



*Evaluation of the Planning, Computation, and
Issuance of the Recovery Rebate Credit*

September 9, 2009

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This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 9, 2009

MEMORANDUM FOR DEPUTY COMMISSIONER FOR OPERATIONS SUPPORT
DEPUTY COMMISSIONER FOR SERVICES AND
ENFORCEMENT

FROM: 
Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Evaluation of the Planning, Computation, and
Issuance of the Recovery Rebate Credit (Audit # 200840030.04)

This report presents the results of our review to evaluate the effectiveness of the Internal Revenue Service's (IRS) efforts to plan and implement the Tax Year 2008 Recovery Rebate Credit. This was our fourth and final review in a series of reviews that evaluated the IRS implementation of the Economic Stimulus Act of 2008¹ from the initial advanced economic stimulus payments through issuance of the recovery rebate credits.²

Impact on the Taxpayer

The recovery rebate credit is provided to those eligible individuals who may not have received an economic stimulus payment or who are entitled to an additional credit. Overall, the IRS successfully planned for the implementation of the recovery rebate credit. The IRS issued more than \$96 billion in advanced economic stimulus payments to more than 119 million individuals in Calendar Year 2008 and approximately \$8.5 billion in recovery rebate credits to almost 21 million taxpayers as of April 17, 2009. The IRS was able to achieve the intent of Congress by providing billions of dollars to millions of Americans.

¹ Pub. L. 110-185, 122 Stat. 613.

² See Appendix V for a listing of the reviews we conducted.



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Synopsis

Overall, the IRS successfully planned for the implementation of the recovery rebate credit. A number of efforts were initiated to educate and assist individuals on the recovery rebate credit.

However, taxpayer confusion in calculating the recovery rebate credit and programming errors presented significant challenges. Despite education and assistance efforts by the IRS, taxpayer confusion in computing the recovery rebate credit resulted in a significant number of errors. Of the 114.3 million tax returns processed as of April 17, 2009, 16.7 million (14.6 percent) included at least 1 error that needed to be addressed by the IRS Error Resolution function (8.4 million had a recovery rebate credit error). This exceeded the total number of returns that the IRS estimated would go to its Error Resolution function by 9.8 million tax returns (142 percent).

The accuracy rate of the IRS' computation of the recovery rebate credit was very high. Our analysis of more than 102 million tax returns as of April 17, 2009,³ showed that the IRS correctly calculated the recovery rebate credit on 99.6 percent (approximately 101.7 million) of the tax returns processed. We identified 399,099 tax returns (0.4 percent) for which our calculation of the recovery rebate credit and the IRS' calculation did not agree. Our analysis indicated that 258,550 taxpayers did not receive \$84.6 million to which they were entitled and 140,549 taxpayers received \$60.6 million more in credits than they were entitled to receive. Differences resulted from errors in the IRS' computer programming as well as procedural errors in resolving IRS and taxpayer computation errors.

In addition to the above computational differences, we identified a programming error that put \$1.6 billion at risk. In December 2008, we notified the IRS of a programming error that could have allowed almost 6.4 million taxpayers to receive almost \$1.6 billion in erroneous recovery rebate credits to which they were not entitled. The Economic Stimulus Act of 2008 specifically prohibits a taxpayer who can be claimed as a dependent on someone else's return from receiving the recovery rebate credit. However, initial

Our analysis of 102 million tax returns as of April 17, 2009, showed that the IRS correctly calculated the recovery rebate credit on 99.6 percent of the tax returns processed.

The IRS took immediate action to correct a programming error we brought to its attention. Correction of the error ensured 6.4 million individuals did not receive \$1.6 billion in erroneous recovery rebate credits.

³ The Returns Transaction File contains all edited, transcribed, and error-corrected data from the U.S. Individual Income Tax Returns (Form 1040 series) and related forms for the current processing year and 2 prior years.



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programming for the recovery rebate credit did not include disallowing the credit when a taxpayer indicated he or she can be claimed as a dependent on someone else's return. The IRS took immediate action to correct this programming error.

Finally, legislation did not provide the IRS with math error authority⁴ to prevent individuals without valid Social Security Numbers from receiving the recovery rebate credit. Although the legislation prohibited individuals without a valid Social Security Number from receiving the rebate credit, the IRS was not provided with math error authority that would have enabled it to effectively prevent the issuance of rebate credits to these individuals at the time a tax return was processed. As a result, the IRS erroneously provided more than \$27 million in recovery rebate credits to more than 44,000 taxpayers who did not have a valid Social Security Number.

