 billion) to FY 2017 ($1.4 billion). Due to cases within the queue not being actively worked, payments received on TDAs assigned to the queue are the result of reminder notices, refund offsets, and voluntary payments, *etc*. IRS management informed us that fluctuations in queue collections are not uncommon and that they attribute the recent increases to an improved economy.

Collections on TDAs assigned to Field Collection and the ACS also increased. Since FY 2016, the amount collected on TDAs assigned to Field Collection increased 5 percent (from $3.1 billion to $3.2 billion), while the same measure in ACS shows a 6 percent increase (from $3.1 billion to $3.3 billion). Although collections on TDAs assigned to Field Collection have not increased significantly over the past five years, collections within the ACS have increased more than 17 percent, from $2.8 billion in FY 2013.

It is important to note that collections on delinquent accounts have increased across the various functions, while the amount of inventory issued to the functions has generally decreased, with the exception of the ACS. This may support the IRS's position that an improved economy has increased the potential for collection on these delinquent accounts. While the amount of TDA inventory issued and closed out of the ACS has increased, the increase in collection case closures during FY 2017 was related to moving cases out of the ACS to an inactive inventory. This is directly associated with the IRS's efforts to provide inventory to private collection agencies (PCA), which is subsequently discussed.

Nonfilers and TDI inventory

In recent years, the IRS has consistently decreased the number of nonfiler cases issued to the Collection functions in the form of TDIs. Nonfiler cases identified by the IRS first go through a

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[19] See Appendix IV, Figure 8.
[20] See Appendix IV, Figures 6 and 7.
[21] Before accounts are assigned to the queue, the IRS has already sent notices to the taxpayers about the delinquencies. After the notices process, some cases go directly to the queue, while others are worked in the ACS. Those cases in the queue that are not assigned may not receive contact aside from annual reminder notices.

notice phase, in which up to two delinquent return notices are sent to the nonfilers to remind them to file a tax return. If the taxpayer fails to resolve the nonfiler case during this notice process, a TDI case may be generated. However, due to resource constraints and the reallocation of employees to handle other types of work, Collection function management has been reducing the number of notices issued to nonfilers in recent years, which in turn has reduced the number of TDI cases.

New TDI inventory has declined approximately 74 percent from FY 2013 (1.6 million) to FY 2017 (430,000). In addition, available inventory at the end of FY 2017 (2.3 million) was 17 percent less than available inventory at the end of FY 2016 (2.8 million) and 37 percent less than available inventory at the end of FY 2013 (3.7 million).

The ACS experienced the greatest decline in available TDI inventory, decreasing 26 percent, from 1.4 million tax periods in FY 2016, to 1.1 million tax periods in FY 2017. Both Field Collection and the queue also saw decreases in TDIs over the same period, by 25 percent (from 31,458 to 23,521) and 19 percent (from 544,754 to 441,482), respectively.

During FY 2016, TIGTA reported on how the IRS identifies and processes cases for taxpayers who had not filed tax returns and concluded that improvements to the nonfiler program could help the IRS more effectively address additional nonfilers.[22] More recently, TIGTA reported on the ASFR program. Through the ASFR program, the IRS secures a valid income tax return or prepares a Substitute for Return for taxpayers with a proposed tax assessment based on third-party information returns reported to the IRS (Information Returns Processing information) combined with other internal data.[23] TIGTA found that normal attrition, the inability to hire, reallocation of staff to other collection work, reduced nonfiler case creation, and changes to ASFR inventory selection/work priorities all contributed to reduced ASFR inventory. TIGTA's analysis of declining statistics for the ASFR program, in addition to the declines in TDIs created through the Case Creation Nonfiler Identification Process, provided evidence that the IRS is not adequately addressing the nonfiler portion of the Tax Gap.[24]

As part of the IRS's current nonfiler strategy, the IRS's Office of Research, Applied Analytics, and Statistics, along with the Small Business/Self-Employed (SB/SE) Division, is collaborating to develop a nonfiler strategy. As part of this work, they developed a tool to estimate the costs and impact of the nonfiler treatment streams, such as notices and automated substitutes for returns. This required gathering extensive program-level data to develop nonfiler case unit costs. The IRS expects this work will allow the Office of Research, Applied Analytics, and Statistics to test via simulation or actual field tests, multiple combinations of behavioral modifications,

[22] TIGTA, Ref. No. 2016-30-085, *Improvements to the Nonfiler Program Could Help the Internal Revenue Service More Effectively Address Additional Nonfilers Owing Billions of Dollars in Taxes* p. 10 (Sep. 2016).
[23] The IRS is authorized under Internal Revenue Code (I.R.C.) Section (§) 6020(b) to use third-party information to determine and assess a tax liability.
[24] TIGTA, Ref. No. 2017-30-078, *A Significantly Reduced Automated Substitute for Return Program Negatively Affected Collection and Filing Compliance* (Sept. 2017).

workload allocations, and case identifications to determine the resource requirements and benefits of each. Efforts and initiatives such as this are necessary, as the IRS will continue to be challenged to balance workload with declining resources.

Inactive inventory

In the past, the inability of the IRS's Collection functions to work all available work, given current resources, resulted in a certain portion of inventory being moved to an inactive state and generally not worked. The work was generally of lower priority than other available inventory. As we noted previously, a large portion of delinquent accounts closed from the Collection functions, specifically the ACS, during FY 2017, were a result of moving these TDAs to inactive, or "shelved," inventory.

The overall number of TDA tax modules and dollars shelved increased 123 percent and 129 percent, respectively, from FY 2016 to FY 2017.[25] Tax modules shelved increased from 1.2 million tax modules (reflecting $8.3 billion in delinquencies) in FY 2016 to 2.6 million tax modules (reflecting $19 billion in delinquencies) in FY 2017. More specifically, the ACS shelved 470 percent more TDAs in FY 2017 (1.8 million) compared to FY 2016 (320,000). The dollar value associated with these shelved delinquencies increased by 434 percent from FY 2016 ($892.0 million) to FY 2017 ($4.8 billion).

The ACS is not the only inventory from which delinquent accounts may be shelved. In past years, the majority of shelved accounts were moved there from the queue. Tax modules that remain unassigned in the queue for 52 weeks or more have the potential to be shelved. Tax modules shelved from the queue decreased 6 percent from FY 2016 (868,308) to FY 2017 (820,196) and, given the increase in shelved accounts from the ACS, in FY 2017 it did not contribute the majority of shelved tax modules.[26]

The rise in shelved cases from the ACS correlates to a significant increase in the number of tax modules being assigned to the function. From FY 2016 to FY 2017, the number of delinquent accounts assigned to the ACS increased from 5.8 million to 6.5 million (13 percent). While the number of delinquent accounts issued to the ACS increased, the number of TDAs issued to Field Collection and the queue decreased by 5 and 14 percent, respectively.

During FY 2017, the significant increase in tax delinquencies being shelved is generally attributed to tax modules being moved to this inactive inventory in order to provide PCAs with inventory. In December 2015, legislation was enacted that requires the IRS to use designated contractors to assist in collecting tax delinquencies. The Fixing America's Surface Transportation Act includes a provision requiring the IRS to enter into qualified tax collection

[25] See Appendix IV, Figure 10.
[26] See Appendix IV, Figure 11.

contracts with PCAs to work these "inactive tax receivables."[27] The Act defines an inactive tax receivable as meeting one or more of the following criteria:

- Removed from active inventory.
- Not assigned to an IRS employee for collection and more than one-third of the applicable statute of limitation has lapsed.
- Assigned for collection, but more than 365 days have passed without interaction with the taxpayer or a third party for purposes of furthering the collection.

IRS management informed us that generally this inactive inventory is provided from those tax modules that had been shelved. The significant increase in TDAs being shelved correlates to April 2017, which is when the IRS indicated that they began providing inventory to the PCAs. The inventory provided to the PCAs during FY 2017 included only TDA cases. The IRS reported that as of September 30, 2017, the PCAs had been issued 128,344 delinquent tax modules from the IRS's inactive inventory. The dollar value of these delinquent accounts totaled $919.6 million. As of May 2018, IRS management indicated that they had assigned nearly 432,000 delinquent tax periods to the PCAs and that these taxpayers owed a total of $3.6 billion. During discussions with IRS management, we were informed that the IRS would begin including TDI inventory as part of the work assigned to the PCAs in FY 2018.

Examination Function Compliance Activities

Examination is a vitally important aspect of maintaining a voluntary tax compliance system because 85 percent of the gross Tax Gap is comprised of underreported tax on timely filed returns.[28] The number of staff assigned to Examination functions decreased 22 percent from FY 2013 to FY 2017, with a recent decline of 7 percent from FY 2016.

The examination staff work in various business units including the Wage and Investment (W&I), SB/SE, and Large Business and International (LB&I) Divisions. Positions include revenue agents, tax compliance officers, revenue officer examiners, tax examiners, and other management and administrative staff. While the number of staff in the Examination function has declined, examination assessments generated 21 percent, or $12.1 billion, of total enforcement revenues ($56.9 billion) in FY 2017. This amounts to 22 percent more than the $9.9 billion in revenues that were the result of examination assessments in FY 2016.

IRS examinations can range from the issuance of an IRS notice asking for clarification of a single tax return item that appears to be incorrect (correspondence examination) to a face-to-face

[27] Pub. L. No. 114-94, Div. C, Title XXXII, § 32102, 129 Stat. 1312, 1733-36 (2015) (codified as I.R.C. § 6306).
[28] IRS, Publication 1415, *Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2008–2010*, p. 9 (May 2016), available at http://www.irs.gov/uac/IRS-The-Tax-Gap.

interview and review of the taxpayer's records. According to recent statistics, taxpayers filed nearly 196 million returns during Calendar Year 2016, of which less than 1 percent, or 1.1 million returns, were examined during FY 2017.[29] This is a 32 percent decline from FY 2013 and a 9 percent decline from FY 2016, when there were approximately 1.6 million and 1.2 million examinations conducted, respectively. The examinations completed during FY 2017 included approximately 751,000 (71 percent) conducted via correspondence and approximately 309,000 (29 percent) conducted in the field. The percentage of examinations conducted through correspondence or in the field have not fluctuated significantly over the past 10 years.

