TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Recurring Identification Is Needed to Ensure That Employers Full Pay the Deferred Social Security Tax

May 22, 2023

Report Number: 2023-46-030

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HIGHLIGHTS: Recurring Identification Is Needed to Ensure That Employers Full Pay the Deferred Social Security Tax

Final Audit Report issued on May 22, 2023 **Report Number 2023-46-030**

Why TIGTA Did This Audit

This audit is a continuation of our review of the IRS's implementation of business tax provisions included in legislation passed in response to the Coronavirus Disease 2019 pandemic. The Coronavirus Aid, Relief, and Economic Security Act was enacted in March 2020. A provision allowed employers and self-employed individuals to defer payment of their Social Security tax. The overall objective of this review was to evaluate the IRS's efforts to ensure that taxpayers pay their deferred Social Security tax as required.

Impact on Tax Administration

Employers that deferred the employer portion of the Social Security tax must pay one-half of the deferral by December 31, 2021, and the remaining one-half by December 31, 2022. Additionally, employers that deferred the employee portion of the Social Security tax must pay the entire amount by December 31, 2021. As of February 23, 2023, the IRS reported that employers paid $123 billion (95 percent) of the total $129 billion in Social Security tax deferrals.

What TIGTA Found

The IRS has developed processes to systemically identify tax accounts with an unpaid December 2021 Social Security tax deferral and manually adjust the tax account. As of April 28, 2022, there were approximately 1 million employers that deferred $129 billion in the Social Security tax, of which employers paid approximately $69 billion by the end of December 2021.

On March 10, 2022, the IRS reported that payments on approximately 22,000 employer tax accounts were posting incorrectly as an additional deferral instead of reducing the unpaid deferral balance. The IRS fixed the programming and took action to correct the impacted tax accounts. Additionally, the IRS was aware of additional tax accounts in which the IRS incorrectly processed duplicate reversals of the deferred Social Security tax on self-employed individuals. The IRS identified 3,231 self-employed individuals as of August 14, 2022, with this error resulting in the unpaid deferral balance in the affected tax accounts being overstated. As of March 2023, the IRS has begun the process to correct the tax accounts.

Due to limited resources, the IRS was unable to develop programming to adjust accounts systemically that did not timely pay on the Social Security tax deferral. As a result, TIGTA estimates $108 million in potential penalties and interest were not assessed on 66,839 tax accounts. Not assessing penalties on these accounts is consistent with other actions taken by the IRS to lessen the burden of the pandemic on taxpayers.

As of December 2022, the IRS has not adjusted all of the tax accounts it identified that did not fully pay the required deferral by December 2021. The IRS plans to continue to identify new tax accounts with a deferral, regardless of the deferral due date, through Calendar Year 2023 to ensure proper identification of the employers that need to pay the deferral. However, amended tax returns can be filed on employment tax returns until March 2024, thus potentially adjusting the deferral amount.

What TIGTA Recommended

TIGTA recommended that the IRS correct tax accounts with incorrect deferral amounts and continue to identify new Social Security tax deferrals through at least Calendar Year 2024.

The IRS agreed with both recommendations. The IRS plans to remove the erroneous duplicate reversals on all accounts as necessary, and ensure that all applicable modules with unpaid deferred Social Security tax properly show the unpaid balances.

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

U.S. DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20024

May 22, 2023

MEMORANDUM FOR: COMMISSIONER OF INTERNAL REVENUE

Heather Hill

FROM: Heather M. Hill
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Recurring Identification Is Needed to Ensure That Employers Full Pay the Deferred Social Security Tax (Audit #202240623)

This report represents the results of our review to evaluate the Internal Revenue Service's efforts to ensure that taxpayers, *i.e.*, businesses and individuals, pay their deferred Social Security taxes as required. This review is part of our Fiscal Year 2023 Annual Audit Plan and addresses the major management and performance challenge of *Administering Tax Law Changes.*

Management's complete response to the draft audit report is included as Appendix III. If you have any questions, please contact me or Diana M. Tengesdal, Acting Assistant Inspector General for Audit (Returns Processing and Account Services).

