



## Treasury Inspector General for Tax Administration Office of Audit

### **NATIONAL RESEARCH PROGRAM AUDITS OF INDIVIDUALS ARE CLOSELY MONITORED, BUT THE QUALITY OF TESTS FOR UNREPORTED INCOME IS A CONCERN**

Issued on September 15, 2011

## Highlights

Highlights of Report Number: 2011-30-102 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division and the Director, Office of Research, Analysis, and Statistics.

### **IMPACT ON TAXPAYERS**

The Internal Revenue Service (IRS) is conducting a multiyear National Research Program (NRP) study to measure the reporting compliance among individual taxpayers. The IRS must ensure the data collected are as reliable as possible because the data are used as planning tools for formulating strategies to meet the goals of improving service and enforcing the tax laws so everyone meets their obligation to pay taxes.

### **WHY TIGTA DID THE AUDIT**

This audit was initiated to determine whether the NRP is being properly implemented and providing reliable results for making strategic planning decisions. The NRP is a unique program because it gives the IRS the capability to make statistically reliable estimates of tax reporting compliance nationwide from a relatively small sample of audits.

This, in turn, provides data needed for measuring the difference between the taxes that taxpayers should pay and the amount that is paid voluntarily and on time (the Tax Gap), updating audit selection and resource allocation systems, identifying ways to improve voluntary compliance, and estimating the revenue from proposed legislative and administrative changes.

### **WHAT TIGTA FOUND**

Because of its statistical validity, legislators and policy makers consider the NRP an extremely important program, and IRS management reflected this priority in the emphasis given to the current phase of individual audits. IRS management closely monitored the sampling methodology and implementation schedule for NRP audits. As a result, the NRP is on track to begin providing updated Tax Gap estimates by the end of Calendar Year 2011.

Although the IRS was successful in implementing the NRP schedule, the tests for unreported income during audits need to be improved. TIGTA evaluated a nonstatistical sample of closed Tax Years 2006, 2007, and 2008 NRP audits (10 for each year) and identified that the income reported on the return was not properly verified for four of the 30 audits, which may have adversely affected the accuracy of the audit results for each of the four audits by \$10,000 or more. NRP quality reviewers found an even higher percentage of audits (roughly 40 percent) in their nonstatistical samples for which the income reflected on returns was not properly verified during the NRP audits conducted in Fiscal Years 2008, 2009, and 2010.

### **WHAT TIGTA RECOMMENDED**

TIGTA has already made recommendations in prior reports to strengthen the weaknesses identified in the tests for unreported income during audits. The SB/SE Division has responded with improvement efforts that are currently underway to address these weaknesses. Consequently, TIGTA is not making any additional recommendations at this time.

Although TIGTA made no recommendations in this report, IRS officials were provided an opportunity to review the draft report. IRS management did not provide any report comments.

### **READ THE FULL REPORT**

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

<http://www.treas.gov/tigta/auditreports/2011reports/201130102fr.pdf>.