

MSP #11 POST-PROCESSING MATH ERROR AUTHORITY: The IRS Has Failed to Exercise Self-Restraint in Its Use of Math Error Authority, Thereby Harming Taxpayers

RESPONSIBLE OFFICIALS

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TAXPAYER RIGHTS IMPACTED¹

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

DEFINITION OF PROBLEM

When a return appears to contain one of 17 types of errors (misleadingly called math errors), the IRS can summarily assess additional tax without first giving the taxpayer a notice of deficiency, which triggers the right to petition the Tax Court (*i.e.*, the normal “deficiency procedures”).² Because this “math error authority” (MEA) is not limited to clear-cut errors, it can deprive taxpayers of benefits to which they are entitled, and leave them with no realistic opportunity for judicial review, as discussed in prior reports.³

The taxpayer is best equipped to receive and understand a math error notice and address any discrepancy immediately after filing. On April 10, 2018, however, the IRS concluded it can use MEA after processing the return, just like an audit.⁴ Such delays increase the risk that taxpayers will not be able to respond timely. Yet, the IRS has used this new post-processing MEA to reverse refundable credits for students, children, and the working poor (*i.e.*, the American Opportunity Tax Credit (AOTC), Child

1 See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 See IRC §§ 6213(b), (g)(2) (listing in (A)-(Q), the 17 specific types of errors). If the taxpayer timely responds to a math error notice, then the IRS abates the assessment and must follow deficiency procedures before making another assessment. See IRC §§ 6213(a), (b)(2).

3 See, e.g., National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress 114-118 (Area of Focus: *The IRS Has Expanded Its Math Error Authority, Reducing Due Process for Vulnerable Taxpayers, Without Legislation and Without Seeking Public Comments*); National Taxpayer Advocate 2014 Annual Report to Congress 163; National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, 5, 91-92; National Taxpayer Advocate 2011 Annual Report to Congress 74; National Taxpayer Advocate 2006 Annual Report to Congress 311; National Taxpayer Advocate 2003 Annual Report to Congress 113; National Taxpayer Advocate 2002 Annual Report to Congress 25, 186; National Taxpayer Advocate 2001 Annual Report to Congress 33. For a proposal to expand the opportunity for judicial review, see Legislative Recommendation: *Fix the Flora Rule: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can*, *infra*.

4 Program Manager Technical Advice (PMTA) 2018-17 (Apr. 10, 2018), https://www.irs.gov/pub/iranoa/pmta_2018_17.pdf.

Tax Credit (CTC), the Additional Child Tax Credit (ACTC), and the Earned Income Tax Credit (EITC), respectively) on 17,691 returns in fiscal year (FY) 2018—often nearly two years after the returns were filed.⁵

The IRS improperly denied credits to 289 of these taxpayers and sent 113 of them the wrong letters to explain why their credits were disallowed, according to the Treasury Inspector General for Tax Administration (TIGTA).⁶ TIGTA also said the IRS wasted over \$400,000 doing manual reviews because it did not address the problem systemically and did not reject e-filed returns immediately—a process that would have allowed taxpayers or their preparers to address the problem right away.⁷

The National Taxpayer Advocate is concerned that the IRS may continue to use MEA and its new post-processing MEA in situations where it poses unreasonable risks to the taxpayer's *right to pay no more than the correct amount of tax, to challenge the IRS's position and be heard, to privacy (i.e., that enforcement will "be no more intrusive than necessary")*, and *to a fair and just tax system (i.e., to "expect the tax system to consider [their specific] facts and circumstances")*. She is also concerned it will waste resources when the resulting assessments are incorrect.

ANALYSIS OF PROBLEM

Discrepancies in Data Do Not Mean an Assessment Is Needed

Discrepancies can appear on returns even if the taxpayer is entitled to the benefits he or she claimed. For example, the IRS has MEA to assess tax when a taxpayer claims a dependent, but does not include the dependent's correct taxpayer identification number (TIN).⁸ Because a TIN is a long string of numbers, it can contain typographical errors.

A TAS study of math errors on dependent TINs found that:⁹

- The IRS subsequently reversed (at least part of) the math errors on 55 percent of the returns with incorrect TINs.
- The IRS could have resolved 56 percent of them using information already in its possession (*e.g.*, the TIN listed on a prior year return).
- In 41 percent of the cases where the IRS could have corrected the TINs (and in another 11 percent where it could have corrected at least one TIN), the taxpayer was denied a tax benefit that he or she was entitled to receive.
- Such taxpayers were denied \$1,274 on average.