The decrease in the number of examinations has a direct impact on the IRS's ability to ensure appropriate reporting of tax obligations and any proposed assessments. As Figure 4 shows, proposed assessments have decreased significantly over the past 10 years. Over the past five years, they have declined by $8 billion (or 22 percent), from $37 billion in FY 2013 to $29 billion in FY 2017.

Figure 4: Proposed Assessments Over the Past Ten Years (in Billions)

	Recommended Additional Tax		
	Total	Field Examinations	Correspondence Examinations
FY2007	$44.3	$34.8	$9.6
FY2008	$43.4	$36.7	$6.7
FY2009	$49.3	$41.3	$8.0
FY2010	$44.8	$36.4	$8.4
FY2011	$43.6	$34.9	$8.8
FY2012	$38.7	$29.4	$9.3
FY2013	$37.1	$28.5	$8.6
FY2014	$33.1	$26.2	$7.0
FY2015	$25.1	$17.8	$7.3
FY2016	$26.9	$21.6	$5.4
FY2017	$29.0	$23.9	$5.1

Source: TIGTA analysis of the IRS Data Book.

Taxpayers may not agree with a portion of these assessments and may appeal the results of the examination or may simply not pay the assessed tax. As such, a large portion of these

[29] IRS, Publication 55B, *Internal Revenue Service Data Book, 2017*, p. 23 (Mar 2018), available at https://www.irs.gov/statistics/soi-tax-stats-irs-data-book. IRS statistics generally associate Calendar Year 2016 data with FY 2017 examination results because, in general, examination activity is associated with returns filed in the previous calendar year.

assessments may be reduced after the Examination function closes the case. We inquired as to whether the Examination functions tracked the amount of adjustments remaining if a case were to be appealed. IRS management stated that they do not track these data. However, comparing the proposed assessments in Figure 4 to the amount of enforcement revenue attributed to the Examination function, which ranged from $9.8 billion to $12.1 billion over the past five years, would indicate that a large portion of the assessments are either not upheld or collected.

Although a portion of assessments may not be collected, past IRS research suggests that in addition to its direct effect, the IRS's Examination function is also an important driver of voluntary compliance. Research identified strong evidence implying that the indirect effect of audits to foster and improve voluntary compliance is significantly more than their effect on direct revenue. More specifically, the deterrent effect of audits started in 1991 was more than 11 times as large as the average adjustment directly proposed by audits closed that year.[30]

Although the aforementioned research concluded that nonfiler notices, information document matching, and return preparation assistance may be more cost-effective at increasing revenue, the results also support the importance of the Examination function. Most notably, that the employees responsible for conducting audits and ensuring taxpayer compliance are both a direct and indirect driver of taxpayer compliance and revenue generation. In contrast with their importance, IRS's statistics show significant reductions in examination staff. These declines have directly decreased the number of examinations that the IRS is capable of conducting each year as well as the assessments made as a result of those examinations.[31] While the indirect effect of the decline in examiners and examinations is unknown, the deterrent effect of examinations identified in past research suggest that these declines may have significantly reduced voluntary reporting of additional income tax. Overall, the total resources, examinations, and proposed assessments for the Examination function have decreased over the years, but the impact within each business operating division varies.

Examination results by business operating division

W&I Division **–** The W&I Division serves individual taxpayers who pay taxes through withholdings, prepare their own tax returns, receive refunds, and generally interact with the IRS one time per year. The W&I Division also works to provide balance in compliance and outreach activities, such as enhancing delivery of Earned Income Tax Credit (EITC) initiatives. In addition, the W&I Division provides staff, training, and direct support for strategic planning; communications and liaison; finance; human resources; equity, diversity, and inclusion; business modernization; and embedded training.

[30] IRS, Publication 1916, *The Determinants of Individual Income Tax Compliance: Estimating The Impacts of Tax Policy, Enforcement, and IRS Responsiveness* (Nov. 1996). This analysis was conducted on individual taxpayer data over a 10-year period, 1982 through 1991, aggregated to the State level.

[31] See Appendix IV, Figure 12.

The W&I Division allocates its resources to two primary areas of service: *Pre-Filing Taxpayer Assistance and Education* and *Filing and Account Services*. Although staff levels at the IRS have declined over the past five years, FTEs in the W&I Division have increased slightly from 28,316 in FY 2016 to 28,455 in FY 2017. Similarly, the W&I Division's appropriated budget remained relatively unchanged at $2.3 billion from FY 2016 to FY 2017.

Examinations within the W&I Division are mainly conducted at an IRS campus via correspondence. Although W&I Division's resources did not change significantly, the number of examinations decreased 8 percent, from 495,000 in FY 2016 to 457,000 in FY 2017. The amount of proposed assessments related to these examinations also declined, by 16 percent, from $2.5 billion in FY 2016 to $2.1 billion in FY 2017. These measures have declined 22 percent and 38 percent, respectively, since FY 2013, from 584,000 examinations and proposed assessments of $3.3 billion.

More than 71 percent of examinations performed within the W&I Division are related to tax returns claiming the EITC. Overall, the number of returns claiming the EITC have not decreased significantly over the past five years, and the number of examinations conducted by the W&I Division for returns claiming the credit have declined by 3 percent, from 336,038 in FY 2013 to 326,197 in FY 2017. These trends indicate a change in priority for the W&I Division, as during FY 2013, 57 percent of examinations were related to returns claiming the EITC.

SB/SE Division **–** The SB/SE Division serves individuals filing Form 1040, *U.S. Individual Income Tax Return*; Form 2106, *Employee Business Expenses*; Form 1120, *U.S. Corporation Income Tax Return*; Form 1120S, *U.S. Income Tax Return for an S Corporation*; or Form 1065, *U.S. Return of Partnership Income*, as well as other business returns with assets less than $10 million. The SB/SE Division serves its taxpayer segment through three organizations: Collections, Operations Support, and Examinations. SB/SE Division examination staff includes revenue agents, tax compliance officers, revenue officer examiners, and tax analysts, who perform examinations either in the field or at a campus via correspondence audit.

The number of tax return examinations performed by the SB/SE Division continued to decline for the fifth straight year. Overall examinations within the SB/SE Division decreased by 38 percent in FY 2017 (571,393) from FY 2013 (920,003). Of the 1.1 million tax returns examined by the IRS in FY 2017, more than half, or 54 percent, were conducted by the SB/SE Division (571,393). Of these, 277,182 were examined in the field, with 294,211 examined at a campus via correspondence.

The amount of proposed assessments in the SB/SE Division also decreased, by 43 percent, from $16 billion in FY 2013 to $9.3 billion in FY 2017. In FY 2017, more than 68 percent of the SB/SE Division's total assessments were the result of field examinations. Field examiners proposed assessments totaling $6.3 billion, while correspondence examinations resulted in $3 billion in proposed assessments.

SB/SE Division field employees examined 36,743 employment tax returns during FY 2017. Examinations of employment tax returns have decreased 20 percent from FY 2013 (45,866) to FY 2017 (36,743). Over the same period, proposed assessments for employment tax examinations decreased 28 percent, from $772 million to $556 million in FY 2017, with nearly half of that decline occurring since FY 2016, when examiners proposed $657 million in adjustments.

In FY 2017, SB/SE Division campus employees conducted 294,211 correspondence examinations, including 52,307 prerefund examinations and 201,413 other discretionary examinations.[32] Although the number of discretionary examinations decreased by 7 percent, the largest decrease occurred with prerefund examinations decreasing 34 percent, from 78,942 in FY 2016 to 52,307 in FY 2017. Proposed assessments associated with these prerefund examinations also decreased, by 30 percent from FY 2016 ($1.8 billion) to FY 2017 ($1.2 billion) and by more than 60 percent since FY 2013 ($3.4 billion).

Overall, IRS statistics also show that the number of returns filed claiming the EITC has not changed significantly, although the portion of taxpayers claiming the EITC who also file a Schedule C, *Profit of Loss From Business*, or Schedule F, *Profit or Loss From Farming*, and report $25,000 or more in gross receipts has increased 10 percent over the past five years. However, the majority of SB/SE Division taxpayers claiming the EITC report less than $25,000 in gross receipts.

One measure of audit productivity is the percentage of audited tax returns that result in recommended adjustments to the tax return. The IRS associates a high percentage of audited tax returns that result in recommended adjustments with greater audit productivity, while audits that result in no change are considered unproductive. Unproductive work is generally measured by the "no-change rate," *i.e.*, the percentage of examinations for which the examiner closed the case with no recommended tax change.

The SB/SE Division reported that examinations of individual and corporate tax returns resulted in 8 percent and 27 percent no-change rates for FY 2017, respectively; this is in line with FY 2016 no-change rates that measured 7 percent and 28 percent. Another measure of productivity is the proposed additional tax per return. In FY 2017, the SB/SE Division reported that field examinations of individual returns resulted in $19,967 in proposed assessments per return, which is more than the $17,474 proposed per return in FY 2016.

[32] During prerefund examinations, the IRS identifies issues that indicate a taxpayer may not be entitled to all or part of the refund amount claimed. The questionable part of the refund is held pending review. The refund is to be released by the Examination function when the taxpayer provides information indicating that he or she is entitled to the refund. Other discretionary examinations exclude flow-through examinations, including those returns subject to the audit and litigation procedures for partnerships as a result of the Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, 96 Stat. 324.

LB&I Division **–** The LB&I Division serves corporations, subchapter S corporations, and partnerships with assets greater than $10 million as well as high-wealth individuals. These taxpayers typically employ large numbers of employees, deal with complicated issues involving tax law and accounting principles, and conduct business in an expanding global environment.