Table of Contents

Background

The Social Security tax is a U.S. Federal payroll tax imposed on both employees and employers to fund Social Security.[1] The employees' portion of the tax is withheld from employees' wages by most employers and paid to the Internal Revenue Service (IRS) on their behalf. The Calendar Year 2020 tax rate for the Social Security tax was 6.2 percent paid by the employer and 6.2 percent withheld from the employee, for a total of 12.4 percent. Self-employed individuals had a 12.4 percent Social Security tax rate for Calendar Year 2020.

Section 2302 of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), passed on March 27, 2020, allows employers, including self-employed taxpayers, to defer deposits of the employer's share of Social Security taxes and Tier 1 Railroad Retirement taxes, *i.e.*, retirement, disability, spousal, and survivors benefits, for wages paid between March 27, 2020, and December 31, 2020.[2] Employers can defer the full amount of the employer's share of the Social Security tax while self-employed taxpayers can defer 50 percent of the total Social Security tax.

On August 8, 2020, the President directed the Secretary of the Treasury to expand the deferral to include the employee's portion of the Social Security tax or the Railroad Retirement tax equivalent for wages paid from September 1, 2020, through December 31, 2020, in order to increase employee paychecks.[3]

The amount of the Social Security tax deferred is reported by businesses on employment tax returns: Form 941, *Employer's QUARTERLY Federal Tax Return*; Form 943, *Employer's Annual Federal Tax Return for Agricultural Employees*; Form 944, *Employer's ANNUAL Federal Tax Return*; and Form CT-1, *Employer's Annual Railroad Retirement Tax Return*; and by self-employed individuals on Form 1040, Schedule 3, *Additional Credits and Payments*; and Form 1041, *U.S. Income Tax Return for Estates and Trusts*. Our analysis of tax account data as of April 28, 2022, identified approximately 1 million businesses and self-employed taxpayers (referred to hereafter collectively as employers) that deferred a total of $129 billion in Social Security taxes.[4] Figure 1 provides an example of the lines used to report the Social Security tax deferral on the Form 941.

[1] Social Security is known as the Old-Age, Survivors, and Disability Insurance program administered by the Social Security Administration, which is financed through a payroll tax.

[2] Pub. L. No. 116-136, 134 Stat. 351.

[3] Memorandum for the Secretary of the Treasury, *Deferring Payroll Tax Obligations in Light on the Ongoing COVID-19 Disaster,* Presidential Document 2020-17899 (Aug. 8, 2020).

[4] The employers include Federal Government agencies responsible for withholding payroll taxes.

Figure 1: Tax Year 2020 Form 941, Pages 2 and 3

Part 1: Answer these questions for this quarter. *(continued)*

11d	**Total nonrefundable credits.** Add lines 11a, 11b, and 11c	11d	.
12	**Total taxes after adjustments and nonrefundable credits.** Subtract line 11d from line 10	12	.
13a	**Total deposits for this quarter,** including overpayment applied from a prior quarter and overpayments applied from Form 941-X, 941-X (PR), 944-X, or 944-X (SP) filed in the current quarter	13a	.
13b	**Deferred amount of social security tax**	13b	.
13c	**Refundable portion of credit for qualified sick and family leave wages from Worksheet 1**	13c	.
13d	**Refundable portion of employee retention credit from Worksheet 1**	13d	.
13e	**Total deposits, deferrals, and refundable credits.** Add lines 13a, 13b, 13c, and 13d	13e	.
13f	**Total advances received from filing Form(s) 7200 for the quarter**	13f	.
13g	**Total deposits, deferrals, and refundable credits less advances.** Subtract line 13f from line 13e	13g	.
14	**Balance due.** If line 12 is more than line 13g, enter the difference and see instructions	14	.
15	**Overpayment.** If line 13g is more than line 12, enter the difference . Check one: ☐ Apply to next return. ☐ Send a refund.		

Part 3: Tell us about your business. If a question does NOT apply to your business, leave it blank.

17	**If your business has closed or you stopped paying wages** ☐ Check here, and enter the final date you paid wages / / ; also attach a statement to your return. See instructions.		
18	**If you're a seasonal employer and you don't have to file a return for every quarter of the year** ☐ Check here.		
19	**Qualified health plan expenses allocable to qualified sick leave wages**	19	.
20	**Qualified health plan expenses allocable to qualified family leave wages**	20	.
21	**Qualified wages for the employee retention credit**	21	.
22	**Qualified health plan expenses allocable to wages reported on line 21**	22	.
23	**Credit from Form 5884-C, line 11, for this quarter**	23	.
24	**Deferred amount of the employee share of social security tax included on line 13b**	24	.
25	**Reserved for future use**	25	.

