Treasury Inspector General for Tax Administration
Office of Audit

SIGNIFICANT DISCREPANCIES EXIST BETWEEN ALIMONY DEDUCTIONS CLAIMED BY PAYERS AND INCOME REPORTED BY RECIPIENTS

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Highlights

Highlights of Report Number: 2014-40-022 to the Internal Revenue Service Commissioners for the Small Business/Self-Employed Division and the Wage and Investment Division.

IMPACT ON TAXPAYERS

Alimony is a payment to or for a spouse or former spouse under a divorce or separation instrument. In Tax Year 2010, a total of 567,887 taxpayers claimed alimony deductions totaling more than $10 billion. An alimony income reporting discrepancy occurs when individuals claim deductions for alimony which they did not pay or individuals do not report alimony income they received.

WHY TIGTA DID THE AUDIT

Individuals who pay alimony can deduct the amount paid from income on their tax return to reduce the amount of tax an individual must pay. Conversely, individuals who receive alimony must claim the amount received as income on their tax return. TIGTA initiated this audit to evaluate the alimony reporting gap and to assess controls the IRS has in place to promote reporting compliance.

WHAT TIGTA FOUND

Processes have not been developed to address the majority of discrepancies between alimony deductions claimed and income reported. TIGTA's analysis of the 567,887 Tax Year 2010 returns with an alimony deduction claim identified 266,190 (47 percent) tax returns in which it appears that individuals claimed alimony deductions for which income was not reported on a corresponding recipient's tax return or the amount of alimony income reported did not agree with the amount of the deduction taken. There is a discrepancy of more than $2.3 billion in deductions claimed without corresponding income reported.

Apart from examining a small number of tax returns, the IRS generally has no processes or procedures to address this substantial compliance gap.

IRS processes also do not ensure that individuals provide a valid recipient Taxpayer Identification Number (TIN) when claiming an alimony deduction as required. TIGTA's analysis of the 567,887 Tax Year 2010 returns that claimed an alimony deduction identified an estimated 6,500 tax returns claiming an alimony deduction for which the IRS did not identify that the recipient TIN was missing or invalid. In addition, because of errors in IRS processing instructions, the IRS did not assess penalties totaling $324,900 on individuals who did not provide a valid recipient TIN as required.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Commissioner, Small Business/Self-Employed Division, work with the Commissioner, Wage and Investment Division, to evaluate current examination filters to ensure that potentially high-risk tax returns are not inappropriately excluded from examination and develop a strategy to address the significant alimony compliance gap. TIGTA also recommended that the Commissioner, Wage and Investment Division, revise processes and procedures to verify that all tax returns include a valid recipient TIN when claiming an alimony deduction and correct errors in IRS processing instructions to ensure that a penalty is accurately assessed on all tax returns on which a valid recipient TIN is not provided.

The IRS agreed with three of TIGTA's recommendations and disagreed with one recommendation. The IRS stated that it enhanced its examination filters and will continue to review and improve its strategy to reduce the compliance gap. In addition, the IRS revised procedures to ensure that penalties are assessed when appropriate. However, because the IRS does not have the authority to deny alimony deductions outside of deficiency processing, it believes verification of the deduction is more efficiently performed in its Compliance function.

READ THE FULL REPORT

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

http://www.treas.gov/tigta/auditreports/2014reports/201440022fr.pdf.