



RECOVERY ACT

*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative
Motor Vehicle Credits*

January 21, 2011

Reference Number: 2011-41-011

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.

Redaction Legend:

1= Tax Return/Return Information



HIGHLIGHTS



INDIVIDUALS RECEIVED MILLIONS OF DOLLARS IN ERRONEOUS PLUG-IN ELECTRIC AND ALTERNATIVE MOTOR VEHICLE CREDITS

Highlights

Final Report issued on January 21, 2010

Highlights of Reference Number: 2011-41-011 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

IMPACT ON TAXPAYERS

The American Recovery and Reinvestment Act of 2009 (Recovery Act) included a number of provisions that encourage the purchase of motor vehicles that operate on clean renewable sources of energy. Individuals claimed more than \$163.9 million in plug-in electric and alternative motor vehicle credits from January 1 through July 24, 2010. Agencies are required to ensure Recovery Act funds are used for authorized purposes and appropriate measures are taken to prevent fraud, waste, and abuse.

WHY TIGTA DID THE AUDIT

This audit was initiated because TIGTA is required to monitor the Internal Revenue Service's (IRS) implementation of Recovery Act provisions. Our overall objective was to assess the effectiveness of IRS processes to identify and prevent erroneous claims for the plug-in electric vehicle credit and alternative motor vehicle credit for tax returns filed from January 1 through July 24, 2010.

WHAT TIGTA FOUND

As of July 24, 2010, TIGTA identified 12,920 individuals who electronically filed their tax returns and erroneously claimed \$33 million in plug-in electric and alternative motor vehicle credits. In addition, 1,719 of the 12,920 individuals also erroneously reduced the amount of Alternative Minimum Tax owed by almost \$5.3 million. During this review, management took corrective actions to reduce erroneous claims when process weaknesses were brought to their attention. These actions have resulted in

an estimated \$3.1 million in revenue protected. The erroneous claims TIGTA identified resulted from inadequate IRS processes to ensure information reported by individuals claiming plug-in electric and alternative motor vehicle credits met qualifying requirements for vehicle year, placed in-service date, and make and model.

In addition, TIGTA found that the IRS is unable to track and account for plug-in electric and alternative motor vehicle credits claimed by individuals on paper-filed tax returns. Processes were not established to capture this information from paper-filed tax returns.

Finally, our review of electronically filed tax returns also identified individuals who erroneously claimed the same vehicle for multiple plug-in electric and alternative motor vehicle credits or claimed an excessive number of vehicles for personal use credits. TIGTA also identified improper claims for the credits by prisoners and IRS employees. TIGTA has referred the information on the IRS employees to its Office of Investigations for further review.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Commissioner, Wage and Investment Division, develop Error Resolution System procedures to not allow credits for vehicles with nonqualifying years, initiate actions to recover erroneous credits identified by TIGTA, and either develop a coding system to identify vehicle makes and models or require the Vehicle Identification Number on the forms used to claim plug-in electric and alternative motor vehicle credits.

IRS management agreed with the recommendations and plans to update procedures to require a review of the make, model, and date vehicles were placed in service to ensure credits are being claimed for qualifying vehicles. In addition, the IRS plans to add a new line on the forms used to claim the credits to require a Vehicle Identification Number and has requested that *e-file* software providers implement programming changes to allow taxpayers to select the make, model, and year of qualifying vehicles from a drop-down menu. The IRS also plans to recover erroneous claims by reversing credits and conducting audits.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

January 21, 2011

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

FROM: *Michael R. Phillips*
Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor Vehicle Credits
(Audit # 201040131)

This report presents the results of our review to assess the effectiveness of Internal Revenue Service (IRS) processes to identify and prevent erroneous claims for the plug-in electric vehicle credit and the alternative motor vehicle credit for tax returns filed from January 1 through July 24, 2010. This review was included in our Fiscal Year 2010 Annual Audit Plan and addresses the major management challenges of Implementing Tax Law Changes and Erroneous and Improper Credits and Payments.

The American Recovery and Reinvestment Act of 2009 (Recovery Act)¹ provides separate funding to the Treasury Inspector General for Tax Administration through September 30, 2013, to be used in oversight activities of IRS programs. This audit was conducted using Recovery Act funds.

Management's complete response to the draft report is included as Appendix V.

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.

¹ Pub. L. No. 111-5, 123 Stat. 115 (2009).



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Table of Contents

BackgroundPage 1

Results of ReviewPage 3

 Processes Were Not Established to Track and Account for
 Recovery Funds Claimed for Plug-in Electric Vehicle CreditsPage 3

 Individuals Claimed Erroneous Plug-in Electric and
 Alternative Motor Vehicle Credits.....Page 5

Recommendations 1 and 2:Page 8

Recommendation 3:.....Page 10

Recommendation 4:Page 13

Recommendation 5:Page 14

 Plug-in Electric and Alternative Motor Vehicle Credits
 Are Being AbusedPage 14

Recommendations 6 through 8:.....Page 16

Appendices

 Appendix I – Detailed Objective, Scope, and MethodologyPage 18

 Appendix II – Major Contributors to This ReportPage 21

 Appendix III – Report Distribution ListPage 22

 Appendix IV – Outcome Measures.....Page 23

 Appendix V – Management’s Response to the Draft ReportPage 26



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Abbreviations

AMT	Alternative Minimum Tax
<i>e-filed; e-filing</i>	Electronically filed; electronic filing
IRS	Internal Revenue Service
TIGTA	Treasury Inspector General for Tax Administration



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Background

The American Recovery and Reinvestment Act of 2009 (Recovery Act)¹ included a number of provisions that encourage the purchase of motor vehicles (or the conversion of motor vehicles to those) that operate on clean renewable sources of energy. Figure 1 provides a comparison of the plug-in electric and alternative motor vehicle credit provisions included in the Recovery Act.

Figure 1: Plug-in Electric and Alternative Motor Vehicle Credits Comparison

Criteria	Plug-in Electric Vehicle Credit	Plug-in Electric Vehicle Conversion Credit	Qualified Plug-in Electric Drive Motor Vehicle Credit	Alternative Motor Vehicle (Nonconversion) Credit
Credit Requirements	Qualified Plug-in Electric and Electric Vehicle Credit (Form 8834)	Alternative Motor Vehicle Credit (Form 8910)	Qualified Plug-in Electric Drive Motor Vehicle Credit (Form 8936)	Alternative Motor Vehicle Credit (Form 8910)
Form Needed to Claim Credit				
How Calculated	Lesser of 10% vehicle cost or maximum vehicle credit	Lesser of 10% cost of vehicle conversion or maximum vehicle credit	\$2,500 plus \$417 per kw/hr in excess of 4.0	Varies with type of vehicle
Maximum Credit Per Vehicle	\$2,500	\$4,000	\$7,500 - \$15,000 depending on gross vehicle weight rating	Varies with type of vehicle
Maximum Vehicles Per Return	Unlimited	Unlimited	Unlimited	Unlimited
Additional Restrictions or Requirements	No double benefit is allowed. A vehicle that qualifies for credit on Form 8910 will not qualify for credit on Form 8834 or Form 8936. A vehicle that qualifies for credit with Form 8834 or 8936 may be claimed on one or the other, but not both.			
	Business use credit is claimed as part of the General Business Credit on General Business Credit (Form 3800).			
	Personal use credit must be reduced by any amount of business use credit.			
	*Credit is limited to reduction of regular and Alternative Minimum Tax (AMT) (i.e., nonrefundable). The AMT may be reduced only by personal part of the credit.			
Qualifying Vehicle				
New or Used	New Only	New or Used	New Only	New Only
Placed In-Service	After 2/17/2009	After 2/17/2009	After 12/31/2008	After 12/31/2008
Additional Restrictions or Requirements	For use on public roads, streets, and highways.			
	Original use must commence with taxpayer claiming credit.			
	If vehicle ceases to qualify for credit, part or all of credit is subject to recapture.			
	Manufacturer's or domestic distributor's certification that vehicle qualifies for credit may be relied on, unless certification has been revoked by the Internal Revenue Service.			