Source: Excerpt from Form 941 obtained from IRS.gov as of July 2020.

The amount of the deferred Social Security tax is recorded on the applicable tax account as a temporary credit. The IRS reduces the amount of credit as payments are made toward the deferral.

Payment of the deferred Social Security tax

The due date for payment of the Social Security tax depends on the type of tax that was deferred, *i.e.*, employer or employee portion. Employers that deferred the employee portion of the tax were required to increase withholding on employees ratably between January 1, 2021, and December 31, 2021, to collect the deferred tax from the employee. Employers that deferred the employer portion of the tax and self-employed individuals who deferred tax must pay a portion of the deferral by December 31, 2021, with the remainder due by December 31, 2022. Payments can be made electronically using the Electronic Federal Tax Payment System, by credit or debit card, or by a check or money order. Figure 2 explains the various due dates for the payment of the deferred Social Security tax.

Figure 2: Due Dates for Payment of the Social Security Tax Deferral for Businesses and Self-Employed Individuals

Payment Due Date		Self-Employed Taxpayers[5]
December 31, 2021	One-half of the employer deferral amount the taxpayer was eligible to defer, *i.e.*, maximum deferral.[6] All employee Social Security tax deferred.	One-half of the employer deferral amount the taxpayer was eligible to defer, *i.e.*, maximum deferral.[7]
December 31, 2022	Remaining balance of employer portion of the Social Security tax deferral.	Remaining balance of employer portion of the Social Security tax deferral.

Source: Treasury Inspector General for Tax Administration (TIGTA) review of the CARES Act.

The following hypothetical example illustrates the calculation of the deferred Social Security tax an employer was required to pay by December 31, 2021.

> *The employer's share of Business A's Social Security tax for the third quarter of Fiscal Year 2020 was $160,000 and was the maximum amount Business A could defer. Business A paid $60,000 in the Social Security tax for the third quarter of Fiscal Year 2020 and deferred $100,000.*
>
> *The maximum amount Business A should have paid by December 31, 2021, was one-half of the maximum eligible deferral amount or $80,000 ($160,000 maximum eligible deferral/2). The actual amount of the third-quarter deferral Business A was required to pay by December 31, 2021, was the maximum payment amount less any Social Security taxes that were not deferred ($80,000 - $60,000) or $20,000. The remaining $80,000 was due by December 31, 2022.*

During October 2021, the IRS sent more than 1.1 million courtesy notices to remind employers that they have an amount due on December 31, 2021, for deferred Social Security taxes, *i.e.*, employer and employee amounts.[8] The notice provided the total unpaid tax amounts due by December 2021 and December 2022.[9] The notices were for information only and did not require a response from employers. During October 2022, the IRS sent more than 1 million second reminder notices to employers that still had an unpaid Social Security tax deferral informing them of the amount due by December 31, 2022. As of February 23, 2023, the IRS

[5] Self-employed taxpayers were not eligible to defer the employee portion of the Social Security tax.

[6] The amount can be less than 50 percent in situations in which the employer made previous payments or if the employer does not defer the maximum deferral.

[7] This assumes that the employer deferred the maximum deferral amount. The amount can be less than 50 percent in situations in which the employer does not defer the maximum deferral.

[8] Computer Paragraph 56V/256V, *CARES Act Social Security Tax Deferral Reminder.*

[9] The employee portion of the deferred Social Security tax is reported in the amount due by December 2021.

reported that employers paid $123 billion (95 percent) of the total $129 billion in Social Security tax deferrals.

