



## Treasury Inspector General for Tax Administration Office of Audit

### IMPROVEMENTS ARE NEEDED TO BETTER ENSURE THAT REFUNDS CLAIMED ON POTENTIALLY FRAUDULENT TAX RETURNS ARE NOT ERRONEOUSLY RELEASED

Issued on November 12, 2015

## Highlights

Highlights of Report Number: 2016-40-006 to the Internal Revenue Service Commissioner for the Wage and Investment Division.

### IMPACT ON TAXPAYERS

The IRS's Return Integrity and Compliance Services organization is responsible for identifying, evaluating, and preventing the issuance of improper refunds. This mission includes the protection of revenue by identifying potentially fraudulent tax returns and verifying the accuracy of reported income and withholding information. The IRS reported that the Integrity and Verification Operations function prevented more than \$15 billion in refunds for over 2 million tax returns for confirmed identity theft or fraud during Calendar Year 2014.

### WHY TIGTA DID THE AUDIT

This audit was initiated because an IRS employee reported to the TIGTA Office of Investigations that the IRS was not working some taxpayer cases in which refunds were held. The Office of Investigations identified that these tax accounts were not timely addressed to ensure that the refunds are not erroneously released. This review assessed IRS processes to ensure that tax refunds are not erroneously released.

### WHAT TIGTA FOUND

TIGTA identified that because of a programming error, over \$27 million of refunds were erroneously issued for 13,043 Tax Year 2013 tax returns. The programming error is overriding the IRS's two-week processing delay on some refund tax returns that are identified by the IRS as potentially fraudulent. These are tax returns that the IRS Examination function also identified as claiming a questionable tax credit. The portion of the refund that is not reviewed by the Examination function is erroneously issued before the IRS can complete its verification of income and withholding.

TIGTA also identified that ineffective monitoring of potentially fraudulent tax returns is resulting in the erroneous release of refunds before the required

verification. TIGTA identified 3,910 Tax Year 2013 tax returns selected for verification with no indication that tax examiners verified the returns. The IRS issued refunds totaling over \$19 million for these tax returns. The IRS did not ensure that tax examiners timely completed their verification work. Name mismatches in IRS systems prevented refund holds from posting to tax accounts. Refund holds were either not set correctly or not functioning as intended.

### WHAT TIGTA RECOMMENDED

TIGTA recommended that the IRS 1) correct the programming that is erroneously overriding the two-week return processing delay needed to ensure that refunds are not issued prior to screening and verification of the tax returns, 2) develop a periodic reconciliation process to ensure that refunds associated with identified potentially fraudulent tax returns are not erroneously released, 3) develop a process to ensure that tax examiners verify a potentially erroneous refund claimed by a taxpayer within the refund hold period or place an unexpiring refund hold on the taxpayer's account until verification can be completed as required, and 4) identify why refund holds placed on some accounts were not delaying processing of the tax returns and address the causes.

The IRS agreed with all recommendations. The IRS stated that it took action to address the programming conflict that was overriding the two-week return processing delay, plans to periodically reconcile account inventory information to identify refunds at jeopardy for erroneous release, initiated actions to change the refund hold from a temporary freeze to an unexpiring freeze, and agreed to periodically reconcile records between computer systems to address anomalies and prevent the issuance of erroneous refunds.

### READ THE FULL REPORT

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

<http://www.treas.gov/tigta/auditreports/2016reports/201640006fr.pdf>.

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