

GAO

Report to the Chairman
Subcommittee on Oversight
Committee on Ways and Means
House of Representatives

April 1996

TAX ADMINISTRATION

Audit Trends and Results for Individual Taxpayers



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United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-261743

April 26, 1996

The Honorable Nancy L. Johnson
Chairman, Subcommittee on Oversight
Committee on Ways and Means
House of Representatives

Dear Chairman Johnson:

IRS annually audits a number of tax returns to determine whether individual taxpayers have voluntarily complied with the tax laws and paid the proper amount of taxes. Section 7602 of the Internal Revenue Code defines an audit as an examination of a taxpayer's books and records for the purpose of determining the correct tax liability. To better use audit resources, IRS attempts to identify and audit returns with the greatest likelihood of noncompliance, while seeking a minimum degree of audit coverage for each type of taxpayer to advance voluntary compliance.

Compared to the 1960s and 1970s, the audit rate—the annual percentage of individual tax returns that IRS has audited of the total number of individual tax returns filed—has dropped, falling below 1 percent in fiscal year 1993. Although IRS believes that its audits induce voluntary taxpayer compliance, no one knows the actual impact, particularly given a decreasing audit rate. Data are available, however, to analyze both the trends in audit rates across the country and the results of these audits, such as the type of tax returns being audited and the productivity of the audits, measured by additional taxes recommended per return and per direct audit hour.

This report responds to your request that we provide information on (1) the trend in IRS' audit rates for individual returns and (2) the overall results of IRS' most recent audits of individual returns. We analyzed the most recent years of available IRS data, including fiscal years 1988 through 1995 for the trend in audit rates, and fiscal years 1992 through 1994 for the overall audit results. We did not attempt an in-depth analysis to identify the reasons for the audit trends and results; however, we obtained the views of IRS Examination Division officials concerning these trends and results.

Background

IRS believes that taxpayers are more likely to voluntarily comply with the tax laws if they believe that their return may be audited and unpaid taxes identified. In concert with audits, IRS uses other enforcement and nonenforcement methods. For example, IRS uses computers to match

information returns filed by banks and other third parties with individual tax returns so it can identify unreported income. In recent years, IRS has also emphasized taxpayer education and assistance to encourage voluntary compliance.

As part of its audit approach, IRS has established 10 audit classes for individual returns based on taxpayer income—5 involving returns without business income, and 5 involving returns with business income from self-employment. IRS tracks audit results by these audit classes and also by various audit sources—programs and techniques used to select potentially noncompliant returns for audit. Audit sources include, among others, suspected tax shelters, IRS and non-IRS referrals, compliance projects, and computer matches of third party information. One of the major audit sources—discriminant function (DIF)—involves returns selected solely because of a computer score¹ designed to predict individual tax returns most likely to result in additional taxes if audited. This scoring provides an objective way to select returns and has helped IRS avoid burdening potentially compliant taxpayers with an audit.

Traditionally, IRS has done two types of face-to-face audits from its district offices to review taxpayers' books and records in support of a filed return: (1) field audits, in which an IRS revenue agent visits an individual taxpayer who has business income or a very complex return and (2) office audits, in which a tax auditor at an IRS office is visited by an individual taxpayer who has a less complex return. Tax examiners at IRS service centers also review returns and third-party information, and contact taxpayers concerning potential discrepancies on their returns. These discrepancies include such items as unreported income, as well as unallowable credits, such as the Earned Income Credit (EIC).

Starting in fiscal year 1994, IRS decided to include all service center contacts by tax examiners as audits. IRS attributed this change to the fact that such contacts are part of its overall efforts to correct inaccurate returns. Unlike traditional field or office audits, these contacts usually involve a single tax issue on the return and do not involve a face-to-face audit. IRS is also counting other nontraditional types of work as audits, such as recent reviews of nonfilers² done by district office auditors.

¹To compute this score, IRS uses a statistical analysis technique known as DIF. This analysis relies on statistically valid data collected during IRS' periodic Taxpayer Compliance Measurement Program (TCMP), which involves detailed audits of a random sample of tax returns. The most recent TCMP for individuals covered tax year 1988.

²IRS began a 2-year initiative in fiscal year 1993, using up to 2,000 auditor staff years annually, to pursue potential nonfiler cases that IRS' Collection Division had not previously pursued.

After reviewing a taxpayer's support for the return, IRS auditors decide whether to recommend changes to tax liability. If a tax change is recommended, the taxpayer has the right to either agree with the recommended tax change or to appeal it through IRS' Office of Appeals or the courts. Depending on the outcome of such appeals, additional recommended tax revenue may or may not ultimately be assessed and collected.

Results in Brief

Between fiscal years 1988 and 1993, IRS' annual audit rates for individuals declined from 1.57 percent to a low of 0.92 percent. According to IRS officials, in fiscal years 1994 and 1995 these rates rebounded mainly because of IRS' nonfiler initiative and a recent emphasis on reviews of EIC claims. Coupled with the recent IRS decision to include all service center contacts in the annual audit rate, these actions contributed to an audit rate of 1.67 percent in fiscal year 1995.

Although generally higher for higher-income individuals, audit rates have generally decreased since fiscal year 1988 for the highest-income individuals, while increasing in the past 2 years for the lowest-income individuals. According to IRS officials, this is a direct result of the recent emphasis on nonfilers and EIC claims.

IRS' audit rates varied significantly in different parts of the country. For example, audit rates tended to be higher in IRS' Western and Southwestern Regions and lower in its Central and Midwest Regions. According to IRS officials, the variance among regions was consistent with IRS' Taxpayer Compliance Program (TCMP) data (which IRS periodically collects from detailed audits of a random sample of tax returns) that showed higher taxpayer noncompliance in the Western and Southwestern Regions compared to the Central and Midwest Regions.

In general, audits of the highest-income individuals resulted in more additional tax recommended per return than did audits of the lowest-income individuals—as much as 4 to 5 times more. However, the amount of additional tax recommended per direct audit hour for the highest-income individuals was less than twice the additional tax recommended for the lowest-income individuals. IRS Examination officials told us that although audits of the highest-income individuals usually result in substantially greater additional tax recommended per audit, they tend to be more complex and time consuming than do audits of the

lowest-income individuals, which tend to focus on single issues and take very little time to complete.

Objectives, Scope, and Methodology

Our objectives were to provide information on the overall trend in IRS' individual audit rates and on the overall results of IRS' most recent individual audits. We did the audit rate analysis for fiscal years 1988 through 1995 because published data were readily available for this period. We did the audit results analysis for fiscal years 1992 through 1994 because this was the most recent readily available data.

To determine the trend in IRS' audit rates, we reviewed IRS' annual reports for fiscal years 1987 through 1994 as well as unpublished data for fiscal year 1995. We collected information on the overall annual audit rates by type of taxpayer. We also collected information on the number of returns filed and the number of returns audited each year by IRS' regions and by the district offices within those regions. We reviewed this information to identify IRS' overall published audit rates for fiscal years 1988 through 1995, which included a combination of district office audits and service center contacts. To show what the overall rates would have been based solely on traditional district office audits, we recalculated these rates excluding service center contacts. We also used this information to calculate regional audit rates, both including and excluding service center contacts, as well as audit rates for each district office.

To determine the specific results of IRS' audit efforts for fiscal years 1992 through 1994, we analyzed IRS Audit Information Management System (AIMS) data. IRS uses AIMS to track its audits of tax returns, including the resources used and any additional taxes recommended. We obtained copies of AIMS tapes for each year from fiscal year 1992 through 1994 and did various analyses to generate overall results for each year by (1) 10 individual audit classes, (2) 15³ major audit sources, (3) 3 types of audit staff, and (4) 4 broad categories of audit closures.⁴ For each of these analyses, we determined the number and percentage of audited returns as well as the total direct hours and the total additional tax recommended for each year. From this information, we computed the direct hours per

³IRS has established over 40 varying audit sources; we selected the largest 14 sources from fiscal years 1992 through 1994 and combined the rest into an "other" category.

⁴An audit closure occurs when an audit is completed, after which a taxpayer can either agree or appeal if there is a proposed tax change; if there is no proposed tax change, the audit may be closed either with or without an adjustment to the return.

return, the taxes recommended per return, and the taxes recommended per direct hour for each year.