Assessment of penalties for late payment of tax

Employers that did not make the required deferred tax payment by December 2021 and December 2022 are subject to collection action, including the assessment of penalties, such as failure to pay tax and failure to make deposit of taxes.[10] The IRS developed processes to identify tax accounts with an unpaid deferral systemically. However, due to limited resources, the IRS was unable to develop programming to adjust accounts systemically that did not timely pay on the Social Security tax deferral. The IRS manually adjusts the deferral balance so that applicable penalties and interest can be applied. Employers, including self-employed individuals, that fail to make the required payment are charged failure to pay penalties. In addition, businesses that do not make the required payment may also be charged failure to deposit penalties. Penalties and interest accrue on the unpaid Social Security deferral until the employer pays the required amount. The IRS notifies employers when penalties and interest are assessed on the tax account.

This review evaluated the IRS's processes and procedures to ensure that employers paid the deferred Social Security tax by December 31, 2021, as required. We plan to conduct a review of the status of the payment of the deferred tax due by December 31, 2022, later in Calendar Year 2023.[11]

Results of Review

Most Employers Made the Required December 2021 Payment of the Deferred Social Security Tax

Our review of the courtesy letters the IRS sent found that each employer that deferred the Social Security tax received a payment reminder. Tax data as of April 28, 2022, showed approximately 1 million employers deferred $129 billion in the Social Security tax on 1.3 million tax accounts.[12] These employers were required to pay $65.6 billion in deferred taxes on 1.2 million of the 1.3 million tax accounts by December 31, 2021. The deferred tax actually paid by the end of December 2021 totaled approximately $69 billion, which represented a combination of payments on the deferral due in December 2021 and excess payments on the deferral reducing the amount due in December 2022.[13] Figures 3 and 4 provide an overview of required payments due on December 31, 2021, for self-employed individuals and businesses.

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[10] Internal Revenue Code Section 6656, *Failure to make deposit of taxes*; and Section 6601, *Interest on underpayment, nonpayment, or extensions of time for payment, of tax*.

[11] TIGTA, Audit No. 202340611, *Continued Assessment of the Repayment of Social Security Tax Deferrals*.

[12] Business taxpayers can have more than one tax account. For example, quarterly employment tax filers can defer tax for multiple quarters for Tax Year 2020.

[13] Due to the timing of the holidays, the IRS considered payments made by January 3, 2022, timely for the December 31, 2021, payment due date.

Figure 3: Social Security Tax Deferral Payments Due December 2021 for Self-Employed Taxpayers

Self-Employed Taxpayers	Tax Accounts	Deferral Due	Deferral Paid
Required to make a payment by December 2021	836,199	$465 million	$383 million
Made the required payment timely	504,345	$230 million	$372 million
Did not make the required payment timely	331,854	$235 million	$11 million

Source: TIGTA analysis of Individual Master File transactions as of April 28, 2022.

Figure 4: Social Security Tax Deferral Payments Due December 2021 for Business Taxpayers

Business Taxpayers	Tax Accounts	Deferral Due	Deferral Paid
Required to make a payment by December 2021	384,989[14]	$65 billion	$69 billion
Made the required payment timely	312,873	$56 billion	$65 billion
Did not make the required payment timely	72,116	$9 billion	$4 billion

Source: TIGTA analysis of Business Master File transactions as of April 28, 2022. The deferral amount due and paid includes the employer and employee portions of the Social Security tax that was deferred.

As of February 23, 2023, the IRS reported that employers paid $123 billion (95 percent) of the total $129 billion in Social Security tax deferrals. The IRS reported that 384,314 employers owe approximately $6 billion in the Social Security tax deferral. Applicable employers will be subjected to the IRS's collection actions, which include sending balance due notices to taxpayers. In February 2023, the IRS started sending balance due notices to the employers that have not timely paid their Social Security tax deferral by December 2022.

Processing errors caused some tax accounts to have an incorrect unpaid deferral balance

On March 10, 2022, the IRS reported that payments of the deferral were posting incorrectly as an additional deferral instead of reducing the unpaid deferral balance in the tax account. The IRS estimated that the error affected approximately 22,000 individual and business tax accounts. The IRS fixed the programming and took actions to correct the impacted tax accounts.

[14] The 384,989 tax accounts are for 158,086 unique business taxpayers.

Additionally, the IRS was aware of additional tax accounts where the IRS incorrectly processed duplicate reversals of the deferred Social Security tax on self-employed individuals. As a result, the IRS identified 3,231 self-employed individual tax accounts as of August 14, 2022, with this error that resulted in the unpaid deferral balance in the affected tax accounts being overstated. IRS management stated that the incorrect reversals are the result of employee error. Management stated that because there is minimal impact to employers, they will work these accounts as time and available resources permit. As of March 2023, the IRS has begun the process to correct the tax accounts.

