

**HEARING BEFORE THE
COMMITTEE ON HOMELAND SECURITY AND
GOVERNMENTAL AFFAIRS
UNITED STATE SENATE**

**“DUPLICATION, WASTE, AND FRAUD IN FEDERAL
PROGRAMS”**



**Testimony of
The Honorable J. Russell George
Treasury Inspector General for Tax Administration**

April 26, 2017

Washington, D.C.

TESTIMONY
OF
THE HONORABLE J. RUSSELL GEORGE
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION
before the
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

“Duplication, Waste, and Fraud in Federal Programs”
April 26, 2017

Chairman Johnson, Ranking Member McCaskill, and Members of the Committee, thank you for the opportunity to testify on refundable tax credit improper payments and their adverse effect on tax administration.

The Treasury Inspector General for Tax Administration (TIGTA) was created by Congress in 1998 and is mandated to promote integrity in America’s tax system. It provides independent audit and investigative services to improve the economy, efficiency, and effectiveness of Internal Revenue Service (IRS) operations. TIGTA’s oversight activities are designed to identify high-risk systemic inefficiencies in IRS operations and to investigate exploited weaknesses in tax administration. TIGTA plays the key role of ensuring that the approximately 83,000 IRS employees¹ who collected more than \$3.3 trillion in tax revenue, processed more than 244 million tax returns, and issued more than \$400 billion in tax refunds during Fiscal Year (FY) 2016,² have done so in an effective and efficient manner while minimizing the risks of waste, fraud, and abuse.

TIGTA’s Office of Audit reviews all aspects of the Federal tax administration system and provides recommendations to: improve IRS systems and operations; ensure the fair and equitable treatment of taxpayers; and detect and prevent waste, fraud, and abuse in tax administration. The Office of Audit places an emphasis on statutory coverage required by the IRS Restructuring and Reform Act of 1998 (RRA 98)³ and other laws, as well as on areas of concern raised by Congress, the Secretary of the Treasury, the Commissioner of Internal Revenue, and other key

¹ Total IRS staffing as of January 7, 2017. Included in the total are approximately 16,200 seasonal and part-time employees.

² IRS, *Management’s Discussion & Analysis, Fiscal Year 2016*.

³ Pub. L. No. 105-206, 112 Stat. 685 (1998) (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

stakeholders. The Office of Audit has examined specific high-risk issues such as identity theft, refund fraud, improper payments, information technology, security vulnerabilities, complex modernized computer systems, tax collections and revenue, and waste and abuse in IRS operations.

TIGTA's Office of Investigations protects the integrity of the IRS by investigating allegations of IRS employee misconduct, external threats to IRS employees and facilities, and other attempts to impede or otherwise interfere with the IRS's ability to collect taxes. The Office of Investigations also investigates misconduct by IRS employees which manifests itself in many ways, including extortion, theft, taxpayer abuses, false statements, financial fraud, and identity theft. The Office of Investigations places a high priority on its statutory responsibility to protect all IRS employees located in over 670 facilities nationwide. In the last several years, threats directed at the IRS have remained the second largest component of the Office of Investigation's work. Physical violence, harassment, and intimidation of IRS employees continue to pose challenges to the implementation of a fair and effective system of tax administration. The Office of Investigations is committed to ensuring the safety of IRS employees and the taxpayers who conduct business in IRS facilities.

TIGTA's Office of Inspections and Evaluations provides responsive, timely, and cost-effective inspections and evaluations of challenging areas within the IRS, providing TIGTA with additional flexibility and capability to produce value-added products and services to improve tax administration. The Inspection and Evaluation's work is not a substitute for audits and investigations. In fact, its findings may result in subsequent audits and/or investigations. Inspections are intended to monitor compliance with applicable law, regulation, and/or policy; assess the effectiveness and efficiency of programs and operations; and inquire into allegations of waste, fraud, abuse, and mismanagement. Evaluations, on the other hand, are intended to provide in-depth reviews of specific management issues, policies, or programs.

