

TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



American Rescue Plan Act: Review of the Reconciliation of the Child Tax Credit

June 14, 2023

Report Number: 2023-47-035

Why TIGTA Did This Audit

The *American Rescue Plan Act of 2021* provided taxpayers the ability to receive up to one half of the estimated Tax Year 2021 Child Tax Credit in advance payments between July and December 2021. The IRS issued 216.9 million advance payments totaling \$93.5 billion. The IRS estimated the advance payments based on prior year tax return information and information reported through its nonfiler tools.

This audit was initiated to assess processes and procedures to ensure that taxpayers properly reconciled the advance Child Tax Credit payments on their Tax Year 2021 tax return.

Impact on Tax Administration

TIGTA previously reported that the IRS erroneously issued 3.3 million advance payments to 1.5 million taxpayers who were not eligible to receive an advance payment. The IRS's reconciliation process addressed both potentially ineligible taxpayers and eligible taxpayers who had not received advance payments when they filed their Tax Year 2021 tax return. However, our review showed that as of October 12, 2022, approximately 4.1 million taxpayers who were issued about \$9 billion in advance payments had not yet filed a tax return.

What TIGTA Found

The IRS created an automated process to recalculate the Child Tax Credit, including the amount of advance payments posted to a taxpayers' tax account. This process identified 3.8 million tax returns that contained a discrepancy between the IRS calculated Child Tax Credit amount and the amount claimed by the taxpayer that required resolution. TIGTA's review of the reconciliation process of tax returns processed through May 5, 2022, identified:

- 6,833 taxpayers who potentially received \$10.5 million in excess Child Tax Credit because tax examiners incorrectly resolved error conditions that allowed more Child Tax Credit than what the taxpayer was eligible to claim on their tax return.
- 105 taxpayers who did not receive all of their eligible Child Tax Credit, resulting in the taxpayers not receiving an estimated \$139,000 in Child Tax Credit.

Further, in response to TIGTA's concerns, the IRS developed a process to identify undeliverable advance payments that occurred after taxpayers filed their Tax Year 2021 tax return. As of October 12, 2022, the IRS reissued payments to 7,877 taxpayers totaling \$5.4 million.

TIGTA's follow up on prior observations through October 12, 2022, showed that:



Of taxpayers with **erroneous advance payments**: **173,000 taxpayers** qualified for repayment protection totaling **\$97.8 million**, **69,000 taxpayers** were required to repay **\$21.6 million**, and **845,000 taxpayers** totaling **\$1 billion** had yet to file a Tax Year 2021 tax return.



Of eligible taxpayers who **did not receive advance payments**: **423,000 taxpayers** claimed the Child Tax Credit on their tax return and **received an estimated \$2.3 billion** that **should have been paid** in advance payments, and **135,000 taxpayers** potentially eligible for the Child Tax Credit had not yet filed a tax return.

What TIGTA Recommended

TIGTA made seven recommendations to the IRS including: identifying and reviewing the instances where taxpayers received more or less Child Tax Credit than they were eligible to receive, sending letters to taxpayers with advance Child Tax Credit payments who have yet to file a Tax Year 2021 tax return, and creating a process to recover potentially erroneous advance payments.

The IRS agreed with four of the seven recommendations and partially agreed with another. The IRS did not agree to identify additional taxpayers with excess Child Tax Credits or to develop a process to recover erroneous advance payments on nonfilers. TIGTA continues to believe that taxpayers received excess Child Tax Credit after the IRS implemented a programming change and that processes are needed to recover erroneous advance payments totaling \$1 billion.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

U.S. DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20024

June 14, 2023

MEMORANDUM FOR: COMMISSIONER OF INTERNAL REVENUE

Heather Hill

FROM: Heather M. Hill
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – American Rescue Plan Act: Review of the
Reconciliation of the Child Tax Credit (Audit # 202240712)

This report presents the results of our review to assess processes and procedures to ensure that taxpayers properly reconciled the advance Child Tax Credit payments on their Tax Year 2021 tax return. This review is part of our Fiscal Year 2023 Annual Audit Plan and addresses the major management and performance challenges of *Administering Tax Law Changes* and *Reducing Tax Fraud and Improper Payments*.

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).

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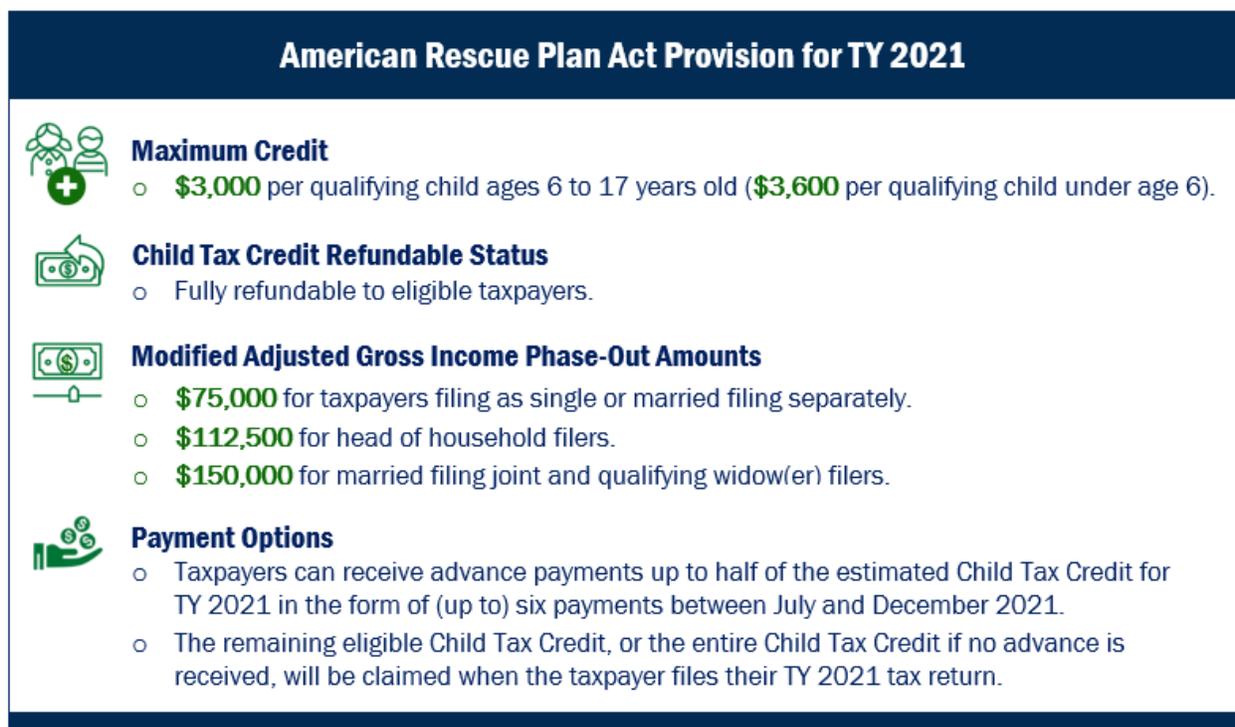
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Background

