



*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

**September 2005**

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TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

September 28, 2005

**MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION**

**FROM:** Pamela J. Gardiner  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices (Audit # 200530004)

This report presents the results of our review to determine whether changes the Internal Revenue Service (IRS) is making to the math error process are having a positive effect on compliance by clearly communicating errors to taxpayers, including clearly explaining their appeal rights.

*Synopsis*

Annually, the IRS sends over 7 million math error notices to taxpayers that make mistakes on tax returns. In 2002 and 2003, the IRS' Taxpayer Advocate reported concerns that the explanations in math error notices were confusing and inadequate. Another concern of the Taxpayer Advocate was that taxpayers did not understand their rights to challenge math error adjustments. To address concerns regarding the math error process, the IRS developed initiatives to redesign notices and improve their clarity, and to simplify procedures for employees to choose the correct notice to correspond to a particular taxpayer's situation.

We reviewed revised notices issued to taxpayers filing individual and business income tax returns.<sup>1</sup> We also performed analyses of steps taken by employees in the IRS Error Resolution function to resolve errors on certain high volume business and individual tax returns.

The IRS' notice redesign efforts have generally been effective. On most of the revised notices, the IRS provided bold headings with easily identifiable answers to questions such as why the taxpayers received the notices and what they needed to do if they disagreed with the IRS'

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<sup>1</sup> We also reviewed unrevised notices issued to business taxpayers.



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changes. Narrative explanations of the taxpayers' errors were usually specific enough to allow them to identify the problems on their returns. However, further improvements could be made to enhance the clarity and usefulness of notices and reduce unnecessary notices.

#### Individual taxpayers

Revised notices issued to taxpayers filing individual income tax returns contained statements in table form comparing the taxpayers' figures with IRS' revised figures. However, these comparisons were shown for only a few summary items and were too general to be of significant use to taxpayers. In addition, the overall formatting and information in the notice referred to as Computer Paragraph 16<sup>2</sup> was much less effective than the information on other notices.

We found that because of a problem with instructions on U.S. Individual Income Tax Returns (Forms 1040 and 1040A) regarding which figures taxpayers should include to calculate amounts they owe on their tax returns, taxpayers received unnecessary math error notices. As of June 3, 2005, over 3,200 taxpayers, who performed the calculation exactly as instructed on their Tax Year 2004 returns, received notices telling them they had calculated the amounts incorrectly. In the prior year, over 8,000 taxpayers received the same inappropriate notice.

#### Business taxpayers

Math error notices issued to taxpayers filing several different business tax returns<sup>3</sup> still have not been revised. We are not commenting on the presentation of these notices, but we believe that immediate interim changes should be made to ensure these taxpayers clearly understand their rights to appeal math error adjustments. Further, certain notices issued to nonprofit organizations contained inaccurate references to lines on tax returns and other spelling and capitalization errors. Immediately after we notified the IRS of the inaccurate references to line items on the returns, IRS management initiated corrective action to address the issue.

We also found while IRS employees properly resolved most taxpayer errors, IRS employee errors could result in inappropriate notices being sent to many taxpayers filing Employer's Annual Federal Unemployment (FUTA) Tax Return (Forms 940).

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<sup>2</sup> This is the notice sent to individual taxpayers with math errors on their tax returns if the return resulted or should have resulted in an overpayment of tax and all or part of the overpayment was used to offset a tax liability from a different tax period.

<sup>3</sup> Includes U.S. Corporation Income Tax Return (Form 1120), U.S. Income Tax Return for Estates and Trusts (Form 1041), Farmers' Cooperative Association Income Tax Return (Form 990-C), and Exempt Organization Business Income Tax Return (Form 990-T).



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### Recommendations

We recommended the Director, Customer Account Services, Wage and Investment (W&I) Division, review the process for revising notices to ensure notices are accurate and consistently formatted, and take actions to address specific problems with the notices referred to in our report. We also recommended the Director, Tax Forms and Publications, W&I Division, add text to Forms 1040 and 1040A instructing taxpayers to include the amount of their estimated tax penalty (if any) when computing the amount they owe with their tax return. The Director should also consider reversing the order in which these two items are presented on the Forms. Until the text is added, we recommended that employees in the Error Resolution function perform research and suppress unnecessary math error notices caused by the problems with the instructions on the Forms. Finally, we recommended the Director, Submission Processing, Customer Account Services, W&I Division, provide specific instructions and training to Error Resolution function quality review employees and tax examiners regarding the appropriate notices to be sent to taxpayers making errors on Forms 940.

### Response

IRS management agreed with six of our eight recommendations. Accordingly, the IRS initiated a new procedure to facilitate review of revised notices. The Director, Submission Processing, W&I Division, and the Director, Customer Assistance, Relationships, and Education, W&I Division, will determine the feasibility of expanding existing Taxpayer Notice Codes<sup>4</sup> to allow greater specificity in the explanation of errors. They will study the possibility of adding additional lines from the Form 1040 payment section to the tax statement table on math error notices. These Directors also agreed to make revisions (or have already made revisions) to specific notices referred to in our report.

IRS management disagreed with two of our recommendations. IRS management did not agree to make changes to Forms 1040 and 1040A, stating there is not sufficient room to add text from the instructions for Line 74 to the front of Form 1040 to advise taxpayers to include the estimated tax penalty from Line 75. The additional instructions would force a reduction in the font size of the reference on “how to pay,” a message impacting a much larger number of taxpayers than those computing the estimated tax penalty. In addition, management believes that reversing the line order would be counterproductive, resulting in increased confusion for many Form 1040 and Form 1040A filers who do not calculate their estimated tax penalty. Management added that the affected taxpayers would not have received unnecessary notices if they had properly followed the instructions contained in the instruction booklets. Also, IRS management stated that

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<sup>4</sup> The information to be included in a math error notice issued to a taxpayer is determined by a Taxpayer Notice Code entered by an IRS employee into its Error Resolution System.



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requiring research by Error Resolution employees is not practical due to the additional cost in both processing time and labor. However, the Director, Submission Processing, W&I Division, will explore the possibility of establishing a systemic solution in the IRS' computer routines that will suppress the notice when a taxpayer actually paid the proper amount of tax, including the estimated tax penalty. Management's complete response to the draft report is included as Appendix VI.

*Office of Audit Comment*

We disagree with management's decision to not make our recommended changes to Forms 1040 and 1040A. We believe there is sufficient room on these forms for the changes we recommend as illustrated in Figure 4 and Appendix V of our report. We agree that, for Form 1040, the font size of the reference on "how to pay" would need to be reduced or changed. However, reduced font sizes are used elsewhere on the Form 1040. For example, there are reduced font sizes on lines 24, 38b, and 69 and for the statement on the signature line (*jurat* statement).

Regarding management's disagreement with our recommendation to ensure Error Resolution employees perform research and suppress unnecessary math notices, we believe the alternative corrective action proposed by management should reasonably suffice to prevent unnecessary notices from being issued to taxpayers.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Curtis Hagan, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-3837.



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## *Background*

Taxpayer compliance can be significantly affected by how well taxpayers understand their tax responsibilities. Noncompliance may not be deliberate and can stem from a wide range of causes including lack of knowledge and confusion, causing taxpayers and preparers to make errors on tax returns.

