

TAS Research Objectives

TAS Research focuses on understanding how IRS procedures and tax law affect taxpayers and how taxpayers react to IRS actions or inactions. We use our research to provide feedback and recommendations based upon our findings. TAS Research's overall objectives are to improve IRS efficiencies and assist the IRS with balancing compliance and enforcement efforts while protecting taxpayer rights and providing quality service. Research into the impact of tax law and the administration of taxes provides the necessary data to recommend changes that are beneficial to taxpayers and tax administration. Over the years, TAS research has led to detecting problems in administering the tax laws. Moreover, this data informs our recommendations for legislative and procedural changes in the design and administration of the tax laws and is shared with the IRS, members of Congress, and the public.

Four research projects are scheduled for the remainder of fiscal year (FY) 2021 and FY 2022.

1. STUDY TAXPAYER NEEDS AND PREFERENCES FOR IRS ONLINE ACCOUNT ACTIVITIES

The IRS allows individual taxpayers to establish an online account and perform online activities¹ including:

- Viewing information such as balance due and payment history;
- Establishing an installment agreement or making a payment;
- Accessing account transcripts;
- Checking on the status of a refund;
- Verifying identity when requested by the IRS or obtaining an Identity Protection Personal Identification Number;
- Applying for an Employer Identification Number; and
- Verifying income for financial transactions such as obtaining a loan.

The National Taxpayer Advocate has advocated for a robust online account containing complete information in an easy-to-understand format with a singular access point that would reduce or eliminate the need for many individuals, businesses, or practitioners to contact the IRS via telephone. Effective self-service tools with specific account details will help save scarce IRS resources. However, to be effective, the IRS needs to offer online services that taxpayers find to be beneficial and easy to use. While the online activities offered are helpful to individual taxpayers, the IRS should prioritize developing additional online functionality and services, considering taxpayer needs and preferences and providing similar services to businesses or other taxpayers.

Additionally, taxpayers must be able to easily establish and maintain online accounts. Current authentication requirements often thwart taxpayers' ability to establish and access online accounts. Fewer than half of

¹ Business and other taxpayers do not always have similar online account functionality.

the individuals who have sought to establish an online account with the IRS have succeeded in doing so.² Taxpayers' inability to establish and use online accounts renders the accounts meaningless. As the IRS moves to the Secure Access Digital Identity system using a credentialing service provider, it should ease the authentication challenges taxpayers are currently experiencing.

This project will review how taxpayers access each digital tool, the online account features offered to taxpayers, the type of taxpayer that can access the tool, and what authentication requirements accompany the IRS digital tools. These features and their authentication requirements will be compared to those established by taxing authorities in states, other countries, and other commercial financial institutions. This study will also determine what account activities individuals, businesses, and other taxpayers or their representatives in the United States would most like to be able to conduct online and what authentication criteria they could meet.

Objective 1 for FY 2022 – TAS will determine taxpayer needs and preferences for establishing online accounts with the IRS and authenticating secure access to those accounts.

- Activity 1: Ascertain what common online account activities taxpayers in states or other nations can perform.
- Activity 2: Determine what authentication procedures taxpayers in states or other nations must use to access their accounts.
- Activity 3: Quantify unauthorized accesses in the online accounts of the taxing authorities of states or other nations or the online accounts of various financial institutions.
- Activity 4: Determine what online account features and capabilities U.S. taxpayers want to access.
- Activity 5: Determine what authentication criteria U.S. taxpayers could meet.
- Activity 6: Analyze if the authentication criteria that U.S. taxpayers can meet differs by demographics such as ethnicity, gender, or income.

2. STUDY TAXPAYER NON-RESPONSE TO CERTAIN IRS ACTIONS

The IRS uses notices and letters to communicate with taxpayers as a relatively inexpensive means of communication. Sometimes, the IRS needs to communicate with taxpayers to obtain additional information, correct perceived inaccuracies, audit reported amounts, or simply transmit information to taxpayers about taxes due and owed to the IRS. When a taxpayer does not respond to the letter or notice, the IRS assumes that its determination is correct. For example, the IRS presumes that a taxpayer whose refund is frozen by the Refund Integrity Verification Organization has submitted a fraudulent refund claim when he or she does not respond to the IRS notice requesting identity verification. Similarly, a taxpayer who does not respond to a correspondence audit notice or a math error notice will be assessed in accordance with the IRS determination.