Source: Treasury Inspector General for Tax Administration (TIGTA) analysis of Internal Revenue Code Sections 30, 30B, and 30D.

¹ Pub. L. No. 111-5, 123 Stat. 115 (2009).



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Figure 2 details the number of claims and amounts claimed on electronically filed (*e-filed*) tax returns for plug-in electric and alternative motor vehicle credits.

Figure 2: Amounts Claimed on E-Filed Tax Returns for Plug-in Electric and Alternative Motor Vehicle Credits As of July 24, 2010

	Form 8834	Form 8910		Form 8936	Total
		Conversions Only	Alternative Motor Vehicle Credits		
Individuals Claiming Credit	2,769	1,522	52,006	13,204	69,501
Credits Claimed	\$3,767,832	\$3,940,612	\$85,405,698	\$70,813,609	\$163,927,751

Source: TIGTA analysis of e-filed tax return volumes from January 1 through July 24, 2010.

Recovery Act activities require a high level of scrutiny, and taxpayer dollars spent on economic recovery must be subject to unprecedented levels of transparency and accountability. Federal agencies are required to ensure Recovery Act funds are used for authorized purposes and that appropriate measures are taken to prevent fraud, waste, and abuse. As such, the TIGTA is required to monitor the Internal Revenue Service's (IRS) implementation of Recovery Act provisions. This audit was conducted to meet those requirements.

This review was performed at the Wage and Investment Division Headquarters in Atlanta, Georgia; the Submission Processing function offices in Lanham, Maryland, and Cincinnati, Ohio; and the Submission Processing Site in Austin, Texas, during the period April through September 2010. 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.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Results of Review

Processes Were Not Established to Track and Account for Recovery Funds Claimed for Plug-in Electric Vehicle Credits

The IRS is unable to track and account for plug-in electric and alternative motor vehicle credits claimed by individuals on paper-filed tax returns. Processes were not established to capture information from the following paper-filed tax forms:

- Qualified Plug-in Electric and Electric Vehicle Credit (Form 8834).
- Plug-in electric vehicle conversion credits on Alternative Motor Vehicle Credit (Form 8910).
- Qualified Plug-in Electric Drive Motor Vehicle Credit (Form 8936).

Plug-in electric vehicle credits claimed on Forms 8834, 8910, and 8936 are carried forward from these forms to the U.S. Individual Income Tax Return (Form 1040), Line 53. Line 53 includes plug-in electric vehicle credit amounts and can include credit amounts from at least 10 other tax credit forms. For credits claimed on *e-filed* tax returns, IRS data files can be used to identify individuals and amounts claimed for plug-in electric vehicle credits. However, for paper-filed tax returns, the IRS did not establish processes to transcribe and capture in IRS data files information relating to plug-in electric vehicle credits claimed. As a result, the IRS is unable to track and account for plug-in electric vehicle credits claimed on paper-filed tax returns.

Figure 3 shows an example of Line 53 on Form 1040 and the instructions to the individuals completing this line.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Figure 3: Example of Line 53 on Form 1040 and Instructions

Tax and Credits	38	Amount from line 37 (adjusted gross income)	38	
	39a	Check <input type="checkbox"/> You were born before January 2, 1945, <input type="checkbox"/> Blind. Total boxes if: <input type="checkbox"/> Spouse was born before January 2, 1945, <input type="checkbox"/> Blind. checked ▶ 39a		
	b	If your spouse itemizes on a separate return or you were a dual-status alien, see page 35 and check here ▶ 39b <input type="checkbox"/>		
Standard Deduction for—	40a	Itemized deductions (from Schedule A) or your standard deduction (see left margin)	40a	
• People who check any box on line 39a, 39b, or 40b or who can be claimed as a dependent, see page 35.	b	If you are increasing your standard deduction by certain real estate taxes, new motor vehicle taxes, or a net disaster loss, attach Schedule L and check here (see page 35) ▶ 40b <input type="checkbox"/>		
• All others:	41	Subtract line 40a from line 38	41	
Single or Married filing separately, \$5,700	42	Exemptions. If line 38 is \$125,100 or less and you did not provide housing to a Midwestern displaced individual, multiply \$3,650 by the number on line 6d. Otherwise, see page 37	42	
Married filing jointly or Qualifying widow(er), \$11,400	43	Taxable income. Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-	43	
Head of household, \$8,350	44	Tax (see page 37). Check if any tax is from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972	44	
	45	Alternative minimum tax (see page 40). Attach Form 6251	45	
	46	Add lines 44 and 45 ▶	46	
	47	Foreign tax credit. Attach Form 1116 if required	47	
	48	Credit for child and dependent care expenses. Attach Form 2441	48	
	49	Education credits from Form 8863, line 29	49	
	50	Retirement savings contributions credit. Attach Form 8880	50	
	51	Child tax credit (see page 42)	51	
	52	Credits from Form: a <input type="checkbox"/> 8396 b <input type="checkbox"/> 8839 c <input type="checkbox"/> 5695	52	
	53	Other credits from Form: a <input type="checkbox"/> 3800 b <input type="checkbox"/> 8801 c <input type="checkbox"/>	53	
	54	Add lines 47 through 53. These are your total credits	54	
	55	Subtract line 54 from line 46. If line 54 is more than line 46, enter -0- ▶	55	

Line 53
Other Credits

Include the following credits on line 53 and check the appropriate box(es). If box c is checked, also enter the applicable form number. To find out if you can take the credit, see the form or publication indicated.

- Credit for the elderly or the disabled. See Schedule R.
- District of Columbia first-time homebuyer credit. See Form 8859.
- Qualified plug-in electric drive motor vehicle credit. See Form 8936.
- Qualified plug-in electric vehicle credit. See Form 8834, Part I.
- Qualified electric vehicle credit. You cannot claim this credit for a vehicle placed in service after 2006. You can claim this credit only if you have a passive activity electric vehicle credit carried forward from a prior year. See Form 8834, Part II.
- Alternative motor vehicle credit. See Form 8910 if you placed an alternative motor vehicle (such as a qualified hybrid vehicle) in service during 2009 or converted a motor vehicle to a qualified plug-in electric drive motor vehicle and placed it in service after February 17, 2009.
- Alternative fuel vehicle refueling property credit. See Form 8911.
- General business credit. This credit consists of a number of credits that usually apply only to individuals who are partners, shareholders in an S corporation, self-employed, or who have rental property. See Form 3800 or Pub. 334.
- Credit for prior year minimum tax. If you paid alternative minimum tax in a prior year, see Form 8801.
- Credit to holders of tax credit bonds. See Form 8912.

Source: 2009 Form 1040 and Instructions.

Government-wide guidance for carrying out the programs and activities of the Recovery Act was issued to include steps Federal agencies must take to meet the goals and to implement the Act effectively. Reporting activities are designed to track Recovery Act tax provision benefits. The Department of the Treasury’s Recovery Act Plan: Tax Provision Implementation Program states that “The Department of the Treasury will provide an estimate of benefits to individuals, businesses, and state and local governments as data becomes available.”

