

TAS Research Initiatives

The National Taxpayer Advocate is a strong proponent for the role of theoretical, cognitive, and applied research in effective tax administration. TAS Research is currently conducting a number of new and continuing research initiatives. A primary focus of these research initiatives is to better understand taxpayer compliance behavior and to evaluate IRS programs by balancing the goals of taxpayer compliance with minimizing taxpayer burden. Several research initiatives that TAS Research continues to conduct for the remainder of fiscal year (FY) 2019 and FY 2020 are detailed below.

TAS Measures the Number and Characteristics of Taxpayers Who Qualify for TAS Services But Do Not Seek TAS Assistance

TAS defines the number of taxpayers who qualify for TAS assistance but who do not seek such assistance as the TAS underserved population. Periodically, TAS measures the underserved population to assess the number and characteristics of taxpayers who are negatively impacted by IRS operations and to determine how well TAS services are known among those taxpayers eligible for TAS assistance. Another purpose of this research is to determine how best to communicate with eligible taxpayers about TAS's existence and to determine the demographics of those taxpayers who are more likely to need TAS assistance. This information allows TAS to target its outreach to underserved demographic groups, while also understanding the best communication channels to reach these taxpayers. Prior to the current study, the most recent study of the TAS underserved population was over six years ago. The 2012 study estimated the TAS underserved population at nearly nine million taxpayers.

This TAS research initiative will also include focus groups with underserved taxpayers to better understand why these taxpayers have not sought TAS assistance. TAS plans to use a contractor to conduct four focus groups in diverse regions of the country. We will target one focus group in an area where we would expect to receive considerably more TAS cases than we have historically received. This work will help us understand how we can improve the communication of TAS services in this area.

The first survey will size the TAS underserved population. The contractor will then conduct a subsequent survey to determine the composition of the underserved population. Additionally, as mentioned, TAS will conduct four focus groups to better understand why some taxpayers who qualify for TAS services do not seek TAS assistance. TAS expects the survey and focus group work to be completed by the end of FY 2019 with the results to be published in FY 2020.

TAS Plans to Test the Effectiveness of Prototype Automated Collection System Letters 11, Which Afford Collection Due Process Rights to Many Taxpayers

The IRS is currently preparing to test four redesigned Automated Collection System (ACS) Letter 11 prototypes. In addition to requesting immediate payment of a tax delinquency now assigned to ACS for collection, this letter also provides the official legal notice of a taxpayer's right to a Collection Due Process (CDP) hearing. While the IRS does intend to measure the number of taxpayers who avail themselves of their CDP rights after receiving one of the new redesigned Letter 11 prototypes being tested, most of the measures are concerned with the letter's effectiveness in securing delinquent payments. In fact, the four redesigned Letter 11 prototypes no longer contain the attachment whereby a taxpayer requests a CDP hearing. Instead, the resigned letters refer the taxpayer to the IRS website to obtain a copy of the form

required to request a CDP hearing. This will present a barrier for the 14 million taxpayers who have no access to the internet and the 41 million taxpayers who do not have broadband access in their homes.¹

During FY 2019, TAS will be testing two redesigned Letter 11 prototypes as part of the IRS study. These letters will focus on taxpayer rights. One version will emphasize that a taxpayer has CDP rights, including the possible beneficial effects of requesting a timely CDP hearing. The second redesigned letter will focus on the rights a taxpayer will forfeit if the taxpayer does not submit a timely CDP request. However, TAS cannot make changes to the letter which deviate from the IRS's baseline redesigned Letter 11. Therefore, TAS plans to contract with external researchers who have specialized experience with both behavioral research and tax compliance to test additional Letter 11 prototypes in FY 2020, which deviate from the IRS baseline. This work will allow TAS to draw upon the experience of external professionals knowledgeable in taxpayer behavior to design this letter in a way that encourages taxpayers to exercise their CDP rights.

Additionally, TAS will test the effectiveness of different letters with different types of taxpayers. As one example, many taxpayers will not currently have the financial wherewithal to afford making payments. TAS believes it is important to send notices to these taxpayers to encourage a resolution of the account, not just elicit a payment the taxpayer cannot really afford. Conversely, an emphasis on information consumption and behavioral messaging can garner a better response and more payments from those taxpayers likely able to afford payments. The IRS has systemically available data to determine with a high degree of accuracy whether the taxpayer can afford to satisfy or make payments towards satisfying their tax delinquency.² Most importantly, all redesigned Letter 11 prototypes should be rights-based and focus on the CDP rights afforded to taxpayers. During recent years, only about two percent of taxpayers have availed themselves of their CDP rights.³ A Letter 11 which focuses on taxpayer rights may increase the extremely low number of taxpayers requesting a CDP hearing. Since the purpose of the CDP hearing is to identify appropriate collection alternatives and other resolutions (*e.g.*, innocent spouse relief) early in the collection process, increased use of these hearings will benefit both taxpayers and the IRS.