Recommendation 1: The Commissioner, Small Business/Self-Employed Division, should ensure that the 3,231 tax accounts are updated to reflect the correct balance due.

> **Management's Response:** IRS management agreed with the recommendation and is removing the erroneous duplicate reversals on all accounts as necessary.

Actions Taken to Address the Late Payment of Deferrals Are Reasonable

Employers that do not timely make the required deferred tax payment are subject to penalties. The IRS developed processes to systemically identify tax accounts with an unpaid December 2021 deferral. The IRS manually adjusts the deferral balance for late payments and assesses applicable penalties. While these processes do not ensure that all employers that made a late deferral payment are assessed a penalty, the processes are consistent with other actions taken by the IRS to lessen the burden of the Coronavirus Disease 2019 pandemic on taxpayers.

Employers underpaid their required December 2021 deferral by $5.4 billion. Beginning in February 2022, the IRS began identifying tax accounts, on a recurring basis, with an unpaid December 2021 deferral for manual adjustment. The programming identifies accounts based on the amount remaining to be paid on the date the program is run rather than the unpaid deferral amount as of December 31, 2021. In addition, due to limited resources, the IRS can only adjust a limited number of tax accounts per month. As such, some employers that made a late payment were either not assessed a penalty or were assessed a lesser penalty amount. As of April 28, 2022, the IRS had assessed an estimated $216.3 million in penalties and interest on 193,325 (151,151 self-employed individuals and 42,174 businesses) tax accounts. We estimate $108 million in potential penalties and interest on 66,839 (55,551 self-employed individuals and 11,288 businesses) tax accounts were not assessed. The following hypothetical example illustrates how the IRS's processes result in reduced deferral-related penalties.

> *Taxpayer A was required to pay $20,000 in the deferred Social Security tax by December 31, 2021. Taxpayer A paid $5,000 before the required payment date and paid the remaining $15,000 in June 2022, i.e., a late payment.*
>
> *In March 2022, the IRS began identifying employers that did not make a timely December 2021 deferral payment. Due to limited resources, the IRS was unable to adjust Taxpayer A's account before June 2022. The IRS also did not adjust Taxpayer A's tax account in July 2022 because Taxpayer A paid the full amount due prior to the IRS adjusting the tax account. As a result, Taxpayer A was not assessed a penalty for paying the remaining $15,000 deferred tax late.*

> *Had Taxpayer A paid $7,000 of the remaining $15,000 in the deferred tax in June 2022, the IRS would have identified Taxpayer A on the July 2022 list and assessed penalties on the $8,000 in the deferred tax that was not paid at that time.*

We shared our observations regarding the inconsistent application of penalties with IRS management. Management stated that they are aware that the process to address late deferral payments results in some employers not being penalized and others receiving reduced penalties. Management stated that they had planned to develop systemic processes to identify employers that did not make the required December 2021 payment and assess applicable penalties. However, the Information Technology organization notified management that it could not complete this request due to limited resources and the complex nature of the programming. As a result, management had to implement processes that balanced the need to ensure that employers are paying the deferred Social Security tax with the resources available to manually review applicable tax accounts. IRS management stated that the process they implemented is in the best interest of the employer by providing additional time to make a payment and avoid penalties and interest.

The IRS has taken actions throughout the pandemic to lessen the burden on taxpayers. For example, to help struggling taxpayers affected by the pandemic, the IRS provided penalty relief to nearly 1.6 million taxpayers for more than $1.2 billion in refunds or credits. Consistent with these actions, the IRS's penalty process for the deferred Social Security tax allows employers additional time to make their required December 2021 payment without penalty. These processes also recognize that not all employers may be in a position to make the required payment. For example, our review of the 403,970 tax accounts with a late deferral payment or no payment found an estimated 60,711 employers may no longer be in business.[15]

Recurring Review of Tax Accounts Is Needed to Ensure That Employers Make the Required December 2021 Payment