We issued a memorandum to the IRS in September 2008 raising concerns about its lack of math error authority. We recommended the IRS work with the Assistant Secretary of the Treasury for Tax Policy to obtain math error authority for recovery rebate claims on tax returns without a valid Social Security Number. IRS management responded that they had raised concerns to the Assistant Secretary about the lack of math error authority for this issue. However, no legislative proposal was put forth to provide this authority.

Recommendations

We recommended that the Commissioner, Wage and Investment Division, issue recovery payments to individuals who did not receive the recovery rebate credit to which they were entitled as a result of programming and Error Resolution function errors.

Response

IRS management agreed with the intent of the recommendations in our report. The IRS is currently reviewing the data provided by the Treasury Inspector General for Tax Administration and will provide appropriate taxpayer relief, if warranted, based on the results of its review. Management's complete response to the draft report is included in Appendix VI.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Michael E. McKenney, Assistant Inspector General for Audit (Returns Processing and Account Services), at (202) 622-5916.

⁴ Math error authority allows the IRS to systemically disallow certain taxpayer claims at the time a tax return is processed.



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Abbreviations

<i>e-file(d)</i>	Electronically file(d)
IRS	Internal Revenue Service
SSN	Social Security Number
TY	Tax Year



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Background

The Economic Stimulus Act of 2008,¹ signed on February 13, 2008, was enacted to energize the national economy. The Act provided for a credit against Tax Year (TY) 2008 taxes paid by individuals. The majority of individuals received the credit in the form of an economic stimulus payment in advance of filing their TY 2008 tax return. The Internal Revenue Service (IRS) estimated the credit based on information on the TY 2007 tax return and began issuing economic stimulus payments on April 28, 2008.

As of April 17, 2009, the IRS had allowed approximately \$8.5 billion in recovery rebate credits to almost 21 million taxpayers.

In general, the law prohibits individuals who do not meet basic requirements from receiving the recovery rebate credit. Taxpayers must have:

- A valid Social Security Number (SSN).
- An income tax liability or at least \$3,000 in qualifying income. Income from wages, tips, and net self-employment earnings, as well as nontaxable combat pay and some Social Security, Veterans disability, and Railroad Retirement benefits qualifies as eligible income.
- An Adjusted Gross Income below \$87,000 for single taxpayers or \$174,000 for married taxpayers.

Although the IRS issued the credit in advance, eligible individuals who may not have received an economic stimulus payment or who are entitled to an additional credit could receive the credit when they file their TY 2008 tax returns. The TY 2008 credit is known as the recovery rebate credit. Individuals who met the following conditions were entitled to receive the recovery rebate credit based on their TY 2008 tax returns, provided they have a valid SSN:

- Taxpayers who were not eligible for an economic stimulus payment because their income was below the \$3,000 qualifying income requirement or whose income was above the maximum income phase-out. If these taxpayers' incomes had dropped and now meet the income requirements in TY 2008, they will be entitled to receive the recovery rebate credit.
- Taxpayers may be entitled to an additional credit because of changes in their income or family status (i.e., birth of a child).
- Taxpayers who could be claimed as a dependent on someone else's tax return in TY 2007 but can no longer be claimed as a dependent in TY 2008.

¹ Pub. L. 110-185, 122 Stat. 613.



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The primary difference between the economic stimulus payment and the recovery rebate credit was the form in which it was issued. The economic stimulus payment was computed by the IRS using information on the TY 2007 tax return and issued as a separate payment to the taxpayer. However, the recovery rebate credit was included as a line item on the TY 2008 income tax return and included in the taxpayer's refund, if applicable.

This was our fourth and final review in a series of reviews that looked at the IRS implementation of the Economic Stimulus Act of 2008 from the initial advanced economic stimulus payments through issuance of the recovery rebate credits.² The IRS issued more than \$96 billion in advanced economic stimulus payments to more than 119 million individuals in Calendar Year 2008 and approximately \$8.5 billion in recovery rebate credits to almost 21 million taxpayers as of April 17, 2009. These payments were issued in conjunction with the processing of millions of individual tax returns. The IRS was able to achieve the intent of Congress by providing billions of dollars to millions of Americans as specified by law.

This review was performed at the IRS National Headquarters of the Wage and Investment Division in Atlanta, Georgia, and the Modernization and Information Technology Services organization in New Carrollton, Maryland, during the period October 2008 through June 2009. 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. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

² See Appendix V for a listing of the reviews we conducted.



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Results of Review

A Number of Efforts Were Initiated to Educate and Assist Individuals on the Recovery Rebate Credit

Overall, the IRS successfully planned for the implementation of the recovery rebate credit. The IRS timely updated its tax forms, instructions, publications, and web site to include key information explaining the recovery rebate credit. Guidance included information to assist taxpayers in determining eligibility for the recovery rebate credit. In addition, the IRS developed a number of tools, including online tools, to assist taxpayers in computing any recovery rebate credit that they may be due.