The American Rescue Plan Act of 2021 (ARPA), enacted on March 11, 2021, increased the amount of the Child Tax Credit from \$2,000 to \$3,000 per child under the age of 18 (\$3,600 for children under the age of 6) for Tax Year (TY)¹ 2021 only and makes the Child Tax Credit fully refundable to eligible taxpayers; thus, eliminating the Additional Child Tax Credit for these taxpayers.² Figure 1 summarizes the changes made to the Child Tax Credit for TY 2021.

Figure 1: Child Tax Credit Changes by the ARPA for TY 2021



Source: Treasury Inspector General for Tax Administration (TIGTA) summary of ARPA legislation.

Advance payment of the Child Tax Credit

To determine eligibility and the amount of these advance payments during Calendar Year 2021, the Internal Revenue Service (IRS) was authorized to use information from:

- Taxpayers' TY 2020 tax returns. However, if the taxpayers had not yet filed a TY 2020 tax return (including instances where the TY 2020 tax return had not yet been processed due to the IRS backlog), the IRS could then use taxpayers' TY 2019 tax return.

¹ See Appendix IV for glossary of terms.

² Pub. L. No. 117-2, 135 Stat. 4 (codified in scattered sections of 7, 12, 15, 19, 20, 26, 29, 42, and 45 U.S.C.).

- The *Non-Filers: Enter Payment Info Here Tool* (also used by taxpayers to receive stimulus payments) or the *Child Tax Credit Non-Filer Sign-up Tool*.³ The *Child Tax Credit Non-Filer Sign-up Tool* allowed taxpayers to file a simplified TY 2020 tax return that contained the information the IRS needed to determine the taxpayer's eligibility and issue the advance payments.

In addition, the ARPA required the IRS to provide taxpayers with the ability to unenroll from receiving advance payments and update information that could modify the amount of advance payments taxpayers were eligible to receive, *e.g.*, taxpayers could update the number of their qualifying children or their marital status. To meet this requirement, the IRS developed an online portal, known as the *Child Tax Credit Update Portal*, and developed non-electronic processes to enable taxpayers to perform many of the same updates that they provided through the *Child Tax Credit Update Portal*.

Reconciliation of the Child Tax Credit on Tax Year 2021 tax returns

The IRS began issuing advance payments of the Child Tax Credit on July 15, 2021, only four months after legislation was enacted, and continued issuing these payments each month through December 2021. As of December 2021, the IRS issued 216.9 million advance payments totaling \$93.5 billion.⁴

In compliance with the ARPA, the IRS provided taxpayers with a written notice of advance payments by January 31, 2022, to assist taxpayers in reconciling advance payments received with the TY 2021 Child Tax Credit allowed. The IRS developed Letter 6419, *2021 Total Advance Child Tax Credit (AdvCTC) Payments*, which includes the total amount of advance payments issued for TY 2021 and the number of qualifying children used to calculate the advance payments.

Taxpayers who received one or more advance Child Tax Credit payments should file Schedule 8812, *Credits for Qualifying Children and Other Dependents*, with their TY 2021 tax return to report advance Child Tax Credit payments received, claim the remaining eligible Child Tax Credit amount, and reconcile the Child Tax Credit allowed with advance payments received. In most instances, this results in the taxpayer receiving the remaining portion of the Child Tax Credit; however, some taxpayers may owe additional tax if they received advance payments for which they were not eligible. These taxpayers will need to report the receipt of their advance payment(s) and potentially repay the amount they were not eligible to receive. Taxpayers who meet the repayment protection conditions summarized in Figure 2 are allowed to keep the excess payments, up to \$2,000 per qualifying child.

³ In Calendar Year 2020, this tool assisted taxpayers who were eligible to receive an economic impact payment but do not have a Federal tax return filing requirement and had not filed a TY 2018 or TY 2019 tax return. In Calendar Year 2021, this tool assisted taxpayers who were eligible to receive advance Child Tax Credit payments but did not have a Federal tax return filing requirement and had not filed a TY 2019 or TY 2020 tax return.

⁴ TIGTA, Report No. 2022-47-070, *American Rescue Plan Act: Accuracy of Advance Child Tax Credit Periodic Payments* (Sept. 2022).