TIGTA has conducted a number of reviews that evaluate the IRS's efforts to reduce erroneous and improper refundable credit payments. My comments today will highlight our prior and ongoing work.

REFUNDABLE TAX CREDITS

The IRS administers numerous refundable tax credits. The number of these credits has varied over time because some credits are available for a limited period that is set by law. Refundable credits are designed to help low-income individuals reduce

their tax burden. For example, the Earned Income Tax Credit (EITC), created in 1975,⁴ is used to offset the impact of Social Security taxes on low-income families and to encourage them to seek employment. Congress later created the Child Tax Credit (CTC) and the Additional Child Tax Credit (ACTC)⁵ to reflect a family's reduced ability to pay taxes as family size increases.

Other refundable credits provide incentives for specific activities, such as obtaining a college education or purchasing health insurance. For example, the American Opportunity Tax Credit (AOTC) allows individuals to receive a credit for higher education expenses up to \$2,500 per student per year, with up to \$1,000 being refundable.⁶ More recently, the Patient Protection and Affordable Care Act⁷ and the Health Care and Education Reconciliation Act of 2010⁸ (collectively referred to as the Affordable Care Act or ACA), includes the Premium Tax Credit (PTC). The PTC is a refundable tax credit to assist individuals and families in purchasing health insurance coverage through an Affordable Insurance Exchange.⁹

Although refundable credits provide benefits to individuals, the unintended consequence of these credits is that they can result in the issuance of improper payments and can be the targets of unscrupulous individuals who file erroneous claims. Refundable credits can result in tax refunds even if no income tax is withheld or paid; that is, the credits can exceed an individual's tax liability. Consequently, they pose a significant risk as an avenue for those seeking to defraud the Government. Whereas, nonrefundable tax credits are limited to the amount of an individual's income tax liability. Refundable credits do not have such a limitation.

⁴ Tax Reduction Act of 1975 § 204, 26 U.S.C § 32.

⁵ The ACTC is the refundable portion of the Child Tax Credit. This credit phases out for taxpayers depending upon their income level. Taxpayers with earned income of less than \$3,000 may be eligible for a refundable credit if they have three or more qualifying children and have paid Social Security taxes that exceed their EITC.

⁶ IRS Publication 970, *IRS Tax Benefits for Education*.

⁷ Pub. L. No. 111-148, 124 Stat. 119 (2010) (codified as amended in scattered sections of U.S. Code), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029.

⁸ *Id.*

⁹ The Exchange – also known as the Health Insurance Marketplace – is the place for people without health insurance to find information about health insurance options and to purchase health insurance.

PROCESS TO ASSESS THE RISK OF REFUNDABLE CREDIT IMPROPER PAYMENTS

The Office of Management and Budget defines an improper payment as any payment that should not have been made, was made in an incorrect amount, or was made to an ineligible recipient.¹⁰ The Improper Payments Information Act (IPIA) of 2002¹¹ requires Federal agencies, including the IRS, to estimate the amount of improper payments and report to Congress annually on the causes of, and the steps taken to reduce improper payments. The IPIA also requires agencies to address whether they have the information systems and other infrastructure needed to reduce improper payments. Subsequent amendments to the IPIA of 2002¹² revised the definition of improper payments and strengthened agency reporting requirements. In addition, the Office of Management and Budget issued supplemental improper payment guidance to the Department of the Treasury clarifying that all refundable tax credits are subject to the improper payment requirements. TIGTA is required to review on an annual basis the IRS's compliance with these requirements.

The IRS assesses the risk of refundable credit improper payments by conducting an improper payment risk assessment for each refundable credit. In March 2017, we issued our draft report detailing the result of our assessment¹³ of whether the IRS complied with the annual reporting requirements for FY 2016. We found that the IRS provided all required improper payment information to Department of the Treasury for inclusion in the *Department of the Treasury Agency Financial Report Fiscal Year 2016*.