While these procedures are efficient from an IRS perspective, taxpayers may be harmed. For instance, a study on taxpayer barriers during Earned Income Tax Credit (EITC) audits indicated that over a quarter of the

² IRS, Office of Privacy, Governmental Liaison and Disclosure response to TAS information request (Oct. 13, 2020) (stating that the authentication rate for IRS online applications requiring the highest level of assurance authentication, including online taxpayer accounts, was 42 percent in FY 2020).

taxpayers did not understand they were being audited.³ Likewise, a 2011 study of math error notices issued to taxpayers where a dependent's Taxpayer Identification Number (TIN) was incorrect indicated that about 40 percent of sampled cases appeared to have a correct TIN for the dependent but with transposed numbers.⁴ Nevertheless, these taxpayers did not respond, costing the taxpayers an estimated \$44 million of potential refunds.⁵ Taxpayers, particularly those with lower incomes, often do not respond to IRS notices.⁶

This project will seek to quantify the reasons taxpayers did not respond to certain IRS notices or letters and to recommend changes to IRS procedures that would improve the response rate to IRS notices. Because the reasons for non-response may vary by the type of IRS notice or other correspondence, we plan to conduct projects that explore the lack of taxpayer response to IRS correspondence depending on the general reason the IRS has contacted the taxpayer. We expect this study may include analysis of internal data along with potential taxpayer focus groups and surveys. Initially, this study will focus on taxpayer non-response in correspondence audits and refund freezes in suspected identity theft. The project will also develop a list of other instances where taxpayers rarely respond to IRS actions, including non-response to collection notices, math error notices, etc.

Objective 2 for FY 2022 – TAS will analyze why taxpayers often do not respond to various types of IRS notices and letters and how to improve the response rate.

- Activity 1: Develop a list of notices and letters with high non-response rates.
- Activity 2: Review internal processes to identify ways to improve efficiency when processing taxpayer responses.
- Activity 3: Identify ways to clarify communication so taxpayers understand what actions they should take.
- Activity 4: Conduct focus groups and surveys with taxpayers who have not responded to specific types of IRS correspondence to determine and quantify the reasons for non-response.

3. STUDY THE EFFECT OF POTENTIAL CHANGES TO THE EARNED INCOME TAX CREDIT STRUCTURE

In its FY 2020 Objectives Report to Congress, TAS included a study that recommended a variety of proposed computational changes to the EITC.⁷ The most significant recommended change included altering the credit to include both a per-worker credit based on income and a universal per-child benefit. The study also recommended revising the definition of a qualifying child to more closely reflect the circumstances of primary caregivers and the children in their care.

3 National Taxpayer Advocate 2007 Annual Report to Congress vol. 2, at 94-116 (*IRS Earned Income Tax Credit Audits – A Challenge to Taxpayers*). Survey results showed that 26.5 percent of taxpayers did not understand their EITC claim was being audited.

4 See National Taxpayer Advocate 2011 Annual Report to Congress vol. 2, at 114-144 (*Math Errors Committed on Individual Tax Returns: A Review of Math Errors Issued for Claimed Dependents*). TAS examined a small sample of cases where EITC was disallowed by the IRS because of a missing or incorrect TIN and had not been subsequently allowed. Our review of this sample showed that over 40 percent of these taxpayers appeared eligible for the credit based on IRS internal records.

5 *Id.*

6 In FY 2020, about 45 percent of taxpayers with total positive incomes under \$50,000 did not respond to the IRS audit of their individual income tax return. National Taxpayer Advocate 2020 Annual Report to Congress, at xiv. This rate includes taxpayers whose audit notices were undeliverable.

7 National Taxpayer Advocate Fiscal Year 2020 Objectives Report to Congress vol. 3, at 1-93 (*Earned Income Tax Credit: Making the EITC Work for Taxpayers and the Government: Improving Administration and Protecting Taxpayer Rights*).

Over 25 million EITC claims are made annually;⁸ however, the current improper payment rate for EITC exceeds \$17 billion annually and over 25 percent of the EITC paid out by the IRS.⁹ The documentation requirements for EITC are onerous and often EITC taxpayers may not be able to provide the documentation, if audited, even when eligible for the credit. Therefore, many eligible taxpayers may “fail” the audit and be denied the credit. While the tax law changes for 2018 modified the way the credit was indexed, the changes did not affect the fundamental structure of the credit or the definition of a qualifying child. This research project will focus on analyzing various worker and child credit scenarios that would allow lower income taxpayers with children to receive similar benefits as under the current EITC structure while also ensuring that other taxpayers would not receive a higher credit per child. It will also explore options to make it easier to verify eligibility requirements, reducing the need for extensive audits of EITC claims.

This project will explore the creation of two credits, which would provide similar economic support to low-income workers with children as the EITC but could be administered without the high improper payment rate. This study will analyze various formulas for replacing the EITC with a per-worker credit based on earned income and establishing a universal per-child benefit for low-income taxpayers.

