Treasury Inspector General for Tax Administration
Office of Audit

ADDITIONAL ACTIONS TO ENFORCE PAYMENT CARD REPORTING REQUIREMENTS COULD REDUCE THE TAX GAP

Issued on September 25, 2015

Highlights

Highlights of Report Number: 2015-40-089 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

IMPACT ON TAXPAYERS

Congress enacted legislation in an effort to narrow the Tax Gap (the estimated difference between the amount of tax that taxpayers should pay and the amount that is paid voluntarily and on time) and increase voluntary compliance of businesses through information reporting. The legislation required information returns to be filed for reportable payment card transactions starting in Calendar Year 2012. The Department of the Treasury estimated that this new law would result in the additional collection of almost $10 billion over 10 years.

WHY TIGTA DID THE AUDIT

In Calendar Year 2012, the IRS committed to a multiyear, multi-treatment stream compliance pilot initiative leveraging Form 1099-K, *Payment Card and Third Party Network Transactions*, information to reduce the Tax Gap. This audit continues our assessment of the IRS's implementation of payment card reporting requirements.

WHAT TIGTA FOUND

The IRS recognizes the challenges associated with using Forms 1099-K to identify noncompliance with income reporting. To address these challenges, the IRS implemented pilot initiatives to identify payment card noncompliance. These initiatives include new processes and changes to existing processes, treatment streams, and capabilities. The IRS continues to use the results from these pilot initiatives to refine the criteria used to identify underreporting of payment card income.

TIGTA found that payers are not compliant with backup withholding requirements directing a payer to immediately withhold 28 percent of amounts reported on Forms 1099-K for payees that failed to provide a valid Taxpayer Identification Number (TIN). For example, TIGTA's review of Calendar Year 2013 Forms 1099-K identified 10,216 Forms 1099-K with a missing TIN. These Forms 1099-K reported gross transactions totaling over $10.6 billion. As such, payers were required to withhold almost $3 billion from these payees, yet no backup withholding was taken.

In addition, TIGTA identified that the TIN Matching Program available to payers to verify a payee TIN does not alert the payer when a TIN of a deceased individual is being used. TIGTA's review of Calendar Year 2013 Forms 1099-K found that the IRS received 2,933 Forms 1099-K with gross transactions totaling $543.9 million for which the payee TIN was that of a deceased individual.

Finally, Form 1099-K information should be included in the IRS's nonfiler identification efforts. Review of Calendar Year 2013 Forms 1099-K identified 84,107 individuals for whom payers reported gross transactions on Forms 1099-K totaling nearly $9.1 billion and 443,528 businesses for which payers reported gross transactions on Forms 1099-K totaling over $164.5 billion that did not file a tax return.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Commissioner, Small Business/Self-Employed Division, ensure that a business case analysis is performed when making decisions to grant transitional relief; assess penalties on certain payers that do not comply with reporting requirements; and use Form 1099-K information as part of the IRS's nonfiler program.

The IRS agreed with six of the seven recommendations and plans appropriate corrective actions. The IRS did not agree to implement a computer programming change because it could not guarantee that changes will be implemented due to budgetary constraints and limited resources. However, TIGTA believes this change should be a priority.

READ THE FULL REPORT

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

http://www.treas.gov/tigta/auditreports/2015reports/201540089fr.pdf.