

MSP  
#4**PROCESSING DELAYS: Refund Fraud Filters Continue to Delay Taxpayer Refunds for Legitimately Filed Returns, Potentially Causing Financial Hardship****RESPONSIBLE OFFICIAL**

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**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

**PROBLEM**

The IRS has designed a number of filters to assist in the detection and prevention of identity theft (IDT) and non-IDT refund fraud. These fraud detection filters are an essential component of combating refund fraud, and from January 1 through September 30, 2019, have protected the IRS from issuing about \$2.7 billion in improper refunds.<sup>2</sup> However, the filters have also created problems for taxpayers, most notably delays in obtaining their refunds, creating a financial hardship for hundreds of thousands of taxpayers. Predictably, this resulted in more taxpayers seeking Taxpayer Advocate Service (TAS) assistance. Specifically, these problems include:

- A new non-IDT refund fraud filter (Filter X) suspended nearly double the returns than projected, and about a quarter of these returns took 40 days or longer to be processed;<sup>3</sup>
- The IRS received most W-2 information timely, but the transmittal of paper W-2s was delayed;<sup>4</sup>
- Other non-IDT refund fraud filters had false positive rates (FPRs) of 71 percent;<sup>5</sup>
- Refund delays were nearly three weeks beyond normal processing times, causing economic hardship for a large number of taxpayers;<sup>6</sup>
- The IRS often provides taxpayers little information regarding the precise reason for refund delays and what steps they can take to expedite the process; and

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://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 IRS response to TAS consolidated end of year information request (Nov. 22, 2019). Filter X also protected about \$1.6 million in revenue after June 15, 2019 (the date that Filter X was retired). The information on these returns was verified after this date. IRS, Identity Theft (IDT) and Integrity and Verification Operations (IVO) Performance Report, Slide 7 (Oct. 9, 2019).

3 IRS Compliance Data Warehouse (CDW), Individual Returns Transaction File (IRTF) Form 1040 (Oct. 23, 2019); IRS CDW, Individual Master File (IMF) Transaction History File (Oct. 23, 2019).

4 By the end of filing season (FS) 2019, the IRS had received information on 2.6 million paper Forms W-2 from the Social Security Administration (SSA), compared to information on 6.2 million paper Forms W-2 during the same period in FS 2018. Generalized Mainline Framework (Jan. 2 through Apr. 26, 2019).

5 IRS response to TAS consolidated end of year information request (Nov. 22, 2019).

6 *Id.*

- The issues with the new Filter X, in conjunction with high FPRs and processing delays, contributed to a 405 percent increase in TAS non-IDT refund fraud inventory from January 1 through September 30, 2019, compared with the same timeframe in 2017.<sup>7</sup>

## IMPACT ON TAXPAYERS

### Background

The IRS's efforts to detect and prevent refund fraud are managed by the Return Integrity Verification Operations (RIVO) of Wage and Investment (W&I), which oversees both the IDT refund fraud program in the Taxpayer Protection Program (TPP) and non-IDT refund fraud in the Pre-Refund Wage Verification Hold Program (PRWVH).<sup>8</sup>

These programs rely primarily on two systems to detect and prevent fraud: the Dependent Database (DDb) to detect IDT, and the Return Review Program (RRP) to detect IDT *and* non-IDT refund fraud. The DDb contains filters comprised of rules that are binary in nature (*i.e.*, if the rule is broken, the return will be selected for further analysis; if the rule is not broken, the return will continue through normal processing).

The RRP, on the other hand, contains filters comprised of both rules and models.<sup>9</sup> Once the models complete their analysis, each return is given a risk score. That score is fed into RRP filters, which will select returns based on whether the score exceeds a specified threshold while considering other information in the system. If the score exceeds the threshold and other conditions are met, the IRS will route the return to either the TPP or PRWVH, whichever is most appropriate.

Figure 1.4.1 provides a simplified flowchart of the complicated processes the IRS uses to screen returns where a taxpayer has claimed a refund and the IRS suspects either IDT or non-IDT refund fraud.