Tax forms, instructions, publications, and the IRS web site were updated with recovery rebate credit information in an effort to educate taxpayers

The IRS initiated a number of efforts to educate individuals on the requirements to receive the recovery rebate credit. These efforts included:

- Developing the *Recovery Rebate Credit Worksheet* to assist taxpayers in computing any recovery rebate credit they may be due. Using the worksheet, taxpayers can calculate the recovery rebate credit based on their TY 2008 tax returns. They would then compare the credit with what they received as an economic stimulus payment in Calendar Year 2008. For most people, the amount will be the same. However, taxpayers may claim the difference between the economic stimulus payment and the recovery rebate credit as a refundable credit against their TY 2008 tax liability. If the taxpayers' economic stimulus payment was greater than the computed recovery rebate credit, taxpayers are not required to pay the difference back to the IRS.
- Developing resource guides for volunteers at free tax assistance sites and for IRS employees working in Taxpayer Assistance Centers and Toll-Free sites. The guides assist these individuals in determining if a taxpayer may be eligible for the recovery rebate credit.
- Distributing information to the public via the media on recovery rebate credit eligibility criteria and how to claim the credit.

The IRS developed the Recovery Rebate Credit Worksheet to assist taxpayers in determining eligibility and computing the recovery rebate credit.



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- Updating the U.S. Individual Income Tax Return (Form 1040) and related instructions as well as other tax publications, such as *Your Federal Income Tax* (Publication 17), to include information to assist taxpayers in claiming the recovery rebate credit.

At the initiation of our audit, we reviewed IRS guidance and made suggestions to improve the clarity of recovery rebate credit instructions in the Form 1040. The IRS agreed and made the following changes:

- Revised the Form 1040 instructions to explain that the economic stimulus payment and the recovery rebate credit were similar. The Form 1040 instructions did not explain the relationship between the economic stimulus payment and the recovery rebate credit. We were concerned taxpayers would mistakenly think the recovery rebate credit was a new tax credit instead of a continuation of the economic stimulus payment.
- Added specific recovery rebate credit eligibility requirements to Form 1040 instructions preceding the rebate credit worksheet so that taxpayers could tell whether they may be eligible for the credit. The Form 1040 instructions did not provide enough information for taxpayers to determine if they qualified for the credit without having to complete the credit worksheet.

The IRS provided a number of options to assist taxpayers in computing the recovery rebate credit

The IRS provided a number of options for taxpayers to obtain assistance in correctly computing their recovery rebate credit for their TY 2008 returns. The efforts included:

- Developing a recovery rebate credit webpage called the *Recovery Rebate Credit Information Center*. The site provides eligibility requirements and instructions on how to compute the credit. The information was also provided in Spanish.
- Developing online tools, available on the IRS web site, to assist taxpayers in computing their recovery rebate credit. The *How Much Was My Stimulus Payment* enabled taxpayers to look up the amount of their economic stimulus payment and the *Recovery Rebate Calculator* enabled taxpayers to determine if they were eligible for the recovery rebate credit. We determined that these online tools correctly provided taxpayers with the amount of their economic stimulus payment and provided accurate responses regarding rebate credit eligibility.

Taxpayer confusion in calculating the recovery rebate credit and programming errors presented significant challenges

Although the IRS initiated a number of efforts to educate and assist individuals, taxpayer confusion in computing the recovery rebate credit resulted in a significant number of taxpayer errors. Of the 114.3 million tax returns processed as of April 17, 2009, 16.7 million



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(14.6 percent) included at least 1 error that needed to be addressed by the IRS Error Resolution function (8.4 million contained a recovery rebate credit error). This exceeded the total number of tax returns the IRS estimated would go to its Error Resolution function by 9.8 million tax returns (142 percent). The IRS assumed taxpayers would understand that they generally were not eligible for the recovery rebate credit if they had already received an economic stimulus payment. However, taxpayers did not understand that the economic stimulus payment and the recovery rebate credit were one in the same or they did not know how to correctly compute and claim the credit.

More than 8.4 million of the 114.3 million returns processed as of April 17, 2009, contained a recovery rebate credit error.

We recognized that the likelihood for taxpayer errors was high because the calculation of the recovery rebate credit was based upon several factors, including the taxpayer's filing status, income, and tax liability. As such, we issued a memorandum to the Commissioner, Wage and Investment Division, dated September 23, 2008, recommending that the IRS compute the credit except for certain situations where the complexities would prevent the IRS from being able to do so. The IRS subsequently informed us that the Economic Stimulus Act requires the IRS to provide the taxpayers with the option to compute the credit themselves.