Figure 2: Summary of Conditions for Repayment Protection



Taxpayers meeting the following conditions will not need to repay any excess payment amounts, up to \$2,000 per qualifying child:

- ✓ There was a net decrease in the number of qualifying children between TY 2020 (or TY 2019) and the TY 2021 return,
- ✓ The taxpayer's main home was in the United States for more than half of Calendar Year 2021, and
- ✓ The taxpayer's modified adjusted gross income is less than or equal to \$40,000 (\$50,000 for head of household filers and \$60,000 for married couples filing a joint return or qualifying widow(er)s).⁵

Source: TIGTA summary of ARPA legislation.

As of October 26, 2022, the IRS reported that approximately 1.3 million taxpayers with payments totaling \$1.9 billion were eligible for partial or full repayment protection. If the taxpayer does not qualify for the repayment protection, the repayment amount is reported on the taxpayer's tax return and either reduces the refund amount or increases the balance due.

Prior audit recommended outreach efforts for potentially misrouted advance payments

In our prior review, we reported that taxpayers had their direct deposit information updated by the IRS's Return Integrity and Compliance Services function with information provided by the Bureau of the Fiscal Service between August 23, 2021, and October 5, 2021. These updates were intended to not only reduce the amount of paper checks being issued, but to also ensure that advance payments were timely delivered to taxpayers.⁶ As a result of this process, 1,519 taxpayers had their advance payments direct deposited into an account used for other government payments (*e.g.*, payroll allotment accounts, such as a health savings account).⁷ Many of these taxpayers did not have immediate access to the advance payments and may not have thought to look for payments in these accounts.

As of September 2022, the Bureau of the Fiscal Service mailed 1,357 letters to impacted taxpayers to officially inform them of the potential location of their advance payments. Additionally, the Bureau of the Fiscal Service established a dedicated telephone line for the impacted taxpayers and included the telephone number on the letter sent to the affected taxpayers. The remaining 162 taxpayers had their payments returned to the IRS, and they are eligible to receive the misdirected payment(s) through the filing of their tax return or the issuance of subsequent payments.

⁵ Taxpayers with an income above these amounts but below \$80,000 for single filers, \$100,000 for head of household filers, and \$120,000 for married joint filers will gradually have the exempted amount reduced to \$0 per qualifying child.

⁶ TIGTA, Report No. 2022-47-070, *American Rescue Plan Act: Accuracy of Advance Child Tax Credit Periodic Payments* (Sept. 2022).

⁷ We were originally provided with 1,610 taxpayers, which was reported in TIGTA, Report No. 2022-47-070, *American Rescue Plan Act: Accuracy of Advance Child Tax Credit Periodic Payments* (Sept. 2022); however, the IRS subsequently provided additional information revising the number to 1,519 taxpayers.

Results of Review

Programming Correctly Reconciled the Child Tax Credit During Tax Return Processing; However, Some Taxpayers Received Incorrect Child Tax Credits

The IRS created an automated process to recalculate the Child Tax Credit, including the amount of advance payments posted to a taxpayer's tax account, regardless of the advance amount reported on a taxpayer's tax return. The programming calculates the total Child Tax Credit taxpayers are eligible to receive based upon their tax return information and reduces that amount by any advance payments received. This automated process creates an error code on the taxpayer's tax account, and for most electronically filed tax returns the process systemically corrected the error code. For those tax returns that do not meet the criteria to be systemically resolved, including paper-filed tax returns, the IRS works the error condition through the manual resolution process.

As of October 12, 2022, 39.8 million taxpayers filed tax returns claiming the Child Tax Credit, totaling approximately \$195 billion. Of which, \$83.8 billion in Child Tax Credit was advance payments that went through the recalculation process to ensure the accuracy of the Child Tax Credit amount. Additionally, as of this same time period, our review showed that approximately 4.1 million taxpayers who were issued about \$9 billion in advance payments had not yet filed a tax return, or their tax return had not yet been processed due to the IRS backlog. Finally, our review showed that approximately 1.1 million taxpayers had over \$900 million in advance payments that have been reversed.

During the processing of tax returns with advance payments, the IRS identified 3.8 million tax returns that contained a discrepancy between the IRS calculated Child Tax Credit amount and the amount claimed by the taxpayer that required resolution.

Tax examiner error resulted in taxpayers receiving additional Child Tax Credit

Our analysis of TY 2021 tax returns processed through May 5, 2022, identified 6,833 taxpayers who received potentially \$10.5 million in excess Child Tax Credit. This occurred during the manual resolution process because tax examiners in the Error Resolution function incorrectly resolved error conditions and allowed more Child Tax Credit than the taxpayer was eligible to claim on their tax return. In response to our concerns, IRS management estimated, based on a judgmental sample, that about 95 percent (6,491) of the taxpayers we identified had an error code that was closed in error, and that they will consider them for treatment (*i.e.*, recover the excess Child Tax Credit) based upon resource availability. We continue to believe that the IRS should review and correct all tax returns that we identified.

These errors go undetected because updates made to tax returns through the Error Resolution function do not have systemic controls to verify the corrections made. In December 2020, we reported a similar concern over the lack of verification/validation of entries by tax examiners.⁸ IRS management agreed with our recommendation to add controls to verify fields to prevent

⁸ TIGTA, Report No. 2021-40-008, *Expansion of Self-Correction for Electronic Filers and Other Improvements Could Reduce Taxpayer Burden and Costs Associated With Tax Return Error Resolution* (Dec. 2020).

erroneous credits; however, at that time, programming was subject to availability of information technology resources and other competing priorities. As a result, the corrective action was placed on hold and erroneous credits continued to be issued to taxpayers.