As an alternative to reporting an overall EITC improper payment rate of less than 10 percent, the Department of the Treasury and the Office of Management and Budget collaborated on the development of a series of EITC supplemental measures. These include the percentage of EITC payments that were improper, the amount of revenue prevented or recovered through compliance activities, as well as the amount of revenue protected from Paid Tax Return Preparer treatments and the number of Due Diligence Penalties Proposed. The IRS complied with the reporting on these supplemental measures.

¹⁰ OMB, Circular A-123 Appendix C, *Requirements for Effective Estimation and Remediation of Improper Payments*, revised Oct. 2014.

¹¹ Pub. L. No. 107-300, 116 Stat. 2350.

¹² *Improper Payments Elimination and Recovery Act of 2010*, Pub. L. No. 111-204, 124 Stat. 2224; and *Improper Payments Elimination and Recovery Improvement Act of 2012*, Pub. L. No. 112-248, 126 Stat. 2390.

¹³ TIGTA, Audit No. 201740001, *Compliance with Improper Payment Reporting Compliance in Fiscal Year 2016*, report planned for April 2017.

The Office of Management and Budget has declared the EITC a high-risk program that is subject to reporting in the Treasury Agency Financial Report. To date, the EITC remains the only refundable credit designated as high risk for improper payments. This is despite TIGTA's continued reporting that the refundable credit risk assessments for the ACTC and AOTC substantially understate the risk of improper payments for these credits. It should be noted that in response to prior TIGTA recommendations, the IRS revised its annual risk assessment process for the ACTC and AOTC credits. Using the revised assessment, the IRS concluded that the ACTC and AOTC presented a medium risk of improper payments for FY 2016. However, the medium risk continues to be contrary to the IRS's own compliance data, which shows that both the ACTC and AOTC programs present a high risk of improper payments. (Details on the estimated dollars in improper payments are provided later in my testimony.)

Our review of these revised assessments found that they still do not include the use of available National Research Program (NRP)¹⁴ and IRS compliance data to quantify erroneous payments. Because the IRS does not rate these programs as high risk, it is not required to establish a corrective action plan to reduce the improper payments. It should be noted that the IRS is not required to perform a risk assessment of the EITC because the EITC is designated as a high-risk program by the Office of Management and Budget. For FY 2016, the IRS estimates EITC payments totaling \$16.8 billion were issued improperly.

To further demonstrate that the revised ACTC and AOTC risk assessments do not provide an accurate measure of improper payments, we used the IRS's methodology for these risk assessments to evaluate the EITC improper payment risk. Using the IRS's revised approach, the risk rating of EITC improper payments would be a medium, when clearly the risk is high and is designated as such by the Office of Management and Budget. In addition, for FY 2016 using the same methodology the IRS uses to estimate the amount of EITC improper payments we estimate \$7.2 billion in ACTC payments and \$1.1 billion in estimated AOTC payments were issued improperly. The dollar amounts of the estimated improper payments alone for these two credits meet the Office of Management and Budget definition of a high-risk program.¹⁵ Yet the

¹⁴ The NRP provides the IRS with compliance information that is statistically representative of the taxpayer population. The IRS uses each tax year's NRP results to update the EITC improper payment rate.

¹⁵ The Office of Management and Budget defines a program as having significant improper payments when improper payments exceed both 1.5 percent of program outlays and \$10 million of all program or

IRS continues to knowingly erroneously classify the risk of these credits by not including a quantitative analysis of existing compliance data similar to the analysis we performed in its annual risk assessment of these credits.