As we anticipated, there was a significant increase in taxpayer errors involving the computing of the recovery rebate credit. The IRS estimated that less than 3 percent (an estimated 4.2 million taxpayers) of taxpayers would be eligible to receive the recovery rebate credit. However, to ensure the accuracy of the taxpayer's computation, the IRS was required to compute the credit on every tax return. Every return for which the IRS' calculation of the credit and the taxpayer's calculation did not agree was sent to the Error Resolution function. These included those tax returns for which the IRS computed the credit for the taxpayer. For example:

- As of April 17, 2009, the IRS received 9.1 million electronically filed (*e-file*) tax returns in the Error Resolution System, almost 7 million more than was scheduled for the filing season.³ Normally, 2 to 3 percent of *e-file* tax returns go to the Error Resolution System; this year the rate was 10.1 percent. The percent of paper tax returns sent to the Error Resolution System, 31.7 percent, was also higher than this time last year.
- As of April 17, 2009, approximately 7.1 million tax returns had at least 1 recovery rebate credit math error. This represents 89 percent of all tax returns with at least 1 math error.⁴ The most common math errors were errors in computing the recovery rebate credit (more than 2.7 million) and the taxpayer not claiming the recovery rebate credit when eligible (more than 4 million).

³ The period from January through mid-April when most individual income tax returns are filed.

⁴ A return may contain more than one math error code.



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In addition, there were more than 1.3 million *e-file* rejects related to the recovery rebate credit as of April 17, 2009.⁵ This represents 7.7 percent of total *e-file* rejects. The most common reason *e-filed* tax returns with recovery rebate claims are being rejected is because the taxpayer already received the maximum economic stimulus payment and tried to claim the credit.

Although planning for the recovery rebate credit was generally successful, we noted areas where improvements were needed. Prior to Congress finalizing the Economic Stimulus Act of 2008, the IRS formed an Executive Steering Committee to coordinate and oversee the IRS-wide planning and implementation of the economic stimulus payment. The Steering Committee coordinated efforts among the various functions responsible for implementing the Act to ensure all aspects of the economic stimulus payment were implemented accurately and timely. However, the IRS dissolved the Executive Steering Committee in August 2008 prior to full implementation of the provisions in the Economic Stimulus Act. Planning for the recovery rebate credit was combined into the IRS' normal planning efforts for the annual filing season. To ensure the success of the annual filing season, the IRS had to divide its focus among several tax changes that needed to be implemented before the beginning of Calendar Year 2009. As a result, the IRS' focus on the implementation of the recovery rebate credit was diminished as the Submission Processing function balanced the need to implement other tax law changes without jeopardizing the timely processing of tax returns.

The Accuracy of the Internal Revenue Service's Computation of the Recovery Rebate Credit Was Very High

Our analysis of more than 102 million tax returns as of April 17, 2009,⁶ showed the IRS correctly calculated the recovery rebate credit on 99.6 percent (approximately 101.7 million) of the tax returns processed. We identified 399,099 tax returns (0.4 percent) for which our calculation of the recovery rebate credit and the IRS' calculation did not agree. These differences resulted in 258,550 taxpayers not receiving \$84.6 million to which they were entitled and 140,549 taxpayers receiving \$60.6 million more credits than they were entitled to receive. Differences resulted from errors in the IRS' computer programming as well as procedural errors in resolving IRS and taxpayer computation errors.

We identified and reported conditions to the IRS throughout our review and management took immediate action when possible to correct these errors. As a result, the impact on taxpayers and the IRS was significantly reduced.

⁵ The number of rejects will be higher than the number of returns rejected since a return can reject more than once.

⁶ The Returns Transaction File contains all edited, transcribed, and error-corrected data from the Form 1040 series and related forms for the current processing year and 2 prior years.



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Errors resulting in taxpayers not receiving recovery rebate credits to which they were entitled:

- 42,250 eligible taxpayers did not receive recovery rebate credits totaling \$17.7 million because the IRS did not compute the credit for eligible taxpayers when the taxpayers did not claim the credit on their tax returns and at least 1 Individual Taxpayer Identification Number⁷ was present on the returns. A taxpayer who files jointly with a spouse is eligible for the recovery rebate credit even if the child claimed on the tax return has an Individual Taxpayer Identification Number as long as both the taxpayer and the spouse have a valid SSN. This condition also included military taxpayers entitled to the credit regardless of the validity of their SSN under the Heroes Earnings Assistance and Relief Tax Act of 2008.⁸
- 216,300 eligible taxpayers did not receive recovery rebate credits totaling \$66.9 million because of manual processing errors made by examiners in the Error Resolution function.