Recognizing that some errors on tax returns did not justify the expense of an audit, the Congress authorized the Internal Revenue Service (IRS) to correct certain math errors that appeared on the face of a tax return. Initially, taxpayers had no right to appeal these corrections. In the Tax Reform Act of 1976,<sup>1</sup> the Congress provided that a

***In 2002 and 2003, the IRS' Taxpayer Advocate reported concerns that the explanations in the math error notices were confusing and inadequate. Another concern of the Taxpayer Advocate was that taxpayers were not sure how to challenge the notices and did not understand their rights to challenge them.***

taxpayer who received a math error notice had 60 days to file a request for abatement of the assessment. The Act also codified the first five definitions of “mathematical or clerical errors” to include:

- An error in addition, subtraction, multiplication, and division shown on a tax return.
- An incorrect use of an IRS table related to the return.
- Inconsistent entries on a return.
- Omitted information required to substantiate an entry on a return.
- An entry that claims a deduction or credit in excess of the statutory limit.

The Congress has expanded the IRS' math error authority over the years to include denial of benefits for exemptions, filing status, and certain tax credits when taxpayers failed to provide valid taxpayer identification numbers.

Annually, the IRS sends over 7 million math error notices to taxpayers for mistakes on tax returns. When IRS computers identify an error on a taxpayer's return, the return is routed to the Error Resolution function and the electronic return information is sent to the Error Resolution System (ERS). The ERS is used to correct errors made by taxpayers or IRS employees during the initial processing of tax returns. The ERS computer assigns an error code to the return which identifies the type of error made. An IRS employee makes changes to the return and communicates these changes by way of an IRS notice.

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<sup>1</sup> Pub. L. 94-455, 90 Stat. 1520.



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The information to be included in the notice is determined by a Taxpayer Notice Code (TPNC) entered into the ERS by the employee. Each TPNC corresponds to a specifically worded paragraph to be included in a notice. For example, if the IRS computer found the taxpayer had made an error in computing their standard deduction, and the IRS employee determined the taxpayer had taken both the standard deduction and itemized deduction, the IRS employee would enter the correct information along with a TPNC 196 into the ERS. As a result, a notice would be sent to the taxpayer stating:

*We changed the amount claimed as a deduction on Line 39 of your Form 1040.<sup>[2]</sup> You may use either the standard deduction or the itemized deductions; however, you cannot use both. We used the amount that resulted in a lower taxable income.*

Notices sent to taxpayers should clearly explain the taxpayers' errors and the changes the IRS made to their tax returns. In 2002 and 2003, the IRS' Taxpayer Advocate reported concerns that the explanations in math error notices were confusing and inadequate. Another concern of the Taxpayer Advocate was that taxpayers were not sure how to challenge the notices and did not understand their rights to challenge them. To address concerns regarding the math error process, the IRS developed initiatives to redesign notices and improve their clarity, to revise TPNCs and simplify the procedures for employees to choose the correct code to correspond to a particular taxpayer's situation, and to resequence TPNCs to correspond to specific sections of the tax return.

The focus of this audit was to determine whether the changes the IRS is making to these notices are having a positive effect on compliance by clearly communicating errors to taxpayers, and whether taxpayers are aware of their rights to challenge these notices.

This review was performed at the Cincinnati, Ohio; Fresno, California; Kansas City, Missouri; and Ogden, Utah, Submission Processing Centers<sup>3</sup> during the period January through May 2005. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

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<sup>2</sup> U.S. Individual Income Tax Return.

<sup>3</sup> IRS Submission Processing Centers are responsible for processing tax returns and payments and issuing refunds.



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## *Results of Review*

### **Math Error Notices Sent to Taxpayers Filing Individual Income Tax Returns Were Significantly Improved, but Further Improvements Could Be Made**

To determine whether the IRS' efforts to improve notices sent to individual taxpayers were effective, we reviewed revised notices issued to 140 taxpayers filing individual income tax returns during 2005. The IRS' notice redesign and training efforts have generally been effective. On most of the revised notices we reviewed, the IRS provided bold headings with easily identifiable answers to the following questions:

- Why the taxpayers received the notices.
- Why the IRS made changes to the returns.
- What the taxpayers needed to do if they agreed with the changes.
- What the taxpayers needed to do if they disagreed with the changes.

Narrative explanations of the taxpayers' errors were usually specific enough to allow the taxpayers to identify the problems on their returns. The taxpayers' appeal rights were clearly explained and readily identifiable on many of the notices.

However, we found the formatting of the revised notices to be inconsistent and some improvements were needed on these notices. We believe this occurred because the notice revisions were assigned to a variety of subject matter experts. Although the revised notices were to be channeled through a single point of contact to ensure quality, this process did not identify the following issues.

#### **Tax statements**

Revised notices for taxpayers filing individual income tax returns contain a statement in table form showing taxpayers certain figures from their tax returns compared to IRS' corrected figures. However, these comparisons are shown for only three items: Adjusted Gross Income, Taxable Income, and Total Tax. Because so many different lines from the tax return are factored into these three items, the table is often of little use to taxpayers when trying to reconcile IRS' adjustments with their originally filed tax returns.



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Further, the table shows only IRS figures for Total Payments. So if a taxpayer makes an error on one of the items included in total payments (e.g., income tax withheld, estimated tax payments, earned income credit, additional child tax credit, etc.), the table would not help the taxpayer see or further understand their error and may even confuse the taxpayer.

For example, in the hypothetical situation below, a taxpayer incorrectly calculated the child tax credit on a U.S. Individual Income Tax Return (Form 1040A). A notice informing the taxpayer of the error would be issued and the explanation of the error would state:

*We didn't allow part or all of your child tax credit on Line 33 and/or additional child tax credit on Line 42 of your Form 1040A. One or more of your children exceeds the age limitation.*

In addition, the notice would contain the information in Figure 1.

**Figure 1: Table on Math Error Notices As Currently Formatted**

**2004 Tax Statement<sup>4</sup>**

<b>Line Item On Return</b>	<b>Your Figures</b>	<b>IRS Figures</b>
Adjusted Gross Income	\$36,740.00	\$36,740.00
Taxable Income	\$11,540.00	\$11,540.00
Total Tax	\$0.00	\$1,153.00
Total Payments		\$3,000.00
Overpayment		\$1,847.00

Neither the narrative nor the table tells the taxpayer what the correct figures should be for the child tax credit.

Further, with the information provided, the taxpayer cannot be sure whether he or she made an error when calculating their additional child tax credit. Revised notices containing these statements were issued to over 7.3 million taxpayers during Calendar Year (CY) 2004.

<sup>4</sup> The amounts used in Figures 1 and 2 are fictitious and are used for illustrative purposes only.



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As illustrated in Figure 2, adding specific data from the lines on the taxpayer's return with errors and including both taxpayer and IRS figures for total payments could make the notice more useful to the taxpayer.

