Treasury Inspector General for Tax Administration
Office of Audit

REDUCTION TARGETS AND STRATEGIES HAVE NOT BEEN ESTABLISHED TO REDUCE THE BILLIONS OF DOLLARS IN IMPROPER EARNED INCOME TAX CREDIT PAYMENTS EACH YEAR

Issued on February 7, 2011

Highlights

Highlights of Report Number: 2011-40-023 to the Internal Revenue Service Deputy Commissioner for Operations Support.

IMPACT ON TAXPAYERS

The Government Accountability Office has listed the Earned Income Tax Credit (EITC) Program as having the second highest dollar amount of improper payments of all Federal programs. The Internal Revenue Service (IRS) has made little improvement in reducing EITC improper payments since 2002 when it was first required to report estimates of these payments to Congress. The IRS continues to report that 23 percent to 28 percent of EITC payments are issued improperly each year. In Fiscal Year 2009, this equated to $11 billion to $13 billion in EITC improper payments.

WHY TIGTA DID THE AUDIT

This audit was initiated because Executive Order 13520 requires the Secretary of the Treasury to provide specific information regarding EITC improper payments to TIGTA. The objective of this review was to assess the IRS's efforts to implement Executive Order 13520.

WHAT TIGTA FOUND

Executive Order 13520 requires the IRS to intensify its efforts and set targets to reduce EITC improper payments. The IRS's report to TIGTA did not include any quantifiable targets to reduce EITC improper payments. IRS management noted that reduction targets were not set because the IRS has to balance enforcement efforts among different taxpayer income levels. The IRS stated that its new efforts to regulate tax return preparers will reduce the improper payment rate. However, it is unknown whether the regulation of tax return preparers will result in a significant reduction in EITC improper payments.

TIGTA has conducted a number of audits that have provided the IRS with specific actions that could be taken to reduce improper payments. While the IRS has implemented some of our recommendations, it has not taken actions to address key recommendations aimed at preventing/reducing EITC improper payments.

TIGTA also found that the methodology used to compute the Fiscal Year 2009 EITC improper payment rate provides a valid estimate of EITC overpayments. The IRS used results from its National Research Program to estimate the 2009 EITC improper payment rate. While one goal of the National Research Program may be to identify noncompliance, the statistical nature of the study provides the IRS the opportunity to estimate EITC underpayments.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Deputy Commissioner for Operations Support 1) establish quantifiable reduction targets and strategies to meet those targets as required by Executive Order 13520, and 2) use the National Research Program sample to estimate instances in which the IRS incorrectly pays less in the EITC than the taxpayer claims (underpayments).

In their response to the report, IRS officials agreed with our first recommendation, stating that the tax return preparer initiative will enable the IRS to have a baseline against which it can set meaningful reduction targets. The IRS agreed in concept with our second recommendation and plans to explore whether using the National Research Program sample to estimate underpayments is possible and practical. The IRS also noted that its focus on tax return preparers will serve to improve EITC tax returns and further reduce EITC errors.

TIGTA agrees that the regulation of tax return preparers will have some impact on reducing EITC improper payments. Nonetheless, the IRS report does not provide details on when or how the IRS plans to measure the impact of the tax return preparer strategy on EITC improper payments. As noted in our report, the IRS has just begun implementing the tax return preparer strategy and does not anticipate the strategy will be fully implemented until 2014. Using IRS estimates for Fiscal Year 2009, it is likely that the IRS will have issued anywhere from $55 billion to $65 billion in improper payments by Fiscal Year 2014.

The loss of billions of dollars in improper EITC payments annually calls for more aggressive and immediate actions to reduce improper payments. Executive Order 13520 requires the IRS to intensify its efforts and set targets to reduce EITC improper payments. The IRS has not met this requirement and, as a result, the risk remains high that no significant improvement will be made in reducing improper EITC payments.

READ THE FULL REPORT

To view the report, including the scope, methodology, and full IRS response, go to:

http://www.treas.gov/tigta/auditreports/2011reports/201140023fr.pdf.

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