Other than reconciling totals from the AIMS database to IRS' annual reports, we did not verify the accuracy of the AIMS data. Nor did we attempt an in-depth analysis to identify the reasons for the audit rate trends and audit results. Rather, we asked IRS Examination officials at the National Office to review our analysis of the audit rate trends and the audit results and provide explanations. We requested comments on a draft of this report from the Commissioner of Internal Revenue. On March 26, 1996, several IRS Examination Division officials, including the Acting Assistant Commissioner (Examination); Director, Management and Analysis; and, Team Leader, Management and Analysis, as well as a representative from IRS' Office of Legislative Affairs, provided us with both oral and written comments. Their comments are summarized on page 14 and have been incorporated in this report where appropriate.

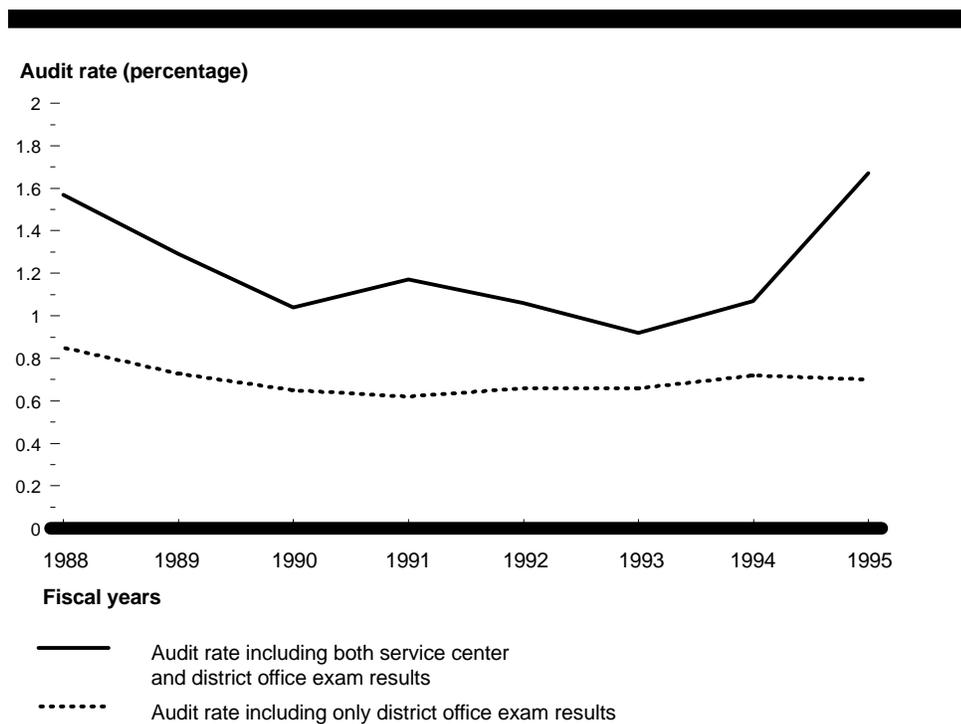
We performed our audit work in Washington, D.C., between August 1995 and February 1996 in accordance with generally accepted government auditing standards.

Trends in IRS' Audit Rates

Between fiscal years 1988 and 1993, IRS' audit rate for individuals decreased from 1.57 percent to 0.92 percent. IRS Examination Division officials told us that they attributed the decrease to more returns being filed by taxpayers; more time spent auditing complex returns by IRS auditors; and, an overall reduction in examination staffing. During fiscal years 1994 and 1995, the audit rate increased, reaching 1.67 percent by 1995. IRS officials told us they attributed this increase to the involvement of district office auditors in pursuing nonfiler cases and the increasing number of EIC claims reviewed by service center examination staff.

Starting in fiscal year 1994, IRS decided to include all service center contacts by tax examiners in its audit rates. As a result, when the annual statistics for fiscal years 1993 and 1994 were published, IRS also recomputed its audit rates for fiscal years 1988 through 1992 to include all service center contacts. Counting such work as part of the audit rate, coupled with IRS recent nonfiler and EIC emphasis, tended to produce higher audit rates, as most of this work takes less time to do than traditional face-to-face audits. Figure 1 shows the trend in individual audit rates from fiscal years 1988 through 1995, based on rates that both include and exclude service center results.

Figure 1: IRS' National Audit Rates, Including and Excluding Service Center Results, FYs 1988 Through 1995

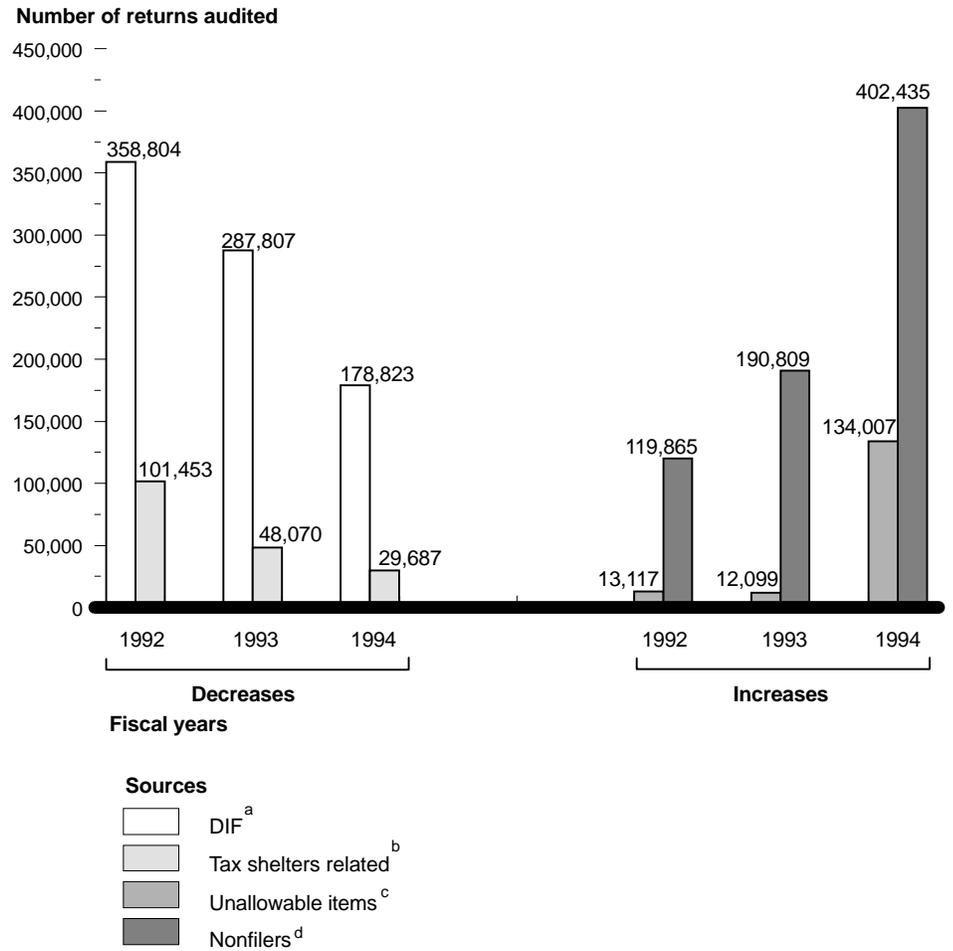


Source: GAO analysis of IRS data.

Major Audit Sources Reflect the Impact of Recent IRS Initiatives

In analyzing the audit results from fiscal year 1992 through 1994, we did an in-depth review of various sources of IRS' audits. Our analysis of these sources illustrated the shift from traditional audits to other types of work. Over these 3 years, four sources accounted for over half of IRS' audits. As shown in figure 2, two of these—returns selected because of DIF or potential tax shelters—declined by at least half, while the other two—returns involving potential nonfilers or unallowable items—at least tripled. The first two sources reflect traditional audits and the latter two sources reflect nontraditional work, such as the nonfiler initiative and EIC claims, respectively.

Figure 2: Number of Returns Audited for Selected IRS Audit Sources, FYs 1992 to 1994



^aComputer identified DIF-scored returns.

^bRelated returns of partners, grantors, beneficiaries, and shareholders identified during audits of either partnerships, fiduciaries, or Subchapter S corporations involving potential tax shelter issues.

^cReturns involving refundable credits and dependency exemptions, e.g., the EIC, initiated by service center examination staff.