Finally, the assessment of the risk related to PTC improper payments continues to present challenges for the IRS. An agency is usually responsible for complying with the improper payment requirements for payments made from the agency's appropriated funds. The funds used to make PTC payments, including payments of the Advance Premium Tax Credit (APTC),¹⁶ are drawn from the PTC budget fund included in the IRS's budget. However, unlike other refundable credits, the IRS is not solely responsible for administering the PTC. For example, the Department of Health and Human Services Centers for Medicare and Medicaid Services oversees implementation of certain ACA provisions related to the Exchanges. The Exchanges have sole responsibility for determining if an individual is eligible to use the Exchange to purchase health insurance as well as determining the amount of the APTC the individual is eligible to receive. Whereas, the IRS is responsible for determining an individual's total allowable PTC and ensuring that APTC paid to insurers is reconciled to the allowable PTC. Individuals whose APTC is less than their allowable PTC receive the additional credit on their tax return and those who received more APTC than the allowable PTC must repay the excess.

Because the IRS and the Department of Health and Human Services are jointly responsible for the administration of the PTC, improper PTC payments can result from weaknesses in either agency's programs. As a result, the IRS alone cannot effectively assess the risk of PTC improper payments, estimate the improper payment rate and dollar amounts, or establish corrective actions to address the causes of and reduce improper PTC payments on its own.

The Office of Management and Budget established an interagency working group in FY 2015 that included representatives from the IRS, the Department of the Treasury, the Department of Health and Human Services, and the Centers for Medicare and Medicaid Services. The group was established as a collaborative effort to develop a methodology to assess the improper payment risk across all payments made from the PTC budget fund account. The *Interagency PTC Improper Payment Working Group* worked with an outside vendor to complete a comprehensive risk assessment for the PTC for use in FY 2016. Using this assessment, the IRS determined that the PTC has

activity payments made during the fiscal year reported or exceed \$100 million at any percent of program outlays.

¹⁶ An APTC is paid in advance to a taxpayer's insurance company to help cover the cost of premiums.

a medium risk of improper payments. We will continue to review and report on IRS efforts to address the challenges in measuring PTC improper payments.

LEGISLATION TO REDUCE FRAUDULENT AND IMPROPER REFUNDABLE CREDIT PAYMENTS

Congress enacted the Protecting Americans from Tax Hikes (PATH) Act¹⁷ on December 18, 2015, which includes “program integrity provisions” intended to reduce fraudulent and improper EITC, CTC, ACTC, and AOTC payments. For example, one of the PATH Act’s provisions is intended to ensure that the IRS has the information and time needed to verify the income of individuals claiming the EITC and ACTC before the related refund is issued. According to the House Committee on Ways and Means, these integrity provisions are projected to save roughly \$7 billion over 10 years by reducing fraud, abuse, and improper payments in refundable credit programs.

TIGTA has multiple ongoing reviews¹⁸ to evaluate IRS actions to implement key provisions of the PATH Act. To date, our work has found that the IRS has withheld refunds as required for returns with an EITC or ACTC claim and released those returns that were not identified for additional review. IRS management informed us that all EITC and ACTC claims are being verified against Forms W-2, *Wage and Tax Statement*, data to identify claims that have unsupported income. Those that are identified as potentially fraudulent will be addressed as part of the IRS’s fraud prevention programs. The remaining returns with an income discrepancy will be addressed as part of the IRS’s overall Questionable Refund Program.¹⁹ In September 2014, TIGTA identified 677,000 Tax Year (TY)²⁰ 2012 tax returns for which third-party Forms W-2 were not sent to the IRS by the employer for either the taxpayer and/or the spouse listed on the tax return. These tax returns claimed EITCs totaling more than \$1.7 billion.²¹

¹⁷ Consolidated Appropriations Act of 2016, Pub. L. No. 114-113, Div. Q (2015).

¹⁸ TIGTA, Audit No. 201640031, *Implementation of Refundable Credit Integrity Provisions*, report planned for May 2017; TIGTA, Audit NO. 201640023, *Individual Taxpayer Identification Number Deactivation Process*, report planned for Aug. 2017; TIGTA, Audit No. 201740005, *2017 Filing Season*, report planned for Sept. 2017; TIGTA, Audit No. 201740031, *Implementation of Refundable Credit Integrity Provisions Phase 2*, report planned for Oct. 2017.

