TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Results of the 2017 Filing Season

January 31, 2018

Reference Number: 2018-40-012

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RESULTS OF THE 2017 FILING SEASON

Highlights

Final Report issued on January 31, 2018

Highlights of Reference Number: 2018-40-012 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

IMPACT ON TAXPAYERS

The filing season, defined as the period from January 1 through mid-April, is critical for the IRS because it is during this time that most individuals file their income tax returns and contact the IRS if they have questions about specific laws or filing procedures. As of May 5, 2017, the IRS received 138.9 million tax returns (with 88.7 percent electronically filed) and issued more than 101.6 million refunds totaling almost $282 billion.

WHY TIGTA DID THE AUDIT

The objective of the review was to evaluate whether the IRS timely and accurately processed individual paper and electronically filed tax returns during the 2017 Filing Season.

WHAT TIGTA FOUND

The IRS generally developed processes to implement key tax provisions affecting the 2017 Filing Season. The IRS began accepting and processing individual tax returns on January 23, 2017, as scheduled.

The IRS processed 5.1 million tax returns that reported nearly $23.9 billion in Premium Tax Credits that were either received in advance or claimed at the time of filing. Taxpayers received $5.8 billion in Advanced Premium Tax Credits to which they were not entitled, of which $3.5 billion was not required to be repaid. In addition, as of May 4, 2017, more than 2.5 million taxpayers filed a return that was silent with respect to their health care coverage.

The IRS held all refunds that include the Earned Income Tax Credit and Additional Child Tax Credit until February 15, 2017, as required. In addition, most tax return preparers complied with the expanded due diligence requirements for the Child Tax Credit, Additional Child Tax Credit, and American Opportunity Tax Credit (AOTC). As of May 4, 2017, 441,071 (93.5 percent) of the 471,518 tax return preparers who filed at least one claim for these credits included Form 8867, *Paid Preparer's Due Diligence Checklist*, as required. However, IRS processes do not ensure that all noncompliant preparers are notified.

The IRS continues to pay the AOTC for ineligible students. TIGTA estimates the IRS erroneously paid $2.8 billion in AOTCs on more than 1.7 million Tax Year 2016 returns on which no educational institution Employer Identification Number was provided as required or the student received the AOTC for more than the four-year limit.

The IRS inappropriately denied approximately $1 million in Residential Energy Efficient Property Credits to 494 taxpayers as of May 4, 2017. In addition, IRS processes do not effectively determine whether taxpayers filing as Married Filing Separately and claiming the Child and Dependent Care Credit are eligible under an exception in the law before denying the credit. Married Filing Separately taxpayers filed 12,057 claims for the Child and Dependent Care Credit totaling $7.4 million, all of which were denied by the IRS.

WHAT TIGTA RECOMMENDED

TIGTA made seven recommendations, including revising procedures to notify all tax preparers filing a Child Tax Credit claim who do not comply with the due diligence requirements; developing math error procedures to deny AOTC claims when the educational institution Employer Identification Number is not provided; and modifying Form 2441, *Child and Dependent Care Expenses*, to allow Married Filing Separately taxpayers to attest that they meet the exception for eligibility. TIGTA also recommended that the IRS review the potentially erroneous returns it identified to ensure that taxpayers receive the benefits to which they are entitled and recover benefits paid in error.

The IRS agreed with all seven recommendations.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

January 31, 2018

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

FROM: Michael E. McKenney
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Results of the 2017 Filing Season
(Audit # 201740005)

This report presents the results of our review to evaluate whether the Internal Revenue Service timely and accurately processed individual paper and electronically filed tax returns during the 2017 Filing Season. This audit was included in our Fiscal Year 2017 Annual Audit Plan and addresses the major management challenge of Implementing the Affordable Care Act and Other Tax Law Changes.

Management's complete response to the draft report is included as Appendix VII.

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. If you have any questions, please contact me or Russell P. Martin, Assistant Inspector General for Audit (Returns Processing and Account Services).

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Abbreviations

ACA	Affordable Care Act
ACTC	Additional Child Tax Credit
AOTC	American Opportunity Tax Credit
APTC	Advance Premium Tax Credit
CTC	Child Tax Credit
e-file(d), e-filing	Electronically File(d); Electronic Filing
EIN	Employer Identification Number
EITC	Earned Income Tax Credit
HCTC	Health Coverage Tax Credit
IRS	Internal Revenue Service
IRTF	Individual Return Transaction File
ITIN	Individual Taxpayer Identification Number
PATH Act	Protecting Americans From Tax Hikes Act of 2015
PTC	Premium Tax Credit
RRP	Return Review Program
SRP	Shared Responsibility Payment
SSN	Social Security Number
TAC	Taxpayer Assistance Center
TIGTA	Treasury Inspector General for Tax Administration

Background

The annual tax return filing season[1] is a critical time for the Internal Revenue Service (IRS) as this is when most individuals file their income tax returns and contact the IRS if they have questions about specific tax laws or filing procedures. As of May 5, 2017, the IRS received 138.9 million individual income tax returns. In addition, the IRS provided assistance to millions of taxpayers via the telephone, website, social media, and face-to-face assistance.

One of the continuing challenges the IRS faces each year in processing tax returns is the implementation of new tax law changes as well as changes resulting from expired tax provisions. Before the filing season begins, the IRS must identify the tax law and administrative changes affecting the upcoming filing season. Once identified, the IRS must develop or revise the various tax forms, instructions, and publications. It also must reprogram its computer systems to ensure that tax returns are accurately processed based on changes in the tax law. Errors in the IRS's tax return processing systems may delay tax refunds, affect the accuracy of taxpayer accounts, or result in incorrect taxpayer notices.

Tax law changes affecting the 2017 Filing Season

- ***The Patient Protection and Affordable Care Act (ACA)***[2] – Enacted March 23, 2010, it provides incentives and tax breaks to individuals and small businesses to offset health care expenses. It also imposes Shared Responsibility Payments (SRP), administered through the tax code, for individuals and businesses that do not obtain health care coverage for themselves or their employees. For the 2017 Filing Season, the IRS continued its efforts to verify claims for the Premium Tax Credit (PTC). Taxpayers who purchase insurance through an Exchange are required to file a tax return and attach Form 8962, *Premium Tax Credit (PTC)*, to claim the PTC and reconcile any Advance PTC (APTC) payments that were made to an insurer on their behalf.

  The ACA also requires individuals to report on their compliance to maintain minimum essential health insurance coverage. Individuals who do not maintain minimum essential coverage or qualify for an exemption from the requirement must make an SRP. On January 20, 2017, the President issued Executive Order 13765 *Minimizing the Economic Burden of the Patient Protection and Affordable Care Act Pending Repeal,*[3] directing

[1] See Appendix VI for a glossary of terms.
[2] Pub. L. No. 111-148, 124 Stat. 119 (2010) (codified as amended in scattered sections of the Internal Revenue Code and 42 U.S.C.), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029.
[3] Exec. Order 13765, 82 Fed. Reg. 8351–8352 (Jan. 24, 2017).

Federal agencies to exercise authority and discretion available to them to reduce potential burden on taxpayers in complying with ACA requirements.

- ***The Trade Preferences Extension Act of 2015***[4] **–** Enacted June 29, 2015, it prohibits individuals claiming the foreign earned income exclusion or housing deduction from receiving the refundable Additional Child Tax Credit (ACTC). In addition, it retroactively extended the Health Coverage Tax Credit (HCTC) for Tax Year 2014 and continued the credit through Tax Year 2019.[5] The HCTC is a tax credit that pays a portion of qualified health insurance premiums for eligible individuals and their families.

  Beginning with Calendar Year 2016, eligible individuals can choose to receive the HCTC on a monthly basis. Individuals can have up to 72.5 percent of their qualified health insurance premiums paid in advance. The Treasury Inspector General for Tax Administration (TIGTA) conducted a separate review to assess the effectiveness of the IRS's implementation of advance HCTC payments.[6] It should be noted that the HCTC is not part of the ACA. However, the legislation contains some important modifications that require coordination of this credit with the PTC under the ACA and other provisions of the ACA.

  Finally, this legislation requires that an individual claiming the American Opportunity Tax Credit (AOTC), Lifetime Learning Credit, or the Tuition and Fees Deduction must receive a statement from the educational institution to claim these benefits. This statement, which is generally a Form 1098-T, *Tuition Statement*, provides the name, address, and Employer Identification Number (EIN) of the educational institution. An exception to the statement requirement is allowed if the taxpayer claiming the benefit has taken certain steps to obtain a statement from the institution. This provision is effective for tax years beginning after June 29, 2015.

- ***Consolidated Appropriations Act of 2016***[7] – Enacted on December 18, 2015, it contains the Protecting Americans From Tax Hikes Act of 2015 (PATH Act), which extended numerous tax provisions that expired at the end of Tax Year 2014. Many of the provisions were permanently extended, while others were extended for either two or five years.

  The PATH Act also contains a number of provisions referred to as program integrity provisions intended to reduce fraudulent and improper Earned Income Tax Credit (EITC), Child Tax Credit (CTC), ACTC, and AOTC payments. The majority of the program integrity provisions were effective January 1, 2016, and affect the processing of

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[4] Pub. L. No. 114-27.
[5] The HCTC originally expired at the end of Calendar Year 2013.
[6] TIGTA, Ref. No. 2017-40-033, *Implementation of the Health Coverage Tax Credit Enrollment and Systemic Advance Monthly Payment Process* (May 2017).
[7] Pub. L. No. 114-113 (H.R. 2029).

Tax Year 2016 returns. Figure 1 provides a description of the integrity provisions included in the PATH Act.

Figure 1: PATH Act Integrity Provisions

Provision	Description	Effective Date
Section 201: Modification of filing dates of returns and statements relating to employee wage information and nonemployee compensation to improve compliance	Modifies the due dates of Forms W-2, *Wage and Tax Statement*, and documents reporting nonemployee compensation such as Forms 1099-MISC, *Miscellaneous Income,* to January 31. Also provides additional time for the IRS to review refund claims based on the EITC and the ACTC in order to reduce fraud and improper payments. No refund based on claims for the EITC or the ACTC shall be made to a taxpayer before February 15.	January 1, 2016 (2017 Filing Season)
Section 203: Requirements for the issuance of Individual Taxpayer Identification Numbers (ITIN)	Modifies the period an ITIN will remain active. The provision requires the IRS to deactivate ITINs that are not used on a tax return at least once in the last three tax years. In addition, starting on January 1, 2017, it requires the IRS to deactivate ITINs issued prior to January 1, 2013.	December 18, 2015 (2016 Filing Season)
Sections 204 - 206: Prevention of retroactive claims	Prevents retroactive claims of the EITC after issuance of a Social Security Number (SSN) and prevents retroactive claims of the CTC/ACTC and the AOTC after the issuance of an SSN, ITIN, or Adoption Taxpayer Identification Number. Taxpayers cannot file an amended tax return or original tax return for prior years to claim credits if the SSN, ITIN, or Adoption Taxpayer Identification Number were not issued prior to the return due date.	December 18, 2015 (2016 Filing Season)
Section 207: Procedures to reduce improper claims	Expands the paid-preparer due diligence requirements with respect to the EITC and the associated $510 penalty for failure to comply to cover returns claiming the CTC/ACTC and the AOTC.	January 1, 2016 (2017 Filing Season)

Provision	Description	Effective Date
Section 208: Restrictions on taxpayers who improperly claimed credits in prior year	Expands, to apply to the CTC/ACTC and the AOTC, the rules under current law that require individuals to recertify eligibility for the EITC claim after disallowance and bars individuals from claiming the EITC for 10 years if the credit was claimed fraudulently and for two years if they recklessly or intentionally disregarded the rules. Adds math error authority, which permits the IRS to disallow improper credits without a formal audit if the taxpayer claims the credit in a period during which he or she is barred.	January 1, 2016 (2017 Filing Season)
Section 211: EIN required for the AOTC	Requires that the individual taxpayer provide the EIN of the educational institution to which qualified tuition and related expenses were paid with respect to that individual in order to claim the AOTC.	January 1, 2016 (2017 Filing Season)

Source: The PATH Act.

Due to the extensive nature of the PATH Act integrity provisions, we conducted (and are still conducting) a series of separate audits to evaluate the IRS's implementation of these provisions.[8]

The 2017 Filing Season results are being presented as of several dates between March 2, 2017, and May 15, 2017, depending on when the data were available. This review was performed with information obtained from the Wage and Investment Division Headquarters located in Atlanta, Georgia; the Wage and Investment Division Submission Processing function offices in Cincinnati, Ohio; and the Information Technology Headquarters organization in Lanham, Maryland, during the period April through September 2017. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

[8] TIGTA, Ref. No. 2017-40-033, *Implementation of the Health Coverage Tax Credit Enrollment and Systemic Advance Monthly Payment Process* (May 2017); TIGTA, Ref. No. 2017-40-042, *Processes Do Not Maximize the Use of Third-Party Income Documents to Identify Potentially Improper Refundable Credit Claims* (July 2017); TIGTA, Ref. No. 2018-40-011, *Some Legal Requirements to Deactivate Individual Taxpayer Identification Numbers Have Not Been Met* (Jan. 2018); and TIGTA, Ref. No. 2018-40-010, *Processes Need to Be Improved to Identify Incomplete and Fraudulent Applications for Individual Taxpayer Identification Numbers* (Jan. 2018).

Results of Review

Processing Tax Returns

In preparation for the 2017 Filing Season, the IRS made significant changes to its processes and procedures to address legislative requirements. The IRS began accepting and processing individual tax returns on January 23, 2017, as scheduled. As of May 5, 2017, the IRS received approximately 138.9 million tax returns. Figure 2 presents comparative filing season statistics as of May 5, 2017.