The Commissioner, Wage and Investment Division, should:

Recommendation 1: Review all of the 6,833 taxpayers with excess Child Tax Credit identified during our review and take appropriate actions to ensure that the taxpayers receive the correct amount of the Child Tax Credit.

Management's Response: IRS management agreed with the recommendation and will review the taxpayers identified and take action as appropriate.

Recommendation 2: Identify additional taxpayers after May 5, 2022, who received excess Child Tax Credit as a result of tax examiner error and take appropriate actions to ensure that these taxpayers receive the correct amount of the Child Tax Credit.

Management's Response: IRS management disagreed with this recommendation due to programming being corrected on March 7, 2022.

Office of Audit Comment: We continue to believe that an assessment of taxpayers receiving the Child Tax Credit after May 5, 2022, is needed as these errors continued to occur after the IRS implemented the programming change. For example, 906 of the 6,833 taxpayers we identified relative to Recommendation 1 were filed after the IRS implemented the programming change and the taxpayers received excess Child Tax Credit.

Taxpayers did not always receive all of their eligible Child Tax Credit

Our analysis of TY 2021 tax returns processed through May 5, 2022, identified 105 taxpayers who potentially did not receive all of their eligible Child Tax Credit (*i.e.*, they received less). These taxpayers should have received an estimated \$139,000 in additional Child Tax Credit.

On October 12, 2022, the IRS informed us of a programming error that occurred during the IRS's Controlled Launch for the 2022 Filing Season. In these instances, the IRS captured the incorrect number of qualifying children and selected the tax returns for Error Resolution. During the error correction process, the taxpayers received less Child Tax Credit than they were eligible to receive. The IRS plans to consider these cases for treatment (*i.e.*, ensure the appropriate amount of Child Tax Credit is given) subject to resource availability. However, we believe that the IRS should ensure that all 105 tax accounts are corrected to ensure that these individuals receive all their eligible Child Tax Credit.

The Commissioner, Wage and Investment Division, should:

Recommendation 3: Review the 105 taxpayers who potentially did not receive all of their eligible Child Tax Credit identified during our review and take appropriate actions to ensure that they receive the correct amount of the Child Tax Credit.

Management's Response: IRS management agreed with the recommendation and will review the taxpayers identified and take action as appropriate.

Recommendation 4: Evaluate the priority of programming to ensure that processes and procedures are developed to identify and correct tax examiner entries input during the error correction process that exceed statutory limits, including a process to systemically reprocess corrected returns through Error Resolution programming before being released for processing.

Management's Response: IRS management partially agreed with this recommendation and implemented programming for electronically filed tax returns at the beginning of the 2023 Filing Season to negate erroneous employee entries as the tax returns are processed systemically.

Office of Audit Comment: While we agree with the actions taken by the IRS to reduce erroneous employee entries, this does not address tax returns that are not subject to this programming (*e.g.*, certain error conditions on electronically filed tax returns and paper-filed tax returns). As a result, erroneous entries by tax examiners on the paper-filed tax returns and electronically filed tax returns not processed through the implemented programming will continue to occur.

Implementation of a new process to reconcile undelivered advance payments

Our analysis determined that the IRS sent the majority of the 57.1 million Letters 6419 to the correct taxpayers and for the correct amount of advance Child Tax Credit payments issued to the taxpayers.⁹ However, we identified differences involving the reversals of advance payments (*i.e.*, undelivered checks) that were not reflected on Letter 6419. These differences occurred due to the timing of the IRS's cutoff date to send the letters and the posting of the reversal to the taxpayer's tax account. To address this issue, the IRS used the amount of advance payments recorded on taxpayers' tax accounts at the time the IRS processed taxpayers' tax returns rather than the amount on Letter 6419.

Recommendation 5 (E-Mail Alert): On February 17, 2022, we notified IRS management of our concerns with undeliverable payments that post after the processing of the tax return. In these instances, the IRS processed the tax return as if the payment was received by the taxpayer. As a result, the taxpayer would receive less Child Tax Credit than they are eligible to receive. We recommended that the IRS develop a process to identify undeliverable payments after processing of the TY 2021 tax return.

Management's Response to E-Mail Alert: The IRS implemented a programming change effective March 3, 2022, to identify undeliverable advance payments that occurred after the tax return processed.

As of October 12, 2022, we identified 7,877 taxpayers with reversals of advance payments totaling \$5.4 million that were addressed by the programming change. As a result, the IRS was able to identify these taxpayers and work to reissue the reversed advance payment(s) due to the taxpayer.

⁹ TIGTA, Report No. 2022-47-070, *American Rescue Plan Act: Accuracy of Advance Child Tax Credit Periodic Payments* (Sept. 2022).

Some Potentially Erroneous Advance Payments Were Recovered Through the Reconciliation Process

Our prior review determined that, between July and November 2021, the IRS erroneously sent 3.3 million payments to 1.5 million taxpayers who were not eligible to receive an advance payment. These payments totaled nearly \$1.1 billion and included instances in which dependents did not meet the age requirements, were deceased, or were claimed on another tax return. Our analysis was based on information from TY 2020 or, when necessary, TY 2019 tax returns; the same approach the IRS used to make the advance payments.¹⁰

We conducted additional analysis of the 1.5 million taxpayers and found that as of October 12, 2022, 845,000 taxpayers with advance payments totaling \$1 billion had not filed a TY 2021 tax return. Further analysis of the remaining 618,000 taxpayers showed that they had filed a TY 2021 tax return, including 242,000 taxpayers (39 percent) who received \$119.4 million in erroneous advance payments during Calendar Year 2021.¹¹ Our analysis showed that of the 618,000 taxpayers:

- 376,000 taxpayers received the correct amount of Child Tax Credit and \$543 million in advance payments based upon the information provided on the TY 2021 tax return.
- 173,000 taxpayers were not eligible for some or all of the advance payments but qualified for repayment protection totaling \$97.8 million.
- 69,000 taxpayers were not eligible for some or all of the advance payments and did not qualify for repayment protection. These taxpayers were required to repay the excess advance payments totaling \$21.6 million.