On December 16, 2009, we alerted IRS management of the inability to track and account for plug-in electric and alternative motor vehicle credits claimed by individuals on paper-filed tax returns. We recommended that the IRS implement programming to enable it to track and account for plug-in electric vehicle credits claimed on paper-filed tax returns.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Management Actions

- February 4, 2010 – IRS management agreed that processes need to be in place for transparent reporting of Recovery Act-related credits and responded that existing and newly created processes will allow it to report on the use of these credits. Programming was to be implemented to enable the IRS to track and account for funds allocated as part of tax provisions included in the Recovery Act for individuals claiming plug-in electric vehicle credits on paper-filed tax returns. The implementation date for the programming was originally February 18, 2010, but was delayed to the end of April 2010, due to the IRS's Modernization and Information Technology Services workload. The IRS subsequently informed us that they decided to delay identifying and tracking these credits until the beginning of the 2011 Filing Season because the April peak processing period had passed.
- September 16, 2010 – In response to the 2010 Filing Season Audit Report,² IRS management agreed to submit programming requests to enable the IRS to capture the data needed from Forms 8834, 8910, and 8936.

We will include tests in our 2011 Filing Season Review to evaluate the IRS's implementation of planned corrective actions.

Individuals Claimed Erroneous Plug-in Electric and Alternative Motor Vehicle Credits

As of July 24, 2010, we identified 12,920 individuals who *e-filed* their tax returns and erroneously claimed³ \$33 million in plug-in electric and alternative motor vehicle credits. We also identified 1,719 of the 12,920 individuals erroneously reduced the amount of the AMT owed by almost \$5.3 million. In addition, we identified IRS employees who erroneously claimed plug-in electric and alternative motor vehicle credits. We have referred these employees to our Office of Investigations for further review. During this review, management took corrective actions to reduce erroneous claims when process weaknesses were brought to their attention. These actions have resulted in an estimated \$3.1 million in revenue protected.

Based on our review of a statistically valid sample of 233 paper-filed tax returns with an amount on Line 53 of Form 1040, we estimate another 1,300 individuals may have erroneously claimed more than \$4.2 million in plug-in electric and alternative motor vehicle credits. As previously discussed, the IRS is unable to track and account for plug-in electric vehicle credits claimed on paper-filed tax

² *Verifying Eligibility for Certain New Tax Benefits Was a Challenge for the 2010 Filing Season* (Reference Number 2010-41-128, dated September 30, 2010).

³ We were unable to track credit amounts received by individuals because Line 53 on Form 1040 is recorded by the IRS as a combined total of at least 10 different credits from which we cannot extract specific data. However, based on information provided by the individuals on their tax returns, they did not qualify for the plug-in electric vehicle and/or alternative motor vehicle credit they claimed.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



returns. Therefore, we are not including potential erroneous claims in our reported outcomes for paper-filed tax returns.

Figure 4 provides a summary of the erroneous claims we identified for *e-filed* tax returns. The information provided by individuals on their *e-filed* tax returns identifies that the individuals did not qualify for the plug-in electric and alternative motor vehicle credits claimed.

***Figure 4: Erroneous Plug-in Electric and
Alternative Motor Vehicle Credit Claimed***

Plug-in Electric and Alternative Motor Vehicle Credits Reason Vehicle Claimed Did Not Qualify	Erroneous Claims Through July 24, 2010	
	Number of Individuals	Dollar Amount
Nonqualifying Vehicle Year	2,710	\$ 4.5 million
Placed In-Service Date	589	\$ 1.4 million
Make of the Vehicle	9,621	\$27.1 million
Total	12,920	\$33.0 million

Source: TIGTA analysis of e-filed tax returns through July 24, 2010.

The erroneous claims resulted from inadequate IRS processes to ensure information reported by individuals claiming plug-in electric and alternative motor vehicle credits met qualifying requirements for vehicle year, placed in-service date, and make and model.

Individuals erroneously claimed plug-in electric and alternative motor vehicle credits for vehicles with a nonqualifying vehicle year

Our review identified 2,710 individuals who *e-filed* their tax returns and erroneously claimed \$4.5 million in plug-in electric and alternative motor vehicle credits for vehicles with a nonqualifying vehicle year. These individuals claimed these credits on Forms 8834, 8936, and 8910, and reported a vehicle with a year earlier than 2009 for Form 8834 and Form 8936 and a vehicle with a year earlier than 2008 for Form 8910. The law requires that vehicles must be new for the vehicle to qualify for these credits. Figure 5 provides examples of nonqualifying vehicle years reported by individuals on *e-filed* tax returns we identified as having erroneous claims for plug-in electric and alternative motor vehicle credits.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



**Figure 5: Examples of Nonqualifying Vehicle Years
Claimed on Tax Returns**

Form	Examples of Nonqualifying Vehicle Years
Form 8834	1010, 1967, 1972, 1974, 1975, 1976, 1977, 1979, 1982, 1984, 1985, 1986, 1987, 1988, 1990, 1991, 1992, 1993
Form 8936	1005, 1979, 1985, 1989, 1990, 1991, 1992, 1993, 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003
Form 8910	1009, 1020, 1300, 1963, 1964, 1966, 1973, 1975, 1977, 1981, 1982, 1983, 1984, 1988, 1989, 1990, 1991, 1992

Source: TIGTA analysis of e-filed tax returns through July 24, 2010.

On February 10, 2010, we alerted IRS management that individuals were erroneously claiming vehicles with a nonqualifying vehicle year. We recommended that reject codes for *e-filed* tax returns and Error Resolution System procedures for paper-filed tax returns be developed to not allow Form 8834 and Form 8936 credits when individuals are claiming credits for vehicles with nonqualifying years. Subsequently, we alerted IRS management on September 7, 2010, that individuals were also erroneously claiming vehicles with nonqualifying vehicle years for the alternative motor vehicle credit. We recommended that reject codes for *e-filed* tax returns and Error Resolution System procedures for paper-filed tax returns be developed to not allow Form 8910 alternative motor vehicle credits when individuals are claiming credits for vehicles with nonqualifying vehicle years.

Management Actions

- March 1, 2010 – Management agreed with the recommendation in our February 2010 alert to develop *e-file* reject codes. On March 29, 2010, management developed two new reject codes to reject *e-filed* tax returns in which the vehicle claimed had a nonqualifying vehicle year. We estimate the implementation of the reject codes resulted in \$1.9 million in revenue protected from rejecting *e-filed* tax returns between March 30, 2010, and July 24, 2010, in which individuals were claiming vehicles that had a nonqualifying year. This estimate is based on 411 rejected *e-filed* tax returns that had an average claim amount of \$4,669.⁴
- September 28, 2010 - Management agreed with recommendations in our September 2010 alert. Management responded that instructions will be issued to the Code and Edit function and the Error Resolution System no later than January 1, 2011, to review Form 8910 and not allow claims for credits for vehicles with years earlier than 2009. In addition, a reject code will be implemented in January 2011 to reject *e-filed* tax returns in which individuals claim the alternative motor vehicle credit for vehicles with a nonqualifying vehicle year.

⁴ Average claim amount was calculated by dividing the total amount of credits claimed with Forms 8834 and 8936 by the number of unique individuals claiming credits with Forms 8834 and 8936.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



We will include tests in our 2011 Filing Season Review to evaluate the IRS's implementation of planned corrective actions.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 1: Develop Error Resolution System procedures for paper-filed tax returns to not allow plug-in electric vehicle credits when individuals claim the credits for vehicles with nonqualifying years.

Management's Response: IRS management agreed with this recommendation. Instructions will be issued to the Code and Edit function tax examiners for the 2011 Filing Season to disallow claims for credits on vehicles with model years earlier than 2009.

Recommendation 2: Initiate actions to recover the \$4.5 million in plug-in electric and alternative motor vehicle credits claimed by the 2,710 individuals the TIGTA identified as having erroneously claimed these credits.