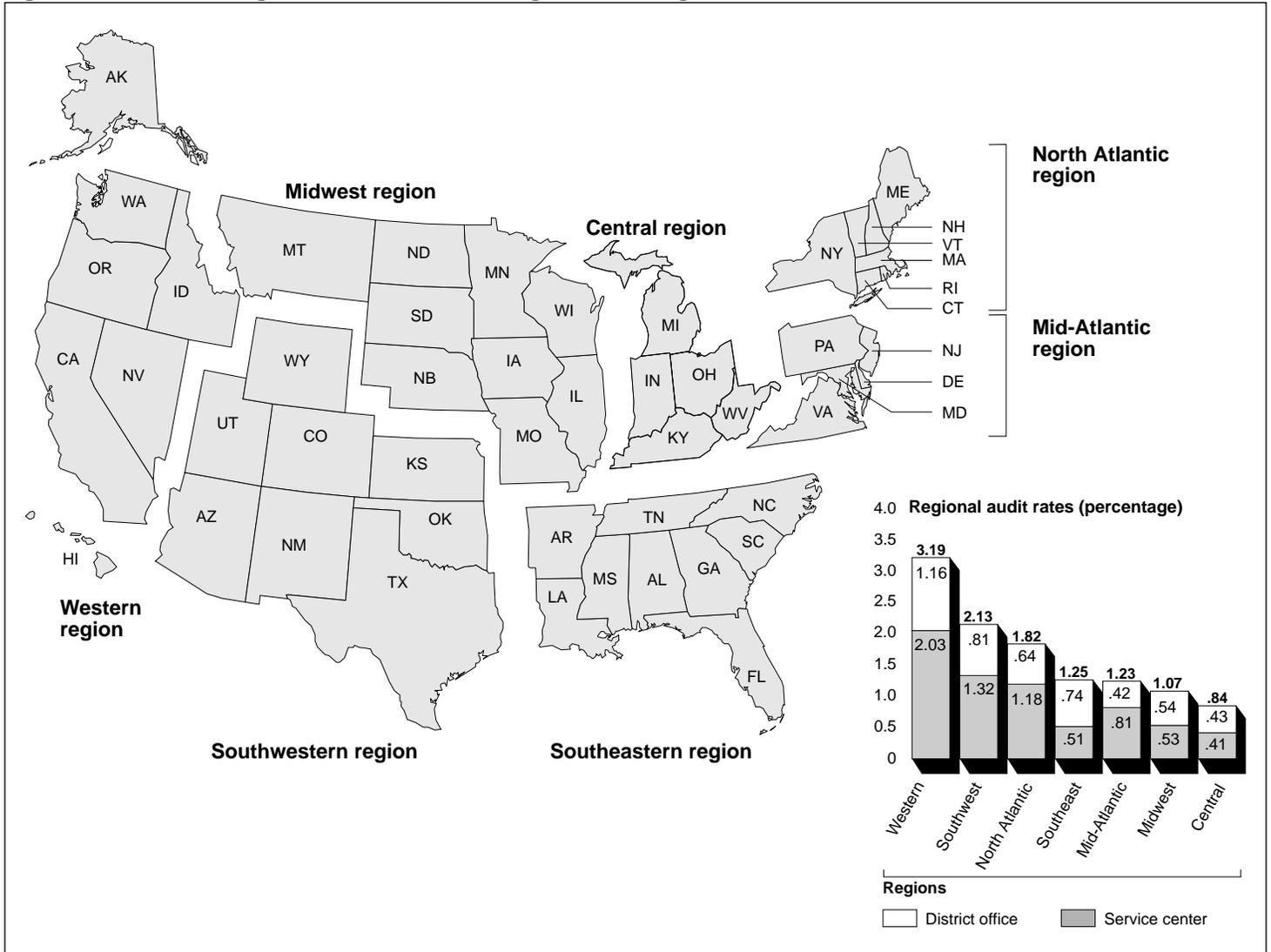
^dReturns involving known taxpayers who appeared to not file as required.

Source: GAO analysis of IRS data.

Audit Rates Varied by Geographic Location

IRS' individual audit rates varied widely by geographic location, regardless of whether service center contacts and other nontraditional audits were included. As figure 3 shows, for fiscal year 1995 the rates tended to be highest in the western regions of the country and lowest in the middle regions. IRS Examination Division officials told us that these trends were consistent with TCMP data, which showed higher taxpayer noncompliance in IRS' Western and Southwest Regions and lower taxpayer noncompliance in its Central and Midwest Regions. With few exceptions, these regional patterns largely held true from fiscal years 1988 through 1995. (See table I.1 for our analysis of regional audit rates.) Throughout this period, audit rates also varied widely by district office. (See table I.2 for our analysis of district office audit rates.)

Figure 3: IRS' FY 1995 Regional Audit Rates, Including and Excluding Service Center Results



Note 1: District rates include only district office results; service center rates include only service center results; overall rate includes district office and service center results.

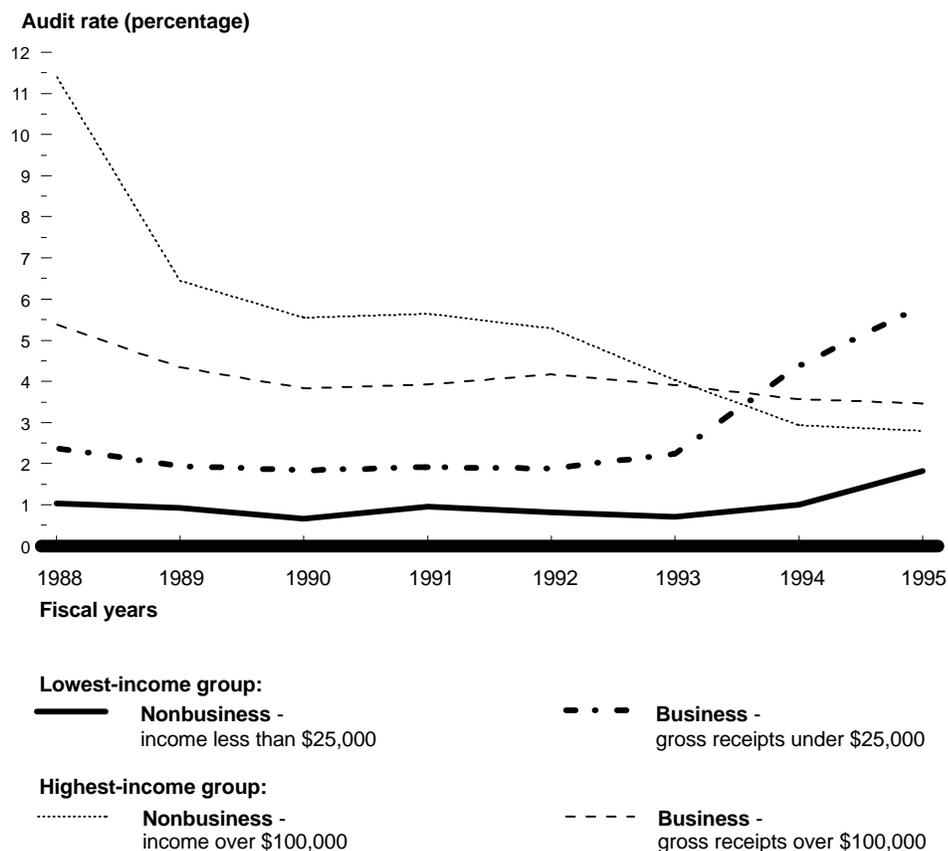
Note 2: Regional audit rate is the annual percentage of individual returns audited of the total individual returns filed in the region.

Source: GAO analysis of IRS data.

Audit Rates Varied Among Income Groups

Our analysis of the audit rates and audit results also identified patterns related to income reported by taxpayers. Our analysis focused on individuals who reported significant amounts of business income and individuals who did not report such income, (i.e., nonbusiness), particularly those that were in the lowest- and highest-income groups. Figure 4 shows that the IRS reported audit rates from fiscal years 1988 to 1995 (1) increased in the last 2 fiscal years among those in the lowest-income group (less than \$25,000), particularly for business individuals, for whom the rate more than doubled, and (2) decreased among those in the highest-income group (\$100,000 or more), particularly for nonbusiness individuals, for whom the fiscal year 1995 rate dropped to about one-fourth of what it had been in fiscal year 1988. IRS Examination Division officials said they attributed the increase in audit rates for the lowest-income groups, which generally occurred in fiscal years 1994 and 1995, to the nonfiler initiative and the recent emphasis on EIC. They said the decrease in audit rates for the highest-income nonbusiness individuals was due to an overall reduction in examination staffing coupled with an increase in the number of returns filed for this income group. (See table I.4 for our analysis of the audit rate trends for all income groups.)