The IRS developed a process to manually adjust employer tax accounts that failed to make the required payment. The IRS adjusts the tax account to report the deferral that the taxpayer failed to pay as a balance due. As of December 2022, the IRS has not adjusted all of the tax accounts it identified that did not fully pay the required amount of the Social Security tax deferral by December 2021, resulting in the tax accounts not reporting a balance due. The IRS prioritized for review those tax accounts that are not controlled by other business units, *e.g.*, Criminal Investigation, because these accounts cannot have penalties and interest assessed on unpaid deferral amounts until the tax account is released or approval is given by the controlling business unit. Additionally, amended tax returns can impact the amount of the deferral. Employers generally have three years from the date the tax return was filed or two years from the date the employer paid the tax reported on the tax return, whichever is later, to file an amended tax return. For example, an employer who files the Form 941 for the fourth quarter on March 1, 2021, will have until March 2024 to file an amended tax return potentially adjusting the Social Security tax deferral.

Due to changing conditions on tax accounts, *i.e.*, amended tax returns, there is no definitive way to determine if all Social Security tax deferral credits have been reversed to accurately show the

[15] Business officials are responsible for paying the deferred Social Security tax if a business becomes defunct.

unpaid balance on the tax account without continually identifying tax returns that are claiming or updating deferral amounts. IRS management stated that they are still developing the procedures to ensure that all accounts with unpaid deferrals are updated correctly. Currently, the IRS plans to continue to identify new tax accounts with a deferral, regardless of the deferral due date, through Calendar Year 2023 to ensure proper identification of employers that need to pay the Social Security tax deferral.

Recommendation 2: The Commissioner, Small Business/Self-Employed Division, should continue to identify new tax accounts with a Social Security tax deferral at least through Calendar Year 2024 to ensure that all unpaid deferrals are identified for collection as appropriate.

> **Management's Response:** IRS management agreed with the recommendation and will ensure that all applicable modules with unpaid deferred Social Security tax properly show the unpaid balances by June 15, 2025.

Appendix I

Detailed Objective, Scope, and Methodology

The objective of this review was to evaluate the IRS's efforts to ensure that taxpayers, *i.e.*, businesses and individuals, pay their deferred Social Security taxes as required. To accomplish our objective, we:

- Evaluated the accuracy of reminder notices that were sent to employers that deferred their Social Security tax.
- Determined whether employers made their required repayment of the deferred Social Security tax by December 31, 2021.
- Determined whether the appropriate penalties and interest were assessed on employers that did not timely pay their deferred Social Security tax.

Performance of This Review

This review was performed with information obtained from the IRS Small Business/Self-Employed Division in Lanham, Maryland, during the period July 2022 through March 2023. 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.

Major contributors to the report were Diana Tengesdal, Acting Assistant Inspector General for Audit (Returns Processing and Account Services); Deann Baiza, Director; Jonathan Lloyd, Audit Manager; Karen Fulte, Senior Auditor; Ryan Kenaley, Auditor; and Dallin West, Auditor.

Validity and Reliability of Data From Computer-Based Systems

During this review, we relied on the Business Master File[1] and Individual Master File[2] data stored on TIGTA's Data Center Warehouse.[3] To assess the reliability of the computer-processed data, we ensured that each data extract contained specific data we needed and that the data were accurate. In addition, we selected judgmental samples from the extracts and verified that the data in the extracts were the same as the data captured in the IRS's Integrated Data Retrieval System.[4] Based on the results of our testing, we believe that the data used in our review were reliable for the purposes of this report.

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[1] The IRS database that consists of Federal tax-related transactions and accounts for businesses. These include employment taxes, income taxes on businesses, and excise taxes.

[2] The IRS database that maintains transactions or records of individual taxpayers.

[3] A TIGTA repository of IRS data.

[4] IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.

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 Internal Revenue Manual, other policies and procedures followed when processing the Social Security tax deferral, and the systems/programming used to process the tax returns and transactions on the tax accounts.[5] We evaluated the controls by reviewing the IRS's internal guidelines, interviewing IRS management, and evaluating applicable documentation and management information reports.[6]

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[5] The Internal Revenue Manual is the primary, official source of IRS instructions to staff related to the organization, administration, and operations of the IRS.

[6] Internal guidelines include the Internal Revenue Manual, desk guides, *etc*.