5 IRS response to TAS information request (Nov. 9, 2018).

6 Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 13 (Feb. 26, 2018).

7 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 11 (Feb. 26, 2018).

8 IRC § 6213(g)(2)(H). In the case of an individual, a taxpayer identification number (TIN) may include a Social Security number (SSN), an Individual TIN (ITIN), or an Adoption TIN (ATIN). IRS, Pub. 1915 (2018). An ITIN is issued to individuals who are required to have a TIN for tax purposes, but are not eligible for a SSN. An ATIN is a temporary number issued to a child who is being adopted in the U.S. before the child can obtain a SSN.

9 National Taxpayer Advocate 2011 Annual Report to Congress vol. 2, 114, 117-120 (Research Study: *Math Errors Committed on Individual Tax Returns – A Review of Math Errors Issued on Claimed Dependents*).

The IRS's failure to investigate potential errors before assessing tax is inconsistent with general direction from Congress that the IRS should not use MEA to resolve uncertainty against the taxpayer.¹⁰

As another example, the IRS also has MEA to reverse EITC claimed by a noncustodial parent for a child who is shown on the Federal Case Registry (FCR) of child support orders as being in someone else's custody.¹¹ An IRS study found that 39 percent of the children reported on the returns selected for audit, based solely on FCR data mismatches were claimed correctly.¹² Because FCR data is not sufficiently reliable, the IRS has adopted the National Taxpayer Advocate's recommendation not to assess math errors based on mismatches between returns and FCR data. However, the IRS may not have undertaken this study without direction from Congress.

MEA Procedures Raise Concerns When the Assessments Are Erroneous

Any expansion of MEA raises the following concerns when the resulting assessments could be in error:¹³

- The IRS does not always try to resolve apparent discrepancies before burdening taxpayers with summary assessments.
- IRS communication difficulties—confusing letters, fewer letters (*i.e.*, one math error notice as compared to three or more letters in an audit), and shorter deadlines (*i.e.*, 60 days as compared to more than 120 days in an audit)—make it more difficult for taxpayers to respond timely.¹⁴
- Because it is easier to miss math error deadlines, more taxpayers—particularly low income taxpayers—will have the burden to prove their returns are correct, and lose access to the Tax Court.

10 H.R. REP. No. 94-658, at 290 (1976) (“... care should be taken to be sure that what appears to be an error in addition or subtraction is not in reality an error in transcribing a number from a work sheet, with the final figure being correct even though an intermediate arithmetical step on the return appears to be wrong ... It is expected that the Service will check such possible sources of arithmetical errors before instituting the summary assessment procedures.”). *Id.* at 291 (“... this summary assessment procedure is not to be used where the Service is merely resolving an uncertainty against the taxpayer.”).

11 Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, § 303(g), 115 Stat. 38, 56-57 (2001) (codified at IRC § 6213(g)(2)(M)). The House Conference Report requested a study of the FCR database by the Department of Treasury, in consultation with the National Taxpayer Advocate, of the accuracy and timeliness of the data in the FCR; the efficacy of using math error authority in this instance in reducing costs due to erroneous or fraudulent claims; and the implications of using math error authority in this instance, given the findings on the accuracy and timeliness of the data. H.R. REP. No. 107-84, at 147 (2001) (Conf. Rep.). See also National Taxpayer Advocate 2002 Annual Report to Congress 189 (Legislative Recommendation: *Math Error Authority*).

12 See IRS, *Federal Case Registry Final Report*, Project 5-02-12-3-005 (CR-39) (July 2003) (“almost 39% of the FCR children were allowed per examination ... With the exclusion of no reply cases ... the rate of FCR children that are allowed per examination increases to 53.5%”).

13 For a more detailed discussion of the differences between the audit and math error procedures, see National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress 114-118. For a detailed discussion of the math error process and math error notices, see Most Serious Problem: *Math Error Notices: Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden*, *infra*.

14 Although it should be easier for taxpayers to understand and respond to audit notices than math error notices, a TAS study found “almost 40 percent [of those receiving an Earned Income Tax Credit (EITC) audit notice] ... did not understand what the IRS was questioning ... [and] only about half of the respondents felt that they knew what they needed to do in response to the audit letter.” National Taxpayer Advocate 2007 Annual Report to Congress vol. 2, 100, 103-104. For a discussion of continuing problems with math error notices see, Most Serious Problem: *Math Error Notices: Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden*, *infra*.