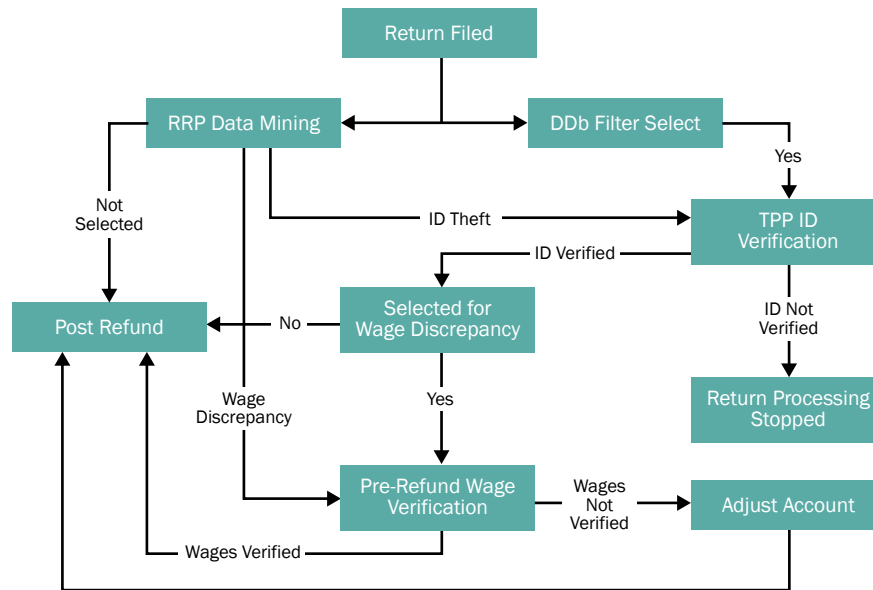
7 Data obtained from Taxpayer Advocate Management Information System (TAMIS). TAS extracts data on the day following the last day of the month.

8 See Internal Revenue Manual (IRM) 25.25.6.1(1) and (3), Program Scope and Objectives (Aug. 20, 2019); IRM 25.25.3.1(1), Program Scope and Objectives (Aug. 30, 2019). For purposes of this Most Serious Problem, we have used "TPP" and "IDT refund fraud program" interchangeably, as well as the terms, "pre-refund wage verification hold program" and "non-IDT refund program."

9 National Taxpayer Advocate 2018 Annual Report to Congress 79-90 (Most Serious Problem: *False Positive Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*). The filter models use techniques such as predictive models, business rules, and clustering.

FIGURE 1.4.1<sup>10</sup>

## Refund Return Screening for Identity Theft and Non-Identity Theft Refund Fraud



Once the IRS selects a taxpayer's return into the TPP program, it asks the taxpayer to authenticate his or her identity either over the phone, online, or by visiting a Taxpayer Assistance Center.<sup>11</sup> For taxpayer returns selected into the PRWVH program, the IRS matches the information on the return with third-party information provided by the taxpayer's employer(s) and payor(s) to the Social Security Administration (SSA) or the IRS. Beginning in Filing Season (FS) 2017, employers and other specified payers were required to submit third-party reporting information (Forms W-2 and 1099-MISC-Nonemployee Compensation) no later than January 31 to the SSA or the IRS.<sup>12</sup> The purpose of this change in the law was to get information to the IRS earlier so it could have more time to match the wage and tax information reported on the taxpayer's return against information submitted by third parties; however, the IRS does not receive all third-party information from SSA by January 31.<sup>13</sup> Once the SSA receives third-party information from employers, it begins the process of transmitting this information to the IRS in accordance with an agreement entered into between both agencies. This transmittal process is efficient for third-party information submitted to the SSA electronically. For paper

10 For a more detailed roadmap of IRS processes, see IRS Pub. 5341, *The Taxpayer Roadmap 2019: An Illustration of the Modern United States Tax System* (Sept. 2019).

11 IRM 25.25.6.1.7(3), *Taxpayer Protection Program Overview* (Aug. 20, 2019). International taxpayers can mail in documentation to authenticate their identity. Letter 5447C, *Potential Identity Theft during Original Processing; Foreign Address* (Sept. 2018).

12 Section 201 of the Protecting Americans From Tax Hikes (PATH) Act of 2015 amended IRC § 6071 to require that certain information returns be filed by January 31, generally the same date as the due date for employee and payee statements and are no longer eligible for the extended filing date for electronically filed returns under IRC § 6071(b). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 201 (2015). However, the January 31 deadline for submitting W-2 information does not apply to other reporting requirements of income sources. For example, state and local refunds are required to be reported to the IRS on or before February 28 (March 31 if filed electronically). 26 C.F.R. § 1.6050E-1.