Figure 4: Trend in Audit Rates for Business and Nonbusiness Individual Taxpayers, FYs 1988 Through 1995



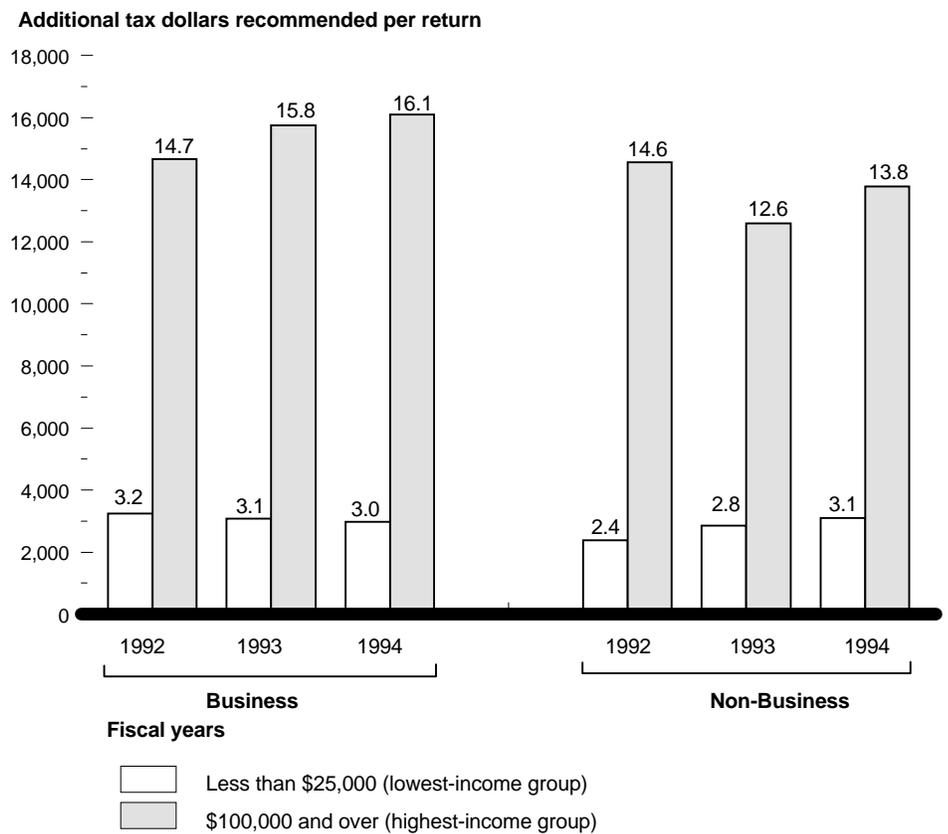
Source: GAO analysis of IRS data.

Audit Productivity Also Varied Among Income Groups

Concerning audit productivity measured by income groups, differing patterns emerged. In general, audits of the highest-income groups resulted in as much as 4 to 5 times more additional tax recommended per return—for both nonbusiness and business individuals—than did audits of the lowest-income groups. As figure 5 shows, from fiscal year 1992 to fiscal year 1994, additional taxes recommended per return (1) decreased among business individuals for the lowest-income group and increased for the highest-income group and (2) increased among nonbusiness individuals for the lowest-income group and decreased for the highest-income group. IRS Examination officials said the increases or decreases in additional taxes recommended from fiscal years 1992 to 1994 for both the highest-income business and nonbusiness individuals were

affected by the small number of individual tax returns that IRS audited as part of its Coordinated Examination Program. This program is designed to audit the largest corporations; individual taxpayers audited under this program are usually corporate officers or shareholders.

Figure 5: Additional Taxes Recommended Per Return for Selected Audit Classes, FYs 1992 to 1994

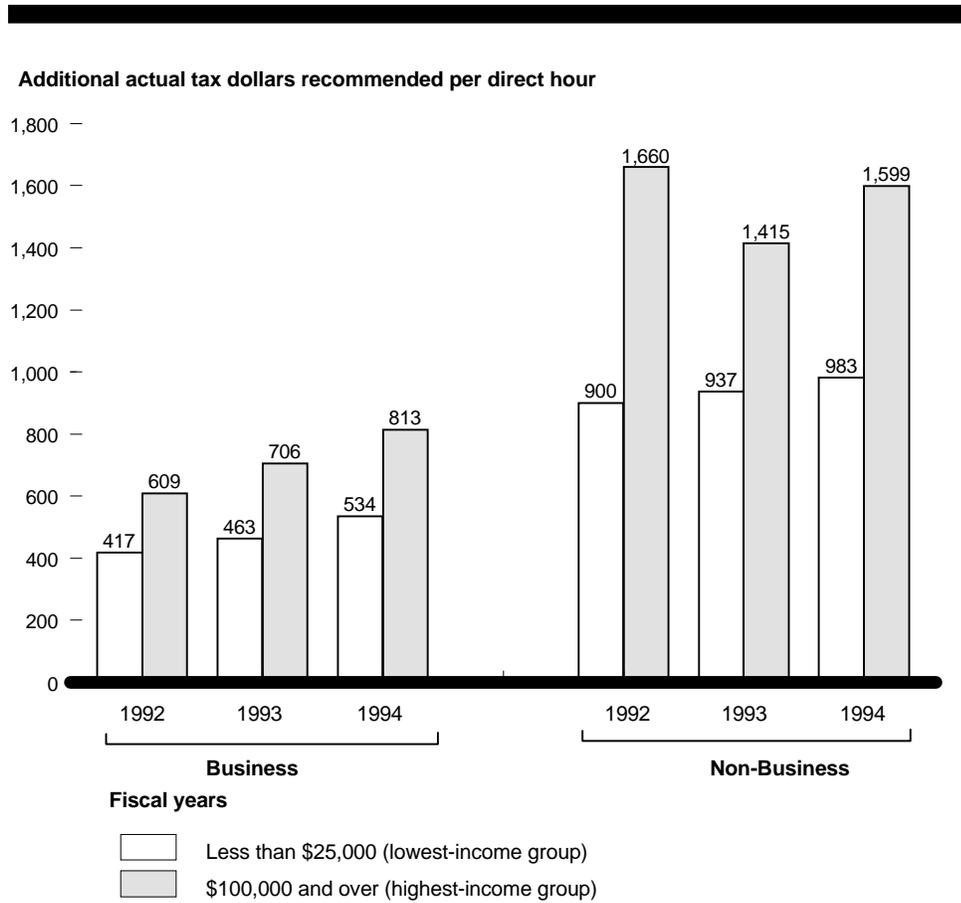


Source: GAO analysis of IRS data.

Another measure of audit productivity is the amount of additional taxes recommended for each direct audit hour used to complete the audit. Whereas from fiscal years 1992 to 1994, the amount of additional taxes recommended per direct hour was similar to the amount of additional taxes recommended per return for nonbusiness individuals; however,

these amounts differed for business individuals. As figure 6 shows, from fiscal years 1992 to 1994, taxes recommended per direct hour (1) among business individuals increased for both the lowest- and highest-income groups and (2) increased among nonbusiness individuals for the lowest-income group and decreased for the highest-income group. (See tables II.1 through II.3 for an overall analysis of the results of audits by income classes.)

Figure 6: Additional Taxes Recommended Per Audit Hour for Selected Audit Classes, FYs 1992 to 1994



Source: GAO analysis of IRS data.

We provide more detailed information from our analyses of various other elements of both the audit rates and the audit results in appendixes I and II. Such elements include audit rates by IRS district offices (tables I.2 and I.3), audit results on whether or not the IRS auditor recommended additional taxes, and if so, whether the taxpayer appealed the additional taxes recommended (tables II.10 through II.12), and the no-change rate for selected audit sources (table II.13).