Figure 2: Comparative Filing Season Statistics (as of May 5, 2017)

Cumulative Filing Season Data	2016 Actual	2017 Actual	% Change
Individual Income Tax Returns			
Total Returns Received (000s)	139,620	138,945	-0.48%
Paper Returns Received (000s)	16,219	15,706	-3.16%
Electronically Filed (E-Filed) Returns Received (000s)	123,401	123,239	-0.13%
Practitioner Prepared (000s)	71,476	71,154	-0.45%
Home Computer (000s)	51,925	52,085	0.31%
Free File (000s) *(also in the Home Computer total)*	2,509	2,448	-2.43%
Fillable Forms (000s) *(also in the Home Computer total)*	310	289	-6.77%
Percentage of Returns E-Filed	88.4%	88.7%	0.34%
Refunds			
Total Number Issued (000s)	101,244	101,641	0.39%
Total Dollars (in millions)	$276,525	$281,661	1.86%
Average Dollars	$2,731	$2,771	1.46%
Total Number of Direct Deposits (000s)	83,669	84,424	0.90%
Total Direct Deposit Dollars (in millions)	$242,820	$248,195	2.21%

Source: Multiple 2017 Filing Season reports. Totals and percentages shown are rounded. The 2016 Filing Season figures are through May 6, 2016, and the 2017 Filing Season figures are through May 5, 2017.

Implementation of Affordable Care Act Provisions

As of May 4, 2017, the IRS processed 5.1 million tax returns that reported nearly $23.9 billion in PTCs that were either received in advance or claimed at the time of filing. A total of $5.8 billion in APTCs received was in excess of PTCs that taxpayers were entitled to—$3.5 billion of this is not required to be repaid.[9] It should be noted that the Exchanges have sole responsibility to determine eligibility to purchase insurance and the amount of the APTC an individual will receive. Figure 3 provides a comparison of PTC statistics for Processing Years 2016 and 2017 based on the results from our analysis of tax returns filed and processed as of May 4, 2017.

Figure 3: PTC Statistics
Processing Years 2016 and 2017

	Processing Year 2016 as of May 5, 2016	Processing Year 2017 as of May 4, 2017
Total Tax Returns With the PTC	**4.7 million**	**5.1 million**
Total PTC Amount (includes the APTC and the PTC)	$18.9 billion	$23.9 billion
Total APTC Amount	*$17.7 billion*	*$22.5 billion*
Total PTC Claimed at Filing in Excess of the APTC	*$1.2 billion*	*$1.4 billion*
Tax Returns in Which the PTC Equals the APTC Received		
Tax Returns	138,252	155,133
Total PTC Amount	$574.7 million	$821.9 million
Tax Returns With Additional PTC – (taxpayer is entitled to more PTC than what was received in the APTC)		
Total Tax Returns	1.9 million	2.1 million
Total PTC Amount (includes APTC and PTC)	$7.9 billion	$9.7 billion
Total APTC Amount	*$6.8 billion*	*$8.3 billion*
Total PTC Claimed at Filing in Excess of APTC	*$1.2 billion*	*$1.4 billion*

[9] The ACA limits the amount of tax that individuals with income between 100 percent and 400 percent of the Federal Poverty Line will have to repay.

Tax Returns With Excess APTC Payments – (taxpayer receives more APTC than PTC entitled to and has to repay)		
Total Tax Returns	2.6 million	2.8 million
Total PTC Amount	$6.1 billion	$7.5 billion
Total APTC Amount	$10.3 billion	$13.4 billion
Total APTC Reported in Excess of PTC	$4.2 billion	$5.8 billion
Total APTC Above the Repayment Limit (not repaid)	*$2.2 billion*	*$3.5 billion*
Total APTC Below the Repayment Limit (repaid)	*$2.0 billion*	*$2.3 billion*

Source: TIGTA analysis of Individual Master File posted tax return information as of May 5, 2016 (Cycle 18), and May 4, 2017 (Cycle 18). Totals may not add due to rounding.

Minimum essential coverage and SRP requirements

As of May 4, 2017, the IRS received approximately 106.2 million tax returns reporting that all members of the taxpayer's family maintained minimum essential coverage as required by the ACA. Another nearly 10.8 million taxpayers filed a return with a Form 8965, *Health Coverage Exemptions*, attached indicating that at least one taxpayer on the tax return is exempt from the minimum essential coverage requirement. In addition, approximately 4.1 million taxpayers self-reported SRPs totaling $2.9 billion for not maintaining required coverage. Figure 4 shows a comparison of taxpayers reporting minimum essential coverage or self-reporting the SRPs for Processing Years 2016 and 2017 as of May 4, 2017.

Figure 4: Minimum Essential Coverage and SRPs – Processing Years 2016 and 2017

	Processing Year 2016	Processing Year 2017	% Change
Returns Reporting All Family Members Had Minimum Essential Coverage	104.7 million	106.2 million	1.4%
Returns Claiming an Exemption From Minimum Essential Coverage	11.2 million	10.8 million	-3.6%
Returns Reporting an SRP	5.6 million	4.1 million	-26.8%

	Processing Year 2016	Processing Year 2017	% Change
Amount of the SRP	$2.5 billion	$2.9 billion[10]	16.0%

Source: TIGTA analysis of individual tax returns processed as of May 5, 2016, and the IRS's ACA Filing Season Statistics Report Filing Season 2017 (Cycle 18), as of May 4, 2017.

Processes established to identify noncompliant filers and assess the SRP were changed in response to an Executive Order

Beginning with the 2017 Filing Season, the IRS developed processes to identify taxpayers at the time tax returns are processed who did not report maintaining minimum essential coverage, self-report an SRP, or claim an exemption. The IRS refers to these returns as "silent returns." The IRS planned to reject e-filed silent returns back to the taxpayer notifying them of the requirement to report minimum essential coverage, submit a Form 8965 to claim an exemption, or pay the SRP. Paper tax returns would be identified, and the IRS would correspond with the taxpayer. Taxpayers who did not respond would be assessed the SRP.

On January 20, 2017, the President issued Executive Order 13765 directing Federal agencies to exercise authority and discretion available to them to reduce potential burden on taxpayers in complying with ACA requirements. In response, on February 3, 2017, the IRS changed its processes and procedures for identifying taxpayers who failed to report on their compliance with the minimum essential coverage requirements at the time tax returns were filed. As a result, the IRS processed all silent e-filed and paper tax returns rather than verifying the taxpayer's compliance before refunds were paid. IRS management noted that it will continue to address noncompliance with the minimum essential coverage and SRP requirements as part of its post-processing compliance program similar to efforts in prior tax years. IRS management also stated that plans are underway to reinstate the processes for silent returns that were discontinued in the 2017 Filing Season for the 2018 Filing Season.

As of May 4, 2017, more than 2.5 million taxpayers filed a Tax Year 2016 return during the 2017 Filing Season that was silent with respect to their health care coverage.[11] In comparing how these taxpayers reported their health care coverage in Tax Year 2015, we found that more than one million (40 percent) taxpayers reported compliance with minimum essential requirements or claimed an exemption on their Tax Year 2015 return with an additional

[10] The SRP increased from Tax Year 2015 to Tax Year 2016. The family maximum for Tax Year 2015 was $975 and increased to $2,085 for Tax Year 2016. However, the maximum SRP is capped at the cost of the national average premium for a bronze-level health plan through the Marketplace. For the 2017 Filing Season, $13,380 is the maximum amount of the SRP for a family with five or more members which is up from the $12,240 maximum the previous year.

[11] The 2.5 million does not include taxpayers who indicated they could be claimed as a dependent on another tax return.

115,085 taxpayers reporting SRPs totaling $65.3 million. Figure 5 shows how taxpayers filing a silent return in Tax Year 2016 reported their health care coverage in Tax Year 2015.

Figure 5: How Tax Year 2016 Silent Return Filers Reported Health Care Coverage in Tax Year 2015 (as of May 4, 2017)

Tax Year 2015 Reporting Method	Returns	Percentage of Silent Returns
Filed a Silent Return or Did Not File	1,401,719	55%
Claimed Minimum Essential Coverage or an Exemption	1,015,562	40%
Reported an SRP[12]	115,085	5%
Tax Year 2016 Silent Returns	***2,532,366***	***100%***

Source: TIGTA analysis of the Individual Return Transaction File (IRTF).

Implementation of Key Tax Provisions of the Protecting Americans From Tax Hikes Act

The IRS has developed processes to implement key tax provisions of the PATH Act. These include the holding of refunds for taxpayers claiming EITCs and ACTCs until February 15 as well as identifying tax returns with CTC, ACTC, and AOTC claims filed by individuals with an inactive ITIN. However, processes did not always ensure that preparers who were not compliant with the due diligence requirements were notified.

Processes were established to hold refunds that include the EITC and the ACTC until February 15 as required

Our analysis of 10.3 million returns with an EITC or ACTC claim processed as of March 2, 2017, found that the IRS held refunds as required until February 15. Refunds associated with these 10.3 million returns totaled $51.2 billion and included EITCs totaling $28.4 billion and ACTCs totaling $10.3 billion. The IRS began releasing refunds on or after February 15, 2017, for those returns being held that were not identified for additional review.

It should be noted that the PATH Act also moved the filing date for Forms W-2 and Forms 1099-MISC that report nonemployee compensation to January 31. This enables the IRS to validate the income used to support EITC and ACTC claims before refunds are issued. We

[12] Included in this category are tax returns that had an SRP but also reported that they had minimum essential coverage or an exemption.

are conducting a separate audit of the IRS's efforts to verify the income reported on EITC and ACTC claims and plan to issue our report later this calendar year.[13]

Processes were established to identify CTC, ACTC, and AOTC claims filed by individuals with an inactive ITIN

The PATH Act also granted the IRS authority to systemically disallow CTC, ACTC, and AOTC claims filed by individuals with an inactive ITIN, including those that are deactivated or revoked by the IRS.[14] In response, the IRS developed processes to identify tax returns filed with an inactive ITIN. As of May 3, 2017, the IRS rejected 195 e-filed returns filed with an inactive ITIN and identified an additional 188,362 e-filed and paper tax returns for review.[15] We are conducting a separate audit on the accuracy of the IRS's deactivation of the ITINs and plan to issue our report later this calendar year.[16]

IRS procedures to notify preparers that they should have filed Form 8867, Paid Preparer's Due Diligence Checklist, are not complete

Prior to the 2017 Filing Season, preparers used Form 8867 to report on their compliance with the EITC due diligence requirements. Beginning with the 2017 Filing Season, the PATH Act expanded these due diligence requirements to include the CTC, ACTC, and AOTC. In response to this legislation, the IRS revised Form 8867 to include the expanded due diligence requirements for the CTC, ACTC, and AOTC. In addition, the IRS developed processes to identify preparers who do not provide Form 8867 as required and notify them of their noncompliance. However, our review of these processes found that they do not ensure that all preparers who do not provide a Form 8867 are notified. For example, as of May 4, 2017, we identified that 30,447 (6.5 percent) of the 471,518 preparers who filed a CTC, ACTC or AOTC claim did not provide the Form 8867 as required.[17] However, the IRS did not send a notice to 23,624 (77.6 percent) of these preparers to notify them of the requirement to file a Form 8867.

The IRS systemically identifies all e-filed tax returns filed by a preparer (excluding those who only provide an EIN as their preparer number) with a CTC, ACTC, AOTC, or EITC claim for which Form 8867 was not included with the tax return. The IRS sends the preparer an automated alert reminding the preparer of the Form 8867 requirement and notifying the preparer that the

[13] TIGTA, Audit Number 201740031, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds are Paid*.

[14] The IRS revokes an ITIN when it later determines the ITIN should not have been issued or is no longer valid given certain conditions, such as the taxpayer is deceased or has been assigned an SSN.

[15] The IRS discontinued use of its e-file reject processes on January 19, 2017. Subsequent to January 19, 2017, all e-filed returns with an inactive ITIN are being identified for additional review.

[16] TIGTA, Audit Number 201640023, *Some Legal Requirements to Deactivate Individual Taxpayer Identification Numbers Have Not Been Met.*

[17] We did not review tax returns with the EITC because it was not a new requirement in Filing Season 2017 and compliance with that requirement had previously been tested.

IRS can impose a $510 penalty for each failure to submit Form 8867. The IRS also identifies preparers who file paper tax returns without a Form 8867 attached and sends a letter to remind these preparers of their due diligence requirement. However, the IRS only sends a letter to preparers who file more than one paper return with no Form 8867 attached. The IRS also does not send a letter to preparers who file returns after the end of the filing season or to preparers who only provided an EIN as their preparer number. In addition, the IRS does not send a letter to preparers when the return claims only the CTC as letters are sent to preparers who only claim a refundable credit.

Further analysis of the 23,624 preparers who did not receive any type of notice from the IRS found that 14,343 (60.7 percent) had filed at least one tax return that included Form 8867, so it appears that the preparer was aware of the requirement to file Form 8867 regardless of whether the IRS told them of the need to do so. None of the tax returns filed by the remaining 9,281 preparers with a CTC, ACTC, or AOTC claim had a Form 8867 attached, and the IRS did not educate them of the requirement to file one.

- 4,966 (53.5 percent) preparers filed tax returns claiming only the CTC. IRS management indicated that it was a business decision to not notify preparers who file paper tax returns claiming only the CTC because their process to notify these preparers is manually intensive and the number of paper returns filed containing only the CTC did not warrant their inclusion. Because the expanded due diligence requirements specifically include the CTC, we believe the IRS should identify and alert these preparers of their requirement to file Form 8867.

- 4,274 (46.1 percent) preparers who filed one paper tax return and the paper return is the only return filed by the preparer with a CTC, ACTC, or AOTC claim; only provided a preparer EIN or provided an invalid Preparer Tax Identification Number; or filed returns after the IRS's cutoff date. IRS management indicated that the cost of identifying these types preparers outweigh the benefit of educating them of the filing requirement. We agree with the IRS's conclusion.

- 41 (0.4 percent) preparers for which we are unable to determine why the IRS did not send a notice or alert. As of October 16, 2017, IRS management has not provided us with the reason why these preparers were not notified of the due diligence filing requirement.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 1***:*** Revise procedures to include issuing letters and alerts to preparers who file tax returns claiming the CTC but do not provide the required Form 8867.

> ***Management's Response:*** The IRS agreed with this recommendation that applies to paper returns and letters. IRS management responded that a process was already in place to issue alerts on electronic returns claiming the CTC. Programming changes to this non-systemic letter process has been implemented and will be effective January 2018.

Recommendation 2: Evaluate the 41 preparers we identified who filed CTC, ACTC, and AOTC claims without a Form 8867 and were not notified by the IRS, and ensure that actions are taken to notify the preparers of the filing requirement if warranted.

> ***Management's Response:*** The IRS agreed with this recommendation. IRS management completed the review and determined 14 were preparers with non-U.S. addresses, seven were cases in which there was known preparer identity theft, two were cases of duplicate returns from the same taxpayer, and 18 were instances in which the returns were adjusted so they did not meet the criteria for notification. As a result, the IRS sent letters to the preparers with non-U.S. addresses to alert them of the Form 8867 requirement in October 2017. IRS management also changed procedures to send letters to all preparers, regardless of address.