TAS expects the design for this study to begin in early FY 2020. We plan to mail the actual letters during the first half of FY 2020, with the analysis to be completed by the end of the year.

TAS Studies the Longer-Term Compliance Effect of its Earned Income Tax Credit (EITC) Educational Letters

In early 2016, prior to the beginning of the filing season for tax year (TY) 2015 returns, TAS sent letters to a random sample of about 7,000 taxpayers who appeared to have erroneously claimed Earned Income Tax Credit (EITC) on their TY 2014 return, but who were not selected for audit. The apparent error was based on a residency, relationship, or duplicate claimed EITC dependent rule tripped in the IRS Dependent Database (DDB) by the taxpayer's TY 2014 return. We also selected a control group comprised of taxpayers whose TY 2014 return was not audited, nor did they receive a TAS educational letter, but they had similar DDB scores to those taxpayers who were audited or received an educational letter.

1 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2 64 (Research Study: *A Further Exploration of Taxpayer Varying Abilities Toward IRS Options for Fulfilling Common Taxpayer Needs*).

2 National Taxpayer Advocates 2018 Annual Report to Congress 236 (Most Serious Problem: *Economic Hardship: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*).

3 *Id.* at 216 (Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*).

The results of the study showed that taxpayers receiving the TAS letter targeted toward taxpayers who broke DDB relationship rules were statistically less likely than the control group to make a relationship error on their TY 2015 return filed in 2016. When projecting the reduction in subsequent EITC claims because of a dependent not meeting the EITC relationship test, the TAS educational letter would be expected to eliminate \$47 million dollars of improper EITC claims annually. The TAS educational letters did not have a statistically significant effect on the number of taxpayers who subsequently filed a TY 2015 return with a dependent who appeared not to meet the residency test. When compared to similar taxpayers who were audited, subsequent EITC compliance improved for both audited taxpayers who broke residency or relationship DDB rules when compared to either the taxpayers who received the TAS educational letter or the control group. Interestingly, however, audited taxpayers who claimed a dependent also claimed on another tax return were more likely to make a different EITC error the next year, when compared to the group receiving a TAS letter or the control group.

In early 2017, TAS repeated this study with taxpayers who tripped DDB rules on their TY 2015 returns. In addition to the three groups of taxpayers used in the prior year, TAS also had a fourth group of taxpayers who tripped a residency DDB rule whose educational letter also contained the offer of a dedicated “Extra Help” toll-free number to call with questions about their EITC eligibility for their upcoming TY 2016 tax return. The results of this study were very similar to the results from the prior year with taxpayer receiving a TAS letter because of tripping a DDB relationship rule in the prior year being again statistically less likely to file a TY 2016 return repeating the relationship error.⁴ The standard TAS educational letter mailed to taxpayers with an apparent residency error in the prior year again showed no statistically significant effect in preventing these taxpayers from making an apparent residency error on their TY 2016 return. However, the TAS educational letter with a dedicated “Extra Help” telephone number to call for assistance mailed to a separate group of taxpayers who also claimed an EITC dependent not appearing to meet the residency requirements in the prior year did show a statistically significant reduction in the number of taxpayers subsequently claiming a child who appeared not to meet the EITC residency requirement. Projected to the entire population of taxpayers who made only an apparent residence error, an educational letter with a dedicated help line would prevent an estimated \$44 million in improper EITC claims.

During FY 2020, TAS will examine the EITC compliance of these taxpayers for returns due in the years after the original TAS educational letter was received. Although the TAS educational letters improved compliance in the immediate year for taxpayers appearing to not meet the relationship EITC eligibility rule and on taxpayers appearing to not meet the EITC residency eligibility rule if a special telephone number to receive assistance was also provided, it is unknown whether the educational letters had a lasting effect on compliance, or if the positive impact of the educational letter is limited to the tax return due immediately after the letter is received. We will compare the longer-term EITC compliance of taxpayers receiving the TAS educational letter, taxpayers who were audited previously, and a control group who were neither audited nor received the TAS letter. The results will assist the IRS by gauging whether “soft” treatments must occur annually or can be issued at less frequent intervals.

⁴ The reduction of improper Change EITC to Earned Income Tax Credit (EITC) claims resulting from EITC dependents not meeting the relationship test was \$53 million, when projected to the entire population of EITC dependents breaking only a Dependent Database (DDB) relationship rule.