The number of examinations performed by the LB&I Division decreased 8 percent from FY 2016 (34,676) to FY 2017 (31,880). This is also significantly less (41 percent) than the 54,211 performed in FY 2013. As would be expected from the types of taxpayers that it serves, more than 87 percent of LB&I Division examinations were associated with individual (22,719) or corporate (5,144) tax returns in FY 2017. Since FY 2016, individual examinations decreased by 671 (from 23,390) and corporate examinations decreased by 109 (from 5,253).

The no-change rate of individual and corporate examinations in FY 2017 was 7 and 36 percent, respectively. This is not a significant change from the FY 2016 rates (9 and 34 percent, respectively); however, the corporate no-change rate associated with LB&I Division examinations has increased from 26 percent in FY 2013, while the rate for individual examinations has decreased from 10 percent during the same period.

Of the $17.6 billion of total proposed assessments within the LB&I Division in FY 2017, only 17 percent were associated with the individual and corporate examinations previously discussed. The majority of proposed adjustments are associated with Coordinated Industry Cases. Examinations involving these types of cases are often complicated and involve issues associated with complex tax laws or regulations. Proposed assessments from Coordinated Industry Cases in FY 2017 totaled $14.3 billion, approximately 82 percent of the LB&I Division's total proposed assessments for the year.

Less than 8 percent of LB&I Division examinations during FY 2017 (2,139) included flow-through returns. Examinations of flow-through taxpayers decreased by 684 returns from FY 2016 (2,823). Examinations of flow-through taxpayers have decreased by more than 52 percent since FY 2013 (4,489).

In early FY 2016, the LB&I Division reorganized into nine practice areas that report to a single Deputy Commissioner. The reorganization eliminated the distinction between domestic and international, intending to bring greater focus to issues. More recently, as part of its Future State model, the LB&I Division developed a campaign issue-based approach to its treatments and examinations. In an effort to mitigate an increasingly difficult tax environment in which its budget and resources were shrinking, the identification and selection of the initial 13 campaign issues was announced in January 2017, followed by 11 additional campaign issues in November 2017. TIGTA is currently reviewing the LB&I Division methodology for identification and selection of the campaign issues for its compliance strategy as well as evaluating available compliance results.

The LB&I Division also has other initiatives or projects in process, including a review on the selection and examination of transfer pricing issues and obtaining data on the technical capabilities and expertise of LB&I Division employees, as well as work to better identify compliance risk within Coordinated Industry Case taxpayers.

Conclusion

The IRS continues to work through the challenges that are a result of fewer employees and an increasing number of taxpayers to serve. Although ensuring sufficient resources has been a challenge, the IRS's compliance functions have increased the amount of enforcement revenue they collected from FY 2013 to FY 2017 as the overall number of examinations conducted has continued to fall for the fifth straight year. While the IRS's enforcement efforts brought in more enforcement revenue in FY 2017, the most significant contributor to enforcement collection occurs in the notice stream (51 percent of total enforcement revenue), where taxpayers voluntarily pay after receiving automated collection notices. The percentage of revenue collected in the notice stream has increased since FY 2013, while the percentage of revenue attributable to the labor-intensive Examination function and Field Collection has decreased. The data show a significant downward trend in the IRS's proposed audit adjustments over recent years. This may suggest that overall increases in enforcement revenues are not necessarily an effective indicator of how well the IRS's traditional tax compliance enforcement tools (*i.e.*, Examination and Collection) are performing under reduced funding. The IRS will need to continue focusing on process improvements to maintain the effectiveness of its compliance functions.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to provide various statistical information regarding Collection and Examination function activities as they relate to the IRS's efforts to bring taxpayers into compliance with their tax obligations. To accomplish our objective, we:

I. Obtained and analyzed data, records, and other documentation to identify data, statistics, and activities related to voluntary compliance during the 2017 Filing Season.[1] We reviewed activities and areas of focus that included trends or changes encompassing:

A. Individual and business return filings.

B. Tax revenue received voluntarily with timely filed tax returns and tax delinquencies as a result of timely filed returns.

C. Estimates of unfiled returns or other noncompliance.

D. Changes in policy that may have affected voluntary compliance.

II. Obtained and analyzed data, records, or other documentation and interviewed key management personnel to identify significant trends or changes relating to the IRS Collection function's FY 2017 enforcement activities. Areas of focus included the ACS and Field Collection as well as related case inventories (the queue) or systemic collection processes (shelving and surveying of cases). Activities and areas of focus included but were not limited to trends or changes encompassing:

A. Staffing.

B. Direct and indirect time.

C. Delinquent account inventories and unfiled return investigations.

D. Implementing legislation or significant changes in policy (such as private debt collection).

III. Obtained and analyzed data, records, or other documentation and interviewed key management personnel to identify significant trends or changes relating to the IRS Examination function's FY 2017 enforcement activities. Areas of focus included the W&I and SB/SE Divisions (including analysis of campus and field functions) as well as

[1] See Appendix VI for a glossary of terms.

the LB&I Division. Activities and areas of focus included but were not limited to trends or changes encompassing:

A. Staffing.

B. Direct and indirect time.

C. Coverage of individual and business tax returns.

D. Productivity results and proposed assessments for individual and business tax returns.

E. Implementing legislation or significant changes in policy.

IV. Obtained and analyzed data, records, or other documentation and interviewed key management personnel to identify significant trends or changes relating to any other Compliance data. Areas of focus included but were not limited to:

A. Enforcement revenue from across the IRS's compliance operations, including enforcement revenue by business operating divisions, compliance functions, and taxpayer types.

B. Gross collections and accounts receivable.

C. Notice stream collections.

V. Reviewed applicable TIGTA, Taxpayer Advocate Service, and Government Accountability Office reports for relevant information associated with trends or statistics identified in the programs referenced within Steps I through IV.

VI. Assessed the impact of new legislation and budget issues on the compliance functions and activities detailed in Steps I through IV.

VII. For any significant trends or aberrations noted within any of the data analysis performed in Steps I through IV, discussed with applicable IRS personnel and considered the taxpayer burden, if any, that the trends may indicate.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We did not assess internal controls because doing so was not applicable within the context of our objective. Our analyses were limited to identifying changes and trends in data prepared and reported by the IRS.

Appendix II

Major Contributors to This Report

Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations)
Glen Rhoades, Director
Curtis Kirschner, Audit Manager
Michele Strong, Lead Auditor

Appendix III

Report Distribution List

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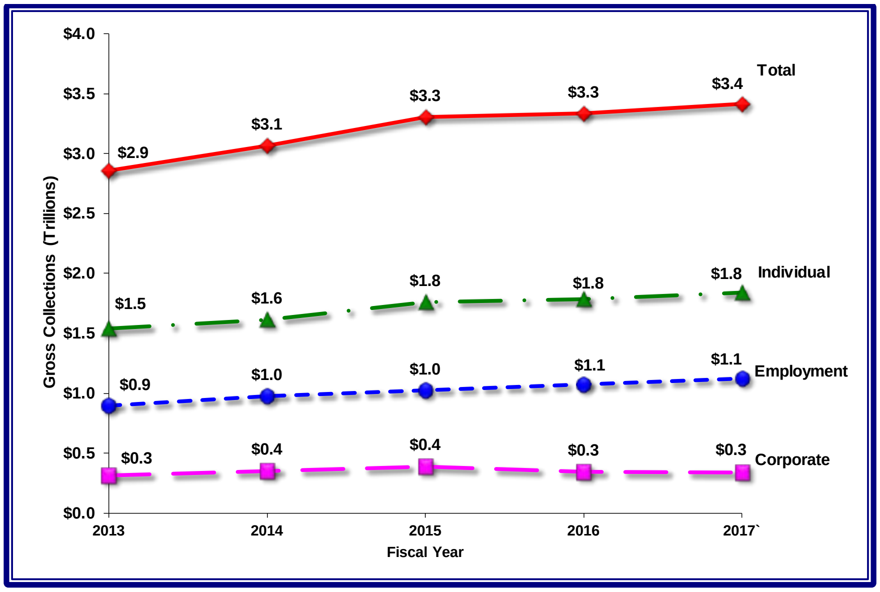
Commissioner, Large Business and International Division
Commissioner, Small Business/Self-Employed Division
Commissioner, Wage and Investment Division
Director, Office of Research, Applied Analytics, and Statistics
Director, Office of Audit Coordination

Appendix IV

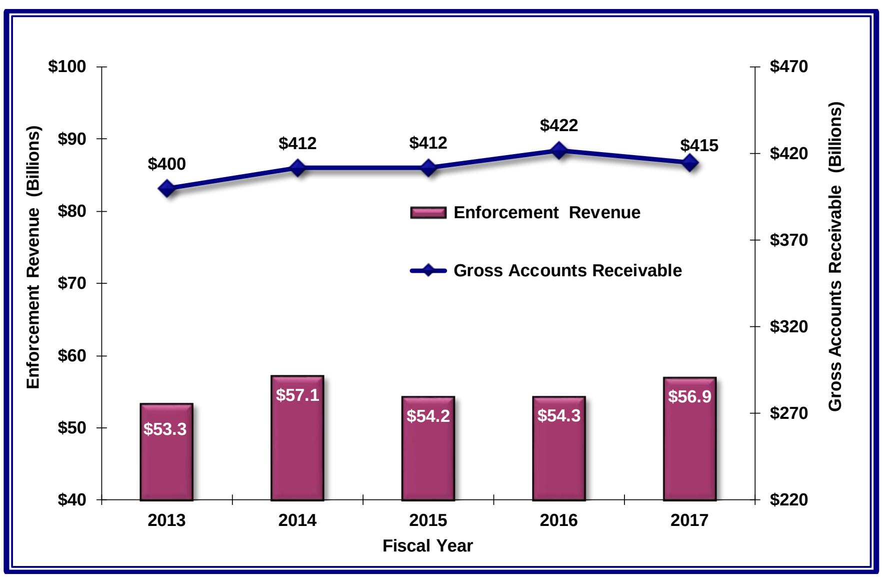
Detailed Charts of Statistical Information

Figure 1: Total Tax Revenue by Type of Tax[1]



Source: TIGTA analysis of the IRS Data Book.