Some Additional Child Tax Credit Claims Associated With Returns Claiming the Foreign Earned Income Exclusion or Housing Deduction Were Erroneously Paid

The IRS implemented processing controls to limit the ACTC on tax returns when the foreign earned income exclusion or housing deduction was claimed on Form 2555, *Foreign Earned Income*. Our analysis of Tax Years 2014 and 2015 tax returns that claimed ACTCs found that the number of taxpayers claiming ACTCs when filing Form 2555 decreased by 99.3 percent (from 17,297 taxpayers for Tax Year 2014 to 124 taxpayers in Tax Year 2015). However, our analysis of the 124 taxpayers who claimed the ACTC with a foreign earned income exclusion in Tax Year 2015 found that the IRS erroneously paid ACTCs totaling $71,918 associated with claims on 45 (36 percent) of these tax returns. Specifically, we identified:

- 38 taxpayers who claimed the foreign earned income exclusion or housing deduction erroneously received $60,177 in ACTCs. Based on our analysis of these returns, the IRS identified these returns for additional review during processing; however, tax examiners incorrectly allowed the ACTC.

- 7 taxpayers who claimed the ACTC and later filed an amended return reporting a foreign earned income exclusion or housing deduction. Because these individuals filed a Form 2555, they are no longer eligible to receive the ACTC. Our analysis of the tax returns filed by these individuals found that the IRS did not recover $11,741 in ACTCs.

We provided IRS management with the results of our analysis on September 6, 2017. Management indicated that the 38 tax returns that were stopped during processing for additional review were incorrectly processed by the Error Resolution function examiner. In addition, management agreed that the ACTC was not recovered for the seven tax returns when the amended return reporting a foreign income exclusion or housing deduction was processed after the ACTC had been allowed.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 3***:*** Ensure that IRS employees who process these credits are aware that taxpayers reporting a foreign income exclusion or housing deduction cannot also receive the ACTC.

> ***Management's Response:*** The IRS agreed with this recommendation. IRS management responded that existing procedures are covered in the International Error Resolution System training material. IRS management also created a Quality Alert on November 7, 2017, for Error Resolution System instructors to reinforce the procedures during annual refresher training and in the initial training for international returns.

Recommendation 4: Review the 45 tax returns we identified for which the IRS erroneously paid the ACTC and take the actions necessary to recover the erroneous payments.

> ***Management's Response:*** The IRS agreed with this recommendation and plans to review the affected returns and take the appropriate action to recover the erroneous payments.

Tax Examiner Errors Result in Some Taxpayers Continuing to Not Receive the Residential Energy Efficient Property Credits to Which They Are Entitled

We continue to identify that the IRS is incorrectly limiting taxpayers' Residential Energy Efficient Property Credit to the $500 ($1,000 if Married Filing Jointly) limit associated with the Nonbusiness Energy Property Credit. Taxpayers can claim a credit based upon the costs of certain property such as solar electric and geothermal heat pump items that is generally limited to their tax liability.[18] We previously reported this condition in the 2015 and 2016 Filing Seasons. A summary of our prior audit findings and the actions taken by the IRS to address our concerns can be found in Appendix V.

On February 10, 2017, we once again alerted IRS management that the corrective actions taken in response to our prior recommendations do not ensure that Residential Energy Efficient Property Credit claims are processed correctly. Our review of tax returns processed as of March 2, 2017, identified 123 tax returns for which the IRS had improperly reduced Residential Energy Efficient Property Credit claims by a total of approximately $241,000. IRS management agreed with our assessment and indicated that computer programming errors would be corrected by March 19, 2017.

Our analysis of tax returns processed as of May 4, 2017, found that the IRS had improperly reduced Residential Energy Efficient Property Credit claims on 494 tax returns by approximately $1 million. The 494 tax returns include 248 paper returns and 246 e-filed returns. The IRS's corrective action implemented in March 2017 only applied to e-filed returns. We found that the 246 e-filed tax returns were processed before the corrective action was implemented. The 248 paper returns are due to human error and are not related to the programming error, which we determined the IRS correctly implemented.

We provided the 494 tax returns we identified to the IRS on July 17, 2017, for its review. The IRS agreed that Residential Energy Efficient Property Credits were being improperly reduced. Management stated that the credits were being limited incorrectly due to employee errors. Parts of the Residential Energy Efficient Property Credit expired on December 31, 2016. As of September 20, 2017, the credit has not been extended.

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[18] Residential Energy Credits are claimed on Line 53 of Form 1040, *U.S. Individual Income Tax Return*, and supported by Form 5695, *Residential Energy Credits*. The Residential Energy Efficient Property Credit is claimed on Part I of Form 5695 and is generally limited to the taxpayer's income tax liability. The Nonbusiness Energy Property Credit is claimed on Part II of Form 5695 and is generally limited to $500 but can be as much as $1,000 for married taxpayers filing jointly if certain conditions are met.

Recommendation

The Commissioner, Wage and Investment Division, should:

Recommendation 5: Review the 494 tax returns we identified and take the actions necessary to ensure that these taxpayers receive the Residential Energy Efficient Property Credit to which they are entitled.

> ***Management's Response:*** The IRS agreed with this recommendation and has corrected 484 of the 494 taxpayers' accounts for the amounts to which they are entitled. Of the remaining 10 accounts, seven require additional research and three cannot be adjusted due to an ongoing examination.

Billions of Dollars in Potentially Erroneous American Opportunity Tax Credits Continue to Be Issued

The IRS continues to not effectively identify potentially erroneous AOTC claims before refunds are paid. Our review of nearly eight million Tax Year 2016 returns processed as of May 4, 2017, receiving approximately $14 billion in AOTCs, identified more than 1.7 million taxpayers who received an estimated $2.8 billion ($1.5 billion in refundable credits and $1.2 billion in nonrefundable credits) in potentially erroneous AOTCs to which they are not entitled.[19] These include taxpayers who did not report an institutional EIN on Form 8863, *Education Credits (American Opportunity and Lifetime Learning Credits)*, as required or claimed the AOTC beyond the four-year limit.[20] In addition, we identified 2.9 million taxpayers who received more than $4.6 billion in potentially erroneous AOTC claims that either did not have a Form 1098-T filed with the IRS or claimed students who did not meet the AOTC eligibility requirements. Figure 6 provides the number of taxpayers we estimate received potentially erroneous AOTCs for Tax Year 2016 as of May 4, 2017. Previously reported deficiencies are marked with an asterisk (*).

[19] Numbers do not total due to rounding.
[20] The 1.7 million taxpayers and $2.8 billion presented here eliminate any duplication between the two categories included in Figure 6.

Figure 6: Estimated Potentially Erroneous AOTCs Received for Tax Year 2016 (as of May 4, 2017)

AOTC Claims	Reason Taxpayer Is Not Entitled to the AOTC	Number of Tax Returns	Amount of AOTCs
Total Claims		7,991,981	$13,915,998,189
No Institution EIN Provided on Form 8863	PATH Act Section 211 requires the taxpayer to include the EIN of the educational institution.	1,293,798	$1,930,913,303
Received the AOTC for More Than Four Tax Years for Same Student*[21]	The American Recovery and Reinvestment Act of 2009[22] allows the AOTC for the first four years of postsecondary education.	612,707	$1,028,933,758[23]
No Form 1098-T Supporting Student Attending a Postsecondary Educational Institution or Eligible Trade School	The Trade Preferences Extension Act of 2015 requires a statement be received from the educational institution.	2,354,418	$3,584,690,247
Student Attended Less Than Half-Time or Graduate Student per Form 1098-T*	The Taxpayer Relief Act of 1997[24] requires that a student be enrolled at least half the normal full-time work load.	471,178	$696,736,879

Source: TIGTA analysis of Tax Year 2016 returns processed as of April 30, 2017, and May 4, 2017.

Processes do not identify all AOTC claims for which the institution EIN is not provided on Form 8863

Our analysis of tax returns with an AOTC claim processed as of May 4, 2017, identified more than 1.2 million claims for which the institution EIN was not listed on Form 8863 as required. This results from the IRS limiting its efforts to *****************2*********************
************************************2***************************************
************************************2***************************************

[21] This category represents tax returns available in IRS records as of April 30, 2017.
[22] Pub. L. No. 111-5, § 1001, 123 Stat. 115, subsequently amended by the Tax Relief Unemployment Insurance Reauthorization and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296. This Act enacted Internal Revenue Code Section 25A(i), which replaced the Hope Credit with a refundable credit known as the AOTC.
[23] Dollar amounts are computed using an average AOTC amount received per tax return.
[24] Pub. L. 105-34, 111 Stat. 788.

***********************************2*************************************
***********************************2*************************************
***********************************2*************************************
***************2**************. As a result, the IRS will accept these tax returns even when the filer does not include the required institution EIN. This is despite the fact that Internal Revenue Code Section (§) 6213 authorizes the IRS to deny any claim, including AOTC claims, when the taxpayer does not provide information that is required to substantiate the claim, *e.g.*, the institution EIN.[25]

We notified IRS management of our concerns on December 2, 2016. In response to our concerns, IRS management stated that current reporting regulations do not require institutions to provide a statement to all students. As such, not all students would know their institution's EIN. We disagree with the IRS's assertion. In fact, our analysis of the Forms 1098-T received by the IRS identified 1.5 million tax returns claiming the AOTC for students without a Form 1098-T, but the taxpayer included the institution EIN on their return.

The IRS does not have authority needed to deny erroneous AOTC claims at the time tax returns are processed when students are claimed for more than four years

Our analysis of tax returns with an AOTC claim processed as of April 30, 2017, identified 612,707 tax returns for which a student claimed had already been claimed for the AOTC for four years. We estimate these taxpayers received more than $1 billion in erroneous AOTCs. The IRS does not have the authority to systemically deny claims, at the time tax returns are processed, for students who have already received the AOTC for four years. As such, the IRS must audit these tax returns. However, the number of potentially erroneous AOTC claims that the IRS can audit is dependent on available resources. For example, according to IRS management, as of August 21, 2017, the IRS has completed audits of 7,047 returns associated with Tax Years 2015 and 2016 claims resulting in assessments totaling more than $8.8 million.[26]

We first reported our concerns with the IRS's inability to identify and address, at the time tax returns are processed, AOTC claims associated with students claimed for more than the four-year lifetime limit in March 2015.[27] In response to our recommendations, the IRS revised its examination filters to identify students who had already received the AOTC for four years. IRS management stated that a compliance project was conducted for Processing Years 2016 and 2017

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[25] Internal Revenue Code § 6213(b) authorizes the IRS to issue notices to taxpayers of additional tax due to math or clerical errors without the need for a notice of deficiency. Internal Revenue Code § 6213(g)(2)(D) defines one such math or clerical error as the omission of information which is required to be supplied on the return to substantiate an entry on the return.
[26] As Tax Year 2016 post-refund audits are not yet complete, this number does not include those tax returns or audit results.
[27] TIGTA, Ref. No. 2015-40-027, *Billions of Dollars in Potentially Erroneous Education Credits Continue to Be Claimed for Ineligible Students and Institutions* (Mar. 2015).

that identified students who received the AOTC for more than four years. The Processing Year 2016 compliance project focused on AOTC claims filed on original income tax returns. The Processing Year 2017 compliance project focused on AOTC claims filed on Form 1040X, *Amended U.S. Individual Income Tax Return*. Returns identified as part of these compliance projects were selected for either a prerefund or post-refund audit.

The IRS, in conjunction with the Assistant Secretary of the Treasury for Tax Policy, has set forth a legislative proposal requesting additional error authority in a new category of "correctable errors" as part of its annual budget submission. Under this proposal, the Department of the Treasury would have regulatory authority to permit the IRS to correct errors in cases for which the taxpayer has exceeded the lifetime limit for claiming a deduction or credit.

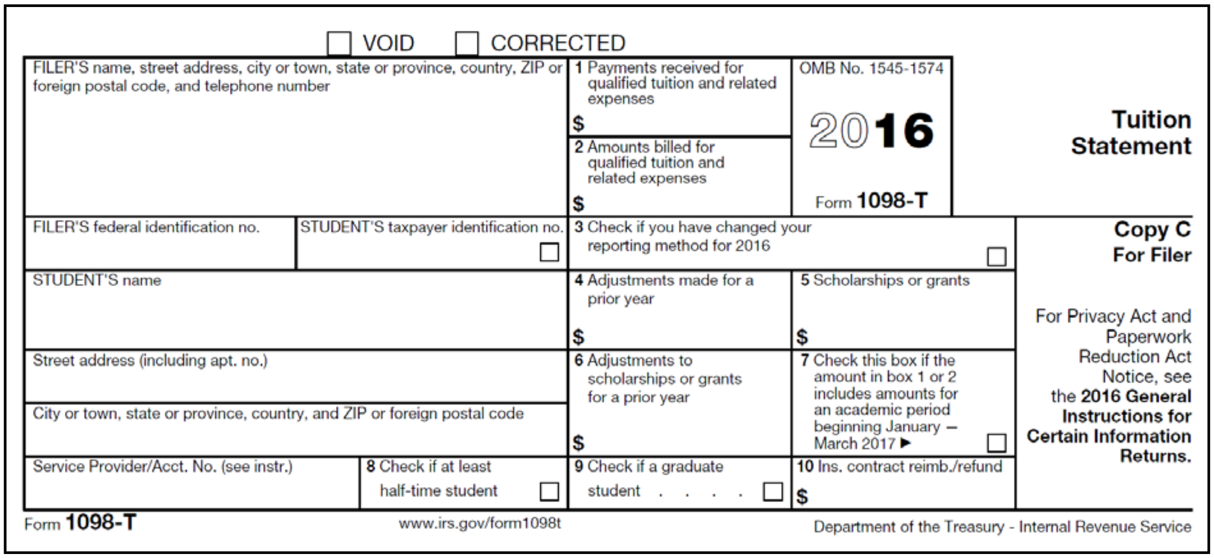
Third-party information could be used to verify student and educational institution eligibility at the time tax returns are filed if Forms 1098-T were required to be filed earlier

Receipt of the Forms 1098-T before tax returns are processed so that information can be used during processing would be the most effective means by which the IRS could identify potentially erroneous education credit claims. However, these forms are not available at the time tax returns are filed. Institutions are generally required to provide Forms 1098-T to the IRS by March 31 each year,[28] which is after many individuals have already filed their individual income tax return.[29] As such, the IRS cannot use the Form 1098-T to verify a student's eligibility for the AOTC at the time the return is processed.