Errors resulting in taxpayers receiving recovery rebate credits to which they were not entitled:

- 38,135 taxpayers incorrectly received recovery rebate credits totaling approximately \$17.9 million because the IRS incorrectly increased the taxpayers' credit claims for children with Individual Taxpayer Identification Numbers.
- 53,253 taxpayers incorrectly received recovery rebate credits totaling approximately \$22.9 million because the IRS incorrectly allowed the child portion of the recovery rebate credit on returns when taxpayers did not have the minimum qualifying income or a tax liability.
- 49,161 taxpayers incorrectly received recovery rebate credits totaling \$19.8 million because of manual processing errors made by examiners in the Error Resolution function.

A programming error could have allowed individuals claimed as a dependent on someone else's tax return to erroneously receive \$1.6 billion

In December 2008, we notified the IRS of a programming error that could have allowed almost 6.4 million taxpayers to receive almost \$1.6 billion in erroneous recovery rebate credits to which they were not entitled. Specifically, the Economic Stimulus Act of 2008 prohibits a taxpayer who can be claimed as a dependent on someone else's tax return from receiving the recovery rebate credit. However, initial programming for the recovery rebate credit did not disallow the credit when a taxpayer indicated he or she can be claimed as a dependent on someone else's tax return. The IRS function responsible for developing the computer programming requirements

⁷ An Individual Taxpayer Identification Number is issued by the IRS to individuals who are required to have a taxpayer identification number for tax purposes, but do not have and are not eligible to obtain an SSN.

⁸ Pub. L. No. 110-245, 122 Stat. 1624 (2008).



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was aware the IRS had the authority to systemically disallow these claims; however, the requirement was not communicated to the computer programmers. The IRS immediately corrected this error by revising its program.

In addition, although the IRS completed testing of the recovery rebate credit programming in January 2009, some errors were not corrected until after the IRS began processing tax returns. For example, we reviewed test documentation dated January 2009 that showed errors in the computation of the recovery rebate credit for some Married Filing Separately individuals. However, corrections to the program were not made until February 6, 2009; approximately 2 weeks after the IRS started processing tax returns. Consequently, 34,304 taxpayers did not receive recovery rebate credits totaling approximately \$10.7 million to which they were entitled. The IRS should ensure computer programs are tested far enough in advance of the upcoming filing season to ensure programming changes to correct errors identified in testing can be corrected prior to the IRS processing tax returns.

Management Actions

We reported our concerns with errors in the initial programming for the recovery rebate credit calculation for individuals who indicate they can be claimed as a dependent on someone else's tax return before the IRS began to process individual tax returns. The IRS took immediate action to address our concerns. As a result, the IRS was able to correctly prevent the issuance of recovery rebate credits totaling almost \$1.6 billion to almost 6.4 million taxpayers who indicated they could be claimed as someone else's dependent.

Legislation did not provide the IRS with math error authority to prevent individuals without valid SSNs from receiving the recovery rebate credit

The Economic Stimulus Act granted the IRS math error authority⁹ to handle some of the credit's eligibility requirements. However, it did not provide the IRS math error authority to address rebate claims filed by taxpayers who did not have a valid SSN. This would include taxpayers filing returns with an Individual Taxpayer Identification Number. Although the legislation prohibited such individuals from receiving the recovery rebate credit, the IRS was not provided with math error authority that would have enabled it to effectively prevent the issuance of recovery rebate credits to these individuals at the time a tax return was processed. As a result, the IRS erroneously issued more than \$27 million in recovery rebate credits to more than 44,000 taxpayers who did not have a valid SSN.¹⁰

⁹ Math error authority allows the IRS to systemically disallow certain taxpayer claims at the time a tax return is processed.

¹⁰ This includes more than 34,000 taxpayers with invalid primary or secondary SSNs who received recovery rebate credits totaling approximately \$23.5 million and 10,153 taxpayers who received approximately \$3.76 million in child rebate credits for children with an invalid SSN.



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We issued a memorandum to the IRS in September 2008 raising concerns about the impact of its lack of math error authority on its ability to effectively prevent recovery rebate credits on tax returns filed by individuals without a valid SSN. Because its Compliance function resources are limited, the IRS had to establish a processing tolerance for deficiency processing of claims on tax returns without a valid SSN. The IRS planned to allow any recovery rebate credit filed on a tax return without a valid SSN if the credit claimed was less than a specified amount. All claims more than that amount would be sent to the IRS Compliance function for deficiency processing.