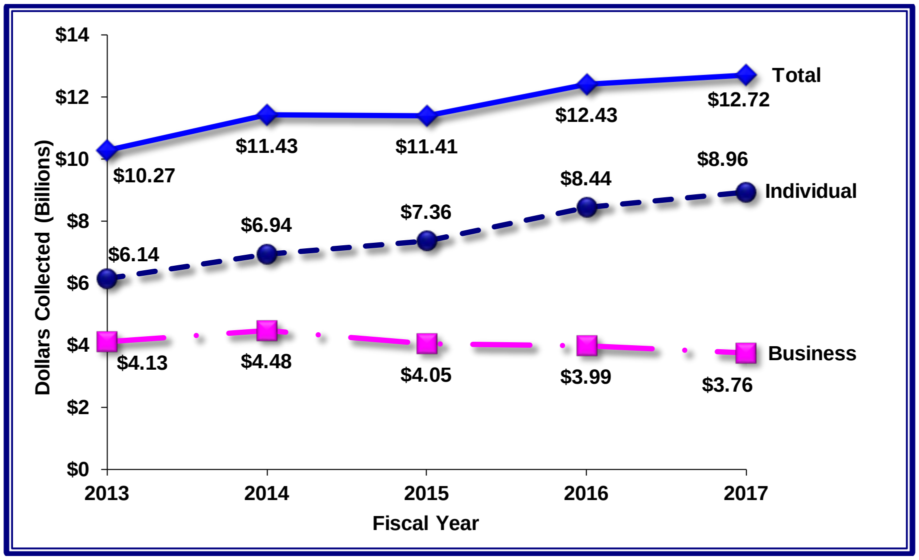
Figure 2: Amount of Enforcement Revenue Collected Compared to Unpaid Assessments



Source: Offices of Research, Applied Analytics, and Statistics and the Chief Financial Officer.

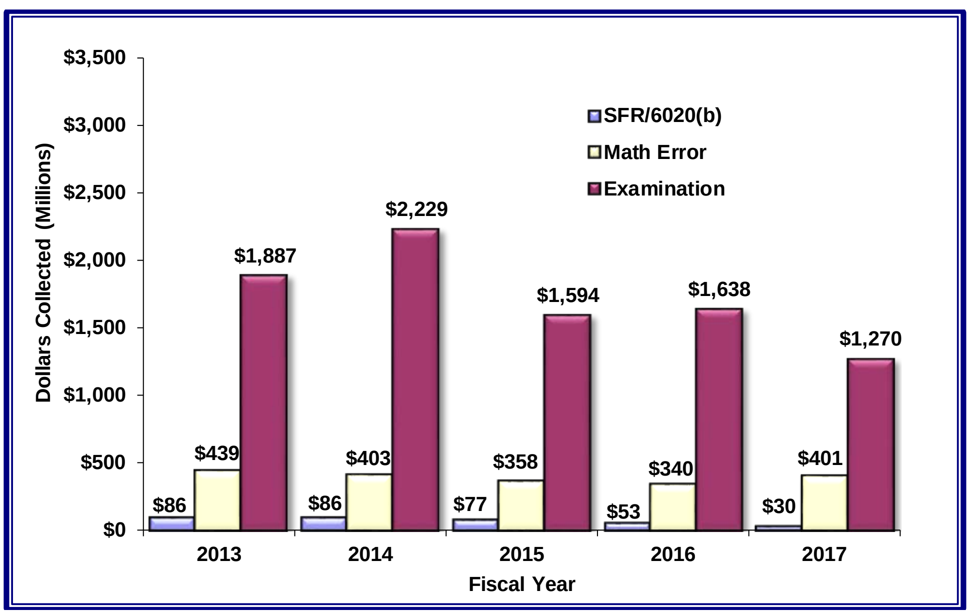
[1] The total line includes excise, estate and trust, and gift taxes, not just individual, corporate, and employment taxes.

Figure 3: Total Amount Collected During Notice Status[2]



Source: Collection Activity Report 5000-2/242.

Figure 4: Amount Collected During Notice Status for Selected Sources of Assessment



Source: Collection Activity Report 5000-2/242. SFR = Substitute for Return.

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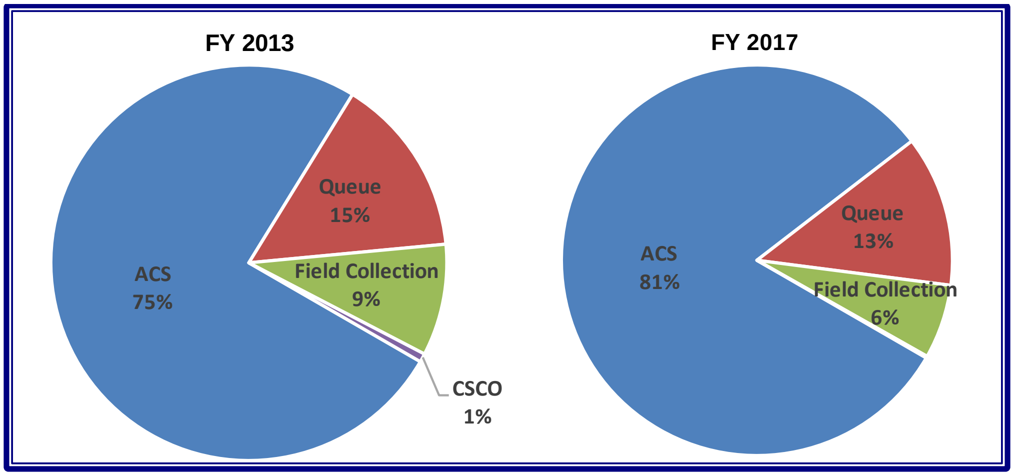
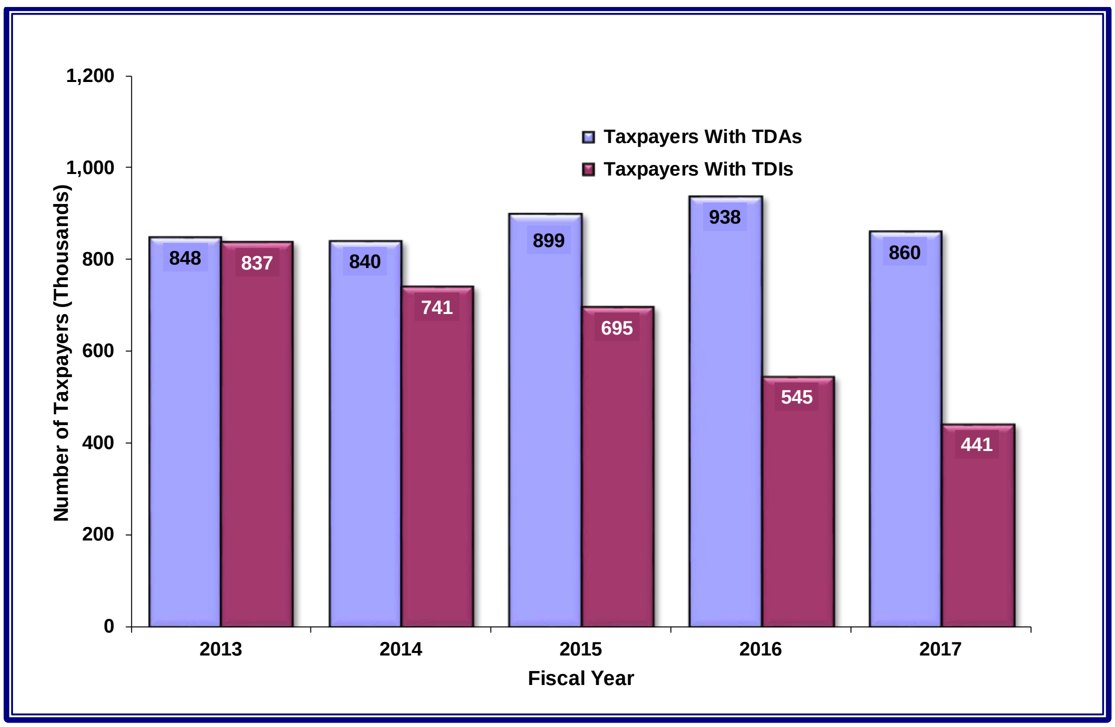
[2] The total of individual and business collections may not equal the total as graphed due to rounding.

Figure 5: Percentage of TDAs Issued to Collection Functions[3]



Source: Collection Activity Report 5000-2.

