



## Treasury Inspector General for Tax Administration Office of Audit

### EXPANDED ACCESS TO WAGE AND WITHHOLDING INFORMATION CAN IMPROVE IDENTIFICATION OF FRAUDULENT TAX RETURNS

Issued on September 30, 2010

## Highlights

Highlights of Report Number: 2010-40-129 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

### IMPACT ON TAXPAYERS

As of April 17, 2010, the Internal Revenue Service (IRS) identified 249,185 tax returns with \$1.51 billion being claimed in fraudulent refunds. While the IRS has shown a significant increase in the number of fraudulent tax returns identified and refunds stopped, it needs expanded and expedited access to wage and withholding information to assist in its efforts.

### WHY TIGTA DID THE AUDIT

This audit was initiated because unscrupulous individuals continue to submit tax returns with false income documents to the IRS for the sole purpose of receiving a fraudulent refund. In October 2009, the IRS transferred responsibility for its pre-refund fraudulent tax return detection activities to its Accounts Management function. Management noted that transferring these activities will capitalize on opportunities to complete this work more efficiently. Our overall objective was to assess the IRS's Taxpayer Assurance Program processes to identify potentially fraudulent tax returns for screening.

### WHAT TIGTA FOUND

Expanded and expedited access to wage and withholding information would significantly increase the IRS's ability to more efficiently and effectively verify wage and withholding information reported on a tax return when processed. Our analysis of the 151,776 Tax Year 2008 tax returns sent to an examiner for screening and then released for processing identified that 96,178 (63 percent) of these tax returns had valid wages reported. TIGTA estimates that the IRS needlessly expended 22,110 hours screening these tax returns. Currently, the law limits IRS access to the United States Department of Health and Human Services wage information. In addition, processes have not been

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developed to expedite the use of wage and withholding data received from the Social Security Administration.

In addition, TIGTA found that the majority of tax returns the IRS identifies as being filed by prisoners are not being sent to screening to assess fraud potential. Our review identified 253,929 (88 percent) of the 287,918 tax returns filed by a prisoner as of March 24, 2010, were not selected for screening. Of those tax returns not screened, 48,887 individuals had no wage information reported to the IRS by employers. These 48,887 prisoners claimed refunds totaling more than \$130 million including Earned Income Tax Credit claims of \$78.5 million. Some of these refunds may have been stopped by other compliance activities. For example, TIGTA found that the IRS prevented the issuance of nearly \$18.1 million in Earned Income Tax Credit claims for 4,532 of the 48,887 prisoner tax returns.

### WHAT TIGTA RECOMMENDED

Legislation is needed to expand IRS access to the United States Department of Health and Human Services wage information. TIGTA recommended that the Commissioner, Wage and Investment Division, develop a process to expedite the availability of wage and withholding information received from the Social Security Administration. The Commissioner should also verify whether the 48,887 tax returns with tax refunds that were filed by prisoners with no reported wages were fraudulent and identify revisions that could be made to data mining criteria to better identify fraudulent tax returns filed by prisoners.

In their response to the report, IRS officials fully agreed with three recommendations and partially agreed with the other.

### 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/201040129fr.pdf>.

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