- Internal Revenue Code (IRC) § 7605(b) generally prohibits the IRS from examining a return more than once, but the IRS can examine a return after making a math error adjustment.¹⁵

For these reasons, the National Taxpayer Advocate has opposed the Treasury Department's repeated requests for Congress to authorize it to use its regulatory authority to expand the types of issues the IRS could address using MEA (called "correctable error" authority).¹⁶ She recommended that Congress limit MEA to the following situations:¹⁷

1. There is a mismatch between the return and unquestionably reliable data.
2. The IRS's math error notice clearly describes the discrepancy and how taxpayers may contest the assessment.
3. The IRS has researched the information in its possession (*e.g.*, information provided on prior-year returns) that could reconcile the apparent discrepancy.¹⁸
4. The IRS does not have to analyze facts and circumstances or weigh the adequacy of information submitted by the taxpayer to determine if the return contains an error.
5. The abatement rate for a particular issue or type of inconsistency is below a specified threshold for those taxpayers who respond.
6. For any new data or criteria, the Department of Treasury, in conjunction with the National Taxpayer Advocate, has evaluated and publicly reported to Congress on the reliability of the data or criteria for purposes of assessing tax using math error procedures.

The IRS could adopt these common-sense limits without legislation. Doing so would minimize risks to the taxpayer's *right to pay no more than the correct amount of tax* or *to challenge the IRS's position and be heard*. It would also help prevent the IRS from wasting resources on incorrect assessments.

Post-Processing Math Error Adjustments Are Even More Burdensome

Post-processing math error adjustments are even more burdensome for taxpayers than regular math error adjustments. If the IRS summarily assesses a liability after processing the return, the taxpayer is less likely to be able to:

- Receive and understand the IRS's communication;
- Discuss the issue with a preparer;
- Access underlying documentation;
- Recall and explain facts relevant to the filing;
- Return any refunds (or endure an offset) without experiencing an economic hardship; and

15 For a detailed discussion of how math errors and other "unreal audits" bypass taxpayer protections, see, *e.g.*, National Taxpayer Advocate 2017 Annual Report to Congress 49-63 (Most Serious Problem: *The IRS Is Conducting Significant Types and Amounts of Compliance Activities That It Does Not Deem to Be Traditional Audits, Thereby Underreporting the Extent of Its Compliance Activity and Return on Investment, and Circumventing Taxpayer Protections*).

16 See, *e.g.*, Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2013 Revenue Proposals* 168-169 (Feb. 2012); Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2017 Revenue Proposals* 225-226 (Feb. 2016). For concerns about the recommendation, see, *e.g.*, National Taxpayer Advocate 2017 Purple Book 44-45; National Taxpayer Advocate 2015 Annual Report to Congress 329-339; Nathan J. Richman, *Expanding Math Error Authority Could Worsen 2 Tax Systems Issues*, 2017 TNT 127-2 (July 5, 2017).

17 See National Taxpayer Advocate 2015 Annual Report to Congress 329-339.

18 It is TAS's understanding that the IRS is legally authorized to correct returns using math error authority so as to benefit the taxpayer (*e.g.*, when it has information sufficient to determine the taxpayer is entitled to a credit).

- Learn how to avoid the problem before the next filing season.

Perhaps for the same reasons, the law limits how long after filing the IRS can make assessments, and the IRS tries to maintain the “currency” of its audits and has a policy statement that generally bars examiners from addressing old delinquencies.¹⁹ Because taxpayers are supposed to have the *right to quality service* and *to privacy* (*i.e.*, the right to expect that enforcement action will be no more intrusive than necessary), the IRS can and should take similar precautions to ensure it detects math errors while processing returns or not at all. If instead, the IRS uses post-processing MEA to recover EITC benefits, it could be sued for violating the taxpayer’s constitutional rights.²⁰

The IRS Is Now Using Post-Processing MEA to Recover Credits

In December 2015, the Protecting Americans From Tax Hikes (PATH) Act barred taxpayers from claiming the AOTC, CTC, ACTC, or EITC using TINs issued after the due date of the return (*e.g.*, using TINs issued in 2015 to file returns for 2014 during 2016, which are called retroactive claims).²¹ TIGTA found the IRS had improperly paid these credits to 15,744 taxpayers who filed 2014 returns during the 2016 filing season.²² TIGTA subsequently found the IRS improperly paid retroactive claims on 2013-2015 returns to 4,509 taxpayers during the 2017 filing season.²³ The IRS used post-processing MEA to recover these credits from 17,691 taxpayers in FY 2018—often nearly two years after they filed the returns.²⁴

Like the TAS study of MEA (discussed above), TIGTA’s review of returns processed during the 2017 filing season found that the IRS sometimes got it wrong—improperly denying credits to 289 taxpayers.²⁵ Moreover, it sent 113 taxpayers the wrong letters to explain why their credits were disallowed, thus giving them the wrong explanations, undermining their ability to correct the IRS’s mistakes or obtain judicial review.²⁶

19 IRC § 6501(a) (assessment limitations period); IRS, *Reducing the Federal Tax Gap, A Report on Improving Voluntary Compliance* 36 (Aug. 2, 2007), https://www.irs.gov/pub/irs-news/tax_gap_report_final_080207_linked.pdf (discussing audit currency); Policy Statement 5-133 (P-5-133), *reprinted as* IRM 1.2.14.1.18(5) (Aug. 4, 2006) (generally limiting the “enforcement of delinquency procedures for not more than six (6) years”).