The IRS stated that there is no compliance strategy to identify potentially erroneous advance payments as the filing of the tax return would reconcile any discrepancies. Management further stated that taxpayers who do not have a filing requirement are not required to file a tax return even if they received advance payments. The reconciliation process only affects taxpayers who file a tax return and does not address potentially erroneous claims on the 845,000 taxpayers with advance payments who have yet to file a tax return. For these taxpayers, the IRS does not know if the taxpayers would claim qualifying children for the Child Tax Credit or have to repay the potentially erroneous advance payments. To assist taxpayers who have yet to file a tax return, the IRS kept the Free File program available through the IRS's webpage at www.irs.gov until November 17, 2022, to encourage taxpayers to file their tax return to claim the remaining Child Tax Credit. Additionally, the IRS provided taxpayers an additional week to electronically file their tax returns and kept electronic filing open through November 26, 2022.

Some taxpayers did not receive notice of their potential eligibility for the Child Tax Credit

In October 2022, the Department of the Treasury, with assistance from the IRS, identified more than 9 million individuals who appear to qualify for the Child Tax Credit, Recovery Rebate Credit, or Earned Income Tax Credit. The Department of the Treasury identified dependents who were not claimed on a TY 2021 tax return and worked with the IRS to send letters to the taxpayers

¹⁰ TIGTA, Report No. 2022-47-070, *American Rescue Plan Act: Accuracy of Advance Child Tax Credit Periodic Payments* (Sept. 2022).

¹¹ The number of taxpayers does not total to 1.5 million due to rounding.

responsible for the unclaimed dependent rather than, for example, taxpayers who had received advance payments that have not yet filed. The letter, issued in English and Spanish, informs the taxpayer that they may be eligible to claim credits and a refund by filing their TY 2021 tax return. Our analysis determined that only 1.1 million of the 4.1 million taxpayers with advance payments who have not filed a tax return were issued a letter. As a result, there are some taxpayers who may be unaware of the need to file their tax return to claim their remaining eligible Child Tax Credit.

The Commissioner, Wage and Investment Division, should:

Recommendation 6: Identify taxpayers with advance payments who have yet to file a TY 2021 tax return and send a reminder notice, similar to the Department of the Treasury, using the advance payments as part of the criteria.

Management's Response: IRS management agreed with the recommendation and will identify and notify taxpayers who have yet to file a tax return, reminding them to file their TY 2021 tax return to claim any remaining credit to which they may be entitled.

Recommendation 7: Work with the Commissioner, Small Business/Self-Employed Division, to create a process to recover potentially erroneous advance payments from taxpayers who have not filed a TY 2021 tax return.

Management's Response: IRS management disagreed with the recommendation. The IRS indicated that by using current criteria for nonfiler case identification and Automated Substitute for Return processes, some erroneous advance payments will be recovered. However, these processes do not have the ability to identify and recover potential erroneous payments by selecting specific credits.

Office of Audit Comment: We agree that the current processes may identify a portion of the taxpayers who have yet to file a tax return; however, other alternatives should be considered for the recovery of the \$1 billion in erroneous advance payments. With continued discussions by Congress on expanding the advance Child Tax Credit, such a process will be needed as part of any efforts to reintroduce advance Child Tax Credit payments.

Eligible taxpayers who were not sent advance payments received the Child Tax Credit during tax return processing

Our prior audit of advance Child Tax Credit payments also identified 4.1 million taxpayers who were eligible to receive almost \$3.7 billion in advance payments, but the IRS failed to send the taxpayers one or more monthly payments between July and November 2021. To resolve some of the missed payments, the IRS issued 1.3 million recovery payments to impacted taxpayers totaling more than \$503.7 million in

Our prior audit of advance Child Tax Credit payments identified 4.1 million taxpayers who were eligible to receive an advance payment but the IRS failed to send the taxpayer one or more monthly payments between July and November 2021.



Further analysis of the 4.1 million taxpayers identified over 606,000 taxpayers who were potentially eligible for advance payments but did not receive any such payments during Calendar Year 2021.

August 2021. The IRS also sent 633,000 recovery payments to affected taxpayers totaling about \$224.1 million in September 2021.¹²

During this review, we conducted additional analysis of the 4.1 million taxpayers and identified 606,000 taxpayers who did not receive any advance payments or recovery payments for TY 2021. Specifically, as of October 12, 2022, we identified:

- 423,000 taxpayers claimed the Child Tax Credit when they filed their tax return confirming that they should have received an estimated \$2.3 billion in advance payments.
- 48,000 taxpayers who filed a tax return but did not claim the Child Tax Credit. In most cases, the taxpayers were no longer eligible to claim the Child Tax Credit as the taxpayer did not report any qualifying children on their TY 2021 tax return. As an example, this can occur when separated/divorced taxpayers alternate claiming a qualifying child based on their custody agreement.
- 135,000 taxpayers did not file a tax return. As stated previously, the IRS encourages taxpayers to file their TY 2021 tax return to receive the remaining Child Tax Credit, if any.