TAS Studies the Effect of Correspondence and Face-to-Face Audits on Subsequent Compliance

TAS has contracted with experts specializing in tax compliance and economic psychology to study if the effect of an audit on subsequent compliance is influenced by whether the audit is conducted through correspondence or through face-to-face contact with an IRS examiner. TAS previously published a study by this contractor which explored the attitudinal effects of audits on Schedule C taxpayers occurring between 2010 and 2015.⁵

The overall audit rate for U.S. individual income tax returns has decreased from one percent of returns filed in 1990 to sixth-tenths of one percent of returns filed in 2016.⁶ The composition of audits has also changed substantially over this period. Whereas face-to-face audits accounted for the majority (62 percent) of all examinations of returns filed in 1990, the lion's share (77 percent) of all audits of returns filed in 2016 were conducted through correspondence.⁷ One of the study findings was that less than 40 percent of taxpayers who experienced an IRS correspondence audit recalled being audited. Conversely, those taxpayers who underwent a face-to-face audit recalled the audit with much greater frequency.⁸

The IRS shift to more correspondence audits and the fact that nearly two-thirds of taxpayers audited by correspondence do not recall the audit compels TAS to compare the effect of correspondence and face-to-face audits on subsequent taxpayer compliance. The contractor will develop an extended statistical framework to distinguish the effects of correspondence and face-to-face examinations on future taxpayer reporting behavior. The contractor will then apply this framework to data samples containing tax-related information on audited and unaudited taxpayers to measure the impact of each type of examination. The research will focus on when the audit method (correspondence or face-to-face) produces significantly different rates of subsequent compliance. The results from this analysis are significant for the IRS's future plans for audit resource allocations. TAS expects this study to be ongoing through FY 2019 with a final report to be published in FY 2020.

TAS Studies the Downstream Effects of Math Errors Issued by the IRS

The IRS issues math errors when IRS computer algorithms detect clerical and mathematical errors. However, apparent errors may actually occur because the taxpayer has entered information incorrectly on another part of the return. Furthermore, some of the clerical errors are simple transpositions of numbers that the IRS has the data to correct without issuing the math error. For example, if a dependent claimed for EITC purposes has a transposed Social Security number (SSN), the IRS will disallow the EITC for that child even though the IRS has access to the child's SSN data and can easily see that the incorrectly entered SSN is a simple transposition error, as the SSN has been entered correctly on the taxpayer's past several years' tax returns. In a TAS study published in 2011, 55 percent of the math errors issued disallowing a dependency exemption because of a child's incorrectly entered SSN were later reversed by the IRS.⁹ In addition to the disallowance of the dependency exemption, the incorrect SSN affected

5 National Taxpayer Advocate 2018 Annual Report to Congress vol. 2 77-130 (Research Study: *What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*).

6 IRS Data Book fiscal year (FY) 1991 IRS, Table 11 and IRS Data Book FY 2017, Table 9a.

7 IRS, 2017 Data Book, Oct. 1, 2016 to Sept. 30, 2017, Table 9a. *Examination Coverage: Recommended and Average Recommended Additional Tax After Examination by Type and Size of Return, FY 2017*.

8 National Taxpayer Advocate 2018 Annual Report to Congress vol. 2 77-130 (Research Study: *What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*).

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

other credits including child and dependent care expenses, child tax credits, additional child tax credits, and education credits.¹⁰ Furthermore, during a review of a sample of these math errors that remain unreversed, we found that over half of the returns were entitled to claim the dependent for one of these credits or the EITC credit; however, the taxpayer never objected to the math error. When projected to the entire population of taxpayers with these unreversed math errors for an incorrect SSN for a dependent, taxpayers forfeited at least \$44 million of credits.

While many IRS math errors have low abatement rates, some IRS math errors do not. TAS has compiled the IRS math errors issued for TY 2016, noting certain math errors, including the ones described above, still have very high abatement rates. TAS is studying those math errors frequently reversed to analyze the subsequent cost to the IRS of reversing the math error as well as the burden placed on taxpayers to correct an error, which could often be corrected by the IRS, without taxpayer involvement. Furthermore, TAS is calculating the amount of unnecessary tax burden being imposed on taxpayers who do not question the IRS decision to issue the math error, even though the taxpayer claim was valid.

During FY 2020, TAS will analyze math errors issued by the IRS for TY 2017 to see if the abatement rates detected in TY 2016 are still present. We will also quantify the cost to the IRS to reverse unnecessary math errors, estimate the taxpayer time to respond to an incorrect math error issued by the IRS, and calculate the amount of additional taxes paid unnecessarily by taxpayers who do not refute the erroneous IRS math error. We expect to complete this study and report on the findings during FY 2020.

¹⁰ For Notice Code 743 (incorrect Taxpayer Identification Number (TIN) for EITC), 61 percent, or 35,000 were resolved fully or partially. *Id.* at 134.