

## **FILING SEASON REVIEW**

Each year, the nation's taxpayers incur a heavy burden, spending an estimated 6.1 billion hours and \$168 billion to comply with the tax code and file their returns, which is often their only interaction with the IRS.<sup>1</sup> Similarly, the IRS faces enormous challenges in each filing season, processing over 145 million individual tax returns while updating its systems to account for legislative changes and revenue protection measures. The IRS views a filing season as a success if it hits certain numerical processing targets. However, taxpayers may have a different experience. The IRS does not consider the long times taxpayers often wait when trying to get help at a Taxpayer Assistance Center (TAC) or on a toll-free line, or even the fact that many of these taxpayers cannot obtain assistance at all, in determining whether a filing season was a success.

From the taxpayers' perspective, a successful filing season means they can submit their returns easily, electronically or on paper. If the IRS finds a problem, the taxpayer would receive a clear explanation and an opportunity to fix the problem in one step, through self-help online tools, a telephone call, correspondence, or a visit to a TAC.

However, in the current environment, this often is not the case. In the 2013 filing season, taxpayers experienced challenges in the following areas:

- A late start to the filing season;
- Additional forms, such as the one required to claim an education credit (Form 8863), were delayed into March;
- Low levels of phone service;
- Long wait times to reach a customer service representative;
- Limited services available at TACs; and
- Fewer TACs that could accept cash payments.

### **Late Legislation Delayed Start of the 2013 Filing Season**

Congress often considers legislation to extend expiring tax provisions and make other changes to the tax code. In recent years, Congress has passed this legislation late in the calendar year, compressing the time available for the IRS to update and test programming for the filing season, and to revise tax forms and instructions. The IRS faced significant hurdles in changing programming to implement late legislative changes enacted on January 2, 2013.<sup>2</sup> While many individuals could file on January 30, about two weeks after the traditional start of the filing season, certain returns were delayed

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<sup>1</sup> National Taxpayer Advocate 2012 Annual Report to Congress 5-6.

<sup>2</sup> American Taxpayer Relief Act (ATRA) (Jan. 2, 2013).

until March 4.<sup>3</sup> The IRS opened the filing season for more taxpayers as it completed programming for additional forms.<sup>4</sup>

- February 10, 2013: Returns with Form 4562, *Depreciation and Amortization (Including Information on Listed Property)*;
- February 14, 2013: Returns with *Form 8863, Education Credits*; and
- March 4, 2013: Filing season open for all individuals.

The late legislation imposed significant burden on taxpayers, return preparers, and the IRS. The compressed timeframe limited software testing and could have contributed to the problems surrounding education credits, discussed later in this section.

In FY 2014, TAS will continue to recommend that Congress pass “extender” legislation early enough to give the IRS adequate time to program and test tax code changes affecting the current filing season. Additionally, TAS will participate in the IRS’s Filing Season Readiness initiative and assist the IRS in identifying potential problems before they arise, such as those associated with the First-Time Homebuyer Credit (FTHBC) repayment programming, discussed below. TAS will continue to encourage TAS and IRS employees, practitioners, and taxpayers to submit potential systemic issues to the Systemic Advocacy Management System (SAMS) to assist TAS in the early identification of problems, such as the missing information from Form 8863, *Education Credits*, discussed below.

### **Miscommunications between the IRS and Modernized E-File (MeF) Software Vendors and Paid Tax Preparers Led To Refund Delays for Taxpayers and Personnel-Intensive Corrective Actions for the IRS**

During the first three weeks of the 2013 filing season, the IRS rejected more individual returns for error resolution than it typically does (8.39 percent versus approximately four to six percent).<sup>5</sup> As of February 22, 2013, inventories of individual returns awaiting correction had increased nearly 330 percent compared to the same period the previous year.<sup>6</sup> Fifty-two percent of that inventory (over 520,000 taxpayers) was over aged,

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<sup>3</sup> IRS, *IRS Plans Jan. 30 Tax Season Opening for 1040 Filers*, IR-2013-2 (Jan. 8, 2013), available at <http://www.irs.gov/uac/Newsroom/IRS-Plans-Jan.-30-Tax-Season-Opening-For-1040-Filers>.

<sup>4</sup> IRS, *IRS to Accept Tax Returns with Education Credits, Depreciation Next Week*, IR-2013-18 (Feb. 8, 2013), available at <http://www.irs.gov/uac/Newsroom/IRS-To-Accept-Tax>Returns-with-Education-Credits,-Depreciation-Next-Week> and *IRS Now Accepting All 2012 Returns*, IR-2013-25 (Mar. 4, 2013), available at <http://www.irs.gov/uac/IRS-Now-Accepting-All-2012>Returns>.

<sup>5</sup> IRS, Submission Processing Miscellaneous Monitoring Report, Headquarters, (week ending Feb. 22, 2013, Feb. 24, 2012, Feb. 25, 2011). Comparatively, in the last week in February of filing season 2012 the ERS error rate was 4.2 percent, and in filing season 2011 it was 6.4 percent.