¹² We did not report on recovery payments for October, November, and December 2021.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to assess processes and procedures to ensure that taxpayers properly reconciled the advance Child Tax Credit payments on their TY 2021 tax return. To accomplish our objective, we:

- Assessed the processing of tax returns with the Child Tax Credit to ensure that the IRS properly calculated the Child Tax Credit and appropriately applied the repayment protection rules, when applicable.
- Assessed the IRS's processes and procedures to address taxpayer accounts with advance Child Tax Credit payment reversals after the issuance of the Letter 6419 and ensured that the IRS provided the taxpayer with their eligible Child Tax Credit.
- Evaluated the steps taken by the IRS to identify and assist taxpayers where the Return Integrity and Compliance Services function updated their direct deposit account used to receive advance payments without the taxpayer's knowledge.
- Reviewed the criteria used to issue 9 million letters to families who were potentially eligible and did not claim stimulus payments, Earned Income Tax Credit, Child Tax Credit, and other benefits.
- Assessed the Error Resolution Codes to ensure that the error codes associated with the Child Tax Credit worked as intended and to ensure that tax examiners worked the error code to ensure accurate claims for the Child Tax Credit.

Performance of This Review

This review was performed with information obtained from the Wage and Investment Division and Return Integrity and Compliance Services function located in Atlanta, Georgia, and the Submission Processing function located in Covington, Kentucky, during the period February 2022 through February 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 M. Tengesdal, Acting Assistant Inspector General for Audit (Returns Processing and Account Services); Darryl J. Roth, Director; Jonathan W. Lloyd, Audit Manager; Kenneth L. Carlson, Senior Auditor; Aranxa J. Delgado, Auditor; Sandy Ramos, Auditor.

Validity and Reliability of Data From Computer-Based Systems

During this review, we obtained taxpayer account information from the IRS's Individual Master File, TY 2021 tax return information from the Individual Returns Transaction File, information about taxpayers from the National Account Profile table, and payment data from the IRS's

Refund File for Processing Years 2021 and 2022 that were available on TIGTA's Data Center Warehouse. We ensured that each file contained the specific data elements relevant to our review. We selected judgmental samples from each extract and verified that the data in the extracts were the same as the data captured in the Integrated Data Retrieval System. We determined that the data were sufficiently reliable for purposes of this report.

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: processes and procedures found in the Internal Revenue Manual and programming guides to ensure that taxpayers are properly reconciling the advance Child Tax Credit payments reported on their TY 2021 tax return. We tested these controls by reviewing and analyzing relevant documents and data and holding discussions with IRS management.

Appendix II

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:

- Cost Savings (Funds Put to Better Use) – Potential; \$9,957,194 in excess Child Tax Credit for 6,491 taxpayers due to incorrect resolution of the error condition (see Recommendation 1).

Methodology Used to Measure the Reported Benefit:

We identified 6,833 taxpayers who potentially received \$10.5 million in excess Child Tax Credit. This occurred during the manual resolution process because tax examiners in the Error Resolution function incorrectly resolved the error condition and allowed more Child Tax Credit than the taxpayer claimed on their tax return. These taxpayers for which the tax return was identified by an Error Resolution Code as of May 5, 2022, had a different number of qualifying children reported on the electronically filed tax returns when compared to the number allowed by tax examiners. These taxpayers reported more qualifying children than they were eligible to claim. When the tax examiner resolved the error condition, they allowed the incorrect number of qualifying children, resulting in excess Child Tax Credit claimed.

We shared our results with IRS management, and they stated that they reviewed a judgmental sample to determine that 95 percent were closed in error. Therefore, we multiplied 6,833 taxpayers by 95 percent to get an estimated 6,491 taxpayers with excess Child Tax Credit. We multiplied these taxpayers by the average amount of excess Child Tax Credit of \$1,534 ($\$10,482,866 / 6,833$), resulting in \$9,957,194 ($6,491 * \$1,534$) in excess Child Tax Credit due to tax examiners incorrectly working the error condition.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; \$130,046 for 98 taxpayers who received less Child Tax Credit than they were eligible to receive due to incorrect resolution of the error condition (see Recommendation 3).

Methodology Used to Measure the Reported Benefit:

We identified 105 taxpayers who potentially did not receive all of their eligible Child Tax Credit. Taxpayers received \$139,347 less in Child Tax Credit as a result of tax examiners incorrectly working error conditions. These taxpayers for which the tax return was identified by an Error Resolution Code as of May 5, 2022, had a different number of qualifying children allowed by tax examiners compared to the number of qualifying children on the electronically filed tax return. These taxpayers for which tax examiners did not correctly calculate the amount of Child Tax Credit, received less Child Tax Credit than what should have been allowed.

We shared our results with IRS management and they stated that they reviewed a judgmental sample of 15 taxpayers to determine that 14 taxpayers (93 percent) we identified had their error code closed in error. Therefore, we multiplied 105 taxpayers by 93 percent to get an estimated 98 taxpayers who did not receive all of their eligible Child Tax Credit. We multiplied these taxpayers by the average amount of Child Tax Credit they potentially did not receive of \$1,327 ($\$139,347 / 105$), resulting in an estimated \$130,046 ($98 * \$1,327$) in Child Tax Credit that is due to the taxpayers because of tax examiners incorrectly working the error conditions.

Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Actual; 7,877 taxpayers with \$5.4 million in undeliverable advance Child Tax Credit payments that posted to their accounts after the filing of their TY 2021 tax returns (see Recommendation 5).

Methodology Used to Measure the Reported Benefit:

We determined Letter 6419 did not always reflect the correct amount of advance Child Tax Credit the taxpayer received. These differences occurred due to the timing of the IRS's cutoff date to send the letters and the posting of reversals (*i.e.*, undeliverable payments) to the taxpayer's tax account. To address this issue, the IRS used the amount of advance payments recorded on taxpayer's tax accounts at the time the IRS processed taxpayers' tax returns rather than the amount on Letter 6419.