We recommended that the IRS work with the Assistant Secretary of the Treasury for Tax Policy to obtain math error authority for recovery rebate claims on tax returns without a valid SSN. IRS management responded that they had raised concerns to the Assistant Secretary about the lack of math error authority for this issue. However, no legislative proposal was put forth to provide this authority.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 1: Issue recovery payments to the 34,304 individuals who did not receive the recovery rebate credit to which they were entitled as a result of programming errors in computing the credit for Married Filing Separately taxpayers.

Management's Response: The IRS agreed with the intent of this recommendation. The IRS is currently reviewing the data provided by the Treasury Inspector General for Tax Administration and will provide appropriate taxpayer relief, if warranted, based on the results of its review.

Recommendation 2: Issue recovery payments to the 258,550 individuals we identified who did not receive the full recovery rebate credit to which they were entitled as a result of computer programming and Error Resolution function errors. The IRS should continue to identify additional taxpayers not receiving the full credit to which they are entitled for those tax returns processed after April 17, 2009.

Management's Response: The IRS agreed with the intent of this recommendation. The IRS is currently reviewing the data provided by the Treasury Inspector General for Tax Administration and will provide appropriate taxpayer relief, if warranted, based on the results of its review. In addition, the IRS will identify any additional taxpayers who filed their returns after April 17, 2009, and did not receive the full credit to which they were entitled and will ensure that they are also provided with the appropriate relief.



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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to evaluate the effectiveness of the IRS' efforts to plan and implement the TY 2008 Recovery Rebate Credit. To accomplish our objective, we:

- I. Evaluated the effectiveness of the IRS' planning process for the implementation of the recovery rebate credit.
 - A. Obtained and reviewed the IRS' overall and functional action plans for implementation.
 - B. Evaluated the adequacy of the IRS' plans for educating and assisting individuals in ensuring they receive the proper recovery rebate credit.
 - C. Evaluated the IRS' readiness plans for processing individual tax returns that are eligible for or claim the recovery rebate credit.
- II. Evaluated the accuracy of the IRS processing of individual tax returns eligible for the recovery rebate credit.
 - A. Verified, through computer analysis of all approximately 102 million individual tax returns from the IRS Individual Returns Transaction File¹ processed between January 1 and April 17, 2009, that only eligible taxpayers received the recovery rebate credits and that the credit amounts were accurate. This computer verification was completed using our calculations based upon the legal requirements of the Economic Stimulus Act of 2008.² We assessed the reliability of the Returns Transaction File by verifying samples of the fields needed to determine the credit agreed with the information present on the IRS Integrated Data Retrieval System.³
 - B. Calculated the amount of the recovery rebate credits that should have been allowed to the 34,304 Married Filing Separately taxpayers where an IRS programming error led to those taxpayers not receiving the correct amount.
 - C. Determined that the recovery rebate credit amounts per the IRS in 399,131 tax returns did not agree with our calculations and further determined, to the extent possible, why

¹ The Returns Transaction File contains all edited, transcribed, and error-corrected data from the U.S. Individual Income Tax Returns (Form 1040 series) and related forms for the current processing year and 2 prior years.

² Pub. L. 110-185, 122 Stat. 613.

³ IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.



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those differences existed. We calculated the correct recovery rebate credit amounts for the 399,099 tax returns where we could determine the reasons for the differences.



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Appendix II

Major Contributors to This Report

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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
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Appendix IV

Outcome Measures

Throughout this review, we notified the IRS of conditions that impacted its ability to ensure only eligible individuals were allowed the recovery rebate credit and for the correct amount. In response, the IRS took corrective actions that limited the number and amount of credit errors. This appendix presents detailed information on the measurable impact of those corrective actions. These benefits will be incorporated into our Semiannual Report to Congress.

For all of the outcomes listed in this appendix, we conducted computer analyses of the IRS Returns Transaction File¹ for 102,073,044 individual tax returns processed between January 1 and April 17, 2009. These analyses determined from the information recorded for all returns if the taxpayers were eligible for the recovery rebate credit and the correct amount of the credit. This information was compared with additional data from the Returns Transaction File that showed the recovery rebate credits allowed by the IRS to the taxpayers.

Type and Value of Outcome Measure:

- Revenue Protected – Actual; \$1,576,636,877 in recovery rebate credits prevented from being issued to 6,387,101 taxpayers who could be claimed on someone else’s tax return (see page 6).

Methodology Used to Measure the Reported Benefit:

In December 2008, prior to the start of the filing season,² we notified the IRS of a programming error that would have allowed individuals who can be claimed as a dependent on someone else’s tax return to incorrectly receive the recovery rebate credit. The IRS implemented a programming change to correct this error before any returns were processed. We identified all individual tax returns through computer analysis where the taxpayer indicated they could be claimed as a dependent on someone else’s return and would have otherwise qualified for the recovery rebate credit. This analysis identified a total of 6,387,101 taxpayers that would have been incorrectly allowed the recovery rebate credit if the programming change had not been made. We then calculated the recovery rebate credit amounts that would have been allowed for each taxpayer based upon the filing status, income, and tax information reported on the tax return.