**Figure 2: Table on Math Error Notices As Proposed by the Treasury Inspector General for Tax Administration (TIGTA)**

**2004 Tax Statement**

<b>Line Item On Return</b>	<b>Your Figures</b>	<b>IRS Figures</b>
<b>Adjusted Gross Income</b>	\$36,740.00	\$36,740.00
<b>Taxable Income</b>	\$11,540.00	\$11,540.00
<b>Child Tax Credit</b>	\$1,153.00	\$0.00
<b>Total Tax</b>	\$0.00	\$1,153.00
<b>Additional Child Tax Credit</b>	\$1,847.00	\$0.00
<b>Total Payments</b>	\$4,847.00	\$3,000.00
<b>Overpayment</b>		\$1,847.00

A significant amount of computer programming would be required to make all the lines on the taxpayer's return available for inclusion in the table on the math error notice. However, by focusing on several high volume errors, the IRS could make math error notices more useful to many taxpayers by adding information from relatively few lines. For example, 2,242,625 taxpayers made errors related to the earned income credit, child tax credit, and additional child tax credit during CY 2004. By adding information to the notice from these four lines of the tax return (as appropriate) the IRS could make math error notices significantly more useful to similar numbers of taxpayers in the future.



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### **Computer Paragraph 16**

Computer Paragraph (CP) 16 is the notice sent to taxpayers with math errors on their Individual Income Tax Returns if the returns resulted in (or should have resulted in) overpayments of tax and all or part of the overpayments were used to offset liabilities from different tax periods.

We found this notice to be significantly less clear and, therefore, more burdensome than other math error notices sent to individual taxpayers for the following reasons:

- Rather than providing an explanation of the changes made to the tax return on the first page, this notice provided the table on the first page. As previously discussed, this table can be confusing to taxpayers. The explanation of changes made to the tax return is on the second page of the notice.
- The notice does not provide the same clear explanation of appeal rights that the other notices to individual taxpayers provide.

During CY 2004, the IRS issued CP 16 to over 300,000 taxpayers.

### **TPNC 299**

Many taxpayers who calculated their own estimated tax penalties received an unnecessary and confusing math error notice telling them they miscalculated the total balance they owed on their tax returns.

As illustrated in Figure 3, instructions on Tax Year 2004 U.S. Individual Income Tax Return (Form 1040), Line 74 (Amount You Owe)<sup>5</sup> tell taxpayers to, “Subtract Line 70 (Total Payments) from Line 62 (Total Tax).”<sup>6</sup>

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<sup>5</sup> Identical instructions appear on Form 1040A, but the line numbers are different.

<sup>6</sup> The Instruction Booklet for Form 1040 Line 74 tells the taxpayer to include the amount on Line 75. However, most taxpayers would not refer to the instruction booklet to figure out how to subtract one line from another. Further, the design of the form, with the estimated tax line after the total tax line, makes it more unlikely that a taxpayer would include the estimated tax in the total.



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**Figure 3: “Amount You Owe” Section of Form 1040 As Currently Formatted**

56	Subtract line 55 from line 45. If line 55 is more than line 45, enter -0-	56	
<b>Other Taxes</b>			
57	Self-employment tax. Attach Schedule SE	57	
58	Social security and Medicare tax on tip income not reported to employer. Attach Form 4137	58	
59	Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required	59	
60	Advance earned income credit payments from Form(s) W-2	60	
61	Household employment taxes. Attach Schedule H	61	
62	Add lines 56 through 61. This is your <b>total tax</b>	62	
<b>Payments</b>			
63	Federal income tax withheld from Forms W-2 and 1099	63	
64	2004 estimated tax payments and amount applied from 2003 return	64	
65a	<b>Earned income credit (EIC)</b>	65a	
b	Nontaxable combat pay election ▶ 65b		
66	Excess social security and tier 1 RRTA tax withheld (see page 54)	66	
67	Additional child tax credit. Attach Form 8812	67	
68	Amount paid with request for extension to file (see page 54)	68	
69	Other payments from: a <input type="checkbox"/> Form 2439 b <input type="checkbox"/> Form 4136 c <input type="checkbox"/> Form 8885	69	
70	Add lines 63, 64, 65a, and 66 through 69. These are your <b>total payments</b>	70	
<b>Refund</b>			
71	If line 70 is more than line 62, subtract line 62 from line 70. This is the amount you <b>overpaid</b>	71	
72a	Amount of line 71 you want <b>refunded to you</b>	72a	
b	Routing number		
c	Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings		
d	Account number		
73	Amount of line 71 you want <b>applied to your 2005 estimated tax</b>	73	
<b>Amount You Owe</b>			
74	<b>Amount you owe.</b> Subtract line 70 from line 62. For details on how to pay, see page 55 ▶	74	
75	<b>Estimated tax penalty</b> (see page 55)	75	

Source: 2004 Form 1040.

However, taxpayers who follow these instructions and also enter an estimated tax penalty on the next line (Line 75) receive a math error notice which states:

*We changed the refund amount on Line 72a or the amount you owe on Line 74 of your Form 1040 because the amount entered on your tax return was computed incorrectly.*

This occurs because IRS computers are programmed to include the amount of the estimated tax penalty (Line 75) in the calculation for Line 74. Taxpayers are not told, on the return itself, to include this line in their calculation. Because the amount calculated by the IRS computer differs from the amount calculated by the taxpayer (in accordance with instructions on the Form 1040) the return is routed to the ERS. IRS employees resolve the issue by entering a TPNC 299 into the ERS which causes a notice to be sent to the taxpayer with the previous statement.

The IRS has committed to eliminate unnecessary notices. By making changes to lines 74 and 75 of Form 1040 as illustrated in Figure 4 and explained below, the IRS could avoid issuing these unnecessary and confusing notices to taxpayers:

- Place the line for estimated tax penalty before “Amount You Owe” to make the calculation process easier and more logical to taxpayers.



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- Add text to the line entitled “Amount You Owe” telling taxpayers to add the amount of their estimated tax penalty to the amount they owe. This line as we recommend now reads, “Subtract line 70 from line 62 and add line 74. For details on how to pay, see page 55.”

**Figure 4: “Amount You Owe” Section of Form 1040 As Proposed by TIGTA**

<b>Other Taxes</b>		56	Subtract line 55 from line 49. If line 55 is more than line 49, enter -0-	56	
57 Self-employment tax. Attach Schedule SE		57		57	
58 Social security and Medicare tax on tip income not reported to employer. Attach Form 4137		58		58	
59 Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required		59		59	
60 Advance earned income credit payments from Form(s) W-2		60		60	
61 Household employment taxes. Attach Schedule H		61		61	
62 Add lines 56 through 61. This is your <b>total tax</b>		62		62	
<b>Payments</b>					
63 Federal income tax withheld from Forms W-2 and 1099		63			
64 2004 estimated tax payments and amount applied from 2003 return		64			
If you have a qualifying child, attach Schedule EIC.	65a <b>Earned income credit (EIC)</b>	65a			
	b Nontaxable combat pay election ▶ 65b				
66 Excess social security and tier 1 RRTA tax withheld (see page 54)		66			
67 Additional child tax credit. Attach Form 8812		67			
68 Amount paid with request for extension to file (see page 54)		68			
69 Other payments from: a <input type="checkbox"/> Form 2439 b <input type="checkbox"/> Form 4136 c <input type="checkbox"/> Form 8885		69			
70 Add lines 63, 64, 65a, and 66 through 69. These are your <b>total payments</b>		70			
<b>Refund</b>					
71 If line 70 is more than line 62, subtract line 62 from line 70. This is the amount you <b>overpaid</b>		71			
72a Amount of line 71 you want <b>refunded to you</b>		72a			
Direct deposit? See page 54 and fill in 72b, 72c, and 72d.	▶ b Routing number				
	▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings				
	▶ d Account number				
73 Amount of line 71 you want <b>applied to your 2005 estimated tax</b>		73			
74 Estimated tax penalty (see page 55)		74			
<b>Amount You Owe</b> 75 <b>Amount you owe.</b> Subtract line 70 from line 62 and add line 74. For details on how to pay, see page 55		75			
Do you want to allow another person to discuss this return with the IRS (see page 56)? <input type="checkbox"/> Yes. Complete the following. <input type="checkbox"/> No					

Source: TIGTA’s Proposed Revisions to Form 1040.