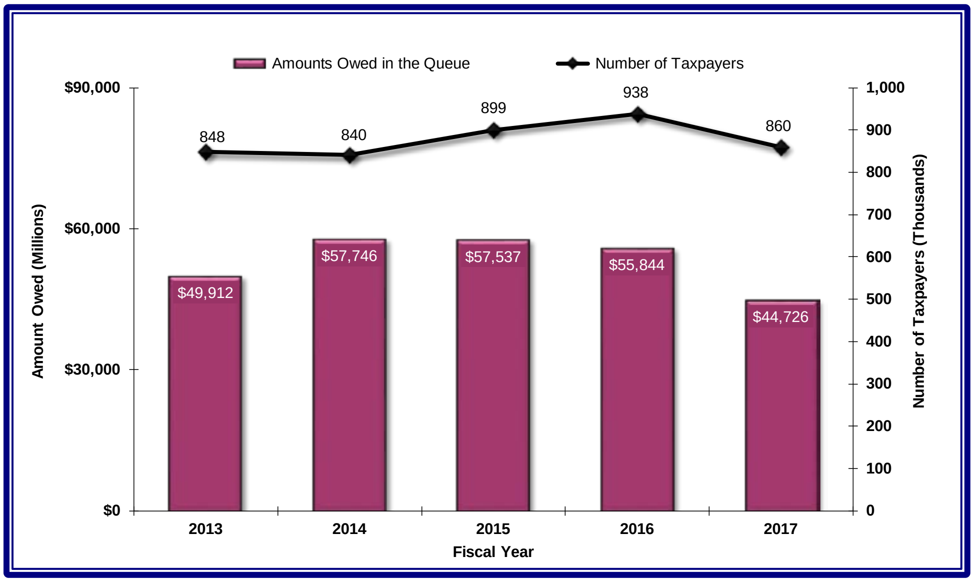
Figure 6: Taxpayers With TDAs and TDIs Maintained in the Queue



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

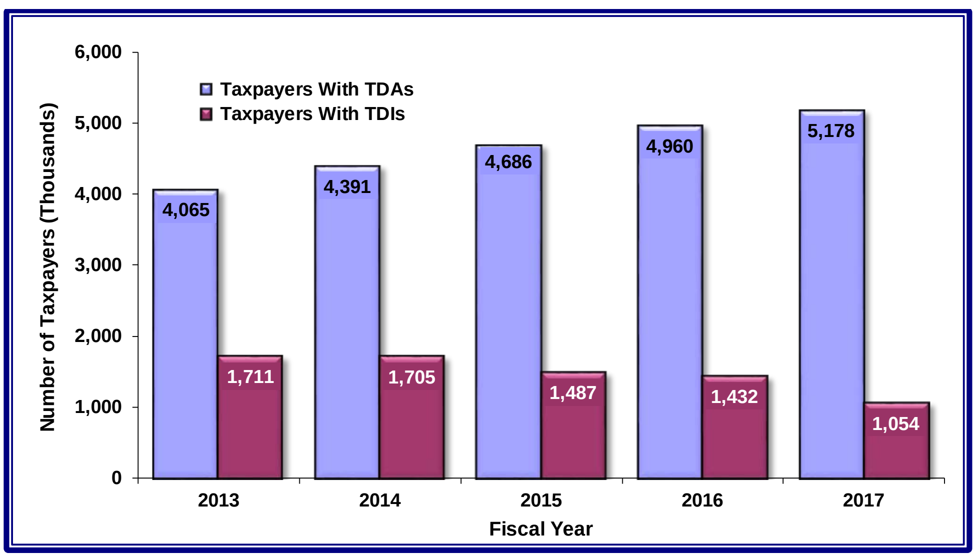
[3] The number of TDAs issued to the CSCO in FY 2017 represented less than one percent of the total and are too small to be represented as part of the FY 2017 data.

Figure 7: Number of Taxpayers With Delinquent Accounts and Amounts Owed in Queue Inventory



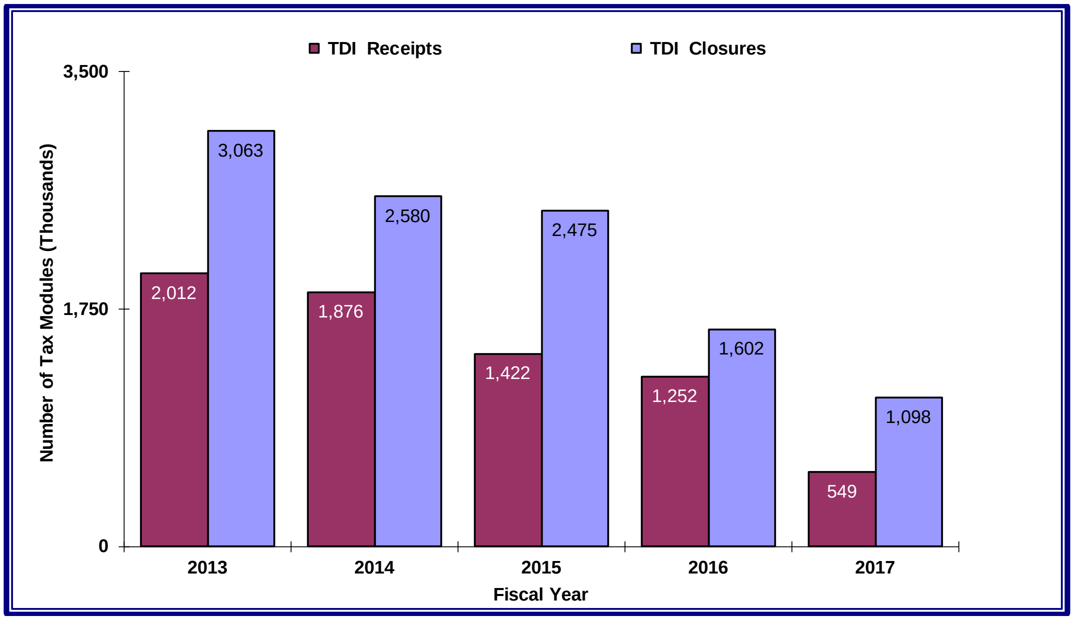
Source: TIGTA analysis of Collection Activity Report 5000-2.

Figure 8: Taxpayers With TDAs and TDIs Maintained in the ACS



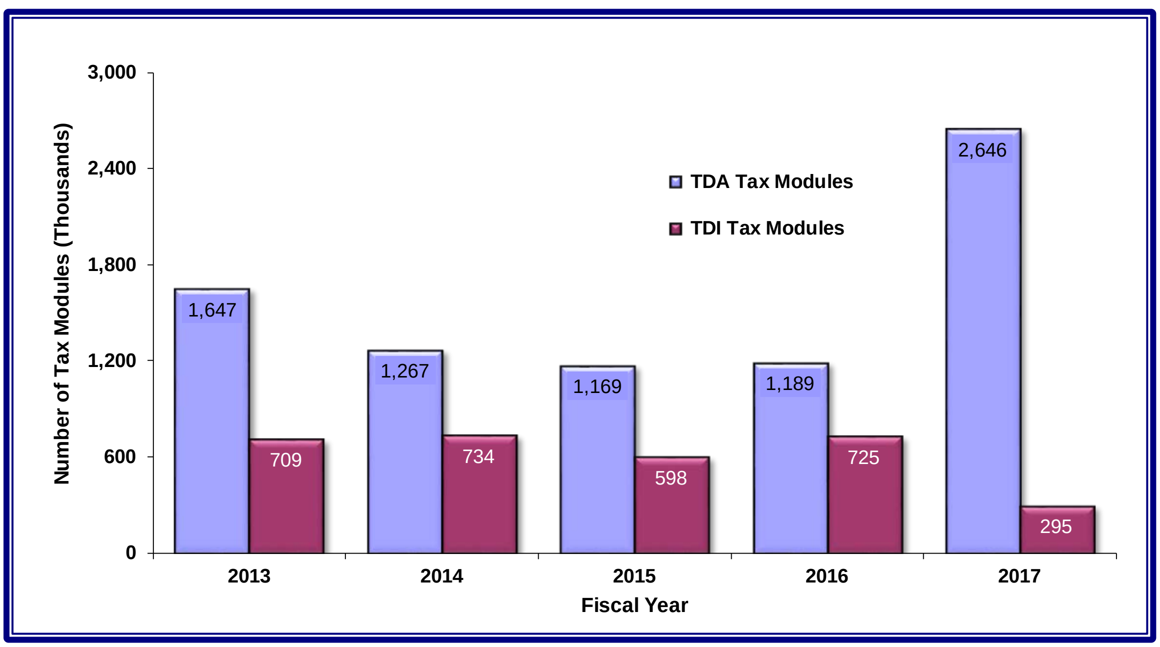
Source: Collection Activity Reports 5000-2 and 5000-4.

Figure 9: Total TDI Modules Issued and Closed



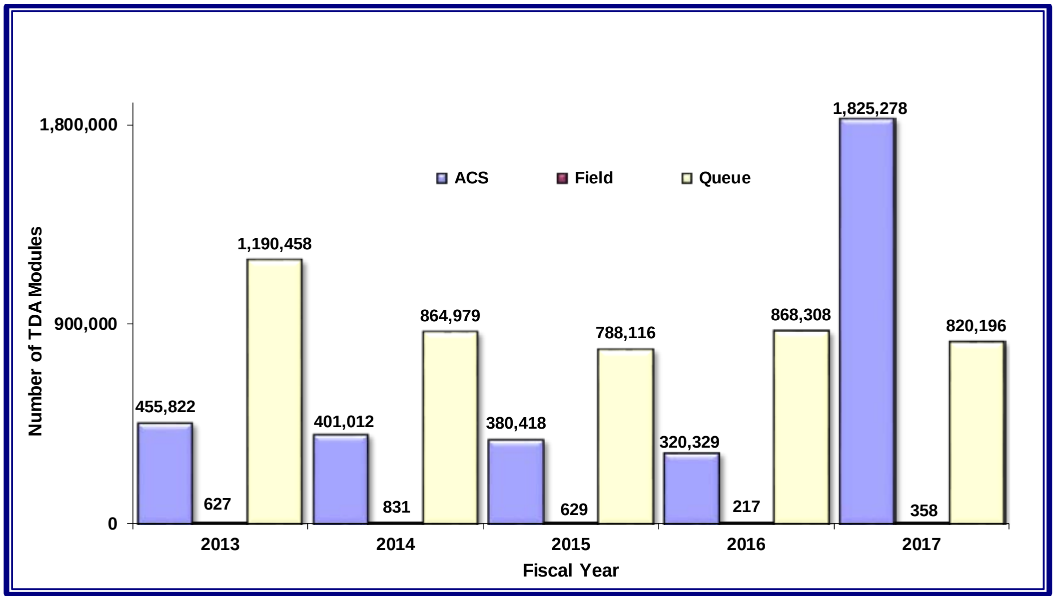
Source: Collection Activity Report 5000-4.