¹ The Returns Transaction File contains all edited, transcribed, and error-corrected data from the U.S. Individual Income Tax Returns (Form 1040 series) and related forms for the current processing year and 2 prior years.

² The period from January through mid-April when most individual income tax returns are filed.



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Type and Value of Outcome Measure:

Funds Put to Better Use – Actual; \$27,300,599 in recovery rebate credits erroneously allowed to 44,261 taxpayers with invalid SSNs³ (see page 6).

Methodology Used to Measure the Reported Benefit:

We issued a memorandum to the IRS in September 2008 raising concerns about the impact of the lack of math error authority on the IRS' ability to effectively prevent recovery rebate credits on tax returns filed by individuals who did not have a valid SSN. Because its Compliance function resources are limited, the IRS had to establish a processing tolerance for deficiency processing of claims on tax returns without valid SSNs. Our analysis of the IRS Returns Transaction File identified 46,628 individuals with an invalid SSN for which the IRS generated recovery rebate credits \$29,882,962. We determined that 2,367 of these tax returns with recovery rebate credits totaling \$2,582,363 were identified for deficiency processing. Therefore, we concluded that the IRS incorrectly allowed recovery rebate credits totaling \$27,300,599 to 44,261 taxpayers who were not eligible for the credit because they had an invalid SSN.

Type and Value of Outcome Measure:

Taxpayer Rights and Entitlements – Actual; 258,550 taxpayers did not receive \$84,565,597 in recovery rebate credits to which they were entitled (see page 6).

Methodology Used to Measure the Reported Benefit:

Based on our analysis of the 102,073,044 individual tax returns processed between January 1 and April 17, 2009, we identified 258,550 taxpayers who did not receive recovery rebate credits totaling \$84,565,597 to which they were entitled. This was the result of errors in the IRS' computer programming to calculate the credit as well as in its manual processes to resolve recovery rebate errors. Specifically:

- 42,250 eligible taxpayers did not receive recovery rebate credits totaling \$17,667,277 because the IRS did not compute the credit for eligible taxpayers when the taxpayer did not claim the credit on his or her tax return and at least 1 Individual Taxpayer Identification Number⁴ was present on the tax return. A taxpayer who files jointly with a spouse is eligible for the rebate credit even if the child claimed on the tax return has an Individual Taxpayer Identification Number as long as both the taxpayer and the spouse have a valid SSN. This

³ Including Individual Taxpayer Identification Numbers.

⁴ An Individual Taxpayer Identification Number is issued by the IRS to individuals who are required to have a taxpayer identification number for tax purposes, but do not have and are not eligible to obtain an SSN.



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condition also included military taxpayers entitled to the credit regardless of the validity of their SSN under the Heroes Earnings Assistance and Relief Tax Act of 2008.⁵

- 216,300 eligible taxpayers did not receive recovery rebate credits totaling \$66,898,320 because of manual processing errors made by examiners in the Error Resolution function.

⁵ Pub. L. No. 110-245, 122 Stat. 1624 (2008).



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Appendix V

*Treasury Inspector General for Tax Administration
Coverage of the Economic Stimulus Act of 2008*

Our review of the recovery rebate credit is the fourth in a series of reviews conducted by the Treasury Inspector General for Tax Administration that evaluated the IRS' implementation of the Economic Stimulus Act of 2008.¹ These reviews evaluated the implementation of the Act from the initial advanced economic stimulus payments through issuance of the recovery rebate credits. A list of the audit reports issued to date is provided below.

- *Evaluation of Planning Efforts for the Issuance of Economic Stimulus Payments* (Reference Number 2008-40-149, dated July 31, 2008).
- *Evaluation of the Computation of Economic Stimulus Payments* (Reference Number 2008-40-174, dated September 4, 2008).
- *Evaluation of Efforts to Ensure Eligible Individuals Received Their Economic Stimulus Payment* (Reference Number 2009-40-069, dated April 24, 2009).

¹ Pub. L. 110-185, 122 Stat. 613.