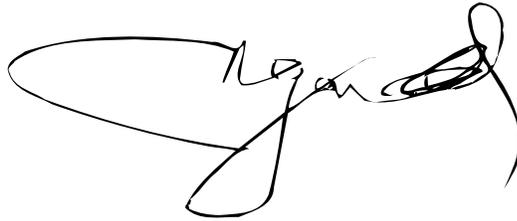
Agency Comments and Our Evaluation

We requested comments on a draft of this report from the Commissioner of Internal Revenue or her designated representative. Responsible IRS Examination Division officials, including the Acting Assistant Commissioner (Examination); Director, Management and Analysis; and, Team Leader, Management and Analysis, as well as a representative from IRS' Office of Legislative Affairs provided IRS' comments in a March 26, 1996, meeting. They basically agreed with the information presented in the report and provided additional explanations for some of the audit trends and results, such as (1) the downward trend in overall audit rates, as well as the rate for the highest-income nonbusiness individuals, from fiscal years 1988 to 1993; (2) the increases or decreases in additional taxes recommended for the highest-income business and nonbusiness individuals from fiscal years 1992 to 1994; (3) the decrease in additional taxes recommended for the lowest-income business individuals from fiscal years 1992 to 1994; and (4) the amount of additional tax recommended per direct hour for the highest-income individuals compared to that for the lowest-income individuals. In response to their comments, we have incorporated the additional explanations in the report where appropriate.

As agreed with you, unless you announce the contents of this report earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies of this report to various congressional committees, the Commissioner of Internal Revenue, and other interested parties. We also will make copies available to others upon request.

The major contributors to this report are listed in Appendix III. If you have any questions concerning this report, please contact me at (202) 512-9044.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Natwar M. Gandhi". The signature is fluid and cursive, with a large loop on the left side and a smaller loop on the right side.

Natwar M. Gandhi
Associate Director, Tax Policy
and Administration Issues

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Abbreviations

AIMS	Audit Information Management System
DIF	Discriminant Function
EIC	Earned Income Credit
IRS	Internal Revenue Service
TCMP	Taxpayer Compliance Measurement Program
TGR	Total Gross Receipts
TPI	Total Positive Income

The Trend in IRS Individual Audit Rates for Fiscal Years 1988 Through 1995

This appendix presents our analysis of the trend in IRS' individual audit rates from fiscal year 1988 through fiscal year 1995. The audit rate is the percentage of individual tax returns that IRS has audited of the total number of individual tax returns filed. The appendix includes a comparison of IRS' published annual audit rates, which include both district office and service center results, with recomputed audit rates that we derived by excluding service center results. It also presents trends in individual audit rates by geographic location as well as by various income groups.

Table I.1: Comparison of IRS Individual Audit Rates, Including and Excluding Service Center Results, FYs 1988 Through 1995

Location	Audit rate by fiscal year							
	1988	1989	1990	1991	1992	1993	1994	1995
United States	1.57%	1.29%	1.04%	1.17%	1.06%	0.92%	1.07%	1.67%
United States	0.85	0.73	0.65	0.62	0.66	0.66	0.72	0.70
North Atlantic	1.83	1.27	1.07	1.15	1.06	0.91	1.03	1.82
North Atlantic	0.73	0.64	0.55	0.53	0.54	0.50	0.59	0.64
Mid-Atlantic	0.99	0.85	0.70	0.65	0.62	0.53	0.70	1.23
Mid-Atlantic	0.64	0.57	0.46	0.41	0.41	0.41	0.47	0.42
Southeast	1.40	1.38	1.14	1.17	1.16	0.98	0.99	1.25
Southeast	0.77	0.73	0.71	0.75	0.76	0.75	0.79	0.74
Central	1.23	1.03	0.85	0.79	0.80	0.66	0.71	0.84
Central	0.66	0.64	0.53	0.47	0.49	0.43	0.47	0.43
Midwest	1.31	1.05	0.79	0.71	0.71	0.64	0.85	1.07
Midwest	0.81	0.66	0.52	0.47	0.43	0.45	0.67	0.54
Southwest	2.45	2.05	1.48	1.37	1.27	1.28	1.37	2.13
Southwest	1.16	0.88	0.82	0.77	0.75	0.79	0.83	0.81
Western	1.82	1.44	1.19	2.13	1.62	1.33	1.75	3.19
Western	1.18	0.96	0.89	0.86	1.05	1.10	1.09	1.16

Note: IRS audit rates, which include both service center and district office results, are in bold. All others are GAO's recomputed audit rates, which include only district office results.

Source: GAO analysis of IRS data.

Appendix I
The Trend in IRS Individual Audit Rates for
Fiscal Years 1988 Through 1995

Table I.2: IRS Individual Audit Rates by District Office, FYs 1988 Through 1995

Region/District	Audit rate by fiscal year							
	1988	1989	1990	1991	1992	1993	1994	1995
North Atlantic								
Brooklyn	0.69%	0.52%	0.43%	0.41%	0.48%	0.42%	0.47%	0.59%
Boston	0.57	0.50	0.41	0.41	0.43	0.36	0.51	0.48
Buffalo	0.66	0.59	0.52	0.41	0.44	0.48	0.52	0.47
Manhattan	1.39	1.23	0.98	0.79	0.78	0.62	0.77	1.07
Hartford	0.63	0.61	0.61	0.52	0.64	0.64	0.79	0.79
Albany	0.52	0.52	0.45	0.47	0.44	0.41	0.41	0.35
Augusta	0.56	0.45	0.38	0.42	0.43	0.59	0.74	0.66
Portsmouth	0.56	0.69	0.54	0.60	0.75	0.73	0.67	0.65
Providence	0.82	0.82	0.74	0.71	0.87	0.84	0.94	0.96
Burlington	0.82	0.65	0.58	2.22	0.66	0.61	0.73	0.64
Mid-Atlantic								
Newark	0.57	0.50	0.36	0.35	0.39	0.42	0.39	0.39
Philadelphia	0.64	0.50	0.37	0.29	0.31	0.33	0.43	0.42
Richmond	0.60	0.59	0.51	0.49	0.48	0.48	0.62	0.45
Baltimore	0.78	0.69	0.50	0.47	0.45	0.39	0.46	0.45
Pittsburgh	0.64	0.62	0.69	0.52	0.46	0.43	0.45	0.36
Wilmington	0.82	1.00	0.83	0.62	0.66	0.62	0.80	0.59
Southeast								
Jacksonville	0.70	0.62	0.65	0.67	0.69	0.67	0.70	0.57
Greensboro	0.54	0.50	0.41	0.44	0.46	0.48	0.50	0.57
Atlanta	1.07	0.90	0.86	0.90	0.92	1.07	1.11	1.14
Ft. Lauderdale	0.76	0.93	0.95	0.87	0.84	0.82	0.88	0.68
Nashville	0.77	0.73	0.66	0.71	0.77	0.62	0.62	0.54
New Orleans	0.89	1.00	1.00	1.19	1.07	0.91	1.02	0.90
Birmingham	0.85	0.63	0.64	0.59	0.65	0.61	0.64	0.74
Columbia	0.54	0.56	0.49	0.60	0.56	0.63	0.64	0.54
Jackson	0.94	0.83	0.72	0.86	0.95	0.92	1.12	1.15
Little Rock	0.69	0.70	0.82	0.92	1.01	0.96	0.92	0.92
Central								
Detroit	0.62	0.58	0.46	0.42	0.45	0.40	0.53	0.47
Cleveland	0.59	0.70	0.58	0.52	0.52	0.40	0.33	0.33
Indianapolis	0.78	0.75	0.57	0.50	0.53	0.51	0.63	0.60
Cincinnati	0.73	0.52	0.50	0.43	0.44	0.36	0.35	0.33
Louisville	0.61	0.71	0.63	0.50	0.54	0.53	0.43	0.32
Parkersburg	0.65	0.60	0.52	0.54	0.54	0.46	0.49	0.47

(continued)

Appendix I
The Trend in IRS Individual Audit Rates for
Fiscal Years 1988 Through 1995