¹⁹ The Questionable Refund Program is a nationwide multifunctional program designed to identify fraudulent returns, to stop the payment of fraudulent refunds, and to refer identified fraudulent refund schemes to IRS Criminal Investigation field offices.

²⁰ 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.

²¹ TIGTA, Ref. No. 2014-40-093, *Existing Compliance Processes Will Not Reduce the Billions of Dollars in Improper Earned Income Tax Credit and Additional Child Tax Credit Payments* (Sept. 2014).

However, IRS management indicated that for the 2017 Filing Season²² they do not plan to use Forms 1099-MISC, *Miscellaneous Income*, to systemically verify income reported on tax returns with EITC or ACTC claims. Management cited a number of challenges that need to be addressed to use this information to verify income reported at the time tax returns are identified. We will continue to review and report on the IRS's efforts to implement processes to use Forms 1099-MISC to verify income reported on returns claiming refundable credits.

In addition, although the majority of the PATH Act provisions were effective January 1, 2016, and affect the processing of (TY) 2016 returns, one provision was effective December 18, 2015. This provision prevents taxpayers from filing an original or amended tax return for prior years (referred to as retroactive claims) to claim the EITC, CTC, ACTC, and AOTC when the Taxpayer Identification Number (TIN)²³ used to claim the credit was not issued prior to the due date of the tax return. Our review of (TY) 2014 tax returns filed and processed during the 2016 Filing Season as of May 26, 2016, identified more than \$34.8 million in CTCs, ACTCs, EITCs, and AOTCs claims that were paid to 15,744 taxpayers filing tax returns for years prior to when their TINs were issued. Each of the refundable credit claims associated with the returns we identified should have been disallowed by the IRS but were not.

Management indicated that although the above provision was effective in December 2015, the IRS was unable to implement processes to identify erroneous claims for the 2016 Filing Season. For example, the IRS did not have the issuance dates associated with a Social Security Number (SSN) and Individual Taxpayer Identification Number (ITIN).²⁴ Consequently, the IRS needed to coordinate with the Social Security Administration to obtain the SSN issuance date and develop a methodology to identify the ITIN issuance date. Management further explained that, even if the IRS had the issuance dates, the modifications to its computer systems necessary to identify claims filed for the 2016 Filing Season would have been impossible to implement because the provision was enacted only 32 days prior to the start of the filing season.

²² The period from January through mid-April when most individual income tax returns are filed.

²³ A nine-digit number assigned to taxpayers for identification purposes. Depending upon the nature of the taxpayer, the TIN is either an Employer Identification Number, a Social Security Number, or an Individual TIN.

²⁴ The IRS created the ITIN to provide Taxpayer Identification Numbers, when needed for tax purposes, to individuals who do not have and are not eligible to obtain an SSN.

Finally, although the PATH Act gives the IRS more time to verify EITC and ACTC claims before refunds are issued, it does not expand the IRS's authority to systemically correct erroneous claims. The IRS, in conjunction with the Assistant Secretary of the Treasury for Tax Policy, has in each year since FY 2013 set forth a legislative proposal requesting additional error authority (hereafter referred to as correctable error authority) as part of its annual budget submission. The requested authority includes allowing the IRS to correct, during processing, tax returns when the information provided by the taxpayer does not match the information contained in Government databases (e.g., income information reported on the tax return does not match Forms W-2 from the Social Security Administration).

In September 2014, we reported²⁵ that because the IRS's compliance resources are limited; the IRS does not address the majority of potentially erroneous EITC claims it identifies. Currently, under the Internal Revenue Code, the IRS can use its math error authority to address erroneous EITC claims by systemically correcting mathematical or clerical errors on such claims. For example, it can correct entries made on the wrong line on the tax return or mathematical errors made in computing income or the EITC. However, the majority of potentially erroneous EITC claims that the IRS identifies do not contain the types of errors for which it has math error authority. To address those potentially erroneous EITC claims identified that cannot be addressed using math error authority the IRS must conduct an audit. The IRS estimated that it costs \$1.50 to resolve an erroneous EITC claim using math error authority compared to \$278 to conduct a pre-refund audit.²⁶