Based on our analysis of Forms 1098-T that the IRS received from the educational institutions that were associated with tax returns processed as of May 4, 2017, we estimate that the IRS erroneously paid more than $3.5 billion on over 2.3 million returns claiming more than 2.4 million students who did not have a Form 1098-T. Figure 7 provides an example of the Form 1098-T.[30]

[28] E-filed Forms 1098-T are required to be filed by March 31 of each year. Paper Forms 1098-T are required to be filed with the IRS generally no later than February 28 of each year.
[29] Most individuals file their individual income tax return no later than April 15 each year.
[30] Educational institutions are required to provide a Form 1098-T to students who attend their institution and file a copy of Form 1098-T with the IRS. The Form 1098-T provides the name and EIN of the institution, the name and Taxpayer Identification Number of the student who attended, and information on whether the student attended half-time or was a graduate student.

Figure 7: Example of Form 1098-T



VOID CORRECTED

FILER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone number

1 Payments received for qualified tuition and related expenses $

2 Amounts billed for qualified tuition and related expenses $

OMB No. 1545-1574

2016

Form 1098-T

Tuition Statement

FILER'S federal identification no.

STUDENT'S taxpayer identification no.

3 Check if you have changed your reporting method for 2016

Copy C For Filer

STUDENT'S name

4 Adjustments made for a prior year $

5 Scholarships or grants $

Street address (including apt. no.)

6 Adjustments to scholarships or grants for a prior year $

7 Check this box if the amount in box 1 or 2 includes amounts for an academic period beginning January – March 2017 ▶

City or town, state or province, country, and ZIP or foreign postal code

For Privacy Act and Paperwork Reduction Act Notice, see the **2016 General Instructions for Certain Information Returns.**

Service Provider/Acct. No. (see instr.)

8 Check if at least half-time student

9 Check if a graduate student . . . .

10 Ins. contract reimb./refund $

Form 1098-T www.irs.gov/form1098t Department of the Treasury - Internal Revenue Service

Source: IRS.gov website.

Earlier access to Forms 1098-T could also improve the IRS's ability to identify AOTC claims for students who do not meet other eligibility requirements. Our analysis of Forms 1098-T that the IRS received from the eligible institutions that were associated with Tax Year 2016 returns processed as of May 4, 2017, identified 471,178 tax returns (claiming 475,787 students) for which taxpayers received AOTCs totaling more than $696 million for students who, based on Forms 1098-T, did not attend school at least half-time as required or were graduate students.

If the IRS had the Forms 1098-T at the time tax returns are processed, the IRS could have identified that these claims should have been disallowed because the student did not attend school at least half-time as required or was a graduate student. See Figure 7 box 8 and box 9 where this information is reported.

In addition, education credit requirements do not specify that the student must be of a specific age to claim the education credit. However, students under the age of 16, or those who are 75 and older, are less likely to be attending a postsecondary educational institution. Our analysis of Forms 1098-T found 17,160 tax returns receiving the AOTC of more than $30 million claimed students of an unlikely age to attend a postsecondary institution or trade school. This is another example of how the information contained on Forms 1098-T could be used by the IRS to identify questionable claims for further review.

In March 2015, we recommended that the IRS coordinate with the Department of the Treasury Office of Tax Policy to consider a legislative proposal to move the required filing date for Form 1098-T to January 31 so that this information can be used at the time tax returns are processed to help identify improper education credit claims. The IRS indicated that a legislative proposal was submitted with the administration's Fiscal Years 2015 and 2016 budget requests, proposing that the filing date for information returns, including the Form 1098-T, be established as January 31. However, neither the Trade Preferences Act nor the PATH Act modified the filing date for Form 1098-T.

Recommendation

Recommendation 6: The Commissioner, Wage and Investment Division, should establish processes to use its math error authority to deny all e-filed and paper AOTC claims for which the taxpayer does not provide the institution EIN for each student claimed on the return.

> ***Management's Response:*** The IRS agreed with this recommendation and plans to submit a Unified Work Request with requirements for Tax Year 2018 AOTC claims for which the institution EIN is not present. IRS management also plans to request requisite programming changes if a systemic process is feasible. Due to limited information technology resources, budget constraints, and competing priorities, IRS management could not provide an implementation date.

Processes and Procedures Are Needed to Ensure Proper Treatment of Claims for the Child and Dependent Care Credit for Taxpayers Filing As Married Filing Separately

Tax returns with a Married Filing Separately filing status claiming the Child and Dependent Care Credit are being disallowed during processing before the IRS determines if the taxpayer may be entitled to the credit due to an exception in the Internal Revenue Code. Our analysis found that there were 12,057 claims for $7.4 million for the Child and Dependent Care Credit by taxpayers with a Married Filing Separately filing status. All of these claims were denied. The IRS cannot determine if a taxpayer meets one of the exceptions in the Internal Revenue Code based on the information provided on the tax return or Form 2441, *Child and Dependent Care Expenses*. As such, we cannot determine if any of the 12,057 tax returns with a Married Filing Separately status and a Child and Dependent Care Credit claim were disallowed incorrectly.

The Internal Revenue Code states that married couples generally must file a joint return. However, the Code also provides that an individual legally separated from his or her spouse under a decree of divorce or of separate maintenance shall not be considered married. In addition, the Code allows for certain married individuals living apart to be considered unmarried for purpose of claiming the Child and Dependent Care Credit if the following requirements are met: an individual who is married and who files a separate return must maintain as his home a household which was the qualifying person's main home for more than one-half of the year; the individual must have furnished more than one-half of the cost of maintaining that household during the taxable year; and the individual's spouse must not have been a member of the household during the last six months of the year.

When we raised our concerns to IRS management on July 26, 2017, the IRS confirmed that all claims for the Child and Dependent Care Credit by taxpayers filing as Married Filing Separately were currently being denied. IRS management stated that, based on an IRS Office of Chief Counsel's opinion and further review, the IRS recognizes that a procedural change is needed. IRS management further stated that math error authority applies only when ineligibility can be determined from information present in the return and as there is no information in the return to indicate the criteria above were not met, the credit should not be removed based on the Married Filing Separately status.[31] The IRS indicated it will revise tax examiner procedures to no longer remove these credits and submit any programming changes needed for Processing Year 2019.

We are concerned that this may not be the best business decision because many of the claims may truly be unallowable. We believe the IRS should evaluate claims for which it denied the credit to determine the number of claims for which the taxpayer responded with support that they fall into one of these exceptions. Based on that information, the IRS can then make any adjustments to processes it feels are needed to more accurately balance compliance and burden. The IRS has other credits with exceptions involving the Married Filing Separately filing status. For example, Form 8962 has a checkbox requesting that the taxpayer check a box indicating they qualify for a special exception to the filing status requirement. If a similar checkbox was added to Form 2441, the IRS could avoid allowing the credit when the taxpayer is not entitled but still be able to identify and allow the credit for those taxpayers who affirm that they do in fact qualify under the exception.

Recommendation

The Commissioner, Wage and Investment Division, should:

Recommendation 7: Modify Form 2441 to ask taxpayers whether or not they fall under one of the exceptions to be able to file as Married Filing Separately and revise computer programs to allow the credit only when a taxpayer attests that he or she meets the exception by checking the applicable box.

> ***Management's Response:*** The IRS agreed with this recommendation and plans to submit the programming and form change requests by January 31, 2018. Due to competing priorities and limited resources, IRS management could not provide an implementation date.

Detecting and Preventing Tax Refund Fraud

For the 2017 Filing Season, the IRS retired its Electronic Fraud Detection System, and the Return Review Program (RRP) is now the IRS's primary individual tax refund fraud selection system. The IRS states that the RRP provides new and improved capabilities in its fraud

[31] The IRS is granted math error authority in 26 U.S.C. § 6213(b).

detection and prevention processes. The RRP has real-time filtering capabilities and is designed to improve the IRS's ability to detect, resolve, and prevent fraud. As of May 6, 2017, the IRS reported that it identified 195,941 tax returns with more than $2.1 billion claimed in fraudulent refunds and prevented the issuance of nearly $2 billion (approximately 92 percent) of those refunds. Figure 8 shows the number of fraudulent tax returns identified by the IRS for Processing Years 2014 through 2016 as well as the refund amounts that were claimed and stopped.

Figure 8: Fraudulent Returns and Refunds Identified and Stopped in Processing Years 2014 Through 2016

Processing Year	Fraudulent Refund Returns Identified	Fraudulent Refund Returns Stopped	Amount of Fraudulent Refunds Identified	Amount of Fraudulent Refunds Stopped
2014	2,180,613	2,066,394	15,724,424,102	$15,209,859,119
2015	1,811,354	1,646,155	12,369,252,837	$11,639,842,002[32]
2016	1,067,878	991,681	$7,970,283,186	$7,648,398,857

Source: IRS fraudulent tax return statistics for Processing Years 2014 through 2016.

The decrease in the number of fraudulent tax refunds the IRS detects and stops continues to be attributable to its expansion of processes to prevent fraudulent tax returns from entering the tax processing system, *i.e.*, rejecting e-filed tax returns and preventing paper tax returns from posting. For example, as of May 15, 2017, the IRS locked approximately 33.9 million taxpayer accounts of deceased individuals. The locking of a tax account results in the rejection of an e-filed tax return and prevention of a paper tax return from posting to the Master File if the SSN associated with a locked tax account is used to file a tax return. According to the IRS, as of April 30, 2017, it had rejected approximately 24,474 fraudulent e-filed tax returns, and as of May 4, 2017, it had stopped 4,672 paper tax returns from posting to the Master File.

Detection of tax returns involving identity theft

For the 2017 Filing Season, the IRS is using both the RRP and the Dependent Database to identify and select tax returns as potential identity theft. The IRS is using 197 identity theft filters to identify these potentially fraudulent tax returns at the time tax returns are processed and prior to the issuance of fraudulent tax refunds. These filters incorporate criteria based on

[32] TIGTA, Ref. No. 2017-40-014, *Results of the 2016 Filing Season* (Jan. 2017) reported $11,439,842,002 based on IRS-provided reports. However, the IRS has since corrected its reporting to reflect $200 million more fraudulent refunds stopped.

characteristics of confirmed identity theft tax returns, including amounts claimed for income and withholding, filing requirements, prisoner status, taxpayer age, and filing history.

Tax returns identified by these filters are held during processing until the IRS can verify the taxpayer's identity. Tax returns identified as potential identity theft are worked by the Taxpayer Protection Program. A notice is sent to the address on the potentially fraudulent tax return requesting the filer to confirm his or her identity. When the taxpayer's identity is verified, the IRS allows the tax return to continue processing and ultimately issues a tax refund. However, when the taxpayer does not verify his or her identity, the IRS considers the tax return to be identity theft, removes the tax return from further processing, *i.e.*, the refund is not issued, and places an identity theft indicator on the taxpayer's account for future reference. As of April 29, 2017, the IRS reported that it had identified and confirmed 75,797 fraudulent tax returns and prevented the issuance of $581.6 million in fraudulent tax refunds as a result of the identity theft filters. Figure 9 shows the number of identity theft tax returns the IRS identified and confirmed as fraudulent as of April 29, 2017, for Processing Year 2017 and as of a comparable time frame for Processing Years 2015 and 2016.

Figure 9: Identity Theft Tax Returns Confirmed As Fraudulent in Processing Years 2015 Through 2017

Processing Year	Number of Identity Theft Returns[33]
2015	111,045
2016	119,798
2017	75,797

Source: IRS fraudulent tax return statistics for Processing Year 2015 (as of April 30, 2015); Processing Year 2016 (as of April 30, 2016); and Processing Year 2017 (as of April 29, 2017).

In February 2017, we reported[34] that, with the passage of legislation to change the reporting date of Forms W-2, the IRS should be able to significantly reduce the number of undetected tax returns reporting false wages and withholding if it compares available Form W-2 information to the tax return at the time the tax return is processed. In addition, similar to Processing Year 2016, the IRS initiated a voluntary program for which 18 payroll providers were requested to submit Forms W-2 directly to the IRS by January 31, 2017. The IRS uses the identity theft

[33] These numbers are different than previously reported in TIGTA, Ref. No. 2017-40-014, *Results of the 2016 Filing Season* (Jan. 2017). The IRS changed its methodology of counting the number of identity theft returns in Calendar Year 2017. Therefore, the numbers were restated for prior years using this updated methodology.
[34] TIGTA, Ref. No. 2017-40-017, *Efforts Continue to Result in Improved Identification of Fraudulent Tax Returns Involving Identity Theft; However, Accuracy of Measures Needs Improvement* (Feb. 2017).

models to compare this accelerated Form W-2 information to the tax return at the time the tax return is processed for identity theft detection. The IRS stated that, as of May 4, 2017, it selected 52,342 tax returns for identity theft treatment based upon the early submission of Forms W-2. We are conducting a separate review of the IRS's use of the RRP to detect and prevent fraud during the 2017 Filing Season, including evaluating the requirement for employers to submit Forms W-2 to the IRS by January 31.[35]

Finally, in response to concerns raised by TIGTA regarding multiple refunds going to the same address or bank account, the IRS continues to use its clustering filter tool to group tax returns based on characteristics that include the address, zip code, and bank routing numbers. For the tax returns identified, the IRS applies a set of business rules in an attempt to ensure that legitimate taxpayers are not included. Tax returns identified are held from processing until the IRS can verify the taxpayer's identity. As of May 4, 2017, the IRS reports that, using this tool, it identified 93,633 tax returns and prevented the issuance of approximately $449.9 million in fraudulent tax refunds pending authentication of the taxpayer's identity.

Converting direct deposits to a paper check

In an effort to further reduce fraudulent tax refunds, the IRS limits the number of direct deposit refunds that can be sent to one bank account to three refunds. The IRS will convert the fourth and subsequent direct deposit refund requests to a paper check and send it to the taxpayer's address of record.[36] Our analysis of direct deposit requests made as of May 4, 2017, found that the IRS generally converts direct deposits to a paper check when required.