Management's Response: IRS management agreed with this recommendation. The IRS will use math error authority to reverse the credit or adjust the taxpayer's account for the 2,710 individuals identified as having erroneously claimed plug-in electric and alternative motor vehicle credits using a nonqualifying vehicle year.

Individuals erroneously claimed plug-in electric and alternative motor vehicle credits for vehicles with nonqualifying placed in-service dates

Our review identified 589 individuals who *e-filed* their tax returns and erroneously claimed more than \$1.4 million in plug-in electric and alternative motor vehicle credits for vehicles with nonqualifying placed in-service dates. These erroneous claims included:

- 131 individuals claiming \$263,715 in plug-in electric vehicle credits on Forms 8834 and 8910 with in-service dates before February 17, 2009, or after December 31, 2009. The law requires that vehicles claimed on Forms 8834 and 8910 have in-service dates after February 17, 2009, and before January 1, 2010.
- 129 individuals claiming \$596,445 in plug-in electric vehicle credits on Form 8936 with in-service dates before January 1, 2009, or after December 31, 2009. The law requires that vehicles claimed on Form 8936 have in-service dates after December 31, 2008, and before January 1, 2010.
- 329 individuals claiming \$596,783 in alternative motor vehicle credits on Form 8910 with in-service dates before January 1, 2009, or after December 31, 2009. The law requires these vehicles have in-service dates after December 31, 2008, and before January 1, 2010.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Figure 6 provides examples of vehicle in-service dates reported by individuals on *e-filed* tax returns we identified as having erroneous claims for plug-in electric and alternative motor vehicle credits.

Figure 6: Examples of Nonqualifying Placed In-Service Dates Claimed on Tax Returns

Form	Examples of Nonqualifying In-Service Dates
Form 8834	03/02/1999, 06/06/2008, 11/14/2008, 12/23/2008, 01/01/2009, 01/05/2009, 01/01/2010, 01/04/2010
Form 8936	01/22/1920, 01/21/1929, 12/20/2007, 01/01/2010, 01/29/2010, 02/28/2010, 03/01/2010, 03/15/2010
Form 8910	03/23/1997, 01/22/2006, 07/01/2006, 11/5/2006, 01/01/2007, 11/01/2007, 01/01/2008, 06/01/2008

Source: TIGTA analysis of e-filed tax returns through July 24, 2010.

On February 10, 2010, we alerted IRS management that individuals were erroneously claiming vehicles with nonqualifying in-service dates. We recommended that reject codes for *e-filed* tax returns and Error Resolution System procedures for paper-filed tax returns be developed to not allow credits when individuals are claiming credits for vehicles with nonqualifying in-service dates.

Management Actions

- March 1, 2010 – Management agreed with our recommendations. On March 29, 2010, management developed three reject codes to reject *e-filed* tax returns with nonqualifying in-service dates. In addition, instructions were issued to tax examiners to enter a Computer Condition Code⁵ to deny the credit on paper tax returns claiming credits for vehicles with nonqualifying in-service dates. We estimate the implementation of these reject codes resulted in more than \$1.2 million in revenue protected from rejecting *e-filed* tax returns between March 30, 2010, and July 24, 2010, in which individuals were claiming vehicles with nonqualifying in-service dates. This estimate is based on 519 rejected *e-filed* tax returns that had an average claim amount of \$2,359.⁶

We will include tests in our 2011 Filing Season Review to evaluate IRS’s implementation of planned corrective actions.

⁵ Computer Condition Codes are assigned by tax examiners or are computer generated and are used to identify a special condition or computation for the computer.

⁶ Average claim amount was calculated by dividing the total amount of credits claimed with Forms 8834, 8910, and 8936 by the number of unique individuals claiming credits with Forms 8834, 8910, and 8936.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Recommendation

The Commissioner, Wage and Investment Division, should:

Recommendation 3: Initiate actions to recover the more than \$1.4 million in plug-in electric and alternative motor vehicle credits claimed by 589 individuals that the TIGTA identified as having erroneously claimed credits for vehicles with nonqualifying in-service dates.

Management's Response: IRS management agreed with this recommendation. The IRS will use math error authority to reverse the credit or adjust the taxpayer's account for the 589 individuals identified as having erroneously claimed plug-in electric and alternative motor vehicle credits for vehicles with an in-service date before January 1, 2009, or after December 31, 2009.

Individuals erroneously claimed plug-in electric and alternative motor vehicle credits for nonqualifying vehicle makes and models

Our review identified 9,621 individuals who *e-filed* their tax returns and erroneously claimed more than \$27.1 million in plug-in electric and alternative motor vehicle credits for vehicles with a nonqualifying make and model. Our analysis of the descriptions provided by these individuals on their *e-filed* tax returns identified vehicles with a make and model that were not on the IRS-approved list of vehicles. The IRS provides a list on IRS.gov (the IRS public web site) of vehicle manufacturers, makes, and models that qualify for the plug-in electric vehicle credits claimed on Form 8834 and Form 8936 and the alternative motor vehicle credit claimed on Form 8910. Figure 7 provides examples of vehicles with a nonqualifying make and model reported by individuals on *e-filed* tax returns we identified as having erroneous claims for plug-in electric and alternative motor vehicle credits.

Figure 7: Examples of Nonqualifying Vehicle Makes and Models Claimed on Tax Returns

Form	Makes/Models of Vehicles
Form 8834	Bicycle, Buick Enclave, Chevrolet Camero, Chevy Truck, Dodge Caravan, Harley Classic, Hyundai Sonata
Form 8936	Acura 2006, Cadillac Escalade, Dodge Durango, Golf Cart, Ford Focus, Lexus RXH, Hummer H3, Mini Cooper
Form 8910	Acura, Hyundai, Jeep, Kia, Lancer, Lexus, Lincoln, Mitsubishi, Moto Guzzi, Pontiac, Smart, SUV, Taxi

Source: TIGTA analysis of e-filed tax returns through July 24, 2010.

On March 1, 2010, we alerted IRS management that individuals were erroneously claiming plug-in electric vehicle credits for vehicles with a nonqualifying make and model. We recommended that reject codes for *e-filed* tax returns and Error Resolution System procedures for paper-filed tax returns



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



be developed to not allow Form 8834 and Form 8936 credits when individuals are erroneously claiming credits for vehicles with a nonqualifying make and model.

On September 7, 2010, we alerted IRS management that individuals were also erroneously claiming the alternative motor vehicle credit for vehicles with a nonqualifying make and model. We recommended that the IRS develop reject codes for *e-filed* tax returns and Error Resolution System procedures for paper-filed tax returns to not allow Form 8910 credits when individuals are claiming credits for vehicles with a nonqualifying make and model.

Management Actions

- March 9, 2010 – IRS management disagreed with our recommendations. The IRS stated that implementation of our recommendations would require IRS employees to review the forms for several hundred different types of qualifying vehicles. Such a review process would have a significant impact on the number of tax returns that could be reviewed per hour. The IRS also believed that this issue would be best handled after the tax return has been processed. A Compliance Strategy being developed for Recovery Act provisions will include tests in Fiscal Year 2011 for this issue.
- September 28, 2010 – Management disagreed with our recommendations, citing the same reasons given previously in their March 9, 2010, response. Management indicated that identifying eligible vehicles would require tax examiners to review information not available on the tax return. A review of just the Qualified Alternative Fuel Motor Vehicles list alone currently shows 18 manufacturers and 771 rows of vehicles. In developing the Compliance Strategy for Recovery Act provisions, the IRS plans to conduct a test for 1,000 post-refund cases in Fiscal Year 2011 that involve claims for plug-in electric and alternative motor vehicle credits.