Figure 10: TDA and TDI Tax Modules Shelved or Surveyed



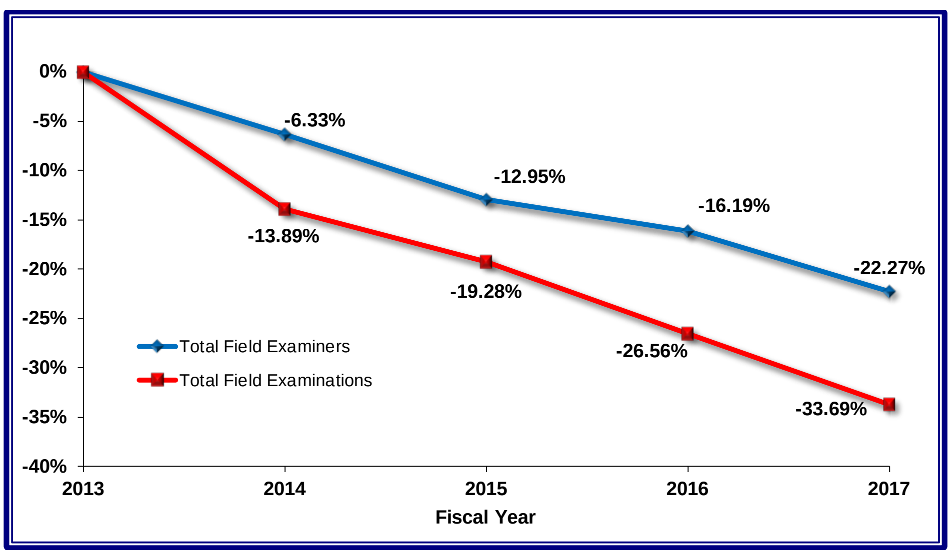
Source: TIGTA analysis of Collection Activity Reports 5000-2 and 5000-4.

Figure 11: TDAs Shelved From Collection Functions[4]



Source: TIGTA analysis of Collection Activity Reports 5000-2.

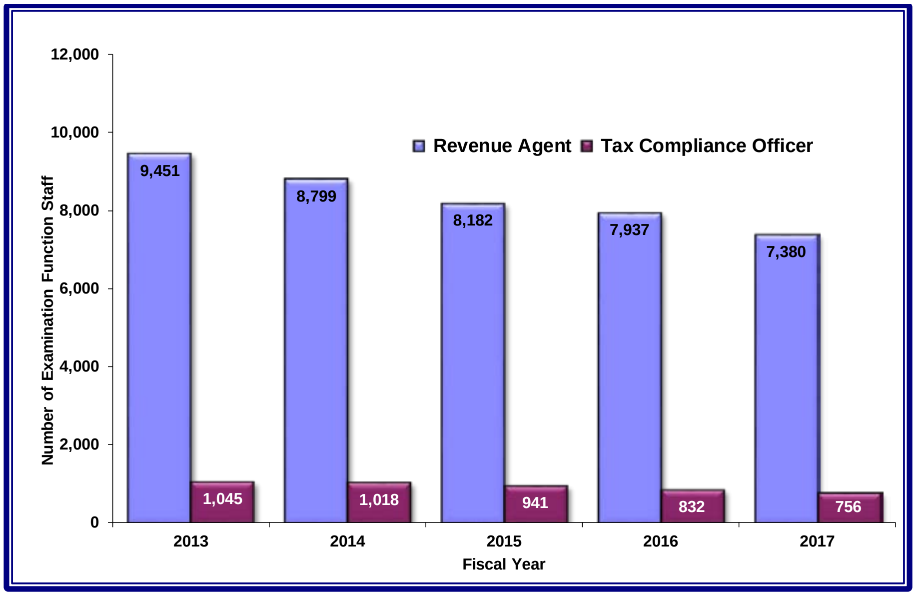
Figure 12: Percentage Change in the Number of Field Examiners and Examinations Since FY 2013



Source: IRS Data Book and Table 37 Examination Program Monitoring.

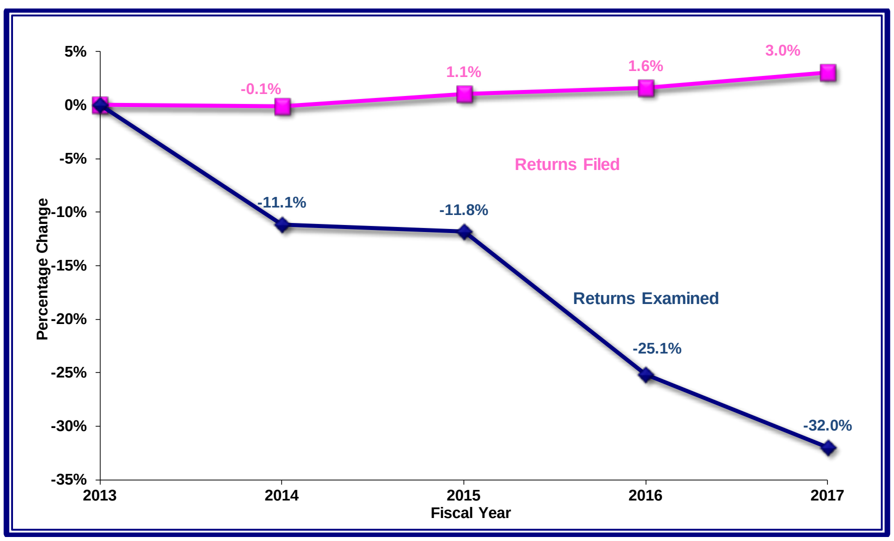
[4] The number of tax modules shelved from Field Collection are not visible due to the scale of the figure and displaying the shelved tax modules from other functions. The number of modules shelved by the CSCO were too small to include and numbered 110 or fewer from FY 2013 to FY 2017.

Figure 13: Number of Examination Function Staff Conducting Examinations of Tax Returns at the End of Each Fiscal Year



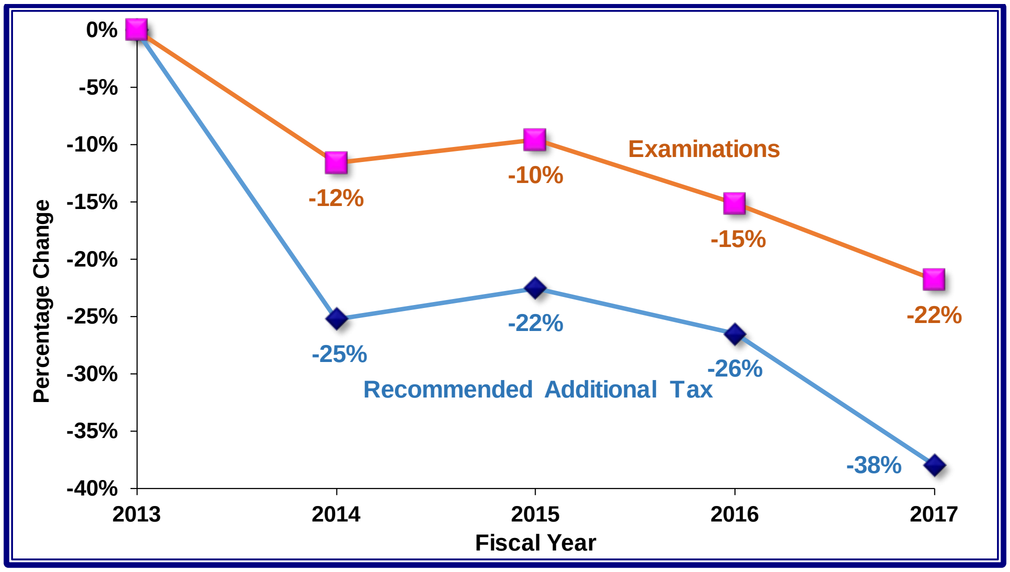
Source: TIGTA analysis of Table 37 Examination Program Monitoring.

Figure 14: Percentage Change From FY 2013 of All Tax Returns Filed and Examined



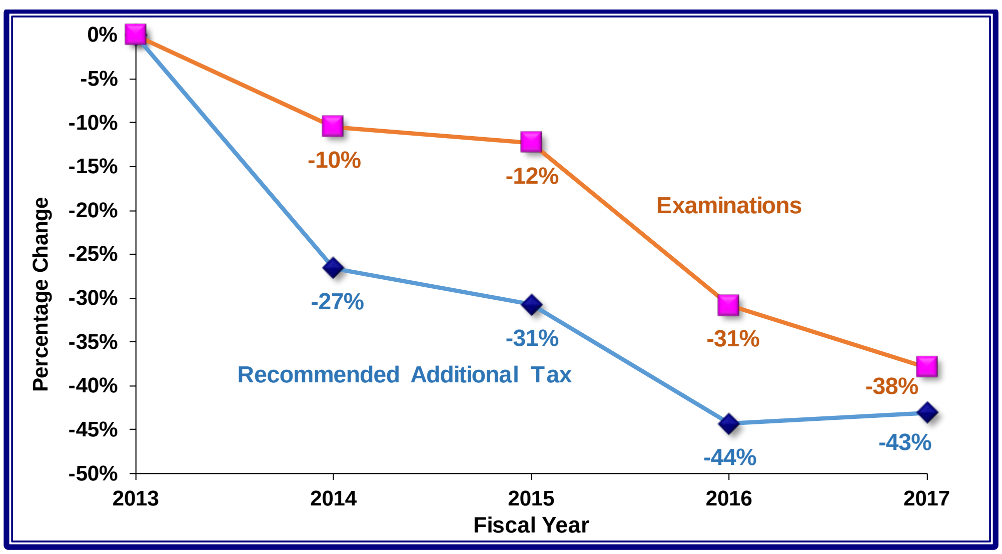
Source: TIGTA analysis of the IRS Data Book.