13 See 42 U.S.C. 432 § 232, *Processing of Tax Data*; 20 C.F.R. § 422.114, *Annual Wage Reporting Process*. "Under the authority of section 232 of the Act, SSA and IRS have entered into an agreement that sets forth the manner in which SSA and IRS will ensure that the processing of employee wage reports is effective and efficient."

information though, the SSA administers a laborious manual process, resulting in backlogs in processing paper W-2s, which keeps the SSA from transmitting some data to the IRS until August or September.<sup>14</sup>

In calendar year (CY) 2019, the IRS made several changes to improve the efficiency and effectiveness of the refund fraud program, namely reducing processing times and increasing the accuracy of filter selections. The changes include:

- During the filing season, the IRS modified its new non-IDT refund fraud filter (Filter X) to systemically check for the posting of third-party information daily instead of weekly;
- When the return was selected due to a mismatch between the information on the return and the third-party information, the IRS conducted additional analysis. If the third-party information had no impact on the amount of the refund, the refund was released immediately; and
- When a return carried with it both an IDT and non-IDT refund fraud concern, IRS systems had the capability to systemically verify income and withholding information upon successful authentication of the taxpayer's identity, thereby compressing the processing time.

During FS 2020, the IRS intends to expand the number of non-IDT refund fraud filters that will check for posting of third-party information daily instead of weekly and release the refunds systemically once the IRS verifies the information on the return.<sup>15</sup> TAS anticipates that this additional automation of the IRS's fraud detection filters will further reduce processing times. These improvements are in addition to a change this year in the IRS's ability to verify returns without third-party information from certain employers' submissions. More specifically, for FS 2019, the IRS identified employers who historically filed late income information. If a taxpayer's return was selected and the information was largely consistent with prior year returns, the IRS presumed the return was legitimate and released the refund.<sup>16</sup> The National Taxpayer Advocate applauds the IRS for implementing these improvements to its filters to help expedite the process while also protecting revenue.

### **A New Non-Identity Theft Refund Fraud Filter (Filter X) Suspended Nearly Double the Returns Projected, and About a Quarter of These Returns Took 40 Days or Longer to Be Processed**

While the IRS has made a number of improvements in its filters, issues remain. For FS 2019, the IRS added Filter X to assist in identifying returns suspected of non-IDT refund fraud. Filter X selects returns where Earned Income Tax Credit (EITC) or the Additional Child Tax Credit (ACTC) is claimed on the return; where there is either no or only some W-2 information available, and thus the information and withholding on the return cannot be verified; and where other criteria programmed into the filter have been met (*i.e.*, the returns that do not meet the programmed criteria will proceed through normal processing channels).<sup>17</sup>

The IRS originally projected that Filter X would suspend about 500,000 returns annually;<sup>18</sup> this projection was a significant understatement, as it ultimately suspended about 1.1 million returns from

14 Government Accountability Office (GAO), GAO-14-633, *Identity Theft: Additional Actions Could Help IRS Combat the Large, Evolving Threat of Refund Fraud* 21 (Aug. 2014).

15 IRS response to TAS information request (July 16, 2019).

16 IRS, IDT and IVO Performance Report, Slide 8 (Oct. 9, 2019). The IRS released 223,515 refunds as a result of the Information Return Processing (IRP) Release Plan.

17 IRS response to TAS information request (Sept. 23, 2019).

18 IRS Processing Year 2019 Treatment Process Update (Dec. 5, 2018).

January 1 through September 26, 2019.<sup>19</sup> Of the returns held by Filter X, about half (590,384) had the original refund claimed on the return released after February 15, 2019, the earliest date under the law that the IRS could release these refunds.<sup>20</sup> The IRS held half of these, or about a quarter of all returns selected by Filter X, for 40 days or longer from the time the return was selected.<sup>21</sup> These delays caused hardship for a number of taxpayers who were relying on their refunds and had to come to TAS for assistance.