We notified IRS management about our concerns and that it would sometimes cause taxpayers to receive less Child Tax Credit than they were eligible to receive. To address our concerns, the IRS implemented a programming change effective March 3, 2022, to identify undeliverable advance payments that occurred after the tax return processed. As of October 12, 2022, we identified 7,877 taxpayers with reversals of advance payments totaling \$5,365,783. The IRS worked to reissue the reversed advance Child Tax Credit payments to these taxpayers.

Appendix III

Management's Response to the Draft Report



COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

May 4, 2023

MEMORANDUM FOR HEATHER M. HILL
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

Kenneth C. Corbin 
Commissioner, Wage and Investment Division

Digitally signed by Kenneth C.
Corbin
Date: 2023.05.05 12:14:45 -04'00'

SUBJECT:

Draft Audit Report – American Rescue Plan Act: Review of the
Reconciliation of the Child Tax Credit (Audit #202240712)

Thank you for the opportunity to review and provide comments on the subject draft report. The American Rescue Plan Act of 2021 was enacted on March 11, 2021, and it significantly changed the Child Tax Credit (CTC) for tax year 2021. Notably, the changes increased the complexity of the credit, increasing the amount of the credit from \$2,000 to \$3,000 or \$3,600 per qualifying child, and modified and added conditions of eligibility. The credit was made fully refundable for some taxpayers, and up to one-half of the estimated CTC allowable for the year could be paid out in installments. For the benefit of families who don't usually file a tax return, the IRS developed the Non-Filer Sign-up tool so eligible families might register for the installment payments. In addition, the IRS developed a CTC Portal, providing taxpayers a means to update the number of their qualifying children, marital status, and other conditions relevant to the credit. We began issuing advance payments on July 15, 2021 and continued with monthly payments through December 15, 2021.

The IRS also issued Letter 6419, *Reconciliation Statement*, which reported to taxpayers the amount of advance CTC paid in 2021 and the number of qualifying children for which payments were made. This letter provided taxpayers the information needed for filing a tax year 2021 return and reconciling the CTC. We issued additional outreach letters: Letter 6416, *Advance Child Tax Credit Outreach*, informed individuals of potential eligibility for the advance payments, and Letter 6417, *Advance Child Tax Credit Payment*, provided notification of the advance payments as they were issued.

The implementation of the provisions for the CTC summoned change, adaptability, and innovation to the forefront. The IRS revised Schedule 8812, *Credits for Qualifying Children and Other Dependents*, converting it from a one-page schedule for tax year

2020 to a three-page schedule for tax year 2021. Addressing extensive changes in the schedule, the IRS created 20 new business rules and one new error code to accurately process returns with this credit. We also created and put in service an automated processing tool that, by eliminating the manual processing of the credit, processed returns with greater speed and accuracy than manual processing could have achieved. The tool directed 13.5 million returns to automated processing and away from manual processing. Programming changes were implemented on March 3, 2022, to generate transcripts when the advance payments are returned after returns have been processed. This change will address all accounts generating a transcript and the reconciliation will occur as the transcripts are processed.

The IRS considers taxpayer service its top priority. We understand TIGTA's concern about taxpayers who received advance payments yet didn't file a tax return for reconciliation of the payments. However, taxpayers who received an advanced payment but did not meet the minimum filing requirement were not required to file a 2021 tax return. Requesting a return from them would not be good customer service.

We assisted the Department of Treasury in the identification of and issuance of Letters 6550, *End of Season Outreach (English & Spanish)* to nine million individuals who may qualify for tax benefits such as the CTC, Earned Income Tax Credit, or Recovery Rebate Credit, but did not claim them on a tax year 2021 return. The IRS kept FreeFile open for an additional month, until November 17, 2022, for eligible taxpayers to file a tax return electronically.

Our responses to your specific recommendations are enclosed. If you have any questions, please contact me, or a member of your staff may contact Dietra D. Grant, Director, Customer Account Services, at 470-639-3504.

Attachment

Attachment

Recommendations

The Commissioner, Wage and Investment Division, should:

RECOMMENDATION 1

Review all of the 6,833 taxpayers with excess Child Tax Credit identified during our review and take appropriate actions to ensure that the taxpayers receive the correct amount of the Child Tax Credit.

CORRECTIVE ACTION

The IRS will review the 6,833 taxpayers and take action as appropriate.

IMPLEMENTATION DATE

March 15, 2024

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 2

Identify additional taxpayers after May 5, 2022, who received excess Child Tax Credit as a result of tax examiner error and take appropriate actions to ensure that these taxpayers receive the correct amount of the Child Tax Credit.

CORRECTIVE ACTION

Early in the 2022 filing season, the IRS discovered a programming error in the computation of the count of children eligible for the Child Tax Credit (CTC) and Other Dependent Credit (ODC). The error caused returns to fall out for review by tax examiners in the Error Resolution function. Procedures for this condition were developed and issued for use by the tax examiners until the programming was revised. The programming was corrected but returns continued to fall out for review. Upon further investigation, we identified a need for a second programming correction that went into production on March 7, 2022, avoiding a need for manual review by tax examiners. Errors in returns with the CTC received after the programming fixes were correctly evaluated and sent to the automated processing tool for resolution. There are erroneous refund procedures in place after original processing is completed when criteria are met. There is not a need for additional review of returns received after May 5, 2022.

2

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 3

Review the 105 taxpayers who potentially did not receive all of their eligible Child Tax Credit identified during our review and take appropriate actions to ensure that they receive the correct amount of the Child Tax Credit.

CORRECTIVE ACTION

We will review the 105 taxpayers and take action as appropriate.

