



Treasury Inspector General for Tax Administration Office of Audit

LOW PARTICIPATION AND TAX RETURN VOLUMES CONTINUE TO HINDER THE TRANSITION OF INDIVIDUAL INCOME TAX RETURNS TO THE MODERNIZED E-FILE SYSTEM

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Highlights

Highlights of Report Number: 2011-40-131 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

IMPACT ON TAXPAYERS

The Internal Revenue Service (IRS) continues to transition from its existing electronic filing (*e-file*) platform, referred to as the Legacy *e-File* system, to a modernized, Internet-based system, the Modernized *e-File* (MeF) system. The MeF system provides real-time processing of tax returns and extensions that will improve error detection, standardize business rules, and expedite acknowledgments.

WHY TIGTA DID THE AUDIT

This audit was initiated because, once fully implemented, the MeF system will replace the current Legacy *e-file* system. The objective of this review was to evaluate the continued implementation of the MeF system to determine whether individual income tax returns will be accurately and timely processed and whether sufficient progress is being made to replace the Legacy *e-File* system.

WHAT TIGTA FOUND

Processes used to test and monitor the MeF system do not ensure MeF system business rules designed to validate basic requirements on a tax return are working as intended. As a result, the IRS continues to have limited assurance that the MeF system is accurately processing individual tax returns. Ineffective or insufficient monitoring of tax return processing increases the risk that tax returns processed through the MeF system will be erroneously accepted or rejected. This risk will grow significantly as the volume of tax returns processed through the MeF system increases and the types of forms and schedules are expanded.

In addition, lower than expected tax return transmitter participation and tax return volumes raise significant concerns regarding the IRS's ability to fully replace the

Legacy *e-File* system for the 2013 Filing Season. For example, only 19 (28 percent) of the 67 tax return preparation software packages used to file tax returns in the Legacy *e-File* system were used to file MeF tax returns. Also, the IRS received only 8.7 million individual tax returns through the MeF system as of April 18, 2011, significantly lower than the 35 million tax returns the IRS expected for the 2011 Filing Season.

Finally, one of the key benefits of the MeF system is the ability for taxpayers to scan and attach supplemental information to their *e-filed* tax returns. However, the IRS has not pursued the use of the MeF system as an option when individuals are required to provide specific documentation with their tax returns.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Commissioner, Wage and Investment Division, develop a comprehensive testing plan to ensure MeF system processing is accurate and adheres to the methodology developed. In addition, the IRS should correct the 12 errors TIGTA identified in our prior review of MeF system processing and continue to work with tax return transmitters and States to identify and address concerns with MeF system performance. The IRS should also ensure MeF system testing includes testing of system performance, stability of web services, and processing capacity. Finally, the IRS should adequately test the MeF system's ability to receive, process, store, and retrieve tax return attachments and promote the use of such attachments.

IRS management agreed with four of our six recommendations. Management disagreed with our recommendation to develop a comprehensive testing plan and indicated that the MeF system was developed under the Enterprise Life Cycle guidance, which included various testing and certification processes. Notwithstanding, the IRS's three-phase plan to test the processing of tax returns through the MeF system in the 2011 Filing Season was incomplete, and the IRS did not fully execute the steps in the test plan.

Management also disagreed with the recommendation to correct the 12 errors TIGTA identified in its review during the 2010 Filing Season that resulted in incorrect notifications to taxpayers when tax returns were rejected. The IRS indicated it had already corrected this problem; however, it has not provided any evidence the problem has been corrected.

READ THE FULL REPORT

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

<http://www.treas.gov/tigta/auditreports/2011reports/201140131fr.pdf>

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