TIGTA has previously reported in August 2015,[37] December 2015,[38] and January 2017,[39] that IRS processes do not always convert direct deposits to a paper check when required. In response to these reports, IRS management stated that computer programming errors resulted in the IRS not properly identifying all direct deposit accounts with multiple deposit requests. According to IRS management, the IRS corrected two of the three issues and planned to implement computer programming changes to correct the third issue in Calendar Year 2016. IRS management stated that additional programming changes were implemented in July 2016 to address the remaining condition we identified during the 2015 Filing Season. Our analysis shows that the IRS programming is working as intended.

The IRS received approximately 87 million requests for direct deposits as of May 4, 2017. Our analysis of the 87 million requests identified 16,547 unique bank accounts with a total of 49,536 direct deposit attempts totaling $82 million that should have converted to a paper check.

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[35] TIGTA, Audit Number 201740029, *Assessment of the IRS's Filing Season 2017 Fraud Detection Activities*.
[36] The most current address the IRS has on record for a taxpayer where communications can be sent.
[37] TIGTA, Ref. No. 2015-40-080, *Results of the 2015 Filing Season* (Aug. 2015).
[38] TIGTA, Ref. No. 2016-40-008, *Continued Refinement of the Return Review Program Identity Theft Detection Models Is Needed to Increase Detection* (Dec. 2015).
[39] TIGTA, Ref. No. 2017-40-014, *Results of the 2016 Filing Season* (Jan. 2017).

Of the 49,536 deposit attempts we identified, only 288 deposit attempts totaling approximately $400,000 did not convert to a paper check. We further determined that the reason these 288 deposit attempts did not convert to a paper check was not a result of the programming errors we previously identified. The majority of the deposits that did not convert to a paper check appear to be the result of the IRS suspending the processing of the tax return during processing for additional review or action.

Screening of prisoner tax returns

Refund fraud associated with prisoner SSNs remains a significant problem for tax administration. For Calendar Year 2015, the IRS confirmed more than 24,000 fraudulent tax returns using a prisoner SSN with refunds claimed on those tax returns totaling more than $1.3 billion. As of May 6, 2017, the IRS reported that it identified for screening 32,319 potentially fraudulent tax returns filed by prisoners.[40] Figure 10 shows the number of prisoner tax returns identified for screening in Processing Years 2015 through 2017.

Figure 10: Prisoner Tax Returns Identified for Screening in Processing Years 2015 Through 2017 (as of May 6, 2017)

Processing Year	Number of Prisoner Tax Returns Identified for Screening
2015	45,316
2016	35,785
2017	32,319

Source: IRS fraudulent tax return statistics for Processing Years 2015 through 2017 as of May 6, 2017.

To combat refund fraud associated with tax returns filed using prisoner SSNs, the IRS compiles a list of prisoners (the Prisoner File) received from the Federal Bureau of Prisons and State Departments of Corrections. In addition, to further its efforts to identify prisoner tax returns, the *Bipartisan Budget Act of 2013*,[41] enacted in December 2013, amended the *Improper Payments Elimination and Recovery and Improvement Act*[42] to give the Secretary of the Treasury the authority to obtain Prisoner Update Processing System data from the Social Security Administration. These lists are the cornerstone of the IRS's efforts to identify and prevent the

[40] Tax returns filed using a prisoner's name and SSN.
[41] Pub. L. No. 113-67, § 204.
[42] Pub. L. No. 112-248, 126 Stat. 2390.

issuance of fraudulent refunds to individuals filing false tax returns using a prisoner SSN. For those returns that include a prisoner SSN, the IRS adds a prisoner indicator.

Tax returns with a prisoner indicator that meet specific criteria are sent for further evaluation to determine if the tax return is fraudulent. This evaluation includes an IRS tax examiner screening and verifying the wage and withholding information reported on the tax return. For example, in the screening process, a tax examiner reviews the tax return income and withholding information. If the tax examiner concludes that the tax return is potentially fraudulent, it is then sent for verification. In the verification process, a tax examiner attempts to contact the employer(s) to confirm the reported income and withholding. If the tax examiner is unable to verify the income and withholding with the employer, the refund is frozen to prevent issuance.

In July 2017, we issued a separate report on the IRS's efforts to identify and prevent prisoner tax fraud that includes our continued evaluation of the effectiveness of the IRS's corrective actions to prior report recommendations to identify and reduce prisoner fraud.[43] We reported that IRS processes still do not effectively ensure that the Federal Bureau of Prisons and the State Departments of Corrections comply with prisoner reporting requirements. TIGTA identified 861 prisons that reported prisoner information to the Social Security Administration but did not report that information to the IRS. In addition, IRS processes to validate and use prisoner data limit its ability to detect potentially fraudulent tax returns. Finally, the IRS did not screen and verify some prisoner tax returns for fraud. TIGTA identified 4,072 prisoner tax returns that reported income and withholding that were not supported by third-party income documents. These filers received potentially fraudulent refunds totaling more than $7.3 million.

Providing Customer Service

Similar to past filing seasons, taxpayers have multiple options to choose from when they need assistance from the IRS, including assistance through the toll-free telephone lines and face-to-face assistance at the Taxpayer Assistance Centers (TAC) and Volunteer Program sites as well as self-assistance through IRS.gov and various other social media channels, *e.g.*, Twitter, Facebook, and YouTube. The IRS continues its trend to depend more on technology-based services and external partners by directing taxpayers to the most cost-effective IRS or partner channel available to provide the needed service. The IRS notes that this approach allows it to focus limited toll-free and walk-in resources on customer issues that can be best resolved with person-to-person interaction. By using this approach, the IRS believes that it is able to improve its service to taxpayers by addressing and resolving more complex matters such as assistance to identity theft victims and people with tax account issues. For example, in an effort to continue to redirect taxpayers to online services, the IRS offers online tools available to taxpayers on IRS.gov:

[43] TIGTA, Ref. No. 2017-40-041, *Actions Need to Be Taken to Ensure Compliance With Prisoner Reporting Requirements and Improve Identification of Prisoner Returns* (July 2017).

- ***Interactive Tax Assistant*** – this tool is a tax law resource that takes taxpayers through a series of questions and provides them with responses to basic tax law questions. The IRS reports that from January 1 through May 4, 2017, a total of 890,567 requests had been completed.
- ***Where's My Refund?*** – this tool allows taxpayers to check the status of their refunds using the most up-to-date information available to the IRS. The IRS reports that as of May 6, 2017, there have been more than 256.2 million uses of the tool.
- ***Am I Eligible for a Coverage Exemption or Required to Make an Individual Shared Responsibility Payment*** – this tool helps taxpayers determine if they are eligible for an exemption from the minimum essential coverage requirement or if they must make an SRP. According to the IRS, 64,538 taxpayers have used this tool as of May 4, 2017.
- ***Individual Shared Responsibility Provision Payment Estimator*** – this tool allows taxpayers to estimate the amount they may have to pay if they did not maintain minimum essential coverage during the year. From January 1 through May 4, 2017, 153,909 taxpayers have used this tool.

Accuracy of IRS tax forms, schedules, publications, and information on IRS.gov

Each year, the IRS must update its tax forms, schedules, and publications as well as information on IRS.gov to accurately reflect tax changes. These changes include: inflationary adjustments, income limit phase-ins or phase-outs, and legislative changes. Overall, our review of the forms, instructions, and publications related to the previously discussed key tax provisions found that most were accurately updated. However, we did identify the following instances in which information was not updated or complete:

- On December 2, 2016, we informed the IRS that our review of the draft instructions for Form 8863 dated August 26, 2016, and for Form 8917, *Tuition and Fees Deduction*, dated July 28, 2016, identified that they were not updated to reflect the new education benefit requirements as well as the exceptions to those requirements. The IRS responded that it is addressing the Form 1098-T requirement by adding only a new item to the "What's New" section of the Form 8863 based on wording used in the proposed regulations.
- On February 9, 2017, we notified the IRS of concerns we identified related to seven IRS instructional YouTube videos that did not contain a detailed description of the changes for the current filing season. The videos we reviewed discussed the refund delay for taxpayers claiming the EITC and the ACTC; taxpayers claiming the AOTC; taxpayers with ITINs; and inflationary adjustments to items such as personal exemptions and the standard deduction. In response to our observations, the IRS deactivated one video that it already had planned to update and removed a reference to a prior year on one video script. In addition, IRS management explained that the YouTube videos are intended to

provide a broad overview of a given topic and refer viewers to available resources for additional details. As such, the information provided in the remaining videos is adequate for the videos' intended purpose.

Self-assistance through IRS.gov and social media channels

The IRS continues to offer self-assistance options that taxpayers can access 24 hours a day, seven days a week. The most notable self-assistance option is the IRS's public Internet site, IRS.gov. The IRS continues to steer taxpayers to its website as the best source for assistance, including answers to their tax questions. The IRS reports 329.4 million visits to IRS.gov this filing season as of May 6, 2017.

Taxpayers can also interact with the IRS using IRS2Go, which is a mobile application that lets taxpayers access information and a limited number of IRS online tools. As of May 4, 2017, the IRS reports that the IRS2Go mobile application had 4.8 million active users.

Finally, the IRS also uses various forms of social media including YouTube, Twitter, Tumblr, and Facebook. As of May 4, 2017, there have been more than 1.5 million new views of IRS YouTube videos and a total of 140,198 Twitter followers as of May 9, 2017.

Toll-free telephone level of assistance continues to increase

As of May 6, 2017, the IRS reports receiving approximately 56.3 million total attempts with 40.6 million net attempts[44] made by taxpayers to contact the IRS by calling the various customer service toll-free telephone assistance lines seeking help to understand the tax law and meet their tax obligations.[45] As of May 6, 2017, the IRS reports that 19.6 million calls were answered with automation. Telephone assistors answered another nearly 11 million calls and provided a 78.9 percent Level of Service with a 6.9 minute Average Speed of Answer. The IRS forecasted a 75 percent Level of Service for the 2017 Filing Season. Figure 11 shows a comparison of IRS toll-free telephone statistics as of May 6, 2017, for Filing Seasons 2014 through 2017.

[44] Total call attempts represent calls received during open and after hours. Total net call attempts represent calls received during open hours.

[45] The IRS refers to the suite of 29 telephone lines to which taxpayers can make calls as "Customer Account Services Toll-Free."

Figure 11: Toll-Free Filing Season Telephone Statistics for Filing Seasons 2014 Through 2017 (as of May 6, 2017)

Statistic	Filing Season			
	2014	2015	2016	2017
Assistor Calls Answered	11,551,001	8,685,947	14,122,334	10,998,399
Level of Service	70.7%	37.7%	69.0%	78.9%
Average Speed of Answer (Minutes)	14.6	23.8	12.2	6.9

Source: IRS management information reports as of May 6, 2017. TIGTA converted the Average Speed of Answer in the reports from seconds to minutes.

The IRS is implementing initiatives in an effort to better assist individuals seeking face-to-face assistance at a TAC

Each year, many taxpayers seek assistance from one of the IRS's 376 TAC walk-in offices. Although the IRS reports 376 TACs for the 2017 Filing Season, 24 TACs were not open because they had not been staffed due to hiring and budget restrictions. The IRS estimates that the number of taxpayers it will assist at its TACs will continue to decline this fiscal year. The IRS plans to assist approximately 3.4 million taxpayers at the TACs in Fiscal Year 2017, an approximately 23.6 percent decrease from Fiscal Year 2016. Figure 12 shows the number of contacts by product line at the TACs for Fiscal Years 2014 through 2017.

Figure 12: TAC Contacts for Fiscal Years 2014 Through 2017 (in millions)

Contacts/Product Lines	Fiscal Year			
	2014	2015	2016	2017 Projections
Tax Accounts Contacts	3.6	3.8	3.1	2.4
Forms Contacts	0.4	0.3	0.1	0.1
Other Contacts[46]	1.4	1.5	1.2	1.0
Tax Law Contacts	0.1	0.1	0.1	<0.04
Totals	**5.5**	**5.6**	**4.5**	**3.4**

Source: IRS management information reports. Numbers shown are rounded and totals may not calculate due to rounding.

The IRS is also implementing other initiatives in an effort to better assist those individuals seeking assistance from a TAC. For example, for the 2017 Filing Season, the IRS transitioned all TACs to appointment service. The IRS indicated that it initially began providing services at the TACs by appointment in an attempt to alleviate long lines that sometimes occur at many TACs and to help ensure that taxpayers' issues are timely resolved. The IRS will attempt to resolve the taxpayer's question or provide the taxpayer with information on alternative services when they call to schedule an appointment. The IRS reports that, as of April 29, 2017,[47] IRS employees answered more than 2.1 million calls resulting in approximately 945,000 that necessitated a TAC appointment. The IRS estimates that, of the 2.1 million taxpayers requesting an appointment, 1.2 million (57 percent) taxpayers were assisted on the telephone, eliminating any need for the taxpayer to incur the time and expense of visiting a TAC.

The IRS also noted that it assisted more than 1.9 million taxpayers face-to-face at a walk in office. Taxpayers served at the walk-in offices include taxpayers who had an appointment and those with an issue that did not require an appointment. In addition, the IRS stated that taxpayers who travel to a TAC without an appointment are assisted if there is availability. According to the IRS, of the 1.9 million who came to the walk-in offices, nearly 264,000 taxpayers with issues that should have required an appointment were assisted without an appointment.

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[46] Other Contacts include but are not limited to: accepting Form 2063, *U.S. Departing Alien Income Tax Statement;* date-stamping tax returns brought in by taxpayers; screening taxpayers for eligibility of service; scheduling appointments (only in Fiscal Year 2015); and helping taxpayers with general information such as addresses and directions to other IRS offices or other Federal Government agencies.

[47] For Fiscal Year 2017 – October 1, 2016, through April 29, 2017.

The IRS also offers Virtual Service Delivery, which integrates video and audio technology to allow taxpayers to see and hear an assistor located at a remote TAC, giving taxpayers "virtual face-to-face interactions" with assistors. According to the IRS, taxpayers can use this technology to obtain many of the TAC's services. The goals for Virtual Service Delivery are to enhance the use of IRS resources, optimize staffing, and balance workload. For the 2017 Filing Season, the IRS offered Virtual Service Delivery at 28 partner site locations, which is a change from the 35 locations where this service was offered the previous year.[48] The IRS reports that, as of April 29, 2017,[49] a total of 1,673 taxpayers have used the service.