Objective 3 for FY 2022 – TAS will analyze tax return data, administrative EITC audit files, and census data to recommend a credit structure that is easier to administer while generating similar benefits to low-income families.

- Activity 1: Identify possible options for a new earnings-based per-worker credit and per-child credit to replace the existing EITC credit.
- Activity 2: Compare the existing EITC to the credit amount afforded by possible new per-worker and per-child structures and the effect to taxpayers not currently eligible for EITC.
- Activity 3: Analyze the outcome of prior EITC audits if the rules for the proposed per-worker and per-child credit were in place.
- Activity 4: Explore IRS and Census Bureau data to quantify the number of children who would qualify their parents for a per-child tax credit under various definitions of a “qualifying child.”
- Activity 5: Estimate the new improper payment rate for EITC based on the rules for the proposed per-worker and per-child credit.

4. STUDY PROCESSING ERRORS IDENTIFIED WITH FORMS 4029

Taxpayers who are members of certain religious groups can qualify to be exempt from Social Security tax if recognized as being officially opposed to Social Security benefits.¹⁰ To be eligible to receive this exemption, taxpayers must file a Form 4029, Application for Exemption From Social Security and Medicare Taxes and Waiver of Benefits, with the Social Security Administration (SSA). If the form is completed correctly, SSA will approve Form 4029, providing the taxpayer an exemption from Social Security taxes. SSA will forward the approved form to the IRS. IRS procedures require it to place a marker on the taxpayer’s entity record

8 IRS, About EITC, <https://www.eitc.irs.gov/eitc-central/about-eitc/about-eitc> (last visited May 25, 2021). The IRS estimates that the EITC program lifts 5.6 million children out of poverty. *Id.*

9 Treasury Inspector General for Tax Administration, Ref. No. 2020-40-025, *Improper Payment Reporting Has Improved; However, There Have Been No Significant Reductions to the Billions of Dollars of Improper Payments* 3 (Apr. 30, 2020).

10 IRC § 1402; Treas. Reg. § 1.1402(h)-1. SSA, Pub. No. 17-018, *How Religious Exemptions Work* (Jan. 2018), <https://www.ssa.gov/pubs/EN-17-018.pdf>.

indicating the approved Social Security tax exemption to prevent the IRS from assessing Social Security tax on reported income.

During FY 2021, TAS analyzed tax year 2018 accounts for taxpayers with approved Form 4029 exemptions. TAS compared those accounts with the accounts of taxpayers who were subsequently assessed Social Security tax on their earned income. These taxpayers did not report Social Security tax on their tax return, suggesting they believed that their exemption request had been approved.

Our initial analysis showed that most Form 4029 indicators were correctly placed on the 2018 tax return account; however, it also indicated that thousands of taxpayers' exemptions from Social Security tax were not recognized, or they were not recognized until after the IRS had already processed the tax return and assessed Social Security tax. TAS reviewed a small sample of those accounts where the Social Security tax exemption was not processed or processed after the IRS assessed the Social Security tax on the 2018 tax return. This small sample indicated that the IRS erroneously assessed Social Security tax on these returns, and in some cases, the taxpayer has never requested a refund of the additionally assessed taxes, even though the taxpayer has a valid 4029 exemption. Based upon our findings, during FY 2022, TAS will review a statistically valid random sample where the IRS assessed additional Social Security tax on tax returns with valid 4029 exemptions.

Objective 4 for FY 2022 – TAS will determine causes of Form 4029 processing errors and work with the IRS to implement changes to its processing procedures. TAS will share the data and our research with the IRS for outreach endeavors to educate taxpayers on potential errors and best practices in filing Form 4029.

- Activity 1: Study a statistically valid sample of tax year 2018 individual income tax returns with unrecognized Form 4029 exemptions to determine how often and why the IRS did not recognize the Social Security tax exemption or did not recognize the exemption until after it processed the return and assessed Social Security tax, and determine whether the IRS corrected its error.
- Activity 2: Recommend processing changes for individual income tax returns, which will prevent the IRS from erroneously assessing Social Security tax against taxpayers with approved Form 4029 exemptions.
- Activity 3: Advocate for the IRS to initiate procedures to refund or abate erroneous assessments of Social Security tax for Form 4029 taxpayers.
- Activity 4: Obtain data to assist TAS with outreach efforts to members of religious groups commonly filing Forms 4029 on how to improve the quality of these forms so the forms can be approved quickly by SSA and processed by the IRS prior to the processing of any tax returns for which the exemption should be applicable.