Variations in vehicle descriptions prevent validation of plug-in electric and alternative motor vehicle credit claims

In the IRS's response to our alerts, it noted that examiners are unable to determine from information provided by individuals on tax returns if a vehicle meets required make and model qualifications. For example, the taxpayer may indicate "Ford Fusion" under make and model, but the description is too vague to determine if the taxpayer purchased a qualifying hybrid model or a nonqualifying entirely gas model of the Ford Fusion.

We agree that there is no consistency in the descriptions individuals include on their tax returns for vehicles being claimed for plug-in electric and alternative motor vehicle credits. Although the IRS provides a list on IRS.gov of specific vehicle makes and models that qualify for each plug-in electric and alternative motor vehicle credit, it has not developed a process to standardize the information on tax returns.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Our review of *e-filed* tax returns identified 34,602 individuals who claimed more than \$50 million in plug-in electric and alternative motor vehicle credits for 34,991 vehicles in which we were unable to determine from the description provided on the tax return if the make and model of the vehicles qualified for the credit claimed. Figure 8 provides examples of the nonstandardized entries input by individuals on *e-filed* tax returns we analyzed.

Figure 8: Examples of Variations in Vehicle Make Entries by Individuals

CHEVROLET	FORD	MERCEDES	NISSAN	
CHEVROLET	FORD	MERCEDES	NIS	TOMB
+CHEVY	FODR	MERCEDE	NISAN	TOMBERLI
CHAVY	FOED	MERCEDEES	NISS	TOMBERLAND
CHECROLET	FOERD	MERCEDES B	NISSA	TOMBORILIN
CHEROLET	FOR	MERCEDES BEN	NISSAL	TOMBRL
CHEV	FORT	MERCEDES BENZ	NISSAN	TUMBERLIN
CHEVE	HONDA	MERCEDES BNZ	NISSAN ALT	TOYOTA
CHEVERLOT	HANDA	MECEDES	NISSAN ALTIM	TOYOTA
CHEVEY	HOMDA	MERC BENZ	NISSAN ALTIMA	JAPEN TOYOTA
CHEVLORET	HON	MERCEDED-BEN	NISSASN	TAYOTA
CHEVOLET	HOND	MERCEDEZ	NISSEN	TOTOTA
CHEVOLETE	HONDA	MERCEDEZ-BENZ	NISSIAN	TOTOYA
CHEVORELET	HONDAI	MERCERDES	NISSON	TOY
CHEVORLET	HONDO	MERCURY	NISSAN	TOYATA
CHEVR	JAPAN	MERCURI	NIZZAN	TOYATO
CHEVRLET	JAPANESE HONDA	MERCURU	TOMBERLIN	TOYOA
CHEVROLETT	HYUNDAI	MERCURY 2/WD	TOMBERLIN	TOYODA
CHEVROLTE	HUNDAI	MERCURY 4X4	TIMBERLINE	TOYOR
CHEVY	HONDAI	MERCUTY	TMBLN	TOYOYA
CHEY	MAZDA	MERURY	TMBO	TOYPTA
CHV	MAZDA	MERC	TMBRLN	TOYTA
CHVROLET	MADZA		TOBERL	TTOTOTA
	MAZADA		TOBERLINE	TYOTA

Source: TIGTA analysis of vehicle make and model names entered by individuals on Forms 8910.

The IRS should develop coding that could be used to identify the specific vehicle make and model an individual is claiming for plug-in electric and alternative motor vehicle credits. For example, the IRS uses a coding classification process for its North American Industry Classification System’s Principal Business or Professional Activity Codes used in the instructions for Form 1040, Profit or Loss from Business (Schedule C), to standardize types of businesses. Figure 9 provides an example of the North American Industry Classification System’s Principal Business or Professional Activity Codes used in Schedule C Instructions.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



**Figure 9: Example of the North American Industry Classification System's
Principal Business or Professional Activity Codes
Used in Schedule C Instructions**

SCHEDULE C (Form 1040) Department of the Treasury Internal Revenue Service (99)	Profit or Loss From Business (Sole Proprietorship) ▶ Partnerships, joint ventures, etc., generally must file Form 1065 or 1065-B. ▶ Attach to Form 1040, 1040NR, or 1041. ▶ See Instructions for Schedule C (Form 1040).	OMB No. 1545-0074 2009 Attachment Sequence No. 09
Name of proprietor		Social security number (SSN)
A Principal business or profession, including product or service (see page C-2 of the Instructions)	B Enter code from pages C-9, 10, & 11 	
C Business name. If no separate business name, leave blank.	D Employer ID number (EIN), if any 	
E Business address (including suite or room no.) ▶ _____ on		
City, town or post office, state, and ZIP code _____		
activity they are engaged in to facilitate the administration of the Internal Revenue Code. These six-digit codes are based on the North American Industry Classification System (NAICS).		
select the activity that best identifies the principal source of your sales or receipts (for example, real estate agent). Now find the six-digit code assigned to this activity (for example, 531210, the code for offices		
Note: If your principal source of income is from farming activities, you should file Schedule F.		
Accommodation, Food Services, & Drinking Places Accommodation 721310 Rooming & boarding houses 721210 RV (recreational vehicle) parks & recreational camps 721100 Traveler accommodation (including hotels, motels, & bed & breakfast inns) Food Services & Drinking Places 722410 Drinking places (alcoholic beverages) 722110 Full-service restaurants	561790 Other services to buildings & dwellings 561900 Other support services (including packaging & labeling services, & convention & trade show organizers) Waste Management & Remediation Services 562000 Waste management & remediation services Agriculture, Forestry, Hunting, & Fishing	711510 Independent artists, writers, & performers 711100 Performing arts companies 711300 Promoters of performing arts, sports, & similar events 711210 Spectator sports (including professional sports clubs & racetrack operations) Construction of Buildings 236200 Nonresidential building construction 236100 Residential building construction
		238990 All other specialty trade contractors Educational Services 611000 Educational services (including schools, colleges, & universities) Finance & Insurance Credit Intermediation & Related Activities 522100 Depository credit intermediation (including commercial banking, savings

Source: 2009 Schedule C Instructions.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 4: Develop a process to ensure individuals are not erroneously claiming vehicles with nonqualifying makes and models. This could include developing a standardized system of codes similar to those used in the instructions for Schedule C to identify vehicle makes and models that qualify for plug-in electric and alternative motor vehicle credits and/or require the Vehicle Identification Number⁷ on the Forms 8834, 8936, and 8910.

⁷ A Vehicle Identification Number is a unique serial number used by the automotive industry to identify individual motor vehicles.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Management's Response: IRS management agreed with this recommendation. For Filing Season 2011, Code and Edit function tax examiners will perform a review of the make and model of the vehicle claimed on the Forms 8834, 8936, and 8910 and disallow any clearly nonqualifying vehicle. Starting in the 2012 Filing Season, a new Line 2, Vehicle Identification Number, will be added to Forms 8834, 8936, and 8910.

Recommendation 5: Initiate actions to recover the \$27.1 million in plug-in electric and alternative motor vehicle credits claimed by 9,621 individuals the TIGTA identified as having erroneously claimed the credit for vehicles with a nonqualifying make and model.

Management's Response: IRS management agreed with this recommendation. The Wage and Investment Division Compliance function will work with the Small Business/Self-Employed Division to include 1,000 cases in the Exam work plan. The results of these audits will be used to determine whether additional audits are warranted.

Plug-in Electric and Alternative Motor Vehicle Credits Are Being Abused

Our review of *e-filed* tax returns identified individuals erroneously claiming the same vehicle for multiple plug-in electric and alternative motor vehicle credits, claiming an excessive number of vehicles for personal use credits, and credits claimed by prisoners. Processes were not established to identify individuals abusing the plug-in electric and alternative motor vehicle credits. We identified 172 individuals who appear to have erroneously claimed more than \$2.1 million in plug-in electric and alternative motor vehicle credits.