20 For a discussion of this argument, see National Taxpayer Advocate, *The IRS Might Recover EITC Using Its Newly Discovered Post-Processing Math Error Authority, but Is It Constitutional?* NTA Blog (Sept. 13, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-the-irs-might-recover-eitc-using-its-newly-discovered-post-processing-math-error-authority-but-is-it-constitutional>.

21 See Sections 204-206 of Division Q of the Consolidated Appropriations Act, Pub. L. No. 114-113, 129 Stat. 2242 (2015) (codified at IRC §§ 32(m), 24(e), and 25A(i)(6)).

22 See TIGTA, Ref. No. 2017-40-042, *Processes Do Not Maximize the Use of Third-Party Income Documents to Identify Potentially Improper Refundable Credit Claims* 5 (July 17, 2017). See also TIGTA, Ref. No. 2018-40-032, *The Internal Revenue Service Is Not in Compliance with Improper Payment Requirements* 11-12 (Apr. 9, 2018); TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 3 (Feb. 26, 2018).

23 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 9-10 (Feb. 26, 2018).

24 IRS response to TAS information request (Nov. 9, 2018).

25 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 10 (Feb. 26, 2018).

26 *Id.* at 13 (Feb. 26, 2018).

However, the IRS did not adopt TIGTA's recommendation to substitute a rejection process for e-filed tax returns, citing technical difficulties.²⁷ Upon receipt of the return, the IRS could reject it and immediately inform the taxpayer that the TIN that was used to claim the credit was not issued before the due date of the return.²⁸ Such a process would give the taxpayer an opportunity to address the apparent discrepancy proactively, often with the assistance of his or her preparer or tax preparation software, and save the IRS resources (*i.e.*, over \$400,000, according to TIGTA).²⁹

CONCLUSION

Because of the lack of due process afforded to taxpayers when the IRS uses MEA, it should only be used for clear errors. Clear errors can be detected and addressed immediately when the taxpayer is best prepared to understand the IRS's communications and respond timely and appropriately. To reduce the temptation to use MEA in ways that trample taxpayer rights and create costly rework, the IRS should publicly announce a policy that limits its use. Such a policy would help it resist calls to use MEA and post-processing MEA inappropriately.

RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS, in collaboration with the National Taxpayer Advocate, adopt a policy statement (or similar guidance) to:

1. Limit the circumstances in which the IRS will use MEA (including post-processing MEA).
2. Voluntarily adopt the limits on the use of MEA recommended to Congress by the National Taxpayer Advocate in her 2015 annual report.³⁰
3. Require the IRS to alert taxpayers to any discrepancies as early as possible, for example, by rejecting an e-filed return, where permissible, rather than waiting to use MEA, or waiting even longer to use post-processing MEA.

27 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 12-13 (Feb. 26, 2018). Any such rejection should obviously be accompanied with a clear and detailed explanation. Before rejecting any return, the IRS's systems should use information in the IRS's possession to help taxpayers correct any apparent discrepancies, such as typos, that might help the taxpayer qualify for the credits they claimed.

28 For the same reasons, the National Taxpayer Advocate recommended the IRS "Reject electronic filed returns when the taxpayer received APTC [the advanced premium tax credit] and did not reconcile on Form 8962, *Premium Tax Credit (PTC)*, as the IRS plans to do for silent returns that do not include Form 8965, *Health Coverage Exemptions*." National Taxpayer Advocate 2017 Annual Report to Congress 266, 276 (Most Serious Problem: *The IRS Has Made Progress in Implementing the Individual and Employer Provisions of the ACA But Challenges Remain*). Of course, the IRS would first have to ensure it is authorized to reject such returns.

29 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 12-13 (Feb. 26, 2018). If the taxpayer felt they were still entitled to the credit, he or she could file on paper and then explain his or her reasons in any subsequent examination or math error process.

30 See National Taxpayer Advocate 2015 Annual Report to Congress 329-339.