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Appendix VI

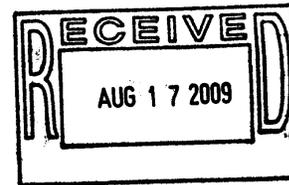
Management's Response to the Draft Report



DEPUTY COMMISSIONER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

August 17, 2009



MEMORANDUM FOR MICHAEL R. PHILLIPS
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Linda E. Stiff *LES*
Deputy Commissioner for Services and Enforcement

SUBJECT: Draft Audit Report – Evaluation of the Planning, Computation,
and Issuance of the Recovery Rebate Credit
(Audit #200840030.04)

I reviewed the subject draft report and appreciate your review of our planning and implementation of the 2008 Recovery Rebate Credit (RRC). Thank you for recognizing our efforts to update tax forms, instructions, publications, and the IRS.gov website to inform and educate taxpayers on how to compute and claim the RRC. These efforts included:

- Developing the *Recovery Rebate Credit Worksheet* to assist taxpayers in computing any RRC they may be due;
- Developing resource guides for volunteers at free tax assistance sites and for IRS employees working in Taxpayer Assistance Centers and Toll-Free sites;
- Distributing information to the public via the media on RRC eligibility criteria and how to claim the credit;
- Updating the U.S. Individual Income Tax Return (Form 1040) and related instructions as well as other tax publications such as Publication 17, *Your Federal Income Tax (For Individuals)* to include information to assist taxpayers in claiming the RRC;
- Developing a RRC webpage called the *Recovery Rebate Credit Information Center*, and
- Developing online tools, available on IRS.gov, to assist taxpayers in computing their RRC.

Despite our efforts, it was evident taxpayers were having difficulty in computing the RRC. Your review identified several problem areas where taxpayers may have been confused. We took immediate action to clarify these issues in the Form 1040 instructions. These actions included:



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- Revising the Form 1040 instructions to explain that the Economic Stimulus Payment and the RRC were similar; and
- Adding specific RRC eligibility requirements to Form 1040 instructions preceding the rebate credit worksheet, so that taxpayers could determine if they were eligible for the credit.

Your review also identified several errors in the initial programming of the RRC. Once problem areas were identified, we took immediate action and corrected all programming issues. One example was the RRC calculation for individuals who indicate they can be claimed as a dependent on someone else's tax return. This error allowed the credit for these individuals when it should have been disallowed. Once this problem was identified, we took immediate action and revised the programming. As a result, we were able to prevent credits totaling almost \$1.6 billion to about 6.4 million impacted taxpayers.

Lastly, your auditors identified over 290,000 tax accounts that may need to be corrected. A review is currently being conducted and the appropriate taxpayer relief, if warranted, will be identified for correction by January 2010.

I agree with the outcome measures reported in Appendix IV. However, I think it is appropriate to point out that the \$27,300,599 in recovery rebate credits allowed to 44,261 taxpayers with invalid Social Security Numbers were not "erroneously allowed" as stated in Appendix IV. This is because the implementing legislation did not grant IRS the math error authority necessary to prevent issuance of the credit to these taxpayers at the time their returns were processed.

Attached are our comments to your recommendations. If you have any questions, please call me at (404) 338-7060, or members of your staff may contact Peter Stipek, Director, Customer Account Services, Wage and Investment Division, at (404) 338-8910.

Attachment



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Attachment

The Commissioner, Wage and Investment Division, should:

RECOMMENDATION 1

Issue recovery payments to the 34,304 individuals who did not receive the recovery rebate credit to which they were entitled as a result of programming errors in computing the credit for Married Filing Separate taxpayers.

CORRECTIVE ACTION

We agree with the intent of this recommendation. We are currently reviewing the data provided by the Treasury Inspector General for Tax Administration (TIGTA) and will provide appropriate taxpayer relief, if warranted, based on the results of our review.

IMPLEMENTATION DATE

January 15, 2010

RESPONSIBLE OFFICIAL

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

CORRECTIVE ACTION MONITORING PLAN

Upon completion of our review, any corrective action will be monitored as part of our internal managerial control system.

RECOMMENDATION 2

Issue recovery payments to the 258,550 individuals we identified who did not receive the full recovery rebate credit to which they were entitled as a result of computer programming and Error Resolution function errors. The IRS should continue to identify additional taxpayers not receiving the full credit to which they are entitled for those tax returns processed after April 17, 2009.

CORRECTIVE ACTION

We agree with the intent of this recommendation. We are currently reviewing the data provided by the TIGTA and will provide appropriate taxpayer relief, if warranted, based on the results of our review. In addition, we will identify any additional taxpayers who filed their returns after April 17, 2009, and did not receive the full credit to which they were entitled, and ensure that they are also provided with the appropriate relief.

IMPLEMENTATION DATE

January 15, 2010



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RESPONSIBLE OFFICIAL

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

CORRECTIVE ACTION MONITORING PLAN

Upon completion of our review, any corrective action will be monitored as part of our internal managerial control system.