Figure 15: W&I Division Percentage Change in Tax Returns Examined and Recommended Additional Tax Since FY 2013



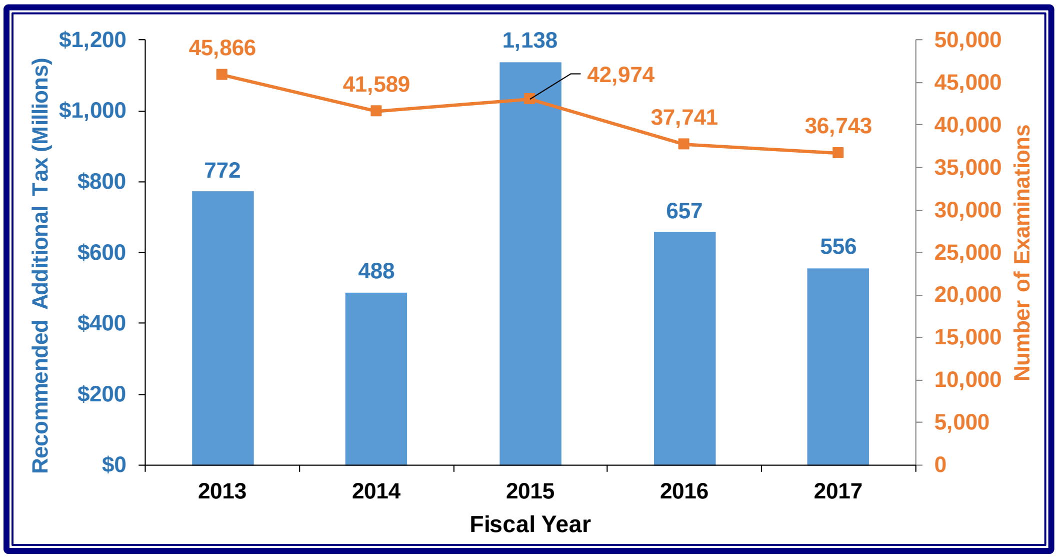
Source: TIGTA analysis of IRS Examination data.

Figure 16: SB/SE Division Percentage Change in Tax Returns Examined and Recommended Additional Tax Since FY 2013



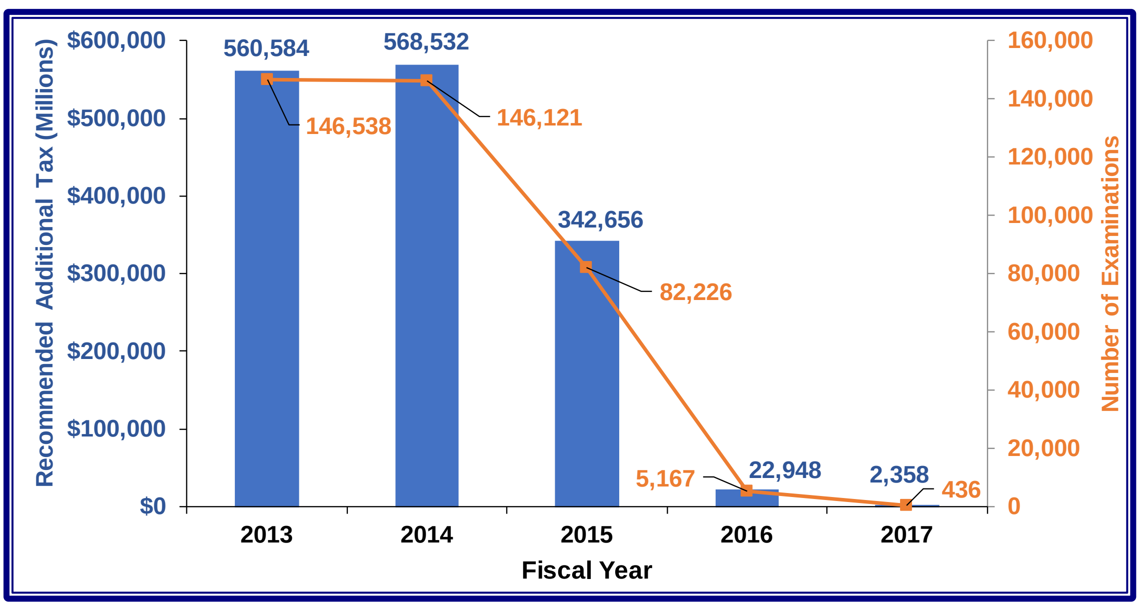
Source: TIGTA analysis of IRS Examination data.

Figure 17: SB/SE Division Number of Employment Tax Examinations and Recommended Additional Tax in the Field



Source: TIGTA analysis of IRS Examination data.

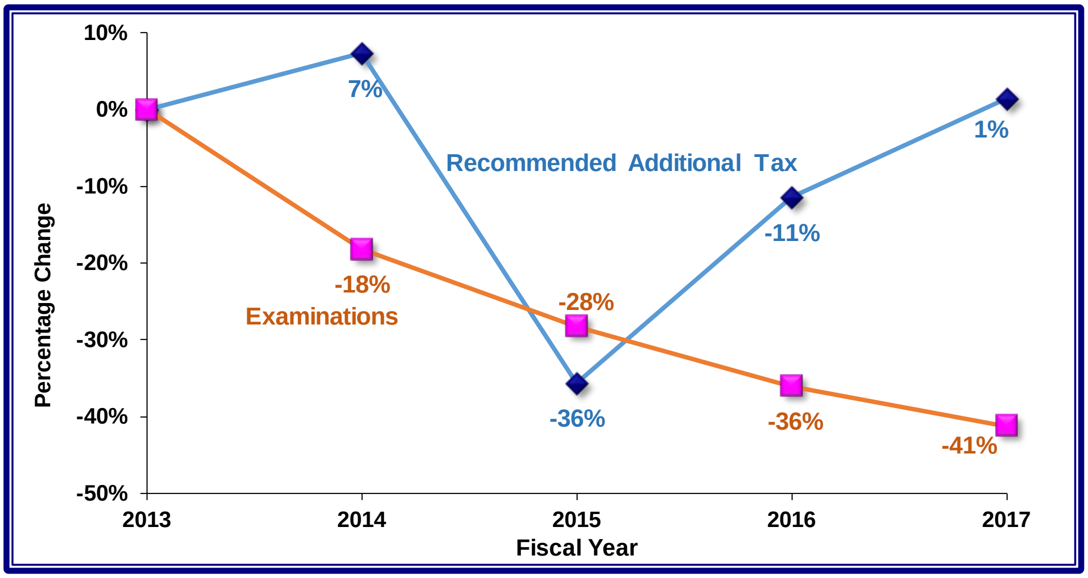
Figure 18: Details of SB/SE Division Examinations of Taxpayers Claiming the EITC[5]



Source: TIGTA analysis of IRS Examination data.

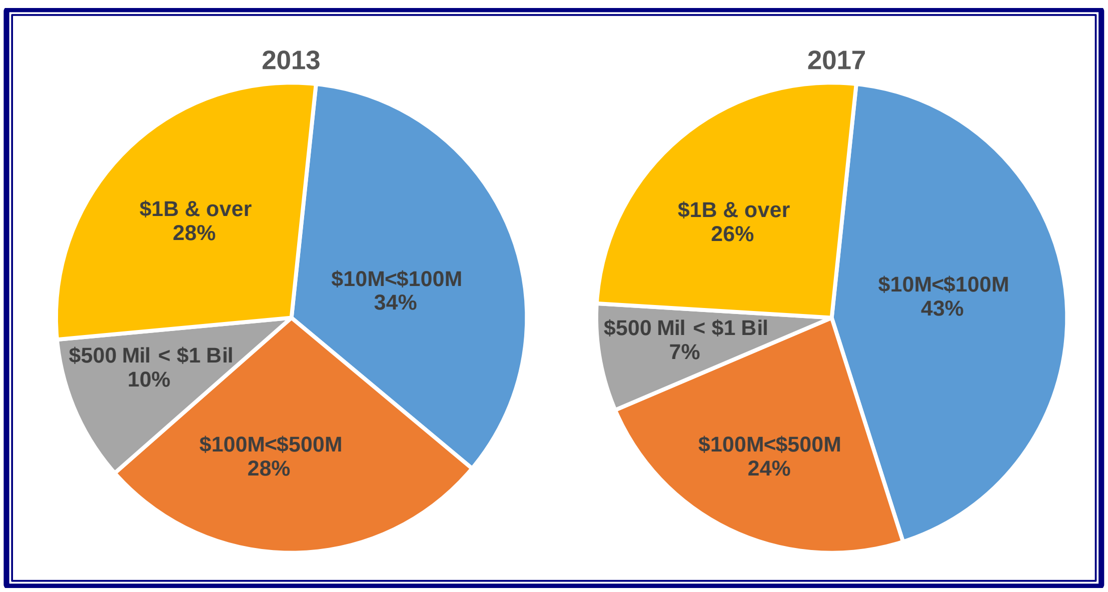
[5] The responsibility for EITC examinations has largely been shifted to the W&I Division.

Figure 19: LB&I Division Percentage Change in Tax Returns Examined and Recommended Additional Tax Since FY 2013



Source: TIGTA analysis of IRS Examination data.

Figure 20: LB&I Division Corporate Examinations by Size of Taxpayers' Total Assets



Source: TIGTA analysis of IRS Examination data.

Figure 21: LB&I Division Recommended Additional Tax for Corporate Examinations by Size of Taxpayers' Assets (in Thousands)

	Fiscal Year				
	FY 2013	**FY 2014**	**FY 2015**	**FY 2016**	**FY 2017**
Corporate Assets					
$10 Million < $100 Million	362,168	1,087,237	366,125	282,580	211,039
$100 Million < $500 Million	497,743	646,679	364,095	370,263	181,555
$500 Million < $1 Billion	231,440	642,492	306,724	145,025	319,695
$1 Billion and Over	14,384,935	13,872,664	7,924,995	12,374,230	15,623,427
Total	**15,476,286**	**16,249,072**	**8,961,939**	**13,172,098**	**16,335,716**

Source: TIGTA analysis of IRS Examination data.

