



U.S. SENATE COMMITTEE ON

# Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

<http://finance.senate.gov>

For Immediate Release  
Tuesday, March 20, 2001

## Grassley Questions Declining IRS Audit Rate

WASHINGTON – Sen. Chuck Grassley, chairman of the Committee on Finance, has asked the Internal Revenue Service to account for a precipitous drop in its taxpayer audit rate. The text of Grassley's letter to the agency follows.

March 19, 2001

Mr. Charles Rossotti  
Commissioner  
Internal Revenue Service  
1111 Constitution Ave., NW  
Washington, D.C. 20224

Dear Commissioner Rossotti:

Coinciding with the administration's consideration of the Internal Revenue Service's (IRS) budget, newspaper accounts carried the story of a declining audit rate at the IRS. As I have read about these statistics, I have also been concerned that enforcement may be slipping.

However, I am deeply concerned that the IRS statistics don't tell the whole story of the actual number of returns that are reviewed by the service. I am also concerned that the understatements may be used to justify budget and staff increases – and that it is statements such as this that could undermine our tax system. Information reported in today's Tax Notes disturbs me. According to the article, the audit numbers fail to consider millions of IRS computer-based reviews of taxpayer returns. If these additional millions of contacts were included, the audit rates would be three to four times higher than reported.

It appears that the IRS fails to give proper and complete accounting of the large number of returns that are subject to automatic review by IRS computer systems and contact under the information reporting program (IRP) -- the invisible audits. For example, an individual has income, dividend and interest – all subject to third party reporting by the IRS. The IRS computers will compare this third party information with what is reported by the taxpayer and, if necessary, send a letter to the taxpayer asking that the discrepancy be explained or that additional tax is due and should be paid. If there are no problems, a review has been conducted, but no letter has been sent. It is my understanding that these types of audits – matching – were done primarily by hand in the 1960's and 1970's and thus would have been included as an audit at that time. In the late 1970's, and particularly with the increased third party reporting requirements provided for in 1986, this work was

more and more performed by computers – yet was not included in the audit rate. It is inexplicable that the same review done by a person is an audit but if done by a computer it is not counted.

I can assure you from my mail, the taxpayer who receives a letter from the IRS demanding additional tax certainly believes that he or she has been subject to review and audit.

By comparison, police departments around the country have begun experimenting with the use of automatic cameras that capture cars that run red lights. This technology break-through has allowed police departments to free up officers to perform other important work. Thus, the new technology allows the police department to continue the task of controlling traffic violations while providing the department an opportunity to make better use of human resources. To ignore the benefits of this technology in the work of the police department and its impact on modifying driver behavior would be foolish.

Similarly, billions of taxpayers' money has been spent by the IRS in upgrading and improving its computer technology. Congress has been told repeatedly that one of the great benefits of this technology is to allow the IRS to conduct millions of invisible audits of taxpayers' returns – and for the IRS to concentrate face-to-face audits on more problematic returns. It is painting an incomplete picture to talk about audits and reviews of taxpayer returns and yet fail to mention the IRP -- the invisible audits. This is not to say that an IRP contact is equal to a face-to-face audit on a one-for-one basis, but rather to highlight that IRP is a critical part of the IRS' arsenal to ensure tax compliance. By not including the IRP contacts, the IRS appears to be providing a distorted picture to the Congress, and more importantly, to the taxpayer – that there is no one in the guardhouse.

For example, while in 1999 there were 715,000 service center audits and 366,000 face-to-face audits there were over 3.6 million IRP contacts. These millions of reviews and letters sent are not included in the audit rate. Further, this does not even include the millions of more taxpayers who were subject to IRP review but received no letter because there was no detected underreporting or no significant underreporting. It is my understanding that these IRP reviews provide the IRS a good look at the accuracy of the tax returns of millions of American taxpayers.

It is my understanding that IRP is included in the enforcement revenue collected. This fact speaks volumes that IRP contacts should be noted in the audit rate. To include IRP dollars in enforcement revenue and not mention IRP contacts in the audit rate is inconsistent and incomplete at best.

I request that you please provide me the following information:

- 1) the number of IRP contacts for 2000 as well as for the last twenty years the number of returns subject to computer-based review that did not result in the sending of a letter to the taxpayer.
- 2) the number of dollars assessed and collected through the IRP program for the last twenty years.
- 3) the cost per IRP review and contact as well as the cost per service center audit and face-to-face audit for the past twenty years.
- 4) the IRS has significant correspondence with taxpayers regarding math error, which realizes millions in additional revenue. Please explain if these dollars are included in enforcement revenue

and also how many math error contacts are done each year for the past twenty years and how much revenue has resulted from this effort for the past twenty years.

5) please explain why the 715,000 Service Center audits, which are essentially correspondence to the taxpayer, are considered an audit for IRS statistical purposes, yet the 3.6 million IRP notices from the service centers are not.

Finally, I ask that you review the IRS' publicized audit rate and consider whether it should be revised to reflect or call attention as well to this invisible audit rate. Particularly, I ask that taking into all the aspects of enforcement -- face-to-face audit, service center audits, IRPs, math errors, automatic penalty notices (of which there were 22 million issued in 1998 according to TRAC at Syracuse University) etc. -- you provide the Finance Committee your assessment of where we are in terms of enforcement and encouraging tax compliance. Please provide this information by March 26<sup>th</sup>, 2001 in preparation for the Finance Committee oversight hearing of the IRS.

Cordially yours,

Charles E. Grassley  
Chairman

cc: Senator Max Baucus  
Ranking Member

Paul O'Neill  
Secretary of the Treasury

Larry Levitan  
Oversight Board