Similar changes should be made to Form 1040A (see Appendix V).

Taxpayers received the math error notice, even if they paid the proper amount (amount of tax owed plus estimated tax penalty). Not only did this result in taxpayer burden and confusion, but many taxpayers most likely called the IRS unnecessarily to resolve the issue. As of June 3, 2005, the IRS had sent these improper math error notices to over 3,200 taxpayers who had completed their 2004 Forms 1040 and 1040A as instructed on the forms. Over 700 of these taxpayers had their returns prepared by paid tax preparers.

### **Recommendations**

**Recommendation 1:** The Director, Customer Account Services, Wage and Investment (W&I) Division, should ensure the review process for revised notices is adequate to produce notices that are accurate, and properly and consistently formatted.



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**Management's Response:** The IRS initiated a new procedure requiring the notice Subject Matter Experts and Single Point of Contact employees to jointly review revised notices during the Modernization and Information Technology Services organization Systems Acceptance Testing process to further improve the accuracy and consistency of the notices.

**Recommendation 2:** The Director, Customer Account Services, W&I Division, should revise tax statement tables contained on notices to include specific amounts from at least some line items on which taxpayers made errors on their tax returns. Because the computer programming to make all line items from the tax returns available for inclusion on the notices may be resource intensive, efforts should be focused on including line items related to very frequently occurring errors.

**Management's Response:** The Director, Submission Processing, and the Director, Customer Assistance, Relationships, and Education (CARE), W&I Division, will review the existing TPNCs and determine the feasibility of expanding them to allow greater specificity in the explanation of the error. They will also study the possibility of adding additional lines from the Form 1040 payment section to the tax statement table on math error notices. Their efforts will focus on the highest volume error conditions in the payment and tax areas of the tax return.

**Recommendation 3:** The Director, Customer Account Services, W&I Division, should revise CP 16 to present information in a manner consistent with other notices sent to individual taxpayers including the location of the error explanation and tax statement, and the wording of the taxpayers' rights to appeal the math error adjustments.

**Management's Response:** The Director, Submission Processing, and the Director, CARE, W&I Division, agreed the CP 16 needs revision. Because of competing priorities among notices, they are unable to commit to a firm completion date for this revision. However, they will look to expedite the revision process. Their prioritization working group will include Taxpayer Advocate Service and external stakeholders, and will establish "TIGTA/GAO Recommendations" as one of the ranking criteria for prioritization.

**Recommendation 4:** The Director, Tax Forms and Publications, W&I Division, should add text on Form 1040 Line 74 "Amount You Owe" instructing taxpayers to include the amount of estimated tax penalty from Line 75. Consideration should be given to reversing the order of these lines on the Form 1040 to make the calculation process easier and more logical to taxpayers. Similar changes should be made to Form 1040A Line 47.

**Management's Response:** IRS management disagreed with our recommendation, and stated there is not sufficient room to add text from the instructions for Line 74 to the front of Form 1040 advising taxpayers to include the estimated tax penalty from Line 75. The additional instructions would force a reduction in the font size of the reference on



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“how to pay,” a message impacting a much larger number of taxpayers than those computing estimated tax penalty. In addition, IRS management believes that reversing the line order would be counterproductive, resulting in increased confusion for 93 percent of the approximately 56 million Form 1040 filers, and 98.5 percent of the approximately 12 million Form 1040A filers who do not calculate their estimated tax penalty. Management added that the affected taxpayers would not have received the notice if they had properly followed the instructions contained in the instruction booklet for Form 1040.

**Office of Audit Comment:** We disagree with management’s decision to not make our recommended changes to Forms 1040 and 1040A. We believe there is sufficient room on these forms for the changes we recommend as illustrated in Figure 4 and Appendix V of our report. We agree that, for Form 1040, the font size of the reference on “how to pay” would need to be reduced or changed. However, reduced or changed font sizes are used elsewhere on Form 1040. For example, there are reduced font sizes on lines 24, 38b, and 69 and the statement on the signature line (*jurat* statement).

**Recommendation 5:** Until sufficient changes are made on Forms 1040 and 1040A to instruct taxpayers to include the estimated tax penalty in the total amount of taxes they owe, the Director, Customer Account Services, W&I Division, should ensure ERS employees perform research and suppress notices from going to taxpayers who paid the proper amounts (amount of tax owed plus estimated tax penalty).

**Management’s Response:** The Director, Submission Processing, W&I Division, stated that requiring research by ERS employees is not practical due to the additional cost in both processing time and labor. However, the Director will explore the possibility of establishing a systemic solution in the IRS’ computer routines that will suppress the notice when a taxpayer actually paid the proper amount of tax, including the estimated tax penalty.

**Office of Audit Comment:** We believe the IRS’ alternative corrective action should reasonably suffice to prevent unnecessary notices from being issued to taxpayers.

## ***Math Error Notices Sent to Many Business Taxpayers Need Improvement***

To determine whether the IRS’ efforts to improve notices sent to business taxpayers were effective, we reviewed revised notices issued to 75 business taxpayers during 2005. We also reviewed unrevised notices that were issued to another 17 business taxpayers during 2005. (Because these notices are yet to be revised, we are not commenting on the presentation of math error information in these notices.)



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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Overall, the revised notices provided adequate descriptions of the taxpayers' errors. However, we found the design and presentation of some of these notices to be less clear than the notices issued to individual taxpayers. Again, the notice revisions were assigned to various subject matter experts and subsequent quality review did not identify the problems with the notices. In addition, taxpayers' rights to appeal math error adjustments were not clearly communicated on unrevised notices.

### **TPNC 08**

Nonprofit organizations paying wages in CY 2004 but reporting no Social Security and/or Medicare taxes on their Employer's Quarterly Federal Tax Returns (Form 941) and failing to check the box indicating the wages were not subject to Social Security and/or Medicare taxes received an inaccurately worded and formatted notice. Line 8 of Form 941 provides a check box for these taxpayers to check if their wages paid were not subject to these taxes. If taxpayers omitted checking this box, their returns were routed to the Error Resolution function. IRS employees would resolve the error by entering a TPNC 08 to the ERS which would generate a notice to the taxpayers with the following text:

*Non-profit organization [sic] became liable for Social security [sic] and/or Medicare taxes effective on 01-01-1984. Since we found no check mark entry in the box on **line 4 [emphasis added]** or other indication that the wages were not subject to social security [sic] and/or Medicare taxes, we have computed the taxes and adjusted your Form 941 accordingly.*

IRS management was unaware of both the erroneous reference to line 4 and the capitalization and spelling errors on this notice. The erroneous reference to line 4 is confusing to taxpayers and the capitalization and spelling errors negatively impact the IRS' professional image. We brought the erroneous line item to the IRS' attention and management initiated immediate corrective action. As of June 1, 2005, this notice had been issued to 470 taxpayers.

