



Treasury Inspector General for Tax Administration Office of Audit

IMPROVEMENTS ARE NEEDED TO VERIFY REFUNDS TO NONRESIDENT ALIENS BEFORE THE REFUNDS ARE SENT OUT OF THE UNITED STATES

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Highlights

Highlights of Report Number: 2010-40-121 to the Internal Revenue Service Deputy Commissioner for Services and Enforcement.

IMPACT ON TAXPAYERS

Control weaknesses in the processing of refunds issued to nonresident aliens could result in significant revenue losses to the United States (U.S.). The probability of recovering fraudulent refunds from nonresidents living outside the U.S. is very low.

WHY TIGTA DID THE AUDIT

The objective of this audit was to review the processing of U.S. Nonresident Alien Income Tax Returns (Form 1040NR) and determine whether controls are in place to ensure taxpayers receiving refunds are entitled to those refunds.

WHAT TIGTA FOUND

Although a statistical sample of Tax Year 2008 returns indicated that control weaknesses discussed in this report had not been exploited to a significant extent, a judgmental sample of Tax Year 2007 and 2008 returns revealed significant control weaknesses in the processing of refunds claimed on Forms 1040NR.

If the Internal Revenue Service (IRS) does not take immediate steps to address these control weaknesses, the problem could increase significantly. The questionable refunds in the 40 cases that TIGTA identified were very high, totaling more than \$2.3 million. During this audit, TIGTA discussed these control weaknesses with the IRS and it is working on actions to address them.

TIGTA also found that tax treaty provisions regarding the taxability of gambling income are not being applied consistently by the IRS, and that other clarification is needed regarding the designation of certain income as U.S. source income.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Commissioner, Large and Mid-Size Business Division, ensure that plans, developed during the course of this audit to address control weaknesses discussed in this report, are implemented. The Commissioner should also work with the Forms and Publications function to clarify instructions on what constitutes U.S source income.

In their response to the report, IRS officials agreed with the recommendations and plan to take appropriate corrective actions.

READ THE FULL REPORT

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

<http://www.treas.gov/tigta/auditreports/2010reports/201040121fr.pdf>.