Should You Itemize or Take the Standard Deduction?

The following are excerpts from the March, 2002 GAO Report[1] to the Honorable Dick Armey, Majority Leader, House of Representatives.

Dear Mr. Armey:

This is our second report in response to your request for an estimate of the number of taxpayers who may have overpaid their taxes by claiming the standard deduction instead of itemizing their deductions, as well as of the amount of taxes that they may have overpaid. In our first report, we estimated that on about 510,000 returns for tax year 1998, taxpayers who claimed the standard deduction had deductible mortgage interest expense in excess of their standard deduction and overpaid their taxes by about $311 million.

In this report, our estimates include payments not only for mortgage interest but also for mortgage points, state and local income taxes, charitable contributions, and real estate and personal property tax for tax year 1998. We developed our estimate for mortgage interest payments, mortgage points, and state and local income taxes by matching a sample of tax year 1998 returns for individuals who did not claim itemized deductions with information in other Internal Revenue Service (IRS) databases. This information was supplied by lending institutions and employers and consisted, respectively, of the mortgage interest and points paid by each taxpayer and the wages paid to each taxpayer. Our estimates for charitable contributions and real estate and personal property taxes are averages for various income classes based on Department of Labor data. We assigned (imputed) these class averages to each taxpayer in the same income class in our sample. In this report, we also present information on the proportion of returns prepared by a third party on which taxpayers may have overpaid their taxes.

We estimate that on about 948,000 tax returns for tax year 1998, taxpayers did not itemize their deductions yet had payments for mortgage interest and points and for state and local income tax that exceeded the standard deduction for their tax filing status. When we impute charitable contributions and real estate and personal property tax payments, the estimate of the total number of taxpayers whose potential itemized deductions exceeded the claimed standard deduction could be as high as 2.2 million tax returns. [2]

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[1] GAO's Mission
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[2] The fastest and easiest way to obtain copies of GAO documents is through the Internet. GAO's Web site (www.gao.gov) contains abstracts and full-text files of current reports and testimony and an expanding archive of older products. The Web site features a search engine to help you locate documents using key words and phrases. You can print these documents in their entirety, including charts and other graphics.

We estimate that these taxpayers with unitemized mortgage interest, mortgage points, and state and local income taxes that exceeded the claimed standard deduction for their tax filing status are likely to have overpaid their taxes by about $473 million. When charitable contributions and real estate and personal property tax payments are included, the total overpayment of taxes could be as high as about $945 million. On the basis of this $945 million estimate, the average overpayment amount was an estimated $438. About 76 percent of these taxpayers may have overpaid by $500 or less, while the remaining 24 percent may have overpaid their taxes by more than $500. We also estimate that a third party prepared about 50 percent of the tax returns on which taxes may have been overpaid.