Finally, the IRS has an initiative to co-locate staff with the Social Security Administration to assist taxpayers. For the 2017 Filing Season, the IRS placed employees in four Social Security Administration locations that provided face-to-face assistance to 1,016 customers. TIGTA is planning a follow-up audit to assess the IRS's efforts to expand customer service options to taxpayers seeking face-to-face assistance. The IRS indicated that its strategy of appointment service at the TACs, along with continued promotion of alternative service options, will result in taxpayers electing to obtain assistance through more convenient service channels.

The volume of tax returns prepared at Volunteer Program sites increased slightly in Fiscal Year 2016

The Volunteer Program continues to play an important role in the IRS's efforts to improve taxpayer service and facilitate participation in the tax system. It provides no-cost Federal tax return preparation and electronic filing (e-filing) to underserved taxpayer segments, including low-income, senior citizens, persons with disabilities, rural, those with limited English proficiency, and Native Americans. As of May 7, 2017, approximately 3.5 million tax returns have been prepared at the 11,469 Volunteer Program sites nationwide.[50] Figure 13 shows the number of tax returns prepared by volunteers for Fiscal Years 2014 through 2016.

[48] For the 2017 Filing Season, the IRS reduced offering Virtual Service Delivery at IRS locations. Access to this service has been relocated to external partner locations.
[49] For Fiscal Year 2017 – October 1, 2016, through April 29, 2017.
[50] As of April 18, 2017, there were 11,469 volunteer sites open at various times during the 2017 Filing Season.

Figure 13: Volunteer Program Statistics for Fiscal Years 2014 Through 2016

	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Percentage Change (Fiscal Year 2015 to Fiscal Year 2016)
Tax Returns	3,646,562	3,756,707	3,813,411	1.5%
Volunteers	93,082	90,826	89,121	-1.9%
Sites	12,319	12,057	11,831	-1.9%

Source: IRS management information system containing Fiscal Years 2014 through 2016 information. Percentages are rounded.

Accounts Management function's over-aged inventory decreased from Calendar Year 2015 to Calendar Year 2016

As of May 6, 2017, the IRS reports 470,817 cases in its over-aged inventory. In comparison, for the 2016 Filing Season, the IRS reported more than one million cases in its over-aged inventory as of May 7, 2016. Accounts Management function inventory includes but is not limited to amended tax returns, responses to taxpayer notices, identity theft cases, and applications for ITINs and is generally considered over-aged when it has been in inventory for more than a designated number of calendar days. Staff responsible for working Accounts Management function inventory are divided between working cases in inventory and staffing the customer service telephone lines.

While over-aged inventory remains high during the filing season, the IRS significantly reduced total over-aged inventory from 1.3 million cases at the end of Processing Year 2015 to 702,437 cases at the end of Processing Year 2016. According to IRS management, the drop in over-aged inventory during Processing Year 2016 was the result of $290 million in additional funding received for Fiscal Year 2016, which allowed the IRS to significantly improve telephone service that year and also freed up more resources to help reduce the Accounts Management function inventory. Figure 14 provides a comparison of the Accounts Management function inventory for Processing Years 2013 through 2016.

Figure 14: Comparison of Accounts Management Function Inventory As of the End of Processing Years 2013 Through 2016

	2013	2014	2015	2016
Total Inventory	2,580,527	2,542,125	2,890,392	1,669,543
Over-Aged Volume	1,187,255	1,168,181	1,318,446	702,437
Percentage Over-Aged	46.0%	46.0%	45.6%	42.1%

Source: IRS Accounts Management Inventory Report – Inventory Age Reports.

Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to evaluate whether the IRS timely and accurately processed individual paper and e-filed tax returns during the 2017 Filing Season.[1] To accomplish our objective, we:

I. Monitored online news outlets and forums to identify any preparation, filing, or processing issues that taxpayers were experiencing.

II. Determined if the IRS's monitoring systems indicated that individual tax returns were being processed timely and accurately.

A. Identified volumes of paper and e-filed tax returns received through May 5, 2017, from the IRS Weekly Filing Season reports that provide a year-to-date comparison of scheduled return receipts to actual return receipts.

B. Monitored key IRS indicators including but not limited to the volume of tax return receipts, e-file business rule reports, and applicable IRS Internet and intranet websites.

III. Determined if the IRS correctly implemented selected tax law changes that affected the processing of individual income tax returns during the 2017 Filing Season.

A. Identified selected provisions that will have an impact on taxpayers:

1. Trade Preferences Extension Act of 2015,[2] Section 804 affects the AOTC, the Lifetime Learning Credit, and the Tuition and Fees Deduction. Individual taxpayers must have a statement from the educational institution to claim any of these benefits.

2. PATH Act,[3] Section 211 affects the AOTC. Individual taxpayers must provide the EIN of the educational institution in order to claim the AOTC.

B. Identified and reviewed specific tax law changes for the provisions listed in Steps III.A.1. and III.A.2. to ensure that they are accurately reflected in all applicable forms, instructions, and publications.

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[1] See Appendix VI for a glossary of terms.
[2] Pub. L. No. 114-27.
[3] Pub. L. No. 114-113 (H.R. 2029).

C. Determined if refunds from EITC/ACTC claims were properly held until at least February 15 as required by the PATH Act.

D. Determined if Form 8867, *Paid Preparer's Due Diligence Checklist*, was attached to each tax return claiming the CTC, ACTC, or AOTC as required and the form was filled out. We also quantified the impact.

E. Conducted an analysis of Tax Year 2015 tax returns with ACTC claims filed with a Form 2555, *Foreign Earned Income*, to determine if the IRS accurately implemented provisions that do not allow the ACTC to individuals who also claim a foreign earned income exclusion or housing deduction and quantified the impact.

F. Identified Tax Year 2016 individual tax returns for which the taxpayer received the AOTC and did not provide an educational institution EIN as required and quantified the impact.

IV. Identified online self-help applications provided by the IRS and ensured that the information and results provided were accurate.

V. Provided statistics related to the IRS's implementation of ACA tax provisions.

VI. Followed up on findings previously reported by TIGTA and quantified the impact of identified errors.

A. Determined if the IRS implemented computer programming changes to properly limit the number of direct deposits to a single bank account.

B. Determined if the IRS is incorrectly limiting residential energy credit claims on Tax Year 2016 tax returns and quantified the effects.

VII. Identified and evaluated issues presented in prior TIGTA audit report (Ref. No. 2015-40-027, *Billions of Dollars in Potentially Erroneous Education Credits Continue to Be Claimed for Ineligible Students and Institutions* (Mar. 2015).

A. Quantified the number of taxpayers claiming the AOTC for more than four years and the amounts paid on all claims and those in excess of the four-year limit.

B. Identified ineligible students, *i.e.*, part-time or graduate, who received the AOTC.

C. Quantified students with an education credit claim to determine how many had a Form 1098-T, *Tuition Statement*, and how many did not have a Form 1098-T.

VIII. Determined if Married Filing Separately filing status tax returns are properly limited for certain tax items at processing.

IX. Identified results of the IRS's identity theft and tax refund fraud programs. We quantified fraudulent tax returns and tax returns filed by prisoners.

X. Identified results for the IRS TAC Program.

XI. Identified results for the Toll-Free Telephone Assistance Program.

XII. Identified results for the Volunteer Income Tax Assistance Program.

XIII. Monitored the Accounts Management function correspondence inventory.

XIV. Identified results for IRS self-assistance through IRS.gov.

Data validation methodology

During this review, we obtained extracts from the IRS's Individual Master File and Return Transaction File databases for Processing Years 2015 and 2016 that were available on TIGTA's Data Center Warehouse. We also obtained extracts of Form 1098-T from the IRS's Information Returns Master File for Processing Year 2017, Tax Year 2016, retrieved by TIGTA's Strategic Data Services. In addition, we obtained extracts from the IRS's IRTF Form 1040, *U.S. Individual Income Tax Return*, Error Resolution System database for Processing Year 2017 and from the IRS's Individual Master File Refund databases for Processing Year 2017 that were available on TIGTA's Data Center Warehouse. Before relying on the data, we ensured that each file contained the specific data elements we requested. In addition, we selected random samples of each extract and verified that the data in the extracts were the same as the data captured in the IRS's Integrated Data Retrieval System. We also performed analysis to ensure the validity and reasonableness of our data such as ranges of dollar values, transaction dates, and tax periods. Based on the results of our testing, we believe that the data used in our review were reliable.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: the process for planning, organizing, directing, and controlling program operations for the 2017 Filing Season. We evaluated these controls by monitoring IRS weekly production meetings, reviewing IRS procedures, and interviewing IRS management.

Appendix II

Major Contributors to This Report

Russell P. Martin, Assistant Inspector General for Audit (Returns Processing and Account Services)
Deann L. Baiza, Director
Sharla J. Robinson, Audit Manager
Sandra L. Hinton, Lead Auditor
John L. Hawkins, Senior Auditor
Nathan J. Cabello, Auditor
Kimberly Holloway, Auditor
Laura P. Haws, Information Technology Specialist (Data Analytics)
Thomas F. Polsfoot, Information Technology Specialist (Data Analytics)

Appendix III

Report Distribution List

Commissioner
Office of the Commissioner – Attn: Chief of Staff
Deputy Commissioner for Services and Enforcement
Director, Accounts Management, Wage and Investment Division
Director, Business Modernization Office, Wage and Investment Division
Director, Customer Account Services, Wage and Investment Division
Director, Customer Assistance, Relationships, and Education, Wage and Investment Division
Director, E-File Services, Wage and Investment Division
Director, Field Assistance, Wage and Investment Division
Director, Joint Operation Center, Wage and Investment Division
Director, Stakeholder Partnership, Education, and Communications, Wage and Investment Division
Director, Strategy and Finance, Wage and Investment Division
Director, Submission Processing, Wage and Investment Division
Chief, Program Evaluation and Improvement, Wage and Investment Division
Director, Office of Audit Coordination

Appendix IV

Outcome Measures

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

Type and Value of Outcome Measure:

- Revenue Protection – Potential; $71,918 in ACTCs[1] associated with 45 taxpayers who received ACTCs to which they were not entitled as a result of the IRS incorrectly allowing the credit amount when the taxpayer was allowed a foreign earned income exclusion or housing deduction (see page 12).

Methodology Used to Measure the Reported Benefit:

The ACTC is generally not allowed on tax returns when the foreign earned income exclusion or housing deduction is claimed on Form 2555, *Foreign Earned Income*. We retrieved the Tax Year 2015 Forms 2555 from TIGTA's Data Center Warehouse and matched them to the taxpayers who filed a tax return claiming the ACTC during Processing Year 2016. We identified 124 Tax Year 2015 returns that claimed the ACTC and also claimed a foreign income exclusion or housing deduction.

Our analysis of the 124 returns found that the taxpayers did not always claim a foreign earned income exclusion or housing deduction on the Forms 2555 filed. Therefore, we removed 26 taxpayers who did not claim an exclusion and analyzed the remaining 98 taxpayers. Of the 98 tax returns, we found 38 that had a Document Locator Number assigned to the Form 2555 that also matched the Document Locator Number assigned to the tax return claiming the ACTC. The IRS stopped the 38 returns during processing for additional review. During its manual review, the IRS erroneously allowed $60,177 in ACTC claims on these 38 returns.

Our further analysis of the 98 returns found that 16 returns were processed with an amended or duplicate return posted on the tax account. Of the 16 returns, seven were processed with an amended return reporting a Form 2555 with a foreign income exclusion or housing deduction claimed after the ACTC was allowed on the first return, but ACTCs totaling $11,741 were not recovered.

[1] See Appendix VI for a glossary of terms.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; 494 taxpayers who did not receive Residential Energy Efficient Property Credits totaling $1,061,691 to which they were entitled as a result of the IRS incorrectly limiting the credit amount (see page 13).

Methodology Used to Measure the Reported Benefit:

The Residential Energy Credit claimed on Form 1040, *U.S. Individual Income Tax Return*, is comprised of two tax credits – the Residential Energy Efficient Property Credit and the Nonbusiness Property Energy Credit. The maximum Nonbusiness Property Energy Credit that can be claimed is $500 ($1,000 if Married Filing Jointly). The maximum Residential Energy Efficient Property Credit that can be claimed is generally limited to the taxpayer's tax liability.

We identified Tax Year 2016 returns from the IRTF on TIGTA's Data Center Warehouse for which the taxpayer's amount for the Residential Energy Credit exceeds the amount allowed by the IRS. In addition, we identified Tax Year 2016 returns from the IRTF for which there was an error code 291 that is associated with Residential Energy Credit errors. We matched these two files and identified 597 returns. Our review of the 597 returns identified 494 Tax Year 2016 individual tax returns for which the taxpayer's amount for the residential energy credit exceeds the IRS amount allowed and the amount allowed equals $500 or $1,000. We found that the IRS incorrectly limited the Residential Energy Efficient Property Credit on these 494 tax returns processed as of May 4, 2017, resulting in these taxpayers receiving $1,061,691 less in credits than they were entitled to receive. We did not include any identity theft cases in our results.

Type and Value of Outcome Measure:

- Cost Savings (Funds Put to Better Use) – Potential; $1,102,764,510 in refundable AOTCs for taxpayers who claimed students who did not include the educational institution EIN on their tax returns as required (see page 15).

Methodology Used to Measure the Reported Benefit:

We identified 10,157,639 Tax Year 2016 tax returns processed as of May 4, 2017, from the IRTF that claimed a tentative AOTC or a Lifetime Learning Credit qualifying expense greater than zero dollars. We matched these returns to the Individual Master File Other Tax Module Transactions Table located on TIGTA's Data Center Warehouse to determine if the Transaction Code 766 with Reference Number 260 was on the tax account indicating a refundable education credit. We also matched these returns to the IRTF to retrieve the education credit per computer field in order to compute the amount of net nonrefundable AOTC.[2] We identified 7,991,981 of the 10,157,639 tax returns that received refundable or nonrefundable AOTCs.

Of the 7,991,981 tax returns, we identified 1,293,798 taxpayers claiming AOTCs totaling $1,930,913,303 for 1,431,043 students who did not include an EIN on their Form 8863, *Education Credits (American Opportunity and Lifetime Learning Credits)*, when claiming the credit. We determined that $1,102,764,510 of the $1,930,913,303 is attributable to refundable AOTCs for taxpayers who claimed students who did not include the educational institution EIN on their tax returns as required.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; $828,148,793 in nonrefundable AOTCs for taxpayers who claimed students who did not include the educational institution EIN on their tax returns as required (see page 15).