Region/District	Audit rate by fiscal year							
	1988	1989	1990	1991	1992	1993	1994	1995
Midwest								
Chicago	0.90	0.73	0.50	0.34	0.38	0.39	0.78	0.56
St. Louis	0.75	0.60	0.52	0.46	0.44	0.61	0.79	0.55
Milwaukee	0.55	0.45	0.34	0.31	0.24	0.25	0.32	0.47
St. Paul	0.88	0.69	0.62	0.54	0.50	0.53	0.82	0.58
Springfield	0.86	0.64	0.49	0.49	0.43	0.39	0.40	0.39
Des Moines	0.74	0.61	0.54	0.49	0.47	0.39	0.74	0.52
Omaha	0.85	0.68	0.55	0.57	0.45	0.57	0.55	0.54
Helena	1.06	1.11	0.95	0.81	0.82	0.79	0.85	0.68
Aberdeen	0.70	0.75	0.59	0.62	0.57	0.67	0.81	0.61
Fargo	1.17	0.96	0.93	1.86	1.11	0.78	0.90	0.90
Southwest								
Dallas	1.19	0.83	0.83	0.81	0.80	0.82	0.90	1.04
Austin	1.15	0.91	0.83	0.72	0.67	0.71	0.72	0.73
Houston	1.53	1.14	1.09	0.85	0.75	0.81	0.86	0.79
Denver	1.11	0.93	0.79	0.93	0.87	0.81	0.93	0.88
Phoenix	0.96	0.80	0.75	0.71	0.80	0.78	0.81	0.70
Oklahoma City	1.33	0.86	0.80	0.89	0.92	0.97	1.08	0.81
Wichita	0.83	0.63	0.65	0.61	0.51	0.89	0.73	0.55
Salt Lake City	1.09	0.78	0.61	0.51	0.48	0.58	0.58	0.72
Albuquerque	0.81	0.83	0.59	0.54	0.63	0.63	0.48	0.63
Cheyenne	1.46	1.13	1.16	0.93	0.90	0.76	0.86	0.92
Western								
Laguna Niguel	1.31	1.12	0.91	0.91	1.10	1.28	1.14	1.57
Los Angeles	1.24	1.01	1.06	1.13	1.37	1.39	1.32	1.34
San Jose	1.22	0.97	0.72	0.85	0.93	0.86	0.74	0.92
Seattle	0.92	0.63	0.65	0.63	0.79	0.75	0.76	0.65
Sacramento	0.98	1.00	0.81	0.57	0.88	0.89	0.89	1.06
San Francisco	1.46	1.08	1.20	0.99	1.30	1.60	1.57	1.36
Portland	0.72	0.55	0.57	0.49	0.52	0.58	0.64	0.66
Honolulu	0.72	0.46	0.45	0.37	0.41	0.47	0.46	0.66
Las Vegas	2.06	1.79	1.84	1.57	1.95	2.02	3.08	2.02
Boise	1.15	0.92	0.89	0.71	0.93	1.13	1.15	1.12
Anchorage	2.08	1.15	1.49	1.87	1.36	1.15	1.30	1.07
International	1.06	0.92	0.88	0.52	0.52	0.29	0.19	0.19

Source: GAO analysis of IRS data.

Appendix I
The Trend in IRS Individual Audit Rates for
Fiscal Years 1988 Through 1995

Table I.3: IRS Districts With the Highest and Lowest Individual Audit Rates, FYs 1988 Through 1995

Districts	Audit rate by fiscal year							
	1988	1989	1990	1991	1992	1993	1994	1995
Highest rates								
Anchorage	2.08%	1.15%	1.49%	1.87%	1.36%	1.15%	1.30%	1.07%
Las Vegas	2.06	1.79	1.84	1.57	1.95	2.02	3.08	2.02
Cheyenne	1.46	1.13	1.16	0.93	0.90	0.76	0.86	0.92
San Francisco	1.46	1.08	1.20	0.99	1.30	1.60	1.57	1.36
Laguna Niguel	1.31	1.12	0.91	0.91	1.10	1.28	1.14	1.57
Los Angeles	1.24	1.01	1.06	1.13	1.37	1.39	1.32	1.34
Boise	1.15	0.92	0.89	0.71	0.93	1.13	1.15	1.12
Atlanta	1.07	0.90	0.86	0.90	0.92	1.07	1.11	1.14
Lowest rates								
Albany	0.52	0.52	0.45	0.47	0.44	0.41	0.41	0.35
Milwaukee	0.55	0.45	0.34	0.31	0.24	0.25	0.32	0.47
Boston	0.57	0.50	0.41	0.41	0.43	0.36	0.51	0.48
Newark	0.57	0.50	0.36	0.35	0.39	0.42	0.39	0.39
Detroit	0.62	0.58	0.46	0.42	0.45	0.40	0.53	0.47
Philadelphia	0.64	0.50	0.37	0.29	0.31	0.33	0.43	0.42
Cincinnati	0.73	0.52	0.50	0.43	0.44	0.36	0.35	0.33
Baltimore	0.78	0.69	0.50	0.47	0.45	0.39	0.46	0.45

Note: Districts with the 15 highest or lowest audit rates for at least 6 of 8 years during fiscal years 1988 through 1995.

Source: GAO analysis of IRS data.

Appendix I
The Trend in IRS Individual Audit Rates for
Fiscal Years 1988 Through 1995

Table I.4: IRS Audit Rates by Individual Audit Class: Nonbusiness and Business Returns, FYs 1988 Through 1995

Audit class	Audit rates by fiscal year							
	1988	1989	1990	1991	1992	1993	1994	1995
Nonbusiness returns								
1040A, TPI < \$25,000	1.03%	1.03%	0.55%	0.94%	0.78%	0.74%	1.04%	1.96%
Non-1040A, TPI < \$25,000	1.04	0.82	0.91	1.03	0.92	0.66	0.88	1.30
TPI \$25,000 < \$50,000	1.72	1.31	0.97	0.77	0.70	0.58	0.53	0.90
TPI \$50,000 < \$100,000	1.53	1.46	1.38	1.24	1.10	0.88	0.72	1.05
TPI \$100,00 and over	11.41	6.45	5.55	5.64	5.28	4.03	2.94	2.79
Business returns								
C-TGR < \$25,000	2.38	1.94	1.84	1.91	1.89	2.24	4.39	5.85
C-TGR \$25,000 < \$100,000	3.09	2.50	2.35	2.22	2.28	2.41	3.01	3.08
C-TGR \$100,000 and over	5.38	4.35	3.84	3.92	4.17	3.91	3.57	3.47
F-TGR < \$100,000	1.59	1.38	1.67	1.53	1.28	1.06	1.16	1.23
F-TGR \$100,000 and over	4.35	2.49	3.09	3.98	2.40	2.06	1.74	2.51

Legend

1040A = nonbusiness returns filed by individuals
TPI = total positive income (Income from positive sources only)
C-TGR = Form 1040 Schedule C (Profit or Loss from Business) total gross receipts
F-TGR = Form 1040 Schedule F (Profit or Loss from Farming) total gross receipts

Source: GAO analysis of IRS data.

The Results of IRS Individual Audits for Fiscal Years 1992 to 1994

This appendix presents our analysis of the results of IRS' individual audits from fiscal year 1992 through fiscal year 1994. It includes information on the number of individual returns audited; the amount of direct hours and additional taxes recommended resulting from these audits; and a computation of the direct hours per return, as well as the additional taxes recommended per return and per direct hour, for the following four categories: (1) taxpayer income groups, (2) audit sources, (3) types of audit staff, and (4) types of audit closures.

Table II.1: Number of Individual Returns Audited by Audit Class, FYs 1992 Through 1994

Audit class	Number and percentage of returns					
	Fiscal year 1992		Fiscal year 1993		Fiscal year 1994	
	Number	Percent	Number	Percent	Number	Percent
1040A, TPI < \$25,000	338,683	28%	315,469	30%	470,723	38%
Non 1040A, TPI < \$25,000	172,557	14	125,697	12	129,132	11
TPI \$25,000 < \$50,000	191,166	16	159,070	15	143,243	12
TPI \$50,000 < \$100,000	150,905	13	127,484	12	110,193	9
TPI \$100,000 and over	167,394	14	136,908	13	110,004	9
C-TGR < \$25,000	41,293	3	51,934	5	106,169	9
C-TGR \$25,000 < \$100,000	64,070	5	69,253	7	87,561	7
C-TGR \$100,000 and over	65,939	5	61,768	6	57,766	5
F-TGR < \$100,000	7,333	1	5,980	1	6,203	1
F-TGR \$100,000 and over	6,679	1	5,403	1	4,713	0
Total	1,206,019	100%	1,058,966	102%	1,225,707	101%

Legend

1040A = nonbusiness returns filed by individuals

TPI = total positive income (income from positive sources only)

C-TGR = Form 1040 Schedule C (Profit or Loss from Business) total gross receipts

F-TGR = Form 1040 Schedule F (Profit or Loss from Farming) total gross receipts

Note: Percentages are the percent of total individual audits for the year and have been rounded to the nearest whole percent.