Without correctable error authority, billions of dollars in identified potentially erroneous claims will continue to go unaddressed each year. It should be noted that the IRS has established processes and procedures that allow taxpayers to question the validity of IRS adjustments to their tax return. In July 2011, we reported that these procedures included sending a notice to taxpayers that shows the adjustments made to their tax returns.²⁷ The notice also provides both a telephone number and mailing address for the taxpayer to contact the IRS should he or she question adjustments made to their tax return. Taxpayers who question the adjustments are given 60 calendar days from the date of the notice to respond to the IRS and dispute the

²⁵ TIGTA, Ref. No. 2014-40-093, *Existing Compliance Processes Will Not Reduce the Billions of Dollars in Improper Earned Income Tax Credit and Additional Child Tax Credit Payments* (Sept. 2014).

²⁶ Cost to use math error authority as of June 25, 2014, as provided by the IRS. The IRS provided the cost of a prerefund audit based on Fiscal Year 2010 financial data, which is the most current estimate available.

²⁷ TIGTA, Ref. No. 2011-40-059, *Some Taxpayer Responses to Math Error Adjustments Were Not Worked Timely and Accurately* (July 2011).

adjustments. During this 60-day period, the IRS will place a freeze on the taxpayer’s account to prevent the issuance of the portion of the refund associated with the error(s) identified or prevent the initiation of collection action resulting from any balance due.

EFFORTS TO IDENTIFY AND REDUCE IMPROPER PAYMENTS

The EITC, ACTC and AOTC are the three largest refundable credits the IRS administers and collectively accounted for more than \$100 billion in credits claimed during TY 2015. The table below shows the amount of EITC, ACTC, and AOTC claimed by taxpayers during TY 2015.²⁸

Refundable Credit	Tax Returns	Amount of Credit Claimed
EITC	27.5 million	\$67.5 billion
ACTC	19.2 million	\$26.0 billion
AOTC	9.6 million	\$8.5 billion
Total	56.3 million	\$102.0 billion

The following highlights some of our work relating to these refundable credits.

Earned Income Tax Credit – For FY 2016, the IRS estimates that more than 24 percent of EITC payments, totaling \$16.8 billion, were issued improperly.

In September 2014,²⁹ we reported that the IRS has developed a strategy to reduce EITC improper payments. This strategy focuses on early intervention to ensure that individuals who claim the credit are in compliance with the EITC rules. The strategy includes education and outreach, enforcement actions, a paid tax return preparer compliance initiative, and legislative proposals. The IRS also performed compliance studies which found that EITC improper payments primarily result from two root causes – authentication and program design.

Authentication errors include errors associated with the lack of available data to which the IRS can verify self-employment income, authenticate qualifying children, and verify filing status. Verification errors relate to the IRS’s inability to identify

²⁸ Source is TIGTA’s analysis of the IRS Individual Return Transaction File for Tax Year 2015. Individuals may have claimed more than one of the credits shown on a tax return.

²⁹ TIGTA, Ref. No. 2014-40-093, *Existing Compliance Processes Will Not Reduce the Billions of Dollars in Improper Earned Income Tax Credit and Additional Child Tax Credit Payments* (Sept. 2014).

underreporting and overreporting of third-party reported income, such as wages and errors that arise when more than one individual can claim a qualifying child. For FY 2016, the IRS estimated that 6 percent, or \$1 billion, of improper EITC payments resulted from verification errors with the remaining 94 percent of improper EITC payments, or \$15.8 billion, resulting from authentication errors.

As previously noted, we have an ongoing review to assess the IRS's use of accelerated filing of income and withholding documents to identify erroneous claims. In addition, we are also conducting a review to assess the IRS's Return Preparer Outreach Strategy processes to identify and address return preparers filing returns with erroneous refundable credit claims.