<sup>6</sup> For a discussion of how this affected TAS case volumes, see *Case Advocacy, infra*. IRS, Submission Processing Miscellaneous Monitoring Report, Headquarters, (week ending Feb. 22, 2013). In filing season 2013, over one million returns were awaiting correction as of Feb. 22, compared to almost 250,000 returns during the same period in 2012.

meaning the IRS did not work the returns in the prescribed timeframe.<sup>7</sup> The IRS determined the increase was due to incomplete Forms 8863, *Education Credits*, and Form 8867, *Paid Preparer's Earned Income Credit Checklist*.

TAS notified the IRS that lines 23 through 26 on Forms 8863 transmitted by a limited number of Modernized e-File (MeF) vendors were not appearing on IRS systems. At the same time, the vendors were reporting the same problem to the IRS, yet the IRS did not change its processes. The IRS determined that the taxpayers had input the information on those lines, but the vendor's software failed to transmit the data to the IRS during e-filing. The vendors fixed the problem on February 22, 2013, yet for nearly three more weeks, the IRS continued to delay return processing and refunds and mailed notices to taxpayers asking for the missing information.<sup>8</sup> After receiving vendor affidavits related to the missing Form 8863 data, on March 12, 2013 the IRS began manually releasing the delayed tax returns for processing without waiting for taxpayer responses.<sup>9</sup> The IRS completed all the manual releases (for those where there was no other issue requiring a taxpayer response) by March 28, 2013, allowing the IRS to resume processing the returns. The missing Form 8863 information impacted over 800,000 returns.<sup>10</sup>

TAS's early alert systems allowed it to identify this issue and advise the IRS that although both TAS and the vendors had found the root cause of the problem, the IRS was still unnecessarily corresponding with taxpayers and delaying their refunds. Over 800 taxpayers contacted TAS for help with missing Form 8863 information.<sup>11</sup> TAS worked with the Wage and Investment division on a streamlined process to resolve over 850 cases.<sup>12</sup> Additionally, 21 SAMS submissions identified the problem with Form 8863.<sup>13</sup> TAS will continue to closely monitor data to identify systemic problems with IRS filing season processes and procedures and will work closely with the IRS to resolve any issues.

Similarly, the IRS discovered many Forms 8867, *Paid Preparer's Earned Income Credit Checklist* were missing or incomplete. Preparers complete this checklist to describe the actions taken during return preparation to verify taxpayers' eligibility for the Earned Income Tax Credit (EITC). The IRS delayed processing the associated tax returns while it contacted the taxpayers for the missing information, even though the preparers were responsible for the form. Requesting Form 8867 directly from the taxpayers imposed an unnecessary burden. This is the second year the IRS required preparers to file Form 8867 with tax returns claiming the EITC, but the first year it delayed return processing because of missing forms. The IRS sent a letter to preparers who submitted 2011 tax returns claiming the EITC without attaching Form 8867, warning them of their

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<sup>7</sup> IRS, Submission Processing Miscellaneous Monitoring Report, Headquarters, (week ending Feb. 22, 2013).

<sup>8</sup> IRS, Servicewide Electronic Research Program (SERP) Alert 13A0205 (Mar. 11, 2013).

<sup>9</sup> IRS, SERP Alert 13A0203 (Mar. 12, 2013).

<sup>10</sup> IRS, SERP Alert 13A0297 (April 16, 2013).

<sup>11</sup> TAMIS Data (Mar. 19 and 22, 2013).

<sup>12</sup> *Id.*

<sup>13</sup> SAMS submissions from Jan. 1, 2013 to June 4, 2013; data retrieved June 4, 2013.

failure to meet due diligence requirements, and stating that the IRS would assert due diligence penalties starting with 2012 returns.<sup>14</sup>

A Treasury Inspector General for Tax Administration (TIGTA) report identified as many as 80,585 preparers who filed 612,622 returns claiming the EITC without the form through March 7, 2013.<sup>15</sup> Two weeks into the filing season, the IRS made a policy decision to cease delaying these returns and instead to address the compliance issue directly with the preparers.<sup>16</sup> The IRS began manually releasing the returns delayed during the first two weeks for processing on February 15, 2013.<sup>17</sup>

In FY 2014, TAS will encourage the IRS to work with software vendors to require e-filed preparer returns that claim the EITC to include Form 8867. The IRS should resolve any due diligence issues from paper returns missing Form 8867 by contacting the preparer, not the taxpayer.

**PLACEHOLDER FOR ADDITIONAL TEXT – APPROXIMATELY 7 PAGES**

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<sup>14</sup> IRS, *Tax Preparer Toolkit – What is Form 8867?* (Oct. 24, 2012), available at <http://www.eitc.irs.gov/rptoolkit/dd/Form8867/>. The IRS sent Letter 4989 to affected preparers in July 2012.

<sup>15</sup> These preparers could face over \$306 million in penalties (\$500 per return) at the completion of the filing season. TIGTA, Ref. No. 2013-40-035, *Interim Results of the 2013 Filing Season 8* (Mar. 29, 2013).

<sup>16</sup> IRS, SERP Alert 13A0168 (Feb. 25, 2013). TIGTA, 2013-40-035, *Interim Results of the 2013 Filing Season 8* (Mar. 29, 2013).

<sup>17</sup> IRS, SERP Alert 13A0152 (Feb. 15, 2013).