Figure 22: Numbers and Percentages of Individual and Business Tax Returns Examined

	Fiscal Year				
	FY 2013	**FY 2014**	**FY 2015**	**FY 2016**	**FY 2017**
Individual Returns					
Individuals (Forms 1040)	1,404,931	1,242,479	1,228,117	1,034,955	933,785
Coverage Rate	0.96%	0.86%	0.84%	0.70%	0.62%
Business Returns					
Corporations < $10 Million	17,604	17,257	16,460	14,136	12,157
Coverage Rate	0.95%	0.95%	0.92%	0.80%	0.69%
Corporations $10 Million and Greater	9,876	7,858	7,410	6,453	6,109
Coverage Rate	15.84%	12.23%	11.15%	9.53%	7.86%
S Corporations (Forms 1120S)	18,670	16,317	18,595	15,869	13,448
Coverage Rate	0.42%	0.36%	0.40%	0.34%	0.28%
Partnerships	14,870	15,779	19,212	14,645	15,275
Coverage Rate	0.42%	0.43%	0.51%	0.38%	0.38%
Fiduciaries	4,501	3,694	5,288	3,284	3,284
Coverage Rate	0.15%	0.12%	0.16%	0.10%	0.10%
Employment	60,801	57,123	54,214	54,652	53,716
Coverage Rate	0.20%	0.19%	0.18%	0.18%	0.18%
Excise	16,509	13,779	13,153	13,440	13,961
Coverage Rate	1.61%	1.50%	1.34%	1.35%	1.40%
Estates	3,250	2,853	2,770	3,187	2,876
Coverage Rate[6]	11.58%	8.46%	7.78%	8.82%	8.21%
Gift	2,775	3,098	2,539	1,843	1,886
Coverage Rate	1.07%	0.83%	0.95%	0.77%	0.77%

Source: TIGTA analysis of the IRS Data Book.

[6] The IRS attributed the increase in filings in FY 2013 and later to a law made permanent by the enactment of the American Taxpayer Relief Act (Pub. L. No. 112-240, 126 Stat. 2313 (2013)). Under the "portability" concept, a deceased spouse's estate exemption may transfer to the surviving spouse so that he or she can use the deceased spouse's unused exemption *plus* his or her own exemption when the surviving spouse later dies. In order to take advantage of the deceased spouse's unused estate tax exemption, the surviving spouse must file Form 706, *United States Estate (and Generation-Skipping Transfer) Tax Return*, otherwise the deceased spouse's exemption is lost.

Appendix V

Recent Treasury Inspector General for Tax Administration Compliance Trends Reports

TIGTA, Ref. No. 2011-30-071, *Trends in Compliance Activities Through Fiscal Year 2010* (July 2011).

TIGTA, Ref. No. 2013-30-078, *Trends in Compliance Activities Through Fiscal Year 2012* (Aug. 2013).

TIGTA, Ref. No. 2014-30-062, *Trends in Compliance Activities Through Fiscal Year 2013* (Sept. 2014).

TIGTA, Ref. No. 2016-30-004, *Trends in Compliance Activities Through Fiscal Year 2014* (Nov. 2015).

TIGTA, Ref. No. 2016-30-073, *Trends in Compliance Activities Through Fiscal Year 2015* (Sept. 2016).

TIGTA, Ref. No. 2017-30-072, *Trends in Compliance Activities Through Fiscal Year 2016* (Sept. 2017).

Appendix VI

Glossary of Terms

Term	Definition
Area Office	A geographic organizational level used by IRS business units and offices to help their specific types of taxpayers understand and comply with tax laws and issues.
Automated Collection System	A telephone contact system through which telephone assistors collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.
Automated Substitute for Return	A system designed to assess taxes on wage earners who fail to file tax returns. It analyzes information submitted to the IRS and historical tax return information.
Campus	The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.
Collection Activity Reports	A group of reports providing management information to field and Headquarters Collection officials. The reports reflect activity associated with TDA and TDI issuances and installment agreements, including issuances, dispositions, and inventories as well as collection-related payments.
Compliance Services Collection Operations	An IRS function that mails the balance due and return delinquency notices to taxpayers and analyzes and responds to taxpayer correspondence. This function was formerly known as the Service Center Collection Branch.
Computing Centers	IRS facilities that support tax processing and information management through a data processing and telecommunications infrastructure.
Coordinated Industry Case	An Examination function classification used for the largest and most complex corporations.
Corporate Income Tax Return	Form 1120, *U.S. Corporation Income Tax Return*. It is used by corporations to report the corporate income tax.

Term	Definition
Employment Tax Returns	Various Form 94X return series (primarily Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, and Form 941, *Employer's QUARTERLY Federal Tax Return*), filed by businesses to report things such as employer's Federal unemployment taxes and Federal taxes withheld.
Enforcement Revenue	Any tax, penalty, or interest received from a taxpayer as a result of an IRS enforcement action (usually an examination or a collection action).
Estate Tax Return	Form 706, *United States Estate (and Generation-Skipping Transfer) Tax Return*, is filed for estates of certain deceased persons.
Examination (Face-to-Face)	Field examinations of individuals, partnerships, or corporations that occur either at the taxpayer's place of business or through interviews at an IRS office.
Excise Tax Return	Form 720, *Quarterly Federal Excise Tax Return*, is used to report and pay certain taxes, such as those on transportation and fuel.
Fiduciary Income Tax Returns	Income tax returns filed for estates and trusts.
Field Collection	The unit in the Area Offices consisting of revenue officers who handle face-to-face contacts with taxpayers to collect delinquent accounts or secure unfiled returns.
Field Office	Examination function Area Offices, consisting of revenue agents and tax compliance officers who primarily perform examinations of individuals, partnerships, and corporations.
Filing Season	The period from January through mid-April when most individual income tax returns are filed.
Fiscal Year	Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.

Term	Definition
Full-Time Equivalent	A figure calculated from the number of full-time and part-time employees in an organization that represents these workers as a comparable number of full-time employees. It is a measure of labor hours in which one full-time equivalent is equal to eight hours multiplied by the number of compensable days in a particular fiscal year. For Fiscal Year 2017, one full-time equivalent was equal to 2,080 staff hours.
Gift Tax Return	Form 709, *United States Gift (and Generation-Skipping Transfer) Tax Return*, is used to report transfers subject to the Federal gift taxes and to calculate the taxes due on those transfers.
Individual Income Tax Returns	Form 1040, *U.S. Individual Income Tax Return*, series are annual income tax returns filed by citizens or residents of the United States.
Installment Agreement	Arrangement in which a taxpayer agrees to pay his or her tax liability over time.
IRS Data Book	Provides information on returns filed and taxes collected, enforcement, taxpayer assistance, the IRS budget and workforce, and other selected activities.
Levy	A method used by the IRS to collect outstanding taxes from sources such as bank accounts and wages.
Lien	An encumbrance on property or rights to property as security for outstanding taxes.
Math Error	A program in which the IRS contacts taxpayers through the mail or by telephone when it identifies mathematical errors or mismatches of taxpayer information that would result in tax changes.
Module	Refers to one specific tax return filed by the taxpayer for one specific tax period (year or quarter) and type of tax.
No-Change Rate	Percentage of examinations for which the examiner closed the case with no recommended tax change.
Notice of Federal Tax Lien	A notice filed with the appropriate local government office, protecting the Federal Government's interest in the taxpayer's assets by providing public notice of the amount of unpaid tax.

Term	Definition
Overhead Staff	Support staff performing indirect duties within the function, such as automation support, technical support, and quality review.
Partnership Return	Form 1065, *U.S. Return of Partnership Income*, is used to report the income and expenses of domestic partnerships and the share distributed to each partner.
Queue	An automated holding file for unassigned inventory of delinquent cases for which the Collection function does not have enough resources to immediately assign for contact.
Revenue Agent	An employee in the Examination function who conducts face-to-face examinations of more complex tax returns, such as businesses, partnerships, corporations, and specialty taxes, *e.g.*, excise tax returns.
Revenue Officer	Employees in the field who attempt to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses or the ACS.
S Corporation Tax Return	Form 1120S, *U.S. Income Tax Return for an S Corporation*, is filed by qualifying small business corporations and includes amounts distributed to shareholders.
Seizure	The taking of a taxpayer's property to satisfy his or her outstanding tax liability.
Shelved and Surveyed Cases	Shelved and surveyed cases are delinquent unpaid accounts or investigations of unfiled tax returns that have been taken out of Collection function inventory because they are lower priority than other available cases.
Substitute for Return/6020(b) Return	Tax returns prepared by the IRS, based on Internal Revenue Code provisions, when taxpayers appear to be liable for taxes but have not voluntarily filed the returns.
Tax Compliance Officer	An employee in the Examination function who primarily conducts examinations of individual taxpayers through interviews at IRS field offices.

Term	Definition
Tax Examiner	In the context of this report, an employee located in a field office who conducts examinations through correspondence. However, the tax examiner position is also used for many other types of positions located in various IRS offices.
Tax Gap	The gross Tax Gap is the estimated difference between the amount of true tax liability and the amount that is paid voluntarily and on time. The net Tax Gap reflects the gross Tax Gap less other late payments and amounts collected through enforcement.
Tax Period	Refers to each tax return filed by the taxpayer for a specific period (year or quarter) during a calendar year for each type of tax.
Tax Year	A 12-month accounting period for keeping records on income and expenses used as the basis for calculating the annual taxes due. For most individual taxpayers, the tax year is synonymous with the calendar year.
Taxpayer Delinquency Investigation	An unfiled tax return(s) for a taxpayer. One TDI is issued for each delinquent tax period for a taxpayer.
Taxpayer Delinquent Account	A balance due account of a taxpayer. One TDA exists for all delinquent tax periods for a taxpayer.
Unpaid Assessments	Includes all unpaid tax, with accrued penalties and interest, on taxpayers' delinquent accounts.