### The IRS Received Most W-2 Information Timely, But the Transmittal of Some Paper W-2s Was Delayed

The IRS's daily posting of third-party information resulted in it posting a large amount of W-2 data to IRS systems sooner. For instance, the IRS received 219 million W-2s through February 4 in FS 2019, compared with 101 million for the same period in FS 2018 — an increase of about 117 percent.<sup>22</sup> The receipt of significantly more W-2s earlier in the filing season helps speed up the processing of returns. As part of the Taxpayer First Act, Congress amended Internal Revenue Code (IRC) § 6011 authorizing the IRS, beginning in 2022, to issue regulations that require employers to file electronic information returns when filing more than ten documents annually.<sup>23</sup> This will continue the earlier receipt of W-2 information, allowing the IRS filters to verify wage information earlier. However, the IRS will continue to struggle with the delays caused by paper W-2s. The IRS should work with SSA to speed up the transmission of paper W-2 data.

### Other Refund Fraud Filters Had False Positive Rates of 71 Percent

Problems persist for the IRS's remaining set of refund fraud filters. Specifically, these filters had an FPR of 71 percent for January 1 through October 2, 2019.<sup>24</sup> The FPR is the number of returns that turned out to be legitimate divided by the number of returns selected by the filter.<sup>25</sup> As Figure 1.4.2 illustrates, this FPR is lower than last year's by about ten percent, but is higher than 2017.

19 IRS, IDT and IVO Performance Report, Slide 8 (Oct. 9, 2019). This filter was retired beginning in June because it is believed that at this point, all the W-2 information that SSA has should have been transmitted to IRS.

20 IRS, CDW, IRTF Form 1040 (Oct. 23, 2019); IRS CDW, IMF Transaction History File (Oct. 23, 2019). Out of the 1,072,192 returns, 419,885 were released shortly after February 15, the earliest date the IRS could release these returns under the law. Of the remaining 652,307 returns, 590,384 had the refunds released because the IRS had received W-2 data from SSA. The remaining 61,923 returns (652,307–590,384) are still being held by Filter X and are not yet resolved, have been sent to a treatment stream such as Exam, or the taxpayer received a partial refund or no refund.

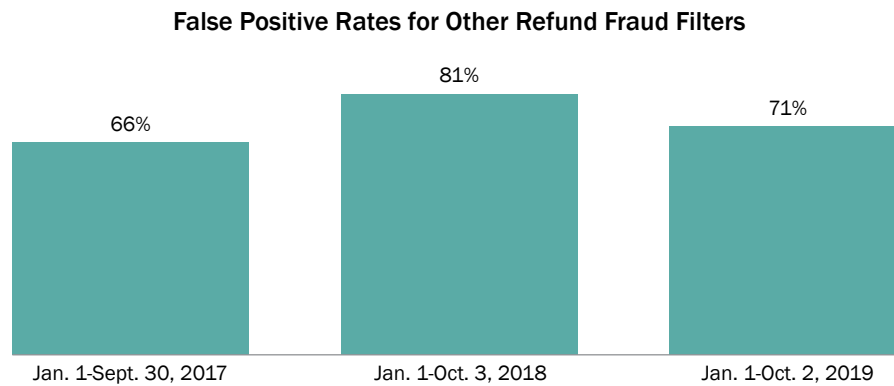
21 IRS, CDW, IRTF Form 1040 (Oct. 23, 2019); IRS CDW, IMF Transaction History File (Oct. 23, 2019).

22 IRS, IDT and IVO Performance Report, Slide 10 (Feb. 6, 2019).

23 Taxpayer First Act of 2019, H.R. 1957, § 2301, 116th Cong. The National Taxpayer Advocate has previously made a similar recommendation. See National Taxpayer Advocate 2017 Annual Report to Congress 267, 276 (Legislative Recommendation: *Timing of Refunds: Direct the IRS to Study the Impact of Delaying the Issuance of Refunds to Allow Sufficient Time to Process Information Returns and Perform Document-Matching*). Treas. Reg. § 301.6011-2(b). This regulation, in certain situations, requires the following to be submitted electronically: Form 1042-S, 1094 series, 1095-B, 1095-C, 1098, 1098-E, 1098-T, 1099 series, 5498, 8027, W-2G, and Form W-2 and other forms treated as Form W-2.