### **Taxpayer rights to appeal an IRS math error adjustment**

Math error notices sent to taxpayers filing U.S. Corporation Income Tax Return (Form 1120), U.S. Income Tax Return for Estates and Trusts (Form 1041), Farmers' Cooperative Association Income Tax Return (Form 990-C), and Exempt Organization Business Income Tax Return (Form 990-T) did not clearly communicate the taxpayers' rights to appeal the math error adjustments. Internal Revenue Code Section 6213(b)(2)(A) allows taxpayers 60 days from the date of a math error notice to request abatement of the additional tax specified in the notice.

In the 2003 Annual Report, the IRS Taxpayer Advocate emphasized the IRS must provide clear guidance to taxpayers about their rights to request abatement of math error adjustments. The IRS agreed to implement changes in notice language on the rights to appeal by January 2005, stating



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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it recognized the importance of this effort and would make every effort to ensure timely implementation.

Math error notices for these forms had not been revised as of the date of our review. Rather than a clear explanation of the taxpayers' appeal rights, these notices included a "stuffer" entitled *Interest and Penalty Information*. Along with information on penalties and interest, the stuffer contained information in small print on the back informing taxpayers that if they wanted to appeal the adjustment they must do so in writing, and that the IRS would notify the taxpayers if it did not accept their written explanations. As of June 14, 2005, over 43,600 math error notices had been sent to taxpayers filing these forms.

## **Recommendations**

**Recommendation 6:** Along with changes already made or being made to text associated with TPNC 08, the Director, Customer Account Services, W&I Division, should ensure changes are made to correct spelling and capitalization errors.

**Management's Response:** IRS management agreed that changes were needed to the text associated with TPNC 08 and the corrections were made when they were brought to management's attention by the TIGTA.

**Recommendation 7:** The Director, Customer Account Services, W&I Division, should ensure taxpayers' rights to appeal math error adjustments are clearly explained to taxpayers on math error notices associated with Forms 1120, 1041, 990-C and 990-T.

**Management's Response:** The Director, Submission Processing, W&I Division, will coordinate the addition of appropriate language to math error notices that explains the taxpayers' rights to appeal math errors identified on their tax returns by the IRS. The additional language will also be added to all math error notices issued on business tax returns meeting math error criteria. The new language will be strategically placed on the notice to ensure that taxpayers are informed of their right to appeal.

## **Internal Revenue Service Employee Errors Resulted in Inappropriate Notices to Taxpayers Filing Forms 940**

To determine whether IRS employees were appropriately resolving errors on tax returns and sending appropriate notices, we performed analyses of steps taken by Error Resolution function employees to resolve errors on certain high volume business and individual tax returns. Overall, we found employees properly resolved most errors on Forms 1040, 1120, and 941.



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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However, we found over one-third of the taxpayers included in our review, who received an error notice related to their Employer's Annual Federal Unemployment (FUTA) Tax Return (Form 940), were sent inappropriate notices. We selected a statistical sample of 97 Forms 940 for which taxpayers were sent an error notice between December 8 and December 30, 2004.<sup>7</sup> Of 97 error notices issued, 37 (38 percent) were inappropriate. Twenty-three notices contained a very general explanation of the taxpayer's error when a more specific explanation was available and should have been sent, and 14 notices were sent in error because the taxpayers' calculations were acceptable.

We determined there were at least two probable causes for these inappropriate notices. First, the Internal Revenue Manual (IRM) did not provide Error Resolution employees specific instructions on the appropriate TPNC to input to address the error situations on the returns included in our review. Job aids available to employees gave suggestions regarding the most appropriate TPNC to use; however, Error Resolution managers hold the IRM to be more authoritative. Second, the significant error rate on these returns during this time period had not been identified by Error Resolution function quality review employees.

We determined a significant number of these erroneous notices were issued by a single employee in one of the two IRS Submission Processing Centers that process these types of tax returns. However, even after eliminating this one employee's cases from our statistics, 18 percent of the notices issued were inappropriate. Had quality review identified these inappropriate notices, this employee as well as other Error Resolution function employees could have received feedback to allow them to avoid similar errors. Our sample was statistically valid for the population of notices issued during this time period in December 2004, but not for the population of notices issued throughout the year. However, based on the results of our samples and the number of notices issued to taxpayers filing Forms 940 in the last calendar year, we believe a significant number of taxpayers filing Forms 940 during 2005 could be sent inappropriate notices.

## ***Recommendation***

***Recommendation 8:*** The Director, Submission Processing, Customer Account Services, W&I Division, should provide specific instructions and training to appropriate Error Resolution function quality review employees and tax examiners regarding the appropriate notices to be sent to taxpayers making errors on Forms 940. Emphasis should be given to the need to use the TPNC which provides the most specific description of the taxpayers' errors.

***Management's Response:*** The Director, Submission Processing, W&I Division, will include additional instructions in the IRM for Error Resolution function employees working Forms 940 which will detail specific guidance for using the most appropriate

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<sup>7</sup> Our sample was selected from returns filed in both the Ogden and Cincinnati Submission Processing Centers.



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TPNC. The importance of using the most specific TPNC will be emphasized during annual training for both tax examiners and quality review employees.



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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## Appendix I

### *Detailed Objective, Scope, and Methodology*

The overall objective of this review was to determine whether the changes the Internal Revenue Service (IRS) is making to the math error process are having a positive effect on compliance by clearly communicating errors to taxpayers, including clearly explaining their appeal rights.

To accomplish this objective, we:

- I. Identified and evaluated the changes planned to clarify math error notices.
  - A. Reviewed the Taxpayer Advocate Report to identify changes the IRS stated would be implemented to clarify the math error notices.
  - B. Reviewed the results of the study performed by the Office of Research to identify any recommended changes to the math error notices.
  - C. Discussed with the Notice Gatekeeper and Program Analysts for the Individual Master File (IMF)<sup>1</sup> and Business Master File (BMF)<sup>2</sup> which notices were changed and what the specific changes were. We also determined what other notices are scheduled for revision.
- II. Determined whether Math Error Notices sent to taxpayers adequately explain the taxpayers' errors and clearly define the taxpayers' appeal rights.
  - A. Reviewed all Math Error Notices revised by the IRS to determine whether the notices adequately explain the taxpayers' errors and clearly define the taxpayers' appeal rights.
  - B. Selected a judgmental sample<sup>3</sup> of 140 IMF and 75 BMF notices being sent to taxpayers and reviewed the notices to determine whether they adequately explained the taxpayers' errors and clearly defined the taxpayers' appeal rights. (We also included in our sample 17 BMF notices that had not been revised).

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<sup>1</sup> The IRS database that maintains transactions or records of individual tax accounts.

<sup>2</sup> The IRS database that consists of Federal tax-related transactions and accounts for businesses. These include employment taxes, income taxes on businesses, and excise taxes.