Individuals claimed multiple credits for the same plug-in electric motor vehicle

Our review identified 129 individuals who *e-filed* their tax returns as of July 24, 2010, and erroneously claimed \$779,000 in multiple plug-in electric and alternative motor vehicle credits for the same vehicle. For Tax Year 2009, an approved plug-in electric drive motor vehicle may be claimed for credit on either Form 8834 or Form 8936, but not on both. If a vehicle qualifies for a plug-in electric motor vehicle credit, it cannot also be claimed for the alternative motor vehicle credit.

On September 7, 2010, we alerted IRS management that individuals were erroneously claiming multiple credits for the same vehicle. We recommended the IRS develop reject codes for *e-filed* tax returns and Error Resolution System procedures for paper-filed tax returns to not allow multiple credits for the same vehicle.

Management Actions

- September 28, 2010 – Management disagreed with this recommendation stating that the Submission Processing function cannot determine which credit is valid without more information than is available on the tax return.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



We agree with management that examiners cannot determine which credit is valid without more information. That is the reason we made our recommendation to reject tax returns in which multiple credits are claimed and implement an unallowable code to review these claims by the Examination function.

Individuals claimed excessive numbers of vehicles for the Form 8936

Our analysis of *e-filed* tax returns identified 14 individuals claiming more than \$1.3 million for 5 or more vehicles as personal use credits. Claiming five or more vehicles for personal use is questionable and it appears the individuals may be purchasing the vehicles for business use. Vehicles used in a business or by the business’ employees are considered business or investment property and if the vehicle is subsequently sold the credit is subject to recapture. A vehicle claimed for personal credit has a tax advantage because the amount can be used to reduce the AMT. If the credits are for business use, the business portion of the credit cannot be used to reduce the AMT. Figure 10 provides a summary of the 223 vehicles claimed by the 14 individuals.

Figure 10: Individuals Claiming Five or More Vehicles

Vehicles Claimed	Business Use Credit Claimed	Personal Use Credit Claimed	Credit Allowed
	*****1*****		
223	0	1,326,731	\$1,326,731

Source: TIGTA analysis of e-filed tax returns through July 24, 2010.

On September 7, 2010, we alerted IRS management of our concern that individuals were claiming credits for five or more vehicles and that processes should be developed to identify these questionable claims and ensure the accuracy of the credits claimed.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Management Actions

- September 28, 2010 – Management agreed with our recommendation and indicated that they will implement an unallowable code for review of these claims by the Examination function.

We will include tests in our 2011 Filing Season Review to evaluate the IRS's implementation of planned corrective actions.

Prisoners erroneously claimed plug-in electric and alternative motor vehicle credits

We identified 29 prisoners who *e-filed* their tax returns and erroneously received \$49,926 in plug-in electric and alternative motor vehicle credits. A plug-in electric and alternative motor vehicle must have been purchased or converted and placed in service during Tax Year 2009 and these individuals were incarcerated for all of Calendar Year 2009. In addition, another 59 prisoners attempted to erroneously claim \$104,795 in plug-in electric and alternative motor vehicle credits. The IRS currently has a hold on these accounts to prevent refunds from being issued. However, these individual accounts have not been adjusted and most have not been referred to the Examination function.

Recommendations

The Commissioner, Wage and Investment Division, should:

Recommendation 6: Develop reject codes to reject *e-filed* returns and implement an unallowable code for paper-filed tax returns to ensure individuals are not erroneously claiming plug-in electric and alternative motor vehicle credits for the same vehicle.

Management's Response: IRS management agreed with this recommendation. The IRS issued two Unified Work Requests on November 18, 2010, for programming Unallowable Code 79 for *e-filed* and paper tax returns when taxpayers are claiming the same vehicle for more than one credit. Because the requested action will be subject to funding and resource prioritization by the Modernization and Information Technology Services organization, submission of the Unified Work Requests will complete the corrective action.

Recommendation 7: Initiate actions to recover the \$779,000 in plug-in electric and alternative motor vehicle credits claimed by 129 individuals the TIGTA identified as having erroneously claimed multiple credits for the same vehicle.

Management's Response: IRS management agreed with this recommendation. The Wage and Investment Division Compliance function will work with the Small Business/Self-Employed Division to review these returns and open audits where warranted.

Recommendation 8: Develop processes to ensure prisoners do not receive erroneous plug-in electric and alternative motor vehicle credits. In addition, initiate actions to recover the \$49,926 in



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



plug-in electric and alternative motor vehicle credits erroneously claimed by 29 prisoners and ensure 59 prisoners with holds are referred to the Examination function.

Management's Response: IRS management agreed with this recommendation. The IRS will continue to check tax returns against the prisoner database and refer them for examination. The IRS will also use existing math error authority to reverse the credits or adjust the taxpayers' accounts for the prisoner claims mentioned in this report. Where math error authority is not possible, the IRS will review and open audits when warranted.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to assess the effectiveness of IRS processes to identify and prevent erroneous claims for the plug-in electric vehicle credit and alternative motor vehicle credit for tax returns filed from January 1 through July 24, 2010. To accomplish our objective, we:

- I. Determined if the IRS had adequate controls to identify erroneous plug-in electric and alternative motor vehicle credit claims at the time a tax return was processed.
- II. Determined if the new tax law provisions were correctly implemented into tax return processing systems for *e-filed* tax returns with claims for the credit for certain plug-in electric vehicles, the alternative motor vehicle credit, and the qualified plug-in electric drive motor vehicle credit. We used computer analysis of 100 percent of the *e-filed* Tax Year 2009 individual income tax returns processed nationally on the Tax Return Data Base between January 1 and July 24, 2010,¹ to identify tax returns with plug-in electric and alternative motor vehicle credits and determined if they were processed correctly.
 - A. We electronically identified 69,496 individuals that claimed a plug-in Electric Vehicle Credit on Qualified Plug-in Electric and Electric Vehicle Credit (Form 8834), Conversion Kits Credit on Alternative Motor Vehicle Credit (Form 8910), and Qualified Plug-in Electric Drive Motor Vehicle Credit (Form 8936) or an Alternative Motor Vehicle Credit (Form 8910) on an *e-filed* tax return through July 24, 2010.
 1. 2,769 individuals with claims on Form 8834.
 2. 53,523² individuals with claims on Form 8910. Of these returns, 1,522 claims were made for plug-in electric conversion vehicles and 52,006 claims were made for nonconversion alternative motor vehicles.
 3. 13,204 individuals with claims on Form 8936.

¹ To assess the reliability of computer-processed data, programmers in the TIGTA Office of Information Systems validated the data that were extracted, and we verified the data with appropriate documentation. Judgmental samples were selected and reviewed to ensure that the amounts presented were supported by external sources. As appropriate, data in the selected data records were compared to the physical tax returns to verify that the amounts were supported.