24 IRS, IDT and IVO Performance Report Appendix, Non-IDT Refile Rate, Slide 1 (Oct. 9, 2019).

25 *Id.*

**FIGURE 1.4.2**<sup>26</sup>

Additionally, the returns that comprise the 71 percent FPR took the IRS, on average, 38 days to process.<sup>27</sup> However, the IRS processed the returns that turned out to be legitimate quicker when compared to the 2018 filing season. The IRS needs to continue to learn from the returns that were part of the FPR to further refine the filters and continually work to lower the FPR.

### Refund Delays Were Nearly Three Weeks Beyond Normal Processing Times, Causing Economic Hardship for a Large Number of Taxpayers

For non-IDT refund fraud, the IRS tracks how long it takes to release legitimate returns selected by fraud detection filters. This is referred to as the “operational performance rate” (OPR).<sup>28</sup> This figure represents the number of legitimate returns the non-IDT refund fraud filters selected that took more than four weeks for the IRS to release from the time of selection.<sup>29</sup> From January 1 through October 2, 2019, the OPR was 34 percent compared to a 64 percent rate for the same time period in the prior year – nearly half last year’s rate.<sup>30</sup> This means it took the IRS more than four weeks to release 34 percent of the returns these filters selected from the time of selection.<sup>31</sup> However, as discussed in last year’s Annual Report to Congress, the Operational FPR, which is the number of returns that comprise the FPR that took more than four weeks from the time of selection to process, better illustrates how many legitimate

26 IRS, IDT and IVO Performance Report, Slides 19 and 32 (Oct. 10, 2018) (showing rate for 2018); IRS response to TAS information request (Oct. 19, 2017) (providing rates for 2017).

27 IRS response to TAS information request (Sept. 23, 2019). W&I response to TAS consolidated end of year information request (Nov. 22, 2019).

28 The IRS defines the OPR as returns that are selected and not released by the pre-wage verification program within two weeks of selection (prior to selection, these returns are screened for an additional two weeks). The National Taxpayer Advocate believes the OPR is not an accurate measure of the post-screening/selection FPR.

29 National Taxpayer Advocate 2018 Annual Report to Congress 79, 84 (Most Serious Problem: *False Positive Rates: The IRS’s Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*). The OPR retains the same denominator as the FPR (the total number of returns selected by the IRS), but the numerator is decreased by the number of returns that the IRS clears as legitimate within two weeks of selection. See also IRS, IDT and IVO Performance Report Appendix, Non-IDT OPR Calculation, Slides 1-2 (Oct. 9, 2019).

30 IRS, IDT and IVO Performance Report Appendix, Non-IDT OPR Calculation, Slides 1-2 (Oct. 9, 2019); IDT and IVO Performance Report, Slide 32 (Oct. 10, 2018).

31 *Id.*

returns selected by the non-IDT refund fraud filters were delayed more than four weeks.<sup>32</sup> This Operational FPR rate has also improved, dropping to 55 percent for January 1 through October 2, 2019, compared to 72 percent for the same time period in the prior year.<sup>33</sup>

Although this drop is an improvement, the IRS still took more than four weeks from the time of selection to release nearly half of the returns that comprise the FPR.<sup>34</sup> The IRS should continue to take steps to reduce the Operational FPR if FPRs are to remain at the same level. Alternatively, the IRS should take steps to reduce the FPR, if it cannot further reduce the Operational FPR.

Additionally, TAS found there were delays in sending returns to the necessary treatment stream where the information on the returns could not be otherwise verified.<sup>35</sup> An analysis of TAS cases showed that out of 309 TAS case receipts with PRWVH indicators received between August 25 and August 31, 2019, 236 waited an average of 141 days from the return filing date for the IRS to screen and determine that it could not verify the information on the returns.<sup>36</sup> Further, as of October 1, 2019, the IRS had assigned only 36 percent of the 236 returns to a particular treatment stream. By October, the IRS should have received all W-2 information, and the fact that it had not yet released or sent to a treatment stream over 60 percent of these cases is concerning.