<sup>3</sup> Since the notices remain consistent, a judgmental sample was used for this step. We wanted to sample a cross section of notices, and we did not expect to make any projections from our sample results. We selected our sample at random from a population of 1,261 IMF notices in the Error Resolution quality review function on April 5, 6, 12, and 13, 2005, and from a population of 218 BMF notices in the quality review function on March 22 and 23, 2005.



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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- C. Developed a computer program to identify all IMF returns where the taxpayers calculated the Estimated Tax Penalty, had a balance due, and received a math error notice with Taxpayer Notice Code<sup>4</sup> (TPNC) 299.<sup>5</sup> We validated the returns identified by our computer run by researching 46 of the accounts on the Integrated Data Retrieval System (IDRS).<sup>6</sup>
- D. Reviewed a statistical sample of IMF and BMF taxpayer accounts for which Math Error Notices were sent to determine if the proper notice was used.
1. Prepared a computer request to select IMF and BMF returns that went to the Error Resolution System (ERS) to identify the Error Code that caused the return to be routed to the ERS.
  2. From the computer request in Step D.1., selected a statistical sample of IMF and BMF returns that received a math error notice between December 8, 2004, and December 30, 2004.<sup>7</sup> The following statistical samples were pulled from the respective populations:

<u>Return</u>	<u>Sample Size</u>	<u>Population</u>
IMF 1040	190	5,967
BMF 940	97	191
BMF 941	179	1,965 <sup>8</sup>
BMF 1120	68	92 <sup>9</sup>

3. From the statistical samples selected in Step D.2., researched the taxpayers' accounts on the IDRS and ordered the tax returns to determine if the TPNC used was appropriate based on the error on the return.

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<sup>4</sup> Each Taxpayer Notice Code corresponds to a specifically worded paragraph to be included in a notice issued to a taxpayer.

<sup>5</sup> TPNC 299 informs the taxpayer that the IRS changed the refund amount or the amount they owed because the amount entered on the tax return was computed incorrectly.

<sup>6</sup> IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.

<sup>7</sup> We selected returns from this date range because they were the most recently processed returns at the time we selected our samples.

<sup>8</sup> We used a 95 percent confidence level, an expected error rate of 15 percent, and precision of  $\pm 5$  percent.

<sup>9</sup> We reviewed the entire population that was available for these returns.



*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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- II. Determined whether changes were made to the training offered to Accounts Management employees to better educate them concerning taxpayer's rights to appeal math error adjustments.
  - A. Interviewed management, employees, and training coordinators in the Error Resolution function to identify any changes that were made to the training concerning taxpayer's rights for math error notices.
  - B. Reviewed the training material for Accounts Management to determine if changes have been made to more clearly address taxpayer's rights to appeal math error adjustments.



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**Appendix II**

*Major Contributors to This Report*

Curtis Hagan, Assistant Inspector General for Audit (Small Business and Corporate Programs)  
Richard J. Dagliolo, Director  
Kyle R. Andersen, Audit Manager  
Robert M. Jenness, Acting Audit Manager  
L. Jeff Anderson, Lead Auditor  
W. George Burleigh, Senior Auditor  
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Layne D. Powell, Information Technology Specialist



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## **Appendix III**

### *Report Distribution List*

Commissioner C  
Office of the Commissioner – Attn: Chief of Staff C  
Deputy Commissioner for Services and Enforcement SE  
Deputy Commissioner, Wage and Investment Division SE:W  
Director, Customer Account Services, Wage and Investment Division SE:W:CAS  
Director, Submission Processing, Wage and Investment Division, SE:W:CAS:SP  
Director, Tax Forms and Publications, Wage and Investment Division SE:W:CAR:MP:T  
Field Director, Submission Processing (Cincinnati) SE:W:CAS:SP:C  
Field Director, Submission Processing (Fresno) SE:W:CAS:SP:F  
Field Director, Submission Processing (Kansas City) SE:W:CAS:SP:KC  
Field Director, Submission Processing (Ogden) SE:W:CAS:SP:O  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Office of Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis RAS:O  
Office of Management Controls OS:CFO:AR:M  
Audit Liaison: Commissioner, Wage and Investment Division SE:W:S:W



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## Appendix IV

### *Outcome Measures*

This appendix presents detailed information on the measurable impact that our recommended corrective action will have on tax administration. This benefit will be incorporated into our Semiannual Report to the Congress.

#### **Type and Value of Outcome Measure:**

- Taxpayer Rights and Entitlements – Potential; 2,294,762 taxpayers (pages 3, 11 and 13).

#### **Methodology Used to Measure the Reported Benefit:**

To determine the numbers of taxpayers affected, we generally used Internal Revenue Service (IRS) records to determine the volumes of notices issued during 2004 for which we recommended changes. To determine the number of taxpayers inappropriately receiving Taxpayer Notice Code (TPNC)<sup>1</sup> 299,<sup>2</sup> we developed a computer program to identify all tax returns posted to the Individual Master File<sup>3</sup> during the current year that reported an estimated tax penalty, had a balance due amount, and a TPNC 299.

- |   |           |
|---|-----------|
| – TPNCs 284, 285, 286, 287, 288, 289, 290, 291, 292, 293, 653, 701, 702, 741, 743, 745 and 748 <sup>4</sup> issued to taxpayers filing individual income tax returns: | 846,913   |
| – TPNCs 251, 252, and 295 <sup>5</sup> issued to taxpayers filing individual income tax returns:  | 1,395,712 |

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<sup>1</sup> Each TPNC corresponds to a specifically worded paragraph to be included in a notice issued to a taxpayer.

<sup>2</sup> Informs the taxpayer that the IRS changed the refund amount or the amount they owed because the amount entered on the tax return was computed incorrectly.

<sup>3</sup> The IRS database that maintains transactions or records of individual tax accounts.

<sup>4</sup> These TPNCs inform taxpayers that the IRS changed amounts on their returns related to the Earned Income Credit.

<sup>5</sup> These TPNCs inform taxpayers that the IRS changed amounts on their returns related to the Child Tax Credit or Additional Child Tax Credit.



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- TPNCs 299 inappropriately issued to taxpayers filing individual income tax returns with estimated tax penalties: 8,030<sup>6</sup>
- TPNCs 08<sup>7</sup> issued to taxpayers filing Employer’s Quarterly Federal Tax Returns (Form 941): 470
- Math Error Notices issued to taxpayers filing U.S. Corporation Income Tax Returns (Form 1120), U.S. Fiduciary Income Tax Returns (Form 1041), Farmers’ Cooperative Association Income Tax Return (Form 990-C), Exempt Organization Business Income Tax Return (Form 990-T): 43,600
- Inappropriate math error notices issued to taxpayers in our sample of 97 taxpayers receiving math error notices for Employer’s Annual Federal Unemployment (FUTA) Tax Return (Form 940): 37

We added all these figures together to determine the total potential number of taxpayers for which taxpayer rights and entitlements could be affected.

$(846,913 + 1,395,712 + 8,030 + 470 + 43,600 + 37 = 2,294,762)$

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<sup>6</sup> This number is based on the number of notices inappropriately issued in the prior year. The number in the draft report was 3,200 which represented notices inappropriately issued during the current year as of June 3, 2005.