² Five individuals claimed both a plug-in conversion and an alternative motor vehicle on Form 8910



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



- B. Determined whether the identified *e-filed* tax returns with claims for the credit for certain plug-in electric vehicles, the alternative motor vehicle credit, and the qualified plug-in electric drive motor vehicle credit had been processed correctly by:
1. Using computer analysis to determine if the qualifying year, the placed in-service date, and the make of vehicle met the established criteria for the individual to be eligible to claim the credit.
 2. Using computer analysis to determine if an individual had used a vehicle for a double benefit or had questionable personal use credits by claiming five or more vehicles.
 3. Using computer analysis to determine if prisoners incarcerated for the entire Calendar Year 2009 and IRS employees erroneously claimed the credit.
- III. Determined if the new tax law provisions were correctly implemented into tax return processing systems for paper-filed tax returns with claims for the credit for certain plug-in electric vehicles, the alternative motor vehicle credit, and the qualified plug-in electric drive motor vehicle credit by:
- A. Using computer analysis of 100 percent of the Tax Year 2009 individual income tax returns processed nationally on the Individual Return Transaction File between January 1 and May 28, 2010,³ to identify a population of 7,769 tax returns to select a sample.
 - B. Using an error rate of 13 percent, a confidence level of 95 percent, and a precision factor of ± 4 percent, we selected a statistically valid sample of 263 paper tax returns. Of the 263 tax returns selected, 233 tax returns were available, which became our actual sample reviewed. This increased the precision factor to ± 4.73 percent.
- IV. Evaluated the accuracy of the implementation of the Treatment of alternative motor vehicle credit as a personal credit allowed against the AMT by matching all of the identified erroneous claims against the Individual Return Transaction File for AMT liability.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems

³ To assess the reliability of computer-processed data, programmers in the TIGTA Office of Information Systems validated the data that were extracted, and we verified the data with appropriate documentation. Judgmental samples were selected and reviewed to ensure that the amounts presented were supported by external sources. As appropriate, data in the selected data records were compared to the physical tax returns to verify that the amounts were supported.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective: the processes for planning, organizing, directing, and controlling program operations for new tax legislation such as the plug-in electric vehicle credits. We also evaluated the controls that are incorporated directly into computer applications to help ensure the validity, completeness, accuracy, and confidentiality of transactions and data during application processing of tax returns with these credits.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Appendix II

Major Contributors to This Report

Michael E. McKenney, Assistant Inspector General for Audit (Returns Processing and Account Services)
Russell Martin, Director
Tina Parmer, Audit Manager
Kathleen Hughes, Senior Auditor
Steve Vandigriff, Senior Auditor
Lawrence White, Senior Auditor
Kim McMenamin, Audit Evaluator
Martha Stewart, Information Technology Specialist



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Appendix III

Report Distribution List

Commissioner C
Office of the Deputy Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Deputy Commissioner of Operations, Wage and Investment Division SE:W
Deputy Commissioner of Services, Wage and Investment Division SE:W
Director, Business Modernization Office, Wage and Investment Division SE:W:BMO
Director, Customer Account Services, Wage and Investment Division SE:W:CAS
Director, Customer Assistance, Relationships, and Education, Wage and Investment Division
SE:W:CAR
Director, Electronic Tax Administration and Refundable Credits, Wage and Investment Division
SE:W:ETARC
Director, Strategy and Finance, Wage and Investment Division SE:W:S
Director, Accounts Management, Wage and Investment Division SE:W:CAS:AM
Director, Field Assistance, Wage and Investment Division SE:W:CAR:FA
Director, Joint Operation Center, Wage and Investment Division SE:W:CAS:JOC
Director, Stakeholder Partnership, Education, and Communications, Wage and Investment
Division SE:W:CAR:SPEC
Director, Submission Processing, Wage and Investment Division SE:W:CAS:SP
Chief, Program Evaluation and Improvement, Wage and Investment Division SE:W:S:PRA:PEI
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaison: Chief, Program Evaluation and Improvement, Wage and Investment Division
SE:W:S:PRA:PEI



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. 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 Calendar Year 2010 individual income tax returns. The returns were received by the IRS Submission Processing sites between January 1 and July 24, 2010.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$33 million from 12,920 individuals erroneously claiming plug-in electric and alternative motor vehicle credits on *e-filed* tax returns (see page 5).

Methodology Used to Measure the Reported Benefit:

We used computer analysis to identify individuals who *e-filed* a tax return claiming plug-in and alternative motor vehicle credits on Qualified Plug-in Electric and Electric Vehicle Credit (Form 8834), Alternative Motor Vehicle Credit (Form 8910), and Qualified Plug-in Electric Drive Motor Vehicle Credit (Form 8936). We identified 12,920 individuals erroneously claiming \$33 million in these credits with nonqualifying vehicle years, nonqualifying vehicle in-service dates, and nonqualifying vehicle makes and models.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$5.3 million from 1,719 individuals erroneously reducing the amount of the AMT owed (see page 5).

Methodology Used to Measure the Reported Benefit:

From the 12,920 individuals who erroneously claimed plug-in or alternative motor vehicle credits, we identified 1,719 individuals who erroneously reduced the amount of AMT owed by almost \$5.3 million.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$3.1 million from 930 individuals who submitted an *e-filed* tax return with erroneous plug-in vehicle credits. These credits were rejected after the IRS



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



implemented new reject codes based on our recommendations during this review (see page 5).

Methodology Used to Measure the Reported Benefit:

Management agreed with our recommendations in an email alert, and on March 29, 2010, implemented 5 new reject codes to reject *e-filed* tax returns with a vehicle year and/or in-service date that do not meet the tax provision requirements for the plug-in vehicle credits. In addition, instructions were issued to tax examiners to enter a Computer Condition Code¹ on paper-filed tax returns with disqualifying in-service dates and the credit will be denied.

We estimate the implementation of these 5 reject codes resulted in revenue protection of an estimated \$3.1 million from March 30, 2010, to July 24, 2010. This estimate is based on 930 *e-filed* tax returns that were rejected with these conditions using an average claim amount of \$2,359 for 519 returns and an average claim amount of \$4,669 for 411 returns.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$779,000 from 129 individuals erroneously claiming more than one plug-in vehicle credit for the same vehicle (see page 14).

Methodology Used to Measure the Reported Benefit:

We matched Form 8834, Form 8910, and Form 8936 and identified 129 individuals who included 142 vehicles that claimed a double benefit for the same vehicle.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$1.3 million from 14 individuals erroneously claiming 5 or more vehicles as a personal use credit (see page 14).

Methodology Used to Measure the Reported Benefit:

From all *e-filed* tax return claims for plug-in electric and alternative motor vehicle credits, we identified 14 individuals claiming more than \$1.3 million in personal use credits for 5 or more vehicles.

Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$49,926 from 29 individuals who were prisoners (see page 14).

¹ Computer Condition Codes are assigned by tax examiners or are computer generated and are used to identify a special condition or computation for the computer.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Methodology Used to Measure the Reported Benefit:

We identified 29 prisoners who *e-filed* their tax returns and erroneously received \$49,926 in erroneous plug-in electric and alternative motor vehicle credits. These individuals were incarcerated for all of Calendar Year 2009.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*

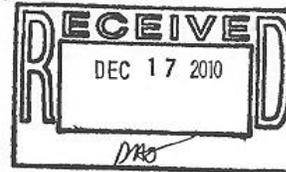


Appendix V

Management's Response to the Draft Report

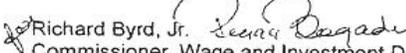


DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308



DEC 17 2010

MEMORANDUM FOR MICHAEL R. PHILLIPS
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:  Richard Byrd, Jr.
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor Vehicle Credits
(Audit # 201040131)

We have reviewed the subject draft report and appreciate you alerting us to several issues during this audit concerning the processing of Plug-in Electric and Alternative Motor Vehicle Credits. As a result, we are implementing some corrective actions immediately and will be implementing the others as soon as possible.

We are updating Code and Edit and Error Resolution System Internal Revenue Manuals (IRMs)¹ for the 2011 Processing Year (PY) to include a check for the model year of the vehicle and the date the vehicle is placed in service.