While it is essential for the IRS to prevent fraud and protect revenue, these processing delays, accompanied with the processing delays experienced by returns selected by Filter X due to the SSA's delays in transmitting paper W-2 data, caused a financial hardship for many taxpayers. These delays have a significant impact on low-income taxpayers. This is especially true for selected returns where EITC or ACTC is claimed. Often, low-income taxpayers are waiting on their refunds to pay day-to-day living expenses such as rent, car repairs, or healthcare, and any delay can cause taxpayers significant hardship. To address these processing delays, the IRS should look to increase staffing for the manual validation process so it can verify returns and assign them to the appropriate treatment stream quickly.

32 National Taxpayer Advocate 2018 Annual Report to Congress 79-91 (Most Serious Problem: *False Positive Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*). The Operational FPR is the ratio of the legitimate returns resolved after the four-week period (the numerator) and the number of returns left after the four-week period (the denominator). This formula is a more accurate depiction of the number of legitimate returns that took more than two weeks to be resolved from the time of selection than the OPR because, unlike the OPR, the numerator and denominator mirror one another. Specifically, both numbers exclude the number of returns resolved within two weeks of selection. On the other hand, the OPR does not exclude the number of returns resolved within two weeks of selection from the formula's denominator, which distorts the percentage and gives an inaccurate appearance of improved performance.

33 IRS, IDT and IVO Performance Report Appendix, Non-IDT Extended Refile Rate Calculation, Slide 3 (Oct. 9, 2019); the IRS did not track this data until FS 2019, but TAS calculated its own rate for FS 2018. See National Taxpayer Advocate 2018 Annual Report to Congress 79-91 (Most Serious Problem: *False Positive Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*). The IRS refers to this as the extended refile rate, but for purposes of this discussion, we will refer to it as the Operational FPR.

34 IRS, IDT and IVO Performance Report Appendix, Non-IDT Extended Refile Rate Calculation, Slide 3 (Oct. 9, 2019).

35 If the information on returns cannot be verified through a verification process, the returns will then be referred to one of three treatment streams: CPO5A/WOW, wage and withholding only issues (no refundable credits to be addressed); Automated Questionable Credit (AQC) Program, for wage and withholding issues where a refundable credit is claimed; or Correspondence Examination, selections by the Examination Department and not eligible for another IVO treatment stream (refund tolerances and the availability of budget resources will affect how many returns are selected).

36 Case receipts data obtained from TAMIS on September 13, 2019. The sample was based on a 95 percent confidence level with a 4.2 percent margin of error rate.



### The IRS Generally Provides Taxpayers Little Information Regarding the Precise Reason for Refund Delays and What Steps They Can Take to Expedite the Process

In prior Annual Reports to Congress, TAS has pointed out that taxpayers who call the IRS because their refunds have been held as part of the non-IDT refund fraud program receive little information regarding the cause of the refund delay.<sup>37</sup> Specifically, prior to April 2019, IRS assistors were advised to tell taxpayers that “...no further action is required.”<sup>38</sup>

As a result of TAS’s successful advocacy, the Accounts Management IRM has been updated to instruct assistors to provide taxpayers with the following information:

Advise the taxpayer that we select some returns to determine if income, expenses, and credits are being reported accurately. Recommend the taxpayer review their return and all income information statements (*e.g.*, Form W-2) to ensure all income and withholding matches the information reported on the return. If they determine they have made an error, file an amended return.<sup>39</sup>

Although the IRS has made improvements regarding the information it gives taxpayers while holding their refunds, communication regarding the status of the taxpayer’s return falls short in several instances and does not fully observe the taxpayer’s *right to be informed*. Specifically:

- Letter 4464C, Questionable Refund 3rd Party Notification Letter, instructs taxpayers that the IRS is holding their refund, but does not provide any guidance as to what they can do to expedite the process (*i.e.*, review their return to ensure the income and withholding reported is accurate, and if it is not, file an amended return);<sup>40</sup>
- Not all taxpayers whose refunds are held as part of the non-IDT refund fraud program receive the same periodic update notices. The IRS sends out Notice CP05, We’re Holding Your Refund Until We Finish Reviewing Your Return, and follows up with a subsequent interim letter it sends every 60 days if it is still holding the refund.<sup>41</sup> Conversely, taxpayers whose returns the IRS selected for verification by other non-IDT refund fraud filters receive Letter 4464C, Questionable Refund 3rd Party Notification, and no other subsequent interim letter while the IRS reviews the return;<sup>42</sup> and
- When an account is transferred by RIVO to a different IRS treatment stream such as Exam, taxpayers receive no notification, and the taxpayer won’t hear from the IRS again until an employee in that treatment stream begins working the account.