Additional Child Tax Credit – Using IRS's compliance data, we estimate that the IRS potentially issued \$7.2 billion in ACTC improper payments during FY 2016.

In March 2009, we reported a significant increase in ACTC claims by filers who were ineligible to obtain a Social Security Number.³⁰ These individuals are not authorized to work in the United States and filed tax returns using an ITIN. For example, our updated analysis in response to a Congressional request³¹ identified that the amount of ACTC paid to these filers has grown substantially from \$62 million in Processing Year 2001 to more than \$3.4 billion in Processing Year 2015. It should be noted that ITIN filers are not eligible to claim the EITC but can claim the ACTC.

In addition, in July 2011, we reported that a significant number of ITIN filers submitted multiple returns with ACTC claims for prior year tax returns (e.g., filing TYs 2007, 2008, and 2009 returns at the same time). For example, in Processing Year 2010, approximately 238,000 ITIN filers submitted more than 608,000 tax returns for multiple years at the same time and claimed just more than a \$1 billion in ACTCs on those returns. The PATH Act contains a provision that excludes retroactive claims and, as previously indicated, we have an ongoing review to assess the IRS's processes to identify and disallow these claims.

American Opportunity Tax Credit – Using IRS's compliance data, we estimate that the IRS potentially issued \$1.1 billion in AOTC improper payments during FY 2016.

³⁰ TIGTA, Ref. No. 2009-40-057, *Actions Are Needed to Ensure Proper Use of Individual Taxpayer Identification Numbers and to Verify or Limit Refundable Credit Claims* (March 2009).

³¹ This analysis was conducted in response to an inquiry from the Legislative Director for the Chairman of the House Committee on Oversight and Government Reform, Subcommittee on Government Relations.

In March 2015, we reported that although the IRS has taken steps to address some of our prior recommendations, processes still do not effectively identify taxpayers who claim erroneous education credits.³² As a result, we estimated that in (TY) 2012 more than 3.6 million taxpayers received more than \$5.6 billion in erroneous education credits (\$2.5 billion in refundable credits and \$3.1 billion in nonrefundable credits). These 3.6 million taxpayers claimed credits but did not meet eligibility requirements and included taxpayers who erroneously claimed students for whom no Form 1098-T, *Tuition Statement*, was received by the IRS to substantiate that the students attended an eligible educational institution,³³ or claimed students who attended ineligible institutions³⁴ or who attended less than half time.

In response to our concerns, the IRS, in coordination with the Assistant Secretary of the Treasury for Tax Policy, submitted legislative proposals to establish the filing date for information returns (including the Form 1098-T) as January 31. This would enable IRS to verify claims at the time tax returns are processed. As of April 2017, such legislation has not been enacted.

Included in the \$5.6 billion erroneous education credit claims we identified are claims totaling an estimated \$494 million whereby the taxpayers erroneously claimed the AOTC for the same students for more than four years. Requirements state that the allowable four-year period for which taxpayers can claim the AOTC for any one student includes any previous claims for the Hope Credit and applies to any four tax years; the tax years do not need to be consecutive. Therefore, if a student was claimed for the AOTC or Hope Credit in any four prior tax years, the student cannot be used by any taxpayer to claim the credit a fifth time. It should be noted that the request for correctable error authority would permit the IRS to correct errors in cases in which the taxpayer has exceeded the lifetime limit for claiming a deduction or credit. As such this authority could be used to address AOTC claims for which taxpayers erroneously claim the credit for the same students for more than four years.

Finally, paid tax return preparers continue to prepare a significant number of returns with questionable education credit claims. More than 1.7 million (49 percent) of

³² 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).

³³ Institutions of higher education are required to provide each student with a Form 1098-T and file a duplicate copy with the IRS. The Form 1098-T is to report payments received for qualified tuition and related expenses, scholarships and grants given, adjustments made for a prior year, and the name and location of the institution.