Methodology Used to Measure the Reported Benefit:

We identified 10,157,639 Tax Year 2016 tax returns processed as of May 4, 2017, from the IRTF that claimed a tentative AOTC or a Lifetime Learning Credit qualifying expense greater than zero dollars. We matched these returns to the Individual Master File Other Tax Module Transactions Table located on TIGTA's Data Center Warehouse to determine if the Transaction Code 766 with Reference Number 260 was on the tax account indicating a refundable education credit. We also matched these returns to the IRTF to retrieve the education credit per computer field in order to compute the amount of net nonrefundable AOTC. We identified 7,991,981 of the 10,157,639 tax returns that received refundable or nonrefundable AOTCs.

Of the 7,991,981 tax returns, we identified 1,293,798 taxpayers claiming AOTCs totaling $1,930,913,303 for 1,431,043 students who did not include an educational institution EIN on their Form 8863 when claiming the credit. We determined that $828,148,793 of the $1,930,913,303 is attributable to nonrefundable AOTCs for taxpayers who claimed students who did not include the educational institution EIN on their tax returns as required.

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[2] For our analysis, the net nonrefundable AOTC is considered equal to $0 when the education credit per computer field minus tentative Lifetime Learning Credit per computer field is less than zero. Otherwise, we computed the amount of net nonrefundable AOTC to be the difference of the education credit per computer field minus tentative Lifetime Learning Credit per computer field.

Type and Value of Outcome Measure:

- Cost Savings (Funds Put to Better Use – Potential; $1,326,450,632 in refundable AOTCs over four years received by 498,794 taxpayers who claimed 505,070 students for more than the four tax years allowed by law (see page 15).

Methodology Used to Measure the Reported Benefit:

We obtained all Tax Year 2010 through Tax Year 2016 tax returns filed as of April 30, 2017, from the Modernized Tax Return Database for which the AOTC was claimed on an e-filed Form 8863. We identified tax returns in Tax Year 2010 through Tax Year 2016 for which the AOTC claimed was greater than zero or for which the AOTC student identification was not missing. We determined that 885,159 students claimed the AOTC for more than four tax years. We matched the 885,159 students to Tax Year 2010 through Tax Year 2016 tax returns and identified 633,565 students on Tax Year 2016 tax returns who were claimed for the AOTC in excess of four years.

The IRS did not capture the education credit amount received per student on Tax Year 2016 returns. Therefore, if a taxpayer claimed more than one student, we could not systemically determine the credit amount attributable to a particular student. In addition, education credit amounts received per tax return are allocated between refundable and nonrefundable portions. To ensure that our outcomes were distributed among refundable and nonrefundable education credits, we calculated the average refundable and nonrefundable credit per student. We matched the tax returns to the Transaction Code File 767 with Reference Number 260 that was on the tax account indicating a refundable education credit was reversed or reduced from an examination. We could not systemically determine when a refundable education credit was reversed or reduced if the nonrefundable education credit was also affected. Therefore, to be conservative, if a tax return indicated that the refundable education credit was reversed, we also reversed the nonrefundable education credit. If a tax return was reduced and there was more than one student on the tax return, we made the assumption that the reduction was for any student who was claimed more than four years. These estimated amounts were used to estimate the dollar value of our outcome measure.

To determine the amount of each refundable and nonrefundable education credit received, we calculated an estimated education credit amount per student based on the total number of students identified on 612,707 tax returns filed and the total amount of education credits received for these Tax Year 2016 returns. We identified 622,369 students on the 612,707 tax returns who received the AOTC. Figure 1 shows how we computed the average refundable and nonrefundable education credit amount received per student.

Figure 1: Computation of the Average Refundable and Nonrefundable Education Credit Received Per Student for Tax Year 2016

	Total Tax Year 2016 Credits	Tax Year 2016 Student	Average Credit Per Student
Refundable Education Credits	$539,375,811	÷ 622,369 Students	**$866.65**
Nonrefundable Education Credits	$489,557,947		**$786.60**
Total Education Credits Received	$1,028,933,758		**$1,653.25**

Source: TIGTA analysis of Tax Year 2016 education credits received per student as of May 4, 2017.

We estimate that the refundable portion of the AOTC totaling $539,375,811 is attributable to the 622,369 students identified who claimed the AOTC exceeding the four-year limit on 612,707 returns.

We adjusted the 612,707 to account for any overlap of exceptions found in our other outcome measure categories. Therefore, from the 7,991,981 tax returns with refundable or net nonrefundable AOTC claimed, we reduced the exception tax returns for Tax Year 2016 for those students who did not include an educational institution EIN on their Form 8863 when claiming that credit. Consequently, the exception tax returns for Tax Year 2016 for those students who claimed the AOTC for more than four years was reduced from 612,707 returns to 498,794 returns claiming 505,070 students.

We multiplied the 505,070 students by four years and multiplied the result by the previously calculated $866.65 average refundable education credit per student to forecast that 498,794 taxpayers would potentially receive $1,750,875,662 in refundable education credits over four years.[3]

Because a prior TIGTA report[4] already included in its outcome measures any Tax Year 2016 returns for which taxpayers who claimed the AOTC for more than the four tax years allowed, we adjusted for Tax Year 2016 in our outcome. We further reduced the $1,750,875,662 four-year estimate by $424,425,030, which was the prior TIGTA outcome measure previously claimed for Tax Year 2016, for a total of $1,326,450,632.

[3] The four-year forecast is based on multiplying the base year by four and assumes, among other considerations, that economic conditions and tax laws do not change.
[4] TIGTA, Ref. No. 2015-40-027, *Billions of Dollars in Potentially Erroneous Education Credits Continue to Be Claimed for Ineligible Students and Institutions* (Mar. 2015).

Type and Value of Outcome Measure:

- Revenue Protection – Potential; $1,077,188,234 in nonrefundable AOTC over four years received by 498,794 taxpayers who claimed 505,070 students for more than the four tax years allowed by law (see page 15).

Methodology Used to Measure the Reported Benefit:

We obtained all Tax Year 2010 through Tax Year 2016 tax returns filed as of April 30, 2017, from the Modernized Tax Return Database for which the AOTC was claimed on an e-filed Form 8863. We identified tax returns in Tax Year 2010 through Tax Year 2016 for which the AOTC claimed was greater than zero or for which the AOTC student identification was not missing. We determined 885,159 students claimed the AOTC for more than four tax years. We matched the 885,159 students to Tax Year 2010 through Tax Year 2016 tax returns and identified 633,565 students on Tax Year 2016 tax returns who were claimed for the AOTC in excess of four years.

The IRS did not capture the education credit amount received per student on Tax Year 2016 returns. Therefore, if a taxpayer claimed more than one student, we could not systemically determine the credit amount attributable to a particular student. In addition, education credit amounts received per tax return are allocated between refundable and nonrefundable portions. To ensure that our outcomes were distributed among refundable and nonrefundable education credits, we calculated the average refundable and nonrefundable credit per student. We matched the tax returns to the Transaction Code File 767 with Reference Number 260 that was on the tax account indicating a refundable education credit was reversed or reduced from an examination. We could not systemically determine when a refundable education credit was reversed or reduced, if the nonrefundable education credit was also affected. Therefore, to be conservative, if a tax return indicated the refundable education credit was reversed, we also reversed the nonrefundable education credit. If a tax return was reduced and there was more than one student on the tax return, we made the assumption that the reduction was for any student that was claimed more than four years. These estimated amounts were used to estimate the dollar value of our outcome measure.

To determine the amount of each refundable and nonrefundable education credit received, we calculated an estimated education credit amount per student based on the total number of students identified on 612,707 tax returns filed and the total amount of education credits received for these Tax Year 2016 returns. We identified 622,369 students on the 612,707 tax returns who received the AOTC. We estimate that the nonrefundable portion of the AOTC totaling $489,557,947[5] is attributable to the 622,369 students we identified that claimed the AOTC exceeding the four-year limit.

[5] See Figure 1.

We adjusted the 612,707 to account for any overlap of exceptions found in our other outcome measure categories. Therefore, from the 7,991,981 tax returns with refundable or net nonrefundable AOTC claimed, we reduced the exception tax returns for Tax Year 2016 for those students who did not include an educational institution EIN on their Form 8863 when claiming that credit. Consequently, the exception tax returns for Tax Year 2016 for those students who claimed the AOTC for more than four years was reduced from 612,707 returns to 498,794 returns claiming 505,070 students.

We multiplied the 505,070 students by four years and multiplied the result by the previously calculated $786.60 average nonrefundable education credit per return to forecast that taxpayers would potentially receive $1,589,152,248 in nonrefundable education credits over four years.[6]

Because a prior TIGTA report[7] already included in its outcome measures any Tax Year 2016 returns for which taxpayers who claimed the AOTC for more than the four tax years allowed, we adjusted for Tax Year 2016 in our outcome. We further reduced the $1,589,152,248 estimate by $511,964,014, which was the prior TIGTA outcome measure previously claimed for Tax Year 2016, for a total of $1,077,188,234.

Type and Value of Outcome Measure:

- Cost Savings (Funds Put to Better Use) – Potential; $867,912,656 in refundable AOTCs over four years received by 369,815 taxpayers who claimed students who did not appear to attend educational institutions the required length of time or were graduate students (see page 15).

Methodology Used to Measure the Reported Benefit:

Based on our analysis of Forms 1098-T, we identified 471,178 taxpayers claiming the AOTC for 475,787 students who appeared not to have attended an educational institution at least half-time as required or were graduate students. We did not include students who received more than one Form 1098-T, *i.e.*, less than half-time on one Form 1098-T and at least half-time on another Form 1098-T. For the returns claiming more than one student, we determined which students were not entitled to receive the credit. We calculated the average amount of refundable AOTC per student and applied this amount to the ineligible students on the return. Our analysis found the 471,178 taxpayers received refundable AOTCs of $346,394,153.

We adjusted the 471,178 taxpayers to account for any overlap of exceptions found in our other outcome measure categories. Therefore, from the 7,991,981 Tax Year 2016 tax returns identified from the Individual Transaction File with refundable or net nonrefundable AOTCs claimed, we reduced the exception tax returns for Tax Year 2016 for those students who did not

[6] The four-year forecast is based on multiplying the base year by four and assumes, among other considerations, that economic conditions and tax laws do not change.

[7] TIGTA, Ref. No. 2015-40-027, *Billions of Dollars in Potentially Erroneous Education Credits Continue to Be Claimed for Ineligible Students and Institutions* (Mar. 2015).

include an educational institution EIN on their Form 8863 when claiming that credit. In addition, we reduced the exception tax returns for taxpayers who claimed students for more than the four tax years allowed by law. Consequently, we reduced the 471,178 taxpayers by 101,363 in order to eliminate the overlap of taxpayers who may be included in other exception categories to arrive at 369,815 taxpayers who appear to have erroneously received refundable education credits for 373,615 students totaling $264,844,986.

We multiplied the $264,844,986 refundable AOTC by four years to forecast that taxpayers would potentially receive $1,059,379,944 in refundable education credits over four years.[8] Because a prior TIGTA report[9] already included in its outcome measures any Tax Year 2016 returns for which Forms 1098-T indicated that the students did not attend the educational institution for more than the required length of time, we adjusted for Tax Year 2016 in our outcome. We further reduced the $1,059,379,944 estimate by $191,467,288, which was the TIGTA outcome measure previously claimed for Tax Year 2016, for a total of $867,912,656.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; $869,056,947 in nonrefundable AOTCs over four years received by 369,815 taxpayers who claimed students who did not appear to attend educational institutions the required length of time or were graduate students (see page 15).

Methodology Used to Measure the Reported Benefit:

We identified 471,178 taxpayers claiming the AOTC for 475,787 students who appeared not to have attended an educational institution at least half-time as required or were graduate students based on our analysis of Forms 1098-T. We did not include students who received more than one Form 1098-T, *i.e.*, less than half-time on one Form 1098-T and at least half-time on another Form 1098-T. For the returns claiming more than one student, we determined which students were not entitled to receive the credit. We calculated the average amount of refundable AOTC per student and applied this amount to the ineligible students on the return. Our analysis found the 471,178 taxpayers received nonrefundable AOTCs of $350,342,727.

We reduced the 471,178 taxpayers by 101,363 in order to eliminate the overlap of taxpayers who may be included in other exception categories to arrive at 369,815 taxpayers who appear to have erroneously received nonrefundable education credits for 373,615 students totaling $275,003,740.

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[8] The four-year forecast is based on multiplying the base year by four and assumes, among other considerations, that economic conditions and tax laws do not change.

[9] TIGTA, Ref. No. 2015-40-027, *Billions of Dollars in Potentially Erroneous Education Credits Continue to Be Claimed for Ineligible Students and Institutions* (Mar. 2015).

We multiplied the $275,003,740 nonrefundable AOTC by four years to forecast that taxpayers would potentially receive $1,100,014,960 in nonrefundable education credits over four years.[10] Because a prior TIGTA report[11] already included in its outcome measures any Tax Year 2016 returns for which Forms 1098-T indicated that the students did not attend the educational institution for more than the required length of time, we adjusted for Tax Year 2016 in our outcome. We further reduced the $1,100,014,960 estimate by $230,958,013, which was the TIGTA outcome measure previously claimed for Tax Year 2016, for a total of $869,056,947.

[10] The four-year forecast is based on multiplying the base year by four and assumes, among other considerations, that economic conditions and tax laws do not change.
[11] TIGTA, Ref. No. 2015-40-027, *Billions of Dollars in Potentially Erroneous Education Credits Continue to Be Claimed for Ineligible Students and Institutions* (Mar. 2015).

Appendix V

Prior TIGTA Audit Findings on the Residential Energy Efficient Property Credit

Figure 1: Prior Audit Findings and Actions Taken by the IRS

Findings	Recommendations	Actions Taken	TIGTA Report Number and Date Issued
The IRS incorrectly limited residential energy credit claims during the 2015 Filing Season. ***Impact:*** *771 tax returns should have received additional credits of $1.5 million.*	None	The IRS agreed to correct the 771 tax accounts. The IRS agreed that the taxpayers' claims were not processed correctly and planned to revise its computer programming and clarify its procedures for the 2016 Filing Season.	**2015-40-080**[1] **Aug. 2015**

[1] TIGTA, Ref. No. 2015-40-080, *Results of the 2015 Filing Season* (Aug. 2015).