37 National Taxpayer Advocate 2017 Annual Report to Congress 219, 225 (Most Serious Problem: *Fraud Detection: The IRS Has Made Improvements to Its Fraud Detection Systems, But a Significant Number of Legitimate Taxpayers Are Still Being Improperly Selected by These Systems, Resulting in Refund Delays*).

38 IRM 21.5.6.4.35.3.1.2(2), -R Freeze with IVO Involvement - No IVO Letter or Notice Issued (Oct. 1, 2018).

39 IRM 21.5.6.4.35.3.1.2(2), -R Freeze with IVO Involvement - No IVO Letter or Notice Issued (Oct. 1, 2019).

40 Letter 4464C, Questionable Refund 3rd Party Notification Letter (“What you need to do: If you filed the tax return: You don’t need to do anything at this time. We understand your tax refund is very important to you and we’ll work to complete our review as quickly as possible.”). TAS received several submissions on this issue to its Systemic Advocacy Management System (SAMS). TAS SAMS issues 40219, 41107, and 41114.

41 IRM 21.5.6.4.35.3.1.4(2), -R Freeze with IVO Involvement - IVO Letter 2645C/2644C Issued (Oct. 1, 2019); Notice CP 05, We’re Holding Your Refund Until We Finish Reviewing Your Return. Although an interim letter is manually issued for accounts where a Letter 4464C is issued and the return review has not been completed, it has been TAS’s experience that this manual issuance of the interim letter is done inconsistently.

42 Although an interim letter is manually issued for accounts where a Letter 4464C is issued and the return review has not been completed, it has been TAS’s experience that this manual issuance of the interim letter is done inconsistently.



Understandably, the IRS needs to be very careful about the amount of information it releases to prevent supporting fraud. However, when taxpayers are provided information regarding the status of their refunds, including what actions they can take to expedite the process, they may be less likely to call the IRS inquiring about their refunds and take steps to help identify if there is an issue with their return. Recently, RIVO has agreed to work with TAS on piloting notices that have more information about why the IRS is holding the taxpayer's return and what they can do to address the problem.<sup>43</sup> TAS looks forward to working with RIVO on this pilot to test the impact on taxpayer behavior and better observe the taxpayer's *right to be informed*.

TAS is also currently working with the e-file industry to ensure that preparation and filing software include sufficient alerts on (1) the importance of accurately reporting on the return information from third-party information reports and (2) when the law allows the IRS to release refunds. For example, taxpayers may not know the importance of information on the return matching other third-party documentation. In an effort to obtain their refunds as early as possible, some taxpayers may use their last paystub of the year to fill in the income and withholding on their return. However, a discrepancy between the year's last paystub and the W-2 may result in the refund fraud filter identifying the return, which will delay the processing of the refund. Additionally, if the taxpayer's refund includes EITC or ACTC, this early filing is futile as, by law, the IRS cannot release their refund until after February 15.<sup>44</sup>

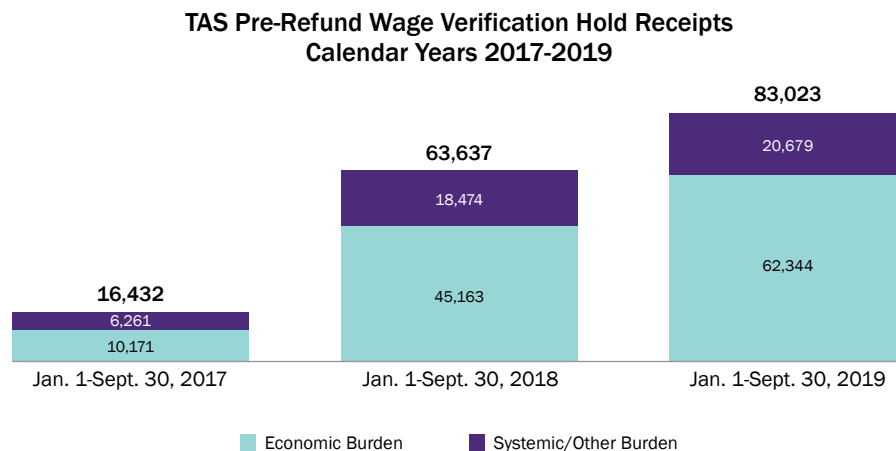
## IMPACT ON THE TAXPAYER ADVOCATE SERVICE