<sup>7</sup> Informs taxpayers that the IRS changed amounts on their returns related to Social Security or Medicare taxes.



The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices

Appendix V

The Treasury Inspector General for Tax Administration's Proposed Changes to U.S. Individual Income Tax Return (Form 1040A)

"Amount You Owe" Section of Form 1040 A as Currently Formatted

	<b>38</b>	Add lines 36 and 37. This is your <b>total tax</b> .	▶ 38	
	<b>39</b>	Federal income tax withheld from Forms W-2 and 1099.	39	
	<b>40</b>	2004 estimated tax payments and amount applied from 2003 return.	40	
If you have a qualifying child, attach Schedule EIC.	<b>41a</b>	<b>Earned income credit (EIC).</b>	41a	
	<b>b</b>	Nontaxable combat pay election.	41b	
	<b>42</b>	Additional child tax credit. Attach Form 8812.	42	
	<b>43</b>	Add lines 39, 40, 41a, and 42. These are your <b>total payments</b> .	▶ 43	
<b>Refund</b>	<b>44</b>	If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you <b>overpaid</b> .	44	
Direct deposit? See page 50 and fill in 45b, 45c, and 45d.	<b>45a</b>	Amount of line 44 you want <b>refunded to you</b> .	▶ 45a	
	▶ <b>b</b>	Routing number <input type="text"/>	▶ <b>c</b> Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	
	▶ <b>d</b>	Account number <input type="text"/>		
	<b>46</b>	Amount of line 44 you want <b>applied to your 2005 estimated tax</b> .	46	
<b>Amount you owe</b>	<b>47</b>	<b>Amount you owe.</b> Subtract line 43 from line 38. For details on how to pay, see page 51.	▶ 47	
	<b>48</b>	Estimated tax penalty (see page 51).	48	

Source: 2004 Form 1040A.

"Amount You Owe" Section of Form 1040A As Proposed by TIGTA

	<b>38</b>	Add lines 36 and 37. This is your <b>total tax</b> .	▶ 38	
	<b>39</b>	Federal income tax withheld from Forms W-2 and 1099.	39	
	<b>40</b>	2004 estimated tax payments and amount applied from 2003 return.	40	
If you have a qualifying child, attach Schedule EIC.	<b>41a</b>	<b>Earned income credit (EIC).</b>	41a	
	<b>b</b>	Nontaxable combat pay election.	41b	
	<b>42</b>	Additional child tax credit. Attach Form 8812.	42	
	<b>43</b>	Add lines 39, 40, 41a, and 42. These are your <b>total payments</b> .	▶ 43	
<b>Refund</b>	<b>44</b>	If line 43 is more than line 38, subtract line 38 from line 43. This is the amount you <b>overpaid</b> .	44	
Direct deposit? See page 50 and fill in 45b, 45c, and 45d.	<b>45a</b>	Amount of line 44 you want <b>refunded to you</b> .	▶ 45a	
	▶ <b>b</b>	Routing number <input type="text"/>	▶ <b>c</b> Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings	
	▶ <b>d</b>	Account number <input type="text"/>		
	<b>46</b>	Amount of line 44 you want <b>applied to your 2005 estimated tax</b> .	46	
<b>Amount you owe</b>	<b>47</b>	Estimated tax penalty (see page 51).	47	
	<b>48</b>	<b>Amount you owe.</b> Subtract line 43 from line 38 and add line 47. For details on how to pay, see page 51.	▶ 48	

Source: Treasury Inspector General for Tax Administration's Proposed Revisions to Form 1040A.



*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

**Appendix VI**

*Management's Response to the Draft Report*



COMMISSIONER  
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
ATLANTA, GA 30308

RECEIVED  
SEP 01 2005

AUG 31 2005

MEMORANDUM FOR PAMELA J. GARDINER  
DEPUTY INSPECTOR GENERAL FOR AUDIT  
FROM: *Pamela B. Watson*  
*for* Richard J. Morgante  
Commissioner, Wage and Investment Division  
SUBJECT: Draft Audit Report – The Clarity of Math Error Notices Has Improved But Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices (Audit # 200530004)

I appreciate your recognition of the substantial progress that we have made in improving our math error notices. All of the Wage and Investment functions working in conjunction with the Single Point of Contact (SPOC) for Notices have made a concerted effort to identify unclear notices and schedule improvements based on impact to our customers. As a result, we have substantially improved the accuracy, clarity and readability of our notices. It is gratifying to have you acknowledge, "The IRS' notice redesign and training efforts have generally been effective." I also appreciate your comments recognizing, "Narrative explanations of the taxpayers' errors were usually specific enough to allow the taxpayers to identify the problems on their returns. The taxpayers' appeal rights were clearly explained and readily identifiable on many of the notices."

We concur that there are opportunities for further improvement. Clearly communicating complex tax calculation errors to our highly diverse customer base will always present challenges and opportunities for improvement. We recognize also that there are limitations impacting our ability to truly individualize our notices to a customer's need. These limitations are computer capacity, programming complexities, and the human resources needed to support such an endeavor. As you noted, we issue over 7 million math error notices annually.

Another major consideration, as we improve communication, is to prevent or reduce the probability of errors. In considering a proposed change to tax forms, we must carefully consider the impact on the total universe of users, not just the identified population who experienced a problem. This is particularly critical in changing high-use tax forms. Your recommendation to reverse the order of Lines 74 and 75 on Form 1040 and the corresponding lines on Form 1040A is a good illustration. While the recommendation would appear to solve a problem you identified impacting 3,200 filers, we estimate that



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*The Clarity of Math Error Notices Has Improved, but Further  
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over 63 million filers would have to adapt to the change. This would cause unnecessary burden and we believe confusion to the majority of filers, resulting in an increase in errors requiring resolution. Further, in this case the 3,200 filers would not have received the notice if they had properly followed the instructions for Lines 74 and 75 contained in the Instruction Booklet for Form 1040. We do acknowledge that the notice sent in this situation is unnecessary. We are exploring an alternate, systemic approach to suppressing the notice in situations where the taxpayer paid the tax and penalty but did not include the penalty amount in the total for Line 74.

I agree with six of the Recommendations but disagree with Recommendation #4 and Recommendation #5. I also agree with the Outcome Measure indicating a Potential Taxpayer Burden impact on approximately 2.3 million taxpayers. Attached are our comments to your recommendations. If you have any questions, please call me at (404) 338-7060, or members of your staff may contact David L. Medeck, Director, Customer Account Services, at (404) 338-8910.

Attachment



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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Attachment

**RECOMMENDATION 1**

The Director, Customer Account Services, Wage & Investment (W&I) Division, should ensure the review process for revised notices is adequate to produce notices that are accurate, and properly and consistently formatted.

**CORRECTIVE ACTION**

We agree that we can improve the existing process. Although we have a disciplined and regimented process already in place, we acknowledge that there are additional refinements which could be made. We have initiated a new procedure requiring the notice Subject Matter Experts and SPOC employees to jointly review revised notices during the Modernization and Information Technology Services Systems Acceptance Testing process to further improve the accuracy and consistency of the notices.