³⁴ An eligible institution is any domestic or foreign postsecondary educational institution or training program that is certified to receive Federal student aid funding from the U.S. Department of Education.

the 3.6 million tax returns we identified were prepared by tax return preparers. The potentially erroneous claims totaled more than \$2.7 billion. This is similar to the percentage we have reported previously.³⁵ In response, the IRS developed a comprehensive enforcement strategy to increase tax return preparer compliance. In addition, the IRS stated that, prior to the start of the 2014 Filing Season, it sent educational letters to approximately 1,000 tax return preparers to alert them that they had filed AOTC claims that appeared to be erroneous. The letters reminded them of their responsibilities as tax return preparers and directed them to additional information. The IRS indicated that these tax return preparers' filing patterns and compliance with future AOTC claims will be tracked to determine if compliance has improved.

We are conducting a follow-up analysis of the IRS's efforts to identify AOTC claims filed for more than four years and will include the results of our assessment in our 2017 Filing Season report, which will be issued later this calendar year. In addition, later this calendar year, we will be initiating a follow-up review to evaluate IRS efforts to identify questionable AOTC claims.

In summary, the IRS issued an estimated \$25 billion in potentially improper EITC, ACTC, and AOTC payments in FY 2016. This represents a significance loss to both the Federal Government and taxpayers. We at TIGTA take seriously our mandate to provide independent oversight of the IRS in its administration of our Nation's tax system. As such, we plan to provide continuing review of the IRS's efforts to identify and reduce improper refundable tax credit payments.

Chairman Johnson, Ranking Member McCaskill, and Members of the Committee, thank you for the opportunity to share my views.

³⁵ TIGTA, Ref. No. 2011-41-083, Billions of Dollars in Education Credits Appear to Be Erroneous (Sept. 2011).



J. Russell George

Treasury Inspector General for Tax Administration

Following his nomination by President George W. Bush, the United States Senate confirmed J. Russell George in November 2004, as the Treasury Inspector General for Tax Administration. Prior to assuming this role, Mr. George served as the Inspector General of the Corporation for National and Community Service, having been nominated to that position by President Bush and confirmed by the Senate

in 2002.

A native of New York City, where he attended public schools, including Brooklyn Technical High School, Mr. George received his Bachelor of Arts degree from Howard University in Washington, DC, and his Doctorate of Jurisprudence from Harvard University's School of Law in Cambridge, MA. After receiving his law degree, he returned to New York and served as a prosecutor in the Queens County District Attorney's Office.

Following his work as a prosecutor, Mr. George joined the Counsel's Office in the White House Office of Management and Budget, where he was Assistant General Counsel. In that capacity, he provided legal guidance on issues concerning presidential and executive branch authority. He was next invited to join the White House Staff as the Associate Director for Policy in the Office of National Service. It was there that he implemented the legislation establishing the Commission for National and Community Service, the precursor to the Corporation for National and Community Service. He then returned to New York and practiced law at Kramer, Levin, Naftalis, Nessen, Kamin & Frankel.

In 1995, Mr. George returned to Washington and joined the staff of the Committee on Government Reform and Oversight and served as the Staff Director and Chief Counsel of the Government Management, Information and Technology subcommittee (later renamed the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations), chaired by Representative Stephen Horn. There he directed a staff that conducted over 200 hearings on legislative and oversight issues pertaining to Federal Government management practices, including procurement policies, the disposition of Government-controlled information, the performance of chief financial officers and inspectors general, and the Government's use of technology. He continued in that position until his appointment by President Bush in 2002.

Mr. George also served as a member of the Integrity Committee of the Council of Inspectors General for Integrity and Efficiency (CIGIE). CIGIE is an independent entity within the executive branch, statutorily established by the Inspector General Act, as amended, to address integrity, economy, and effectiveness issues that transcend individual Government agencies and to increase the professionalism and effectiveness of personnel by developing policies, standards, and approaches to aid in the establishment of a well-trained and highly skilled workforce in the offices of the Inspectors General. The CIGIE Integrity Committee serves as an independent review and investigative mechanism for allegations of wrongdoing brought against Inspectors General.