Appendix II

Tax Year 2020 Forms That Report the Deferred Social Security Tax

Form	Form Name
Form 941	*Employer's QUARTERLY Federal Tax Return*
Form 943	*Employer's Annual Federal Tax Return for Agricultural Employees*
Form 944	*Employer's ANNUAL Federal Tax Return*
Form CT-1	*Employer's Annual Railroad Retirement Tax Return*
Form 1040	*U.S. Individual Income Tax Return*
Form 1041	*U.S. Income Tax Return for Estates and Trusts*

Source: Tax returns that report the Social Security tax deferral for Tax Year 2020.

Appendix III

Management's Response to the Draft Report

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

May 2, 2023

MEMORANDUM FOR HEATHER M. HILL
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Lia Colbert Amalia C. Colbert Digitally signed by Amalia C. Colbert Date: 2023.05.02 15:17:17 -04'00'
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report - Recurring Identification Is Needed to Ensure That Employers Full Pay the Deferred Social Security Tax (Audit #202240623)

Thank you for the opportunity to review and comment on the subject draft audit report. We have worked hard through many unique technical and procedural challenges to implement processes to ensure taxpayers pay their deferred Social Security tax as required by the Coronavirus Aid, Relief, and Economic Security (CARES) Act. This work has included collaborating with multiple functions within the Wage and Investment Division to prioritize the identification and adjustment of accounts with unpaid deferred tax.

Per Section 2302 of the CARES Act, employers and taxpayers were allowed to defer the employers' share of Social Security taxes during the 2020 tax year for taxes imposed from March 27, 2020, to December 31, 2020. To account for this special circumstance, the IRS created a false credit to temporarily record the deferral in our systems. Taxpayers were required to pay and deposit 50 percent of the eligible amount to be deferred by December 31, 2021, and the remainder by December 31, 2022. When the employer or taxpayer does not pay or deposit the required amount by the installment due dates, the IRS reverses the false credit on the applicable accounts.

We have completed 98 percent of all reversals for the first installment and will proceed with adjustments for the remaining 2 percent as account conditions, such as freeze codes, allow. Additionally, we have completed 27 percent of all reversals on the second installment. We are continuing to work the reversals for both the first and second installment on a biweekly basis and will continue working the reversals until all tax accounts have been addressed.

If you have any questions, please contact me, or Victor Onorato, Director, Operations Support, Small Business/Self-Employed Division.

Attachment

Attachment

RECOMMENDATION 1:
The Commissioner, Small Business/Self-Employed Division, should ensure that the 3,231 tax accounts are updated to reflect the correct balance due.

CORRECTIVE ACTION:
We are currently removing the erroneous duplicate reversals on all accounts as necessary. The accounts are being manually reviewed and monitored and a tool is being run to correct each module. We have corrected 61 percent of these tax accounts, with 1,973 of the 3,231 modules adjusted as of April 20, 2023.

RESPONSIBLE OFFICIAL:
Director, Business Support Office, Small Business/Self-Employed Division

IMPLEMENTATION DATE:
June 15, 2023

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 2:
The Commissioner, Small Business/Self-Employed Division, should continue to identify new tax accounts with a Social Security tax deferral at least through Calendar Year 2024 to ensure that all unpaid deferrals are identified for collection as appropriate.

CORRECTIVE ACTION:
By 6/15/25, we will ensure all applicable modules with unpaid deferred Social Security tax properly show the unpaid balances.

RESPONSIBLE OFFICIAL:
Director, Business Support Office, Small Business/Self-Employed Division

IMPLEMENTATION DATE:
June 15, 2025

CORRECTIVE ACTION MONITORING PLAN:
IRS will monitor this corrective action as part of our internal management system of controls.

Appendix IV

Abbreviations

CARES Act	Coronavirus Aid, Relief, and Economic Security Act
IRS	Internal Revenue Service
TIGTA	Treasury Inspector General for Tax Administration

To report fraud, waste, or abuse,
call our toll-free hotline at:

(800) 366-4484

By Web:

www.treasury.gov/tigta/

Or Write:

Treasury Inspector General for Tax Administration

P.O. Box 23291

Washington, D.C. 20026

Information you provide is confidential, and you may remain anonymous.