Source: GAO analysis of IRS data.

Appendix II
The Results of IRS Individual Audits for
Fiscal Years 1992 to 1994

Table II.2: Direct Audit Hours and Additional Recommended Tax by Audit Class, FYs 1992 Through 1994

Dollars rounded to nearest thousand

Audit class	Direct audit hours			Additional tax recommended		
	1992	1993	1994	1992	1993	1994
1040A, TPI < \$25,000	682,099	779,762	1,327,898	\$ 851,498	\$ 923,444	\$ 1,458,449
Non-1040A, TPI < \$25,000	669,346	560,972	569,194	365,082	332,917	406,007
TPI \$25,000 < \$50,000	1,036,641	879,258	756,338	523,852	494,225	392,401
TPI \$50,000 < \$100,000	1,049,245	845,911	692,853	497,592	469,763	422,755
TPI \$100,00 and over	1,469,274	1,219,437	948,220	2,439,614	1,725,394	1,516,202
C-TGR < \$25,000	321,615	344,307	590,905	134,133	159,564	315,412
C-TGR \$25,000 < \$100,000	825,277	725,075	765,024	404,824	455,335	570,837
C-TGR \$100,000 and over	1,586,402	1,378,512	1,142,811	966,855	972,900	929,553
F-TGR < \$100,000	66,266	47,541	43,316	16,597	12,295	15,676
F-TGR \$100,000 and over	129,366	87,292	67,053	108,378	107,257	139,734

Legend

1040A = nonbusiness returns filed by individuals
TPI = total positive income (Income from positive sources only)
C-TGR = Form 1040 Schedule C (Profit or Loss from Business) total gross receipts
F-TGR = Form 1040 Schedule F (Profit or Loss from Farming) total gross receipts

Source: GAO analysis of IRS data.

Appendix II
The Results of IRS Individual Audits for
Fiscal Years 1992 to 1994

Table II.3: Audit Productivity by Audit Class, FYs 1992 Through 1994

Audit class	Direct audit hours per return			Taxes recommended per return			Taxes recommended per direct hour		
	1992	1993	1994	1992	1993	1994	1992	1993	1994
1040A, TPI < \$25,000	2.01	2.47	2.82	\$ 2,514	\$ 2,927	\$ 3,098	\$1,248	\$1,184	\$1,098
Non-1040A, TPI < \$25,000	3.88	4.46	4.41	2,116	2,649	3,144	545	593	713
TPI \$25,000 < \$50,000	5.42	5.53	5.28	2,740	3,107	2,739	505	562	519
TPI \$50,000 < \$100,000	6.95	6.64	6.29	3,297	3,685	3,837	474	555	610
TPI \$100,00 and over	8.78	8.91	8.62	14,574	12,603	13,783	1,660	1,415	1,599
C-TGR < \$25,000	7.79	6.63	5.57	3,248	3,072	2,971	417	463	534
C-TGR \$25,000 < \$100,000	12.88	10.47	8.74	6,318	6,575	6,519	491	628	746
C-TGR \$100,000 and over	24.06	22.32	19.78	14,663	15,751	16,092	609	706	813
F-TGR < \$100,000	9.04	7.95	6.98	2,263	2,056	2,527	250	259	362
F-TGR \$100,000 and over	19.37	16.16	14.23	16,227	19,851	29,649	838	1,229	2,084

Legend

1040A = nonbusiness returns filed by individuals
TPI = total positive income (Income from positive sources only)
C-TGR = Form 1040 Schedule C (Profit or Loss from Business) total gross receipts
F-TGR = Form 1040 Schedule F (Profit or Loss from Farming) total gross receipts

Note: Dollars rounded to the nearest whole dollar.

Source: GAO analysis of IRS data.

Table II.4: Number of Individual Returns Audited by Examination Position, FYs 1992 Through 1994

Examination position	Number and percentage of returns					
	Fiscal year 1992		Fiscal year 1993		Fiscal year 1994	
	Number	Percent	Number	Percent	Number	Percent
Revenue agents	210,166	17%	250,712	24%	364,016	30%
Tax auditors	536,640	45	505,539	48	456,216	37
Tax examiners	459,213	38	302,715	29	405,475	33
Total	1,206,019	100%	1,058,966	101%	1,225,707	100%

Note: Percentages are the percent of total individual audits for the year and have been rounded to the nearest whole percent.

Source: GAO analysis of IRS data.

Appendix II
The Results of IRS Individual Audits for
Fiscal Years 1992 to 1994

Table II.5: Direct Audit Hours and Additional Tax Recommended by Examination Position, FYs 1992 Through 1994

Dollars rounded to nearest thousand

Examination position	Direct audit hours			Additional tax recommended		
	1992	1993	1994	1992	1993	1994
Revenue agents	4,941,483	4,306,076	4,484,756	\$3,919,209	\$3,425,739	\$3,950,704
Tax auditors	2,334,506	2,140,219	1,963,335	1,223,307	1,327,048	1,420,275
Tax examiners	559,541	421,770	455,521	1,165,908	900,307	796,047

Source: GAO analysis of IRS data.

Table II.6: Audit Productivity by Examination Position, FYs 1992 Through 1994

Examination position	Direct audit hours per return			Taxes recommended per return			Taxes recommended per direct hour		
	1992	1993	1994	1992	1993	1994	1992	1993	1994
Revenue agents	23.51	17.18	12.32	\$18,648	\$13,664	\$10,853	\$793	\$796	\$881
Tax auditors	4.35	4.23	4.30	2,280	2,625	3,113	524	620	723
Tax examiners	1.22	1.39	1.12	2,539	2,974	1,963	2,084	2,135	1,748

Note: Dollars have been rounded to the nearest whole dollar.

Source: GAO analysis of IRS data.

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The Results of IRS Individual Audits for
Fiscal Years 1992 to 1994**

Table II.7: Number of Individual Returns Audited by Audit Sources, FYs 1992 Through 1994

Audit sources	Fiscal year 1992		Fiscal year 1993		Fiscal year 1994	
	Number	Percent	Number	Percent	Number	Percent
DIF	358,804	30%	287,807	27%	178,823	15%
Nonfilers	119,865	10	190,809	18	402,435	33
Tax shelter related	101,453	8	48,070	5	29,687	2
Self-employment tax	71,126	6	46,310	4	43,032	4
DIF multiyear	61,551	5	51,617	5	38,180	3
Regular classification	52,528	4	50,709	5	47,170	4
State information	48,418	4	3,564	0	4,573	0
Service center studies and tests	43,333	4	20,059	2	22,825	2
Compliance projects	40,403	3	44,267	4	41,959	3
Claims for refund	33,163	3	37,203	4	26,412	2
DIF related	32,090	3	32,692	3	22,554	2
Return preparers	27,706	2	28,231	3	27,708	2
Non-DIF multiyear	26,866	2	29,373	3	26,742	2
Unallowable items	13,117	1	12,099	1	134,007	11
Other sources	175,596	15	176,156	16	179,600	15
Total	1,206,019	100%	1,058,966	100%	1,225,707	100%

Note 1: See glossary for definition of terms used in this table.

Note 2: Percentages are the percent of total audits for the year and have been rounded to the nearest whole percent.

Source: GAO analysis of IRS data.

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The Results of IRS Individual Audits for
Fiscal Years 1992 to 1994

Table II.8: Direct Audit Hours and Additional Recommended Tax by Audit Source, FYs 1992 Through 1994

Dollars rounded to nearest thousand

Audit source	Direct audit hours			Additional tax recommended		
	1992	1993	1994	1992	1993	1994
DIF	3,272,708	2,401,818	1,529,068	\$985,975	\$884,954	\$776,252
Nonfilers	120,009	609,587	2,097,658	540,828	859,618	2,143,788
Tax shelter related	275,870	153,785	88,541	467,443	455,858	170,780
Self-employment tax	84,659	74,168	82,373	83,301	61,717	63,861
DIF multiyear	673,995	535,756	368,151	356,591	368,611	285,089
Regular classification	255,628	209,782	187,845	127,149	127,892	127,993
State information	31,895	19,424	17,865	46,898	27,029	22,110
Service center studies and tests	42,892	32,377	70,024	36,727	55,721	48,512
Compliance projects	303,224	311,120	275,226	220,111	207,895	203,778
Claims for refund	84,822	92,807	85,048	63,305	47,506	31,232
DIF related	411,627	398,175	299,706	426,792	293,627	276,142
Return preparers	169,005	148,753	125,572	58,544	58,508	63,758
Non-DIF multiyear	374,002	323,690	300,065	521,406	287,462	408,369
Unallowable items	20,505	21,030	59,474	12,078	14,537	126,118
Other sources	1,714,692	1,535,793	1,316,995	2,361,274	1,902,160	1,419,244
Total	7,835,530	6,868,066	6,903,611	\$6,308,424	\$5,653,094	\$6,167,026

Note: See glossary for definition of terms used in this table.