Findings	Recommendations	Actions Taken	TIGTA Report Number and Date Issued
For Filing Season 2016, the IRS has not implemented computer programming changes to correct Residential Energy Efficient Property Credit processing errors identified during the 2015 Filing Season. ***Impact:*** *731 tax returns should have received additional credits of $1.2 million.*	1. Implement the computer programming changes to ensure that Residential Energy Efficient Property Credit claims are not inappropriately limited to $500 or $1,000. 2. Review the 731 tax returns and ensure that individuals receive the credit to which they are entitled. 3. Identify additional Residential Energy Efficient Property Credit claims processed after April 28, 2016, to ensure that individuals receive the credit to which they are entitled.	The IRS agreed to all recommendations. However, the IRS did not revise the computer programming for the 2016 Filing Season because the tax extender changes required immediate action, which caused them to postpone the programming changes.	**2017-40-014**[2] **Jan. 2017**
E-Mail Alert – notified the IRS on February 10, 2017 ***Impact:*** *123 tax returns claimed approximately $241,000.*	We alerted IRS management that corrective actions taken in response to our prior recommendations do not ensure that Residential Energy Efficient Property Credit claims are not improperly limited.	The IRS agreed and expected to correct computer programming errors on March 19, 2017.	**2017-40-028**[3] **Mar. 2017**

Source: TIGTA analysis of actions taken in response to prior audit reports.

[2] TIGTA, Ref. No. 2017-40-014, *Results of the 2016 Filing Season* (Jan. 2017).
[3] TIGTA, Ref. No. 2017-40-028, *Interim Results of the 2017 Filing Season* (Mar. 2017).

Appendix VI

Glossary of Terms

Term	Definition
Additional Child Tax Credit	The refundable portion of the CTC that was designed to reduce the income tax burden for families with dependent children. It is used to adjust the individual income tax structure to reflect a family's reduced ability to pay taxes as family size increases.
Advance Premium Tax Credit	A tax credit that is paid in advance to a taxpayer's insurance company to help cover the cost of premiums.
American Opportunity Tax Credit	A partially refundable Federal tax credit used to help parents and college students offset the costs of college.
Average Speed of Answer	The average number of seconds taxpayers waited in the assistor queue (on hold) before receiving services.
Child Tax Credit	A tax credit for families with dependent children that is used to reduce the individual income tax burden for families, better recognize the financial responsibilities of raising dependent children, and promote family values.
Data Center Warehouse	A TIGTA repository of IRS data.
Dependent Database	A risk-based audit selection tool used by the IRS to identify tax returns for audit. The Dependent Database scoring system uses business rules to identify EITC and other refundable credits noncompliance at the point of filing through use of internal and external data elements. The IRS implemented identity theft rules within the Dependent Database in Processing Year 2012. Tax returns are analyzed to identify potentially fraudulent tax returns involving identity theft.
Document Locator Number	A unique number assigned to every tax return to assist in controlling, identifying, and locating the return.
Earned Income Tax Credit	The EITC is used to offset the impact of Social Security taxes on low-income families and to encourage them to seek employment.

Term	Definition
Exchange	The Exchange is where taxpayers find information about health insurance options, purchase qualified health plans, and, if eligible, obtain help paying premiums and out-of-pocket costs. It is also known as the Health Insurance Marketplace or Health Insurance Exchange.
Filing Season	The period from January 1 through mid-April when most individual income tax returns are filed.
Fiscal Year	Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.
Free File	A free Federal tax preparation and e-filing program for eligible taxpayers developed through a partnership between the IRS and the Free File Alliance, LLC. The Alliance is a group of private sector tax software companies.
Individual Master File	An IRS database that maintains transactions or records of individual tax accounts.
Individual Return Transaction File	A database the IRS maintains that contains information on the individual tax returns it receives.
Individual Taxpayer Identification Number	A number created by the IRS to provide Taxpayer Identification Numbers to individuals who do not have and are not eligible to obtain an SSN.
Information Returns Master File	A database containing data from Information Returns, also called "payer documents" or "third-party returns."
Integrated Data Retrieval System	IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.
Level of Service	The primary measure of service to taxpayers. It is the relative success rate of taxpayers who call for live assistance on the IRS toll-free telephone lines.
Marketplace	The Marketplace is the place for people without health insurance to find information about health insurance options and to purchase health insurance. It is also known as the Health Insurance Marketplace or Health Insurance Exchange.

Term	Definition
Master File	The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.
Minimum Essential Coverage	Health insurance coverage that contains essential health benefits including emergency services, maternity and newborn care, and preventive and wellness services. Minimum essential coverage also includes doctor visits, hospitalization, mental health services, and prescription drugs.
Modernized Tax Return Database	The legal repository for original e-filed returns received by the IRS through the Modernized e-File system.
Premium Tax Credit	A refundable tax credit created by the ACA to assist eligible taxpayers with paying their health insurance premiums.
Processing Year	The calendar year in which the return or document is processed by the IRS.
Shared Responsibility Payment	Beginning with the 2015 Filing Season, if a taxpayer or anyone in the taxpayer's tax household does not have minimum essential coverage and does not qualify for a coverage exemption, the taxpayer will need to make an SRP when filing his or her Federal income tax return.
Tax Year	The 12-month period for which tax is calculated. For most individual taxpayers, the tax year is synonymous with the calendar year.
Taxpayer Assistance Centers	Walk-in sites where taxpayers can receive assistance when they believe their tax issue cannot be handled online or by telephone or when they want face-to-face assistance.
Volunteer Program	Includes the Volunteer Income Tax Assistance Program, including the Volunteer Income Tax Assistance Grant Program and the Tax Counseling for the Elderly Program. The Volunteer Program provides free tax assistance to persons with low- to moderate-income (generally defined as within the EITC threshold), senior citizens, persons with disabilities, rural, those with limited English proficiency, and Native Americans.

Appendix VII

Management's Response to the Draft Report

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEC 2 9 2017

MEMORANDUM FOR MICHAEL E. MCKENNEY
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Kenneth C. Corbin Kenneth C. Corbin
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Results of the 2017 Filing Season (Audit # 201740005)

Thank you for the opportunity to review the subject draft report and provide comments. As of November 3, 2017, the IRS has processed over 150 million individual income tax returns and issued more than 111 million refunds totaling $318.4 billion. Face-to-face assistance was provided to taxpayers at our Taxpayer Assistance Centers, which logged more than 2.8 million visits, and telephone assistance was provided to over 20.9 million callers.

As noted in the report, a significant number of provisions of the Protecting Americans From Tax Hikes Act of 2015 (PATH Act) became effective for the 2016 tax year. Foremost among them was acceleration of the due date by which employers are required to file Forms W-2, *Wage and Tax Statement*. The IRS communicated this change to employers and tax return professionals during 2016 to promote awareness of the change to those affected. This resulted in more than twice the number of Forms W-2 being available to the IRS by January 31, 2017, compared to the same date in 2016. Having Form W-2 data available earlier in the processing year substantially improved our ability to detect questionable returns that required additional review. It also allowed us to authenticate returns that had otherwise been flagged as questionable by our identity theft detection processes, permitting those returns to complete processing without taxpayer contact. Education and outreach efforts are ongoing to improve compliance with the January 31 filing deadline for the upcoming 2018 filing season.

In conjunction with advancing the due date for Form W-2 to January 31, the PATH Act also requires the IRS to hold those refunds that included amounts claimed for the Earned Income Tax Credit (EITC) or the Additional Child Tax Credit (ACTC) until February 15. Through February 14, 2017, the IRS had received 13.4 million returns claiming refunds of $115.6 billion that included EITC and ACTC. Those returns were processed through the Return Review Program (RRP), which is the IRS' fraud detection system. The RRP includes the Systemic Verification process that evaluates returns against Form W-2 and other information returns data, along with applying fraud and identity theft filters and models to detect questionable returns that require additional scrutiny before processing can continue. After the Systemic Verification process, fraud detection filters and models, and other processes had been performed, 10.3 million returns with refunds totaling $51.2 billion were cleared for release on February 15, 2017. Having stopped $64.4 billion in questionable refunds demonstrates the importance of having third-party data available for use earlier in the filing season.

Earlier availability of Form 1098-T, *Tuition Statement*, in addition to correctable error authority, as noted in the report, would greatly improve the ability to detect and stop questionable claims for the American Opportunity Tax Credit (AOTC). The IRS is working with the Department of Treasury and Counsel to amend regulatory guidance that would make Form 1098-T data available to the IRS earlier in the filing season. With earlier availability of the data, we could identify those claims where taxpayers made a clerical error by omitting an educational institution's Employer Identification Number (EIN) but the student, nonetheless, qualified for the AOTC. Our preliminary research for the 2016 tax year indicates that 44 percent of the students who did not include an EIN on Form 8863, *Education Credits (American Opportunity and Lifetime Learning Credits)*, did, in fact, receive Form 1098-T. This translates to 668,000 taxpayers who would have been contacted to resolve a claim to which they were entitled. This would have resulted in a significant amount of taxpayer burden and would have also severely impacted the ability of our limited resources to address those returns that truly are questionable.

However, it should be noted regarding those claims identified where the student exceeded the four-year lifetime limit, expanded correctible error authority would still be needed to effectively address this area of non-compliance. Our processing systems can identify such claims where the limit has been exceeded, but those returns must be treated under deficiency procedures that are resource-intensive and compete with other areas of non-compliance (such as EITC or ACTC) for limited resources available to address them. Consequently, we are unable to address all returns where students are not eligible to receive the AOTC.

We agree with the recommendations contained in the report, as well as the associated outcome measures. Attached are our comments and proposed actions to your recommendations. If you have any questions, please contact me, or a member of your staff may contact James P. Clifford, Director, Customer Account Services, Wage and Investment Division, at (470) 639-3504.

Attachment

Attachment

Recommendations

The Commissioner, Wage and Investment Division, should:

RECOMMENDATION 1
Revise procedures to include issuing letters and alerts to preparers who file tax returns claiming the CTC but do not provide the required Form 8867.

CORRECTIVE ACTION
We agree with this recommendation that applies to paper returns and letters. A process was already in place to issue alerts on electronic returns claiming Child Tax Credit (CTC). IRS has already implemented programming changes to this non-systemic letter process that will be effective January 2018.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
Director, Refundable Credits Policy and Program Management, Return Integrity and Compliance Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
N/A

RECOMMENDATION 2
Evaluate the 41 preparers we identified who filed CTC, ACTC, and AOTC claims without a Form 8867 and were not notified by the IRS and ensure that actions are taken to notify the preparers of the filing requirement if warranted.

CORRECTIVE ACTION
We agree with this recommendation. IRS completed the review and determined 14 were preparers with non-US addresses, 7 were cases where there was known preparer ID theft, 2 were cases of duplicate returns from the same taxpayer, and 18 were instances where the returns were adjusted so did not meet criteria for notification. As a result, IRS sent letters to the preparers with non-US addresses to alert them of the Form 8867, *Paid Preparer's Due Diligence Checklist* requirement in October 2017. IRS has also changed procedures to send letters to all preparers, regardless of address.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
N/A

2

CORRECTIVE ACTION MONITORING PLAN
N/A

RECOMMENDATION 3
Ensure that IRS employees who process these credits are aware that taxpayers reporting a foreign income exclusion or housing deduction cannot also receive the ACTC.

CORRECTIVE ACTION
We agree with this recommendation. The existing procedures in Internal Revenue Manual 3.22.3, *International Error Resolution - Individual Income Tax Returns,* are correct and covered in Lesson 3A of the International Error Resolution System (ERS) student guide 2512-002. To reinforce the existing procedures, a Quality Alert was created on November 7, 2017, for ERS instructors to address the issue during annual refresher training and in the initial training for international returns.

IMPLEMENTATION DATE
May 15, 2018

RESPONSIBLE OFFICIAL
Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 4
Review the 45 tax returns we identified for which the IRS erroneously paid the ACTC and take the actions necessary to recover the erroneous payments.

CORRECTIVE ACTION
We agree with this recommendation. The affected returns will be reviewed and the appropriate action will be taken to recover erroneously paid credits.

IMPLEMENTATION DATE
March 15, 2018

RESPONSIBLE OFFICIAL
Director, Accounts Management, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
We will monitor this corrective action as part of our internal management control system.

RECOMMENDATION 5
Review the 494 tax returns we identified and take the actions necessary to ensure that these taxpayers receive the Residential Energy Efficient Property Credit to which they are entitled.

CORRECTIVE ACTION
We agree with this recommendation. We have corrected 484 of the 494 taxpayers' accounts for the amounts to which they are entitled. Of the remaining ten accounts, seven require additional research and three cannot be adjusted due to an ongoing Examination.

IMPLEMENTATION DATE
Implemented

RESPONSIBLE OFFICIAL
Director, Accounts Management, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
N/A

Recommendation

RECOMMENDATION 6
The Commissioner, Wage and Investment Division, should establish processes to use its math error authority to deny all e-filed and paper AOTC claims for which the taxpayer does not provide the institution EIN for each student claimed on the return.

CORRECTIVE ACTION
We agree and will submit a Unified Work Request (UWR) with requirements for Tax Year 2018 AOTC claims for which the institution EIN is not present. If a systemic process is feasible, the requisite programming changes will be requested; however, Information Technology resources are limited and are subject to budgetary constraints and competing priorities. Therefore, we cannot provide an implementation date.

IMPLEMENTATION DATE
N/A

4

RESPONSIBLE OFFICIAL
Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
We will monitor this corrective action as part of our internal management control system.

Recommendation

The Commissioner, Wage and Investment Division, should:

RECOMMENDATION 7
Modify Form 2441 to ask taxpayers whether or not they fall under one of the exceptions to be able to file as Married Filing Separately and revise computer programs to allow the credit only when a taxpayer attests that he or she meets the exception by checking the applicable box.

CORRECTIVE ACTION
We agree with this recommendation. We will submit the programming and form change requests by January 31, 2018; however, programming changes are subject to competing priorities and limited resources. Consequently, we cannot provide an implementation date.

IMPLEMENTATION DATE
N/A

RESPONSIBLE OFFICIAL
Director, Submission Processing, Customer Account Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN
We will monitor this corrective action as part of our internal management control system.