### Issues With the New Filter X, in Conjunction With High False Positive Rates and Processing Delays, Contributed to a 405 Percent Increase in TAS Non-Identity Theft Refund Fraud Cases

As discussed above, IRS challenges with PRWVH cases have resulted in a large number of taxpayers seeking TAS assistance. As shown in Figure 1.4.3, TAS PRWVH case receipts have increased over five times over the past three years, from over 16,000 cases in CY 2017 to over 83,000 in CY 2019, and about 75 percent of the case receipts for CY 2019 were accepted under TAS's economic hardship criteria.

43 TAS/Return Integrity and Compliance Services (RICS) Executive Meeting (Sept. 9, 2019).

44 See PATH Act of 2015, Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 201 (2015).

FIGURE 1.4.3<sup>45</sup>

The increase in cases — significantly more than TAS anticipated — resulted in delays in TAS’s ability to timely respond to and work cases.

To more precisely identify the root of this increase, TAS Research reviewed nearly 32,000 TAS closed cases involving PRWVH, received between January 28 and June 30, 2019, where the taxpayers ultimately received the refund claimed on their original returns. A majority of these involved the new Filter X.<sup>46</sup> As discussed above, a number of returns selected by Filter X were delayed due to the slow transmittal of paper W-2 data by SSA. Additionally, there were also a subset of cases where delays in sending cases to the necessary treatment stream resulted in taxpayers seeking TAS assistance. These issues, which the IRS can take steps to improve, delayed the processing of returns and were the primary factors behind TAS’s significant increase in PRWVH case receipts. For a more in-depth discussion of TAS’s non-IDT refund fraud case receipts, see the Case Advocacy section in this report.<sup>47</sup>

## CONCLUSION

When taxpayers file their tax returns, they anxiously await the receipt of their refunds and actively monitor their status. Taxpayers who have filed on time and done everything right do not understand why the IRS holds their refunds for more than a month and why it does not explain exactly what is happening and how to fix the issue. The IRS has made significant improvements to its refund fraud program and plans to continue making improvements in the upcoming filing season. However, refund delays and high false positive rates continue, harming significant numbers of taxpayers. These delays create anxiety and frustration for taxpayers, infringe on taxpayers’ rights, and result in more requests for TAS assistance. The IRS needs to take additional steps to improve its filters, improve communications with taxpayers, and improve the time in which it processes legitimate returns.

<sup>45</sup> Data obtained from TAMIS (Oct. 1, 2019; Oct. 1, 2018; Oct. 1, 2017).

<sup>46</sup> TAMIS cases for tax year 2018, Master File Tax Code (MFT) 30, received between January 28, 2019, and June 30, 2019, with primary core issue code 045 or secondary core issue code 045 and other specifications and exclusions matched to selection tables 2019\_SV\_Selection and 2019\_IW\_Selection.

<sup>47</sup> National Taxpayer Advocate 2019 Annual Report to Congress TAS Case Advocacy section, *infra*.

## RECOMMENDATIONS

### Administrative Recommendations to the IRS

The National Taxpayer Advocate recommends that the IRS:

1. Work with SSA to speed up the transmission of paper W-2 data to earlier in the year.
2. Identify acceptable FPR and Operational FPR ranges each year as part of its refund fraud projections.
3. Continue to learn from the returns that were part of the FPR to further refine the filters and continually work to lower the false positive rate.
4. Increase RIVO staffing to improve the processing time for validating information on returns and assigning returns to a compliance stream for further treatment.
5. Send an interim letter every 60 days to all taxpayers whose returns it is holding in the PRWVH program.
6. Revise the Letter 4464C initial contact notice instructing taxpayers to review their returns to verify the income and withholding reported is accurate and correct, and if a mistake is identified, to file an amended return.
7. Instruct RIVO to send Letter 86C, Referring Taxpayer Inquiry/Forms to Another Office, informing taxpayers that it has referred their return to another IRS function and providing them with the name of the specific function and contact information.