**IMPLEMENTATION DATE**

Completed – August 10, 2005

**RESPONSIBLE OFFICIAL**

N/A

**CORRECTIVE ACTION MONITORING PLAN**

N/A

**RECOMMENDATION 2**

The Director, Customer Account Services, W&I Division, should revise tax statement tables contained on notices to include specific amounts from at least some line items on which taxpayers made errors on their tax returns. Because the computer programming to make all line items from the tax returns available for inclusion on the notices may be resource intensive, efforts should be focused on including line items related to very frequently occurring errors.

**CORRECTIVE ACTION**

We agree in concept with this recommendation. We will review the existing Taxpayer Notice Codes (TPNC) and determine the feasibility of expanding them to allow greater specificity in the explanation of the error. If additional TPNCs can be added, we will be able to better explain the nature of the error in the text of the notice and its relevance to the tax statement portion of the notice. We will also study the possibility of adding additional lines from the 1040 payment section to the tax statement table on Math Error notices. Due to system capacity and other resource restrictions, our efforts will focus on the highest volume error conditions in the payment and tax areas of the tax return. The review of the TPNCs and the review of our ability to add additional lines will be completed by March 15, 2006.



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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**IMPLEMENTATION DATE**

March 15, 2006

**RESPONSIBLE OFFICIAL**

Director, W&I, Submission Processing  
Director, CARE, Media & Pubs, SPOC

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 3**

The Director, Customer Account Services, W&I Division, should revise CP16 to present information in a manner consistent with the other notices sent to individual taxpayers including the location of the error explanation and tax statement, and the wording of the taxpayers' rights to appeal with the math error adjustment.

**CORRECTIVE ACTION**

While we agree that the CP16 (Overpayment with an Offset to Another Obligation) needs revision, we are unable to commit to a firm completion date for this action. Recently, the W&I Notice SPOC organization has taken ownership of notices that were previously the responsibility of the Small Business/Self-Employed Notice SPOC. The combined function's first step is to prioritize all Individual Master File and Business Master File notices for revision. We had previously determined that the CP16 needed revision. The CP16 was one of the six Proof of Performance notices for the Document Sciences notice creation software. Although we did not include this notice in a major revision effort, MITS indicated they could add some of the design features of another notice to enhance the current CP16 notice. Eventually we will revise all notices. Although we cannot determine the priority to be assigned to the CP16 at this time, we will look for opportunities to expedite the revision process. Our prioritization working group will include Taxpayer Advocate Service and external stakeholders, and we will establish "TIGTA/GAO Recommendation" as one of the ranking criteria for prioritization.

**IMPLEMENTATION DATE**

Prioritization will be completed by March 15, 2006.

**RESPONSIBLE OFFICIAL**

Director, W&I, Submission Processing  
Director, CARE, Media & Pubs, SPOC



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*The Clarity of Math Error Notices Has Improved, but Further Changes Could Enhance Notice Clarity and Reduce Unnecessary Notices*

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**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 4**

The Director, Tax Forms and Publications, W&I Division, should add text on Form 1040 Line 74 "Amount You Owe" instructing taxpayers to include the amount of estimated tax penalty from Line 75. Consideration should be given to reversing the order of these lines on the Form 1040 to make the calculation process easier and more logical to taxpayers. Similar changes should be made to Form 1040A Line 47.

**CORRECTIVE ACTION**

There is not sufficient room to add text from the instructions for Line 74 to the front of Form 1040 advising taxpayers to include the estimated tax penalty from Line 75. The additional instructions would force a reduction in the font size of the reference on "how to pay", a message impacting a much larger number of taxpayers than those computing estimated tax penalty. In addition, we believe that reversing the line order would be counterproductive, resulting in increased confusion rather than clarity. Reversing the order of these lines would confuse and burden the 93 percent of approximately 56 million Form 1040 filers, and 98.5 percent of approximately 12 million Form 1040A filers who do not calculate their estimated tax penalty. Therefore, we will not implement this recommendation.

**IMPLEMENTATION DATE**

N/A

**RESPONSIBLE OFFICIAL**

N/A

**CORRECTIVE ACTION MONITORING PLAN**

N/A

**RECOMMENDATION 5**

Until sufficient changes are made on Forms 1040 and 1040A to instruct taxpayers to include the estimated tax penalty in the total amount of taxes they owe, the Director, Customer Account Services, W&I Division, should ensure that Error Resolution System (ERS) employees perform research and suppress notices from going to taxpayers who paid the proper amounts (amount of tax owed plus estimated tax penalty).

**CORRECTIVE ACTION**

As stated earlier, we do not believe changes should be made to Form 1040 and 1040A. Requiring research by ERS employees is not practical due to the additional cost in both processing time and labor. However, we will explore the possibility of establishing a systemic solution in the computer routine that will suppress the notice when a taxpayer



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actually paid the proper amount of tax, including the estimated tax penalty, but did not follow the guidance in the Form 1040 Instruction Booklet to include the penalty amount in line 74.

**IMPLEMENTATION DATE**

January 15, 2007

**RESPONSIBLE OFFICIAL**

Director, W&I, Submission Processing

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 6**

Along with changes already made or being made to text associated with TPNC 08, the Director of Customer Account Services, W&I Division, should ensure that changes are made to correct spelling and capitalization errors.

**CORRECTIVE ACTION**

We agree that corrections were needed to the text associated with TPNC 08. As noted in your report, corrections were made when they were brought to management's attention.

**IMPLEMENTATION DATE**

Completed – May 2005

**RESPONSIBLE OFFICIAL**

N/A

**CORRECTIVE ACTION MONITORING PLAN**

N/A

**RECOMMENDATION 7**

The Director of Customer Account Services, W&I Division, should ensure taxpayers' rights to appeal math error adjustments are clearly explained to taxpayers on math error notices associated with Forms 1120, 1041, 990-C, and 990-T.

**CORRECTIVE ACTION**

We agree with this recommendation. W&I Submission Processing has taken the lead role in coordinating the addition of appropriate language to Math Error notices that explain the taxpayers' rights to appeal math errors identified on their tax returns by IRS. The additional language will also be added to all Math Error notices issued on BMF Income Tax Returns meeting math error criteria. The new language will replace Notice



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433 (Interest and Penalty Information) and will be strategically placed on the notice to ensure that taxpayers are informed of their right to appeal. The additional language will be added to all applicable notices beginning January 2006.

**IMPLEMENTATION DATE**

February 15, 2006

**RESPONSIBLE OFFICIAL**

Director, W&I, Submission Processing

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.

**RECOMMENDATION 8**

The Director, Submission Processing, Customer Account Services, W&I Division, should provide specific instructions and training to appropriate ERS quality review employees and tax examiners regarding the appropriate notices to be sent to taxpayers making errors on Forms 940. Emphasis should be given to the need to use the TPNC which provides the most specific description of the taxpayers' errors.

**CORRECTIVE ACTION**

We agree with this recommendation. Additional instructions will be included in IRM 3.12.154, Unemployment Tax Returns, Error Resolution, which will detail specific guidance for using the most appropriate TPNC. The importance of using the most specific TPNC will be emphasized during annual CPE training for both tax examiners and quality review employees.

**IMPLEMENTATION DATE**

February 15, 2006

**RESPONSIBLE OFFICIAL**

Director, W&I, Submission Processing

**CORRECTIVE ACTION MONITORING PLAN**

We will monitor this corrective action as part of our internal management control system.