IMPLEMENTATION DATE

March 15, 2024

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

Evaluate the priority of programming to ensure that processes and procedures are developed to identify and correct tax examiner entries input during the error correction process that exceed statutory limits, including a process to systemically reprocess corrected returns through Error Resolution programming before being released for processing.

CORRECTIVE ACTION

At the beginning of the 2023 filing season, programming was implemented for the Child Tax and Other Dependent Credit, and Additional Child Tax Credit. The IRS enhanced the automated processing tool for resolution of taxpayer returns which fall-out to the Error Resolution System. This automation process negates erroneous employee entries as the tax returns are processed systemically through the tool.

IMPLEMENTATION DATE

Implemented

3

RESPONSIBLE OFFICIAL

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

CORRECTIVE ACTION MONITORING PLAN

N/A.

RECOMMENDATION 5 (E-Mail Alert):

On February 17, 2022, we notified IRS management of our concerns with undeliverable payments that post after the processing of the tax return. In these instances, the IRS processed the tax return as if the payment was received by the taxpayer. As a result, the taxpayer would receive less Child Tax Credit than they are eligible to receive. We recommended that the IRS develop a process to identify undeliverable payments after processing of the TY 2021 tax return.

CORRECTIVE ACTION

We previously implemented the necessary programming to identify any undeliverable advance payments that occurred after the tax return was processed. The programming generates internal transcripts which allow for the reissuance of the reversed advance payment as the transcripts are processed.

IMPLEMENTATION DATE

Implemented

RESPONSIBLE OFFICIAL

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

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 6

Identify taxpayers with advance payments who have yet to file a TY 2021 tax return and send a reminder notice, similar to the Department of the Treasury, using the advance payments as part of the criteria.

CORRECTIVE ACTION

The IRS will identify taxpayers for whom our records indicate Advance Child Tax Credit payments were issued but have not yet filed a tax year (TY) 2021 return. We will send the identified taxpayers a letter reminding them to file their TY 2021 return to claim any remaining credit to which they may be entitled.

IMPLEMENTATION DATE

December 15, 2023

RESPONSIBLE OFFICIAL

Director, Refundable Credit Program Management, Return Integrity and Compliance Services, Wage and Investment Division

CORRECTIVE ACTION MONITORING PLAN

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

RECOMMENDATION 7

Work with the Commissioner, Small Business/Self-Employed Division to create a process to recover potentially erroneous advance payments from taxpayers who have not filed a TY 2021 tax return.

CORRECTIVE ACTION

Using the current criteria in the Individual Master File (IMF) Case Creation Non-filer Identification Process (CCNIP) and Automated Substitute for Return (ASFR) process, some erroneous advance payments will be recovered. The CCNIP does not have the ability to identify and recover potential erroneous advance payments from taxpayers by selecting specific credits. However, some non-filers who obtained erroneous payments may receive notification of requirements to file a tax year 2021 tax return as part of the current IMF CCNIP selection process. If a tax return is not filed in response, the tax module may potentially be selected for the ASFR process and notices will be issued informing the taxpayer of their requirement to file. If the taxpayer does not respond, a return will be filed on behalf of the taxpayer through the ASFR process. The ASFR process does not allow dependents unless the taxpayer files a tax return; as a result, the erroneously claimed credit will be eliminated from the return.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

Appendix IV

Glossary of Terms

Term	Definition
Data Center Warehouse	A collection of IRS databases containing various types of taxpayer accounts and IRS and TIGTA employee information that is maintained by TIGTA for purposes of analyzing data for ongoing audits.
Filing Season	The period from January 1 through mid-April when most individual income tax returns are filed.
Individual Master File	The IRS database that maintains transactions or records of individual tax accounts.
Individual Return Transaction File	A database maintained by the IRS that contains information on the individual tax returns it receives.
Integrated Data Retrieval System	IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.
Internal Revenue Manual	Primary source of instructions to employees relating to the administration and operation of the IRS. The Manual contains the directions employees need to carry out their operational responsibilities.
Judgmental sample	A judgmental sample is a nonprobability sample, the results of which cannot be used to project to the population.
Modified adjusted gross income	Modified adjusted gross income is adjusted gross income, plus any foreign earned income excluded from gross income, and any amount excluded from gross income because it was received from sources in Puerto Rico or American Samoa. For most individuals, modified adjusted gross income is the same as adjusted gross income.
National Account Profile	A compilation of selected entity data from various IRS Master Files and the Social Security Administration.
Recovery payment	A recovery payment is issued by the IRS to provide advance Child Tax Credit payment to taxpayers who were eligible, but did not receive, an advance payment in a prior month.

Refund File	This file captures all refunds that are sent by the IRS to the Bureau of the Fiscal Service for processing. The Bureau of the Fiscal Service is responsible for generating the actual refunds based upon the information provided by the IRS. The refunds are sent by the Bureau of the Fiscal Service to the taxpayers in the form of bank account direct deposits or mailed paper checks. The file captures the name, address, and account information for the individuals receiving the refunds and are useful for identifying tax refund fraud.
Tax Year	A 12-month accounting period for keeping records on income and expenses used as the basis for calculating the annual taxes due. For most individual taxpayers, the tax year is synonymous with the calendar year.

Appendix V

Abbreviations

ARPA	American Rescue Plan Act of 2021
IRS	Internal Revenue Service
TIGTA	Treasury Inspector General for Tax Administration
TY	Tax Year



**To report fraud, waste, or abuse,
contact our hotline on the web at www.tigta.gov or via e-mail at
oi.govreports@tigta.treas.gov.**

**To make suggestions to improve IRS policies, processes, or systems
affecting taxpayers, contact us at www.tigta.gov/form/suggestions.**

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