For PY 2011, Code and Edit will also do a review of the make and model of vehicles to ensure taxpayers do not claim clearly nonqualifying vehicles. In addition, we requested that e-file software providers implement programming changes for taxpayers to select the make, model, and year of these qualifying vehicles from a drop down box to ensure that returns are complete and the information provided by taxpayers substantiates the credit.

For PY 2012 (Tax Year 2011), we will revise Form 8834, *Qualified Plug-In Electric and Electric Vehicle Credit*, Form 8910, *Alternative Motor Vehicle Credit*, and Form 8936, *Qualified Plug-In Electric Drive Motor Vehicle Credit*, to add a new Line 2 requiring the 17-character alpha-numeric vehicle identification number (VIN) for qualifying vehicles. Various characters in a VIN identify the make, model, and year of the vehicle. This

¹ IRM 3.11.3, *Returns and Document Analysis, Individual Income Tax Returns*, for Code & Edit and IRM 3.11.12, *Error Resolution, Individual Income Tax Returns*, for ERS.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



2

requirement is expected to increase taxpayer compliance with the rules for qualifying vehicles.

For the 3,516 erroneous claims mentioned in your report, we will use existing math error authority to reverse the credits or adjust taxpayer accounts. Where math error authority is not possible we will review and open audits where warranted. For the additional 9,621 claims you identified as having erroneously claimed the credit for vehicles with a nonqualifying make and model, Wage and Investment Division and Small Business/Self-Employed Division Compliance organizations will include 1,000 cases (500 for each operating division) in the Exam work plan. The results of these audits will determine if additional audits are warranted.

We reviewed the outcome measures identified in Appendix IV and agree with your assessment. Our comments to your recommendations are attached. If you have any questions, please contact me, or a member of your staff may contact Peter J. Stipek, Director, Customer Account Services, Wage and Investment Division, at (404) 338-8910.

Attachment



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



Attachment

The Commissioner, Wage and Investment Division, should:

Recommendation 1

Develop Error Resolution System procedures for paper-filed tax returns to not allow plug-in electric vehicle credits when individuals claim the credits for vehicles with nonqualifying years.

Corrective Action

We agree with this recommendation. Instructions will be issued to Code and Edit tax examiners for the 2011 Filing Season to disallow claims for credits on vehicles with model years earlier than 2009.

Implementation Date

January 15, 2011

Responsible Official

Director, Submission Processing, Wage and Investment Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.

Recommendation 2

Initiate actions to recover the \$4.5 million in plug-in electric and alternative motor vehicle credits claimed by the 2,710 individuals the TIGTA identified as having erroneously claimed these credits.

Corrective Action

We agree with this recommendation. We will use math error authority to reverse the credit, or adjust the taxpayer's account for the 2,710 individuals identified by the Treasury Inspector General for Tax Administration (TIGTA) as having erroneously claimed plug-in electric and alternative motor vehicle credits using a nonqualifying vehicle year.

Implementation Date

January 15, 2012

Responsible Officials

Director, Accounts Management, Wage and Investment Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



2

Recommendation 3

Initiate actions to recover the more than \$1.4 million in plug-in electric and alternative motor vehicle credits claimed by 589 individuals that the TIGTA identified as having erroneously claimed credits for vehicles with nonqualifying in-service dates.

Corrective Action

We agree with this recommendation. We will use math error authority to reverse the credit or adjust the taxpayer's account for the 589 individuals identified by TIGTA who erroneously claimed plug-in electric and alternative motor vehicle credits for vehicles with an in-service date before January 1, 2009, or after December 31, 2009.

Implementation Date

January 15, 2012

Responsible Officials

Director, Accounts Management, Wage and Investment Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.

Recommendation 4

Develop a process to ensure individuals are not erroneously claiming vehicles with nonqualifying makes and models. This could include developing a standardized system of codes similar to those used in the instructions for Schedule C to identify vehicle makes and models that qualify for plug-in electric and alternative motor vehicle credits and/or require the Vehicle Identification Number² on the Forms 8834, 8936, and 8910.

Corrective Action

We agree with this recommendation. For the 2011 Filing Season, Code and Edit tax examiners will perform a review of the make and model of the vehicle claimed on Form 8834, *Qualified Plug-In Electric and Electric Vehicle Credit*, Form 8936, *Qualified Plug-In Electric Drive Motor Vehicle Credit*, and Form 8910, *Alternative Motor Vehicle Credit*, and disallow any clearly nonqualifying vehicle. Starting in the 2012 Filing Season, a new Line 2, Vehicle Identification Number will be added to Forms 8834, 8936, and 8910.

Implementation Date

January 15, 2011 Code and Edit procedures
January 15, 2012 Forms revision

² A Vehicle Identification Number is a unique serial number used by the automotive industry to identify individual motor vehicles.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



3

Responsible Officials

Director, Submission Processing, Wage and Investment Division
Director, Tax Forms and Publications, Wage and Investment Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.

Recommendation 5

Initiate actions to recover the \$27.1 million in plug-in electric and alternative motor vehicle credits claimed by 9,621 individuals the TIGTA identified as having erroneously claimed credit for vehicles with a nonqualifying make and model.

Corrective Action

We agree with this recommendation. The Wage and Investment (W&I) Division Compliance Function will work with the Small Business/Self-Employed Division (SB/SE) to include 1,000 cases in the Exam work plan. The results of these audits will be used to determine whether additional audits are warranted.

Implementation Date

January 15, 2012

Responsible Officials

Director, Reporting Compliance, Wage and Investment Division
Director, Campus Reporting Compliance, Small Business/Self-Employed Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.

Recommendation 6

Develop reject codes to reject *e-filed* returns and implement an unallowable code for paper-filed tax returns to ensure individuals are not erroneously claiming plug-in electric and alternative motor vehicle credits for the same vehicle.

Corrective Action

We agree with this recommendation. We submitted two Unified Work Requests (UWRs) on November 18, 2010, for programming Unallowable Code 79 for e-filed and paper tax returns when the taxpayer is claiming the same vehicle for more than one credit. Since the requested action will be subject to funding and resource prioritization by Modernization and Information Technology Services, submission of the UWRs will complete the corrective action.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



4

Implementation Date

November 18, 2010

Responsible Official

Director, Submission Processing, Wage and Investment Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.

Recommendation 7

Initiate actions to recover the \$779,000 in plug-in electric and alternative motor vehicle credits claimed by 129 individuals the TIGTA identified as having erroneously claimed multiple credits for the same vehicle.

Corrective Action

We agree with this recommendation. The W&I Division Compliance Function will work with the SB/SE Division to review these returns and open audits where warranted.

Implementation Date

January 15, 2012

Responsible Officials

Director, Reporting Compliance, Wage and Investment Division
Director, Campus Reporting Compliance, Small Business/Self-Employed Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.

Recommendation 8

Develop processes to ensure prisoners do not receive erroneous plug-in electric and alternative motor vehicle credits. In addition, initiate actions to recover the \$49,926 in plug-in electric and alternative motor vehicle credits erroneously claimed by 29 prisoners and ensure 59 prisoners with holds are referred to the Examination function.

Corrective Action

We agree with this recommendation. Returns will continue to be checked against the prisoner database and referred for examination. For the prisoner claims mentioned in your report, we will use existing math error authority to reverse the credits or adjust taxpayer accounts. Where math error authority is not possible we will review and open audits where warranted.



*Individuals Received Millions of Dollars in
Erroneous Plug-in Electric and Alternative Motor
Vehicle Credits*



5

Implementation Date

January 15, 2012

Responsible Officials

Director, Compliance, Wage and Investment Division

Director, Compliance, Small Business/Self-Employed Division

Director, Accounts Management, Wage and Investment Division

Corrective Action Monitoring Plan

IRS will monitor this corrective action as part of our internal management control system.