Source: GAO analysis of IRS data.

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Table II.9: Audit Productivity by Audit Source, FYs 1992 Through 1994

Audit source	Direct audit hours per return			Taxes recommended per return			Taxes recommended per direct hour		
	1992	1993	1994	1992	1993	1994	1992	1993	1994
DIF	9.12	8.35	8.55	\$2,748	\$3,075	\$4,341	\$301	\$368	\$508
Tax shelter related	2.72	3.20	2.98	4,607	9,483	5,753	1,694	2,964	1,929
State information	0.66	5.45	3.91	969	7,584	4,835	1,470	1,392	1,238
Self-employment tax	1.19	1.60	1.91	1,171	1,333	1,484	984	832	775
DIF multiyear	10.95	10.38	9.64	5,793	7,141	7,467	529	688	774
Service center studies and tests	0.99	1.61	3.07	848	2,778	2,125	856	1,721	693
Claims for refund	2.56	2.49	3.22	1,909	1,277	1,182	746	512	367
DIF related	12.83	12.18	13.29	13,300	8,982	12,244	1,037	737	921
Regular classification	4.87	4.14	3.98	2,421	2,522	2,713	497	610	681
Non-DIF multiyear	13.92	11.02	11.22	19,408	9,787	15,271	1,394	888	1,361
Nonfilers	1.00	3.19	5.21	4,512	4,505	5,327	4,507	1,410	1,022
Unallowable items	1.56	1.74	.44	921	1,202	941	589	691	2,121
Compliance projects	7.51	7.03	6.56	5,448	4,696	4,857	726	668	740
Return preparers	6.10	5.27	4.53	2,113	2,072	2,301	346	393	508
Other sources	9.77	8.72	7.33	13,447	10,798	7,902	1,377	1,239	1,078
Total	6.50	6.49	5.63	5,231	5,338	5,031	805	823	893

Note 1: See glossary for definition of terms used in this table.

Note 2: Dollars rounded to the nearest whole dollar.

Source: GAO analysis of IRS data.

Table II.10: Number of Returns Audited by Type of Closure, FYs 1992 Through 1994

Type of closure	Number and percentage of returns					
	Fiscal year 1992		Fiscal year 1993		Fiscal year 1994	
	Number	Percent	Number	Percent	Number	Percent
Agreed	895,905	74%	744,442	70%	844,848	69%
Appealed	64,239	5	57,010	5	49,778	4
No change with adjustments	62,386	5	112,186	11	168,231	14
No change without adjustments	183,489	15	145,328	14	162,850	13
Total	1,206,019	100%	1,058,966	100%	1,225,707	100%

Note: Percentages are the percent of total individual audits for the year and have been rounded to the nearest whole percent.

Source: GAO analysis of IRS data.

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The Results of IRS Individual Audits for
Fiscal Years 1992 to 1994

Table II.11: Direct Audit Hours and Additional Tax Recommended by Type of Closure, FYs 1992 Through 1994

Dollars rounded to nearest thousand

Type of closure	Direct audit hours			Additional tax recommended		
	1992	1993	1994	1992	1993	1994
Agreed	5,236,378	4,452,221	4,454,030	\$3,560,822	\$3,427,851	\$3,992,453
Appealed	1,326,168	1,116,546	920,893	2,705,925	1,982,679	1,715,805
No change with adjustments	430,643	613,840	963,405	41,678	242,564	458,768
No change without adjustments	842,342	685,459	565,284	0	0	0

Source: GAO analysis of IRS data.

Table II.12: Audit Productivity by Type of Closure, FYs 1992 Through 1994

Type of closure	Direct audit hours per return			Taxes recommended per return			Taxes recommended per direct hour		
	1992	1993	1994	1992	1993	1994	1992	1993	1994
Agreed	5.84	5.98	5.27	\$3,975	\$4,605	\$4,726	\$680	\$770	\$896
Appealed	20.64	19.59	18.50	42,123	34,778	34,469	2,040	1,776	1,863
No change with adjustments	6.90	5.47	5.73	668	2,162	2,727	97	395	476
No change without adjustments	4.59	4.72	3.47	0	0	0	0	0	0

Note: Dollars rounded to the nearest whole dollar.

Source: GAO analysis of IRS data.

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The Results of IRS Individual Audits for
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Table II.13: Number of Audits Resulting in No Change Without Adjustment, FYs 1992 Through 1994

Audit source	Fiscal year 1992			Fiscal year 1993			Fiscal year 1994		
	Returns	Number	Percent	Returns	Number	Percent	Returns	Number	Percent
DIF	358,804	71,641	20%	287,807	55,384	19%	178,823	34,956	20%
Nonfilers	119,865	4,199	4	190,809	5,832	3	402,435	5,320	1
Tax shelter related	101,453	26,639	26	48,070	13,171	27	29,687	10,177	34
Self-employment tax	71,126	6,899	10	46,310	8,998	19	43,032	7,939	18
DIF multiyear	61,551	3,745	6	51,617	3,095	6	38,180	2,172	6
Regular classification	52,528	8,273	16	50,709	8,026	16	47,170	8,414	18
State information	48,418	11,743	24	3,564	295	8	4,573	261	6
Service center studies and tests	43,333	6,814	16	20,059	3,896	19	22,825	7,055	31
Compliance projects	40,403	6,389	16	44,267	8,114	18	41,959	6,746	16
Claims for refund	33,163	462	1	37,203	135	0	26,412	0	0
DIF related	32,090	2,089	7	32,692	2,113	6	22,554	1,581	7
Return preparers	27,706	3,069	11	28,231	2,838	10	27,708	2,778	10
Non-DIF multiyear	26,866	1,667	6	29,373	1,624	6	26,742	1,689	6
Unallowable items	13,117	2,290	17	12,099	2,525	21	134,007	39,622	30
Other sources	175,596	27,570	16	176,156	29,282	16	179,600	34,140	19
Total	1,206,019	183,489	15%	1,058,966	145,328	14%	1,225,707	162,850	13%

Note 1: See glossary for definition of terms.

Note 2: Percentages are the percent of individual audits resulting in No Change Without Adjustments by the specific audit source for the year, rounded to the nearest whole percent.

Source: GAO analysis of IRS data.

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Glossary

Claims for Refund	Returns involving an audit of an amended return in which the taxpayer has claimed a refund.
Compliance Projects	Returns identified through IRS' information gathering projects.
DIF	Returns selected on the basis of a computer generated score (the scoring is based on an analysis technique known as discriminate function).
DIF Multiyear	Related returns from prior or subsequent years for the same taxpayer identified during the audit of a DIF-source return.
DIF Related	Related returns identified during an audit of a DIF-source return, other than returns from prior or subsequent years.
Non-DIF Multiyear	Related returns from prior or subsequent years for the same taxpayer, when the initial source was other than a DIF-source return.
Nonfilers	Audits initiated against known taxpayers who did not file a return with IRS.
Other Sources	Over 25 other audit sources, such as referrals from other IRS Divisions, which were not one of the 10 largest sources during the period of our review.
Regular Classification	Manually selected returns for audit that do not result from other specified audit sources.
Return Preparers	Returns identified for audit due to questionable tax practitioners.
Self-Employment Tax	Returns involving self-employment tax issues initiated by IRS service center examination staff.
Service Center Studies and Tests	Returns identified through service center projects initiated by the IRS National Office.

Glossary

State Information	Returns identified from various state sources, generally under exchange agreements between the IRS and the states.
Tax Shelter Related	Related returns of partners, grantors, beneficiaries, and shareholders identified during audits of either partnerships, fiduciaries, or Subchapter S corporations involving potential tax shelter issues.
Total Personal Income	Total income, such as wages and interest, reported on a tax return prior to any deductions or adjustments.
Unallowable Items	Returns involving refundable credits and dependency exemptions, such as the Earned Income